



CA FINAL

ADVANCED AUDITING, ASSURANCE, AND PROFESSIONAL ETHICS

**CONCEPTS + QUESTION BANK
TOGETHER**

CA Hemant Somani

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PREFACE

A highly skilled professional team of CA Wallah works arduously to ensure that the students receive the best content for their CA-Final exams.

A plethora of CA Study Material is available in the market but CA Wallah professionals at PW are continuously working to provide supreme quality study material for the CA Final students. From the beginning, the content team comprising Subject Matter Experts, Content Creators, Reviewers, DTP operators, Proofreaders, and others is involved in shaping the material to their best knowledge and experience to produce powerful content for the students.

CA Wallah Faculties have adopted a novel style of presenting the content in easy-to-understand language and have provided the content team with expert guidance and supervision throughout the creation and curation of this book.

PW's CA Wallah strongly believes in conceptual and fun-based learning. CA Wallah provides highly exam-oriented content to bring quality and clarity to the students.

This book adopts a multi-faceted approach to mastering and understanding the concepts by having a rich diversity of questions asked in the CA Final examination and equipping the students with the knowledge for this highly competitive exam.

The main objective of this book is to provide an edge to your preparation with short & crisp yet high quality content

ABOUT AUTHOR

Hellow Doston !!

When I was a student I also faced the same problem that you may be facing right now, Audit is very much vast, need Full Ratta-Fication as well as understading for MCQ & Case scenerios,

So I always wanted to create a Single book which is All in One solution of all the problem, i.e. Comprehensive coverage in Summarised manner, Memory techniques for rattafication & all the question at one place. Which I can cover easily in 1.5 day also (Without compromising Quantity & Quality of content)

So here I am with the dream book,

In Audit each and every chapter have different approach of studying, Some require rattafication, some requires deep understanding, Some topics are just for MCQ's, Some topics are extremely important ... etc etc.. So I have prepared this book keeping all these things in mind, which will be fully exam oriented.

The BEST FEATURE of this book is all the question of ICAI are covered in this book together with the concepts (i.e., Just below the concepts), So that During exam time your duplicacy of efforts will be reduced (i.e., No need to refer Concept book & then again question bank for same concepts)

Rest of the amazing features you will understand only when you will read it.... ;

Warm Regards,

CA Hemant Somani

- **All India Ranker | AIR 46**
- **Exemption in 7 papers (Including Audit** paper of May 2021, Which was the toughest paper, As each & every question was new)
- Secured **All India Ranks in Many Competition** exams (IIT Ghuwati talent Search, ICAI Wizard Etc)
- **Statutory Audit** Domain in **PwC Mumbai**
- Served at Some **MNC's** in Field of **Audit, Taxation (GST) & Finance**
- Currently serving as **consultant in UAE & Africa**
- Faculty of **Audit & GST at CA Final & Inter Level**

A Motivation CUM Story

I always needed a single digit rank in CA Final, But Luck factor was not in my favor, just before 15 days of my exams, me & my family got infected by COVID, and last 15 days are equivalent to 3 months, But I didn't loose hope and gave exam at that time also, During exams also I was suffering from many post COVID symptoms

And Finally, I Secured AIR 46 (Not single digit),

I just want to convey that while doing your preparation, "Always Aim for the BEST & Prepare for the Worst scenario"

FEATURES & COVERAGE OF AUDIT - ALL IN ONE BOOK:

- 1) **Concepts + Question bank together** (i.e, Questions are given just below concepts)
- 2) No need to refer separate-separate Book for Concepts & question bank
- 3) **100% Coverage:** Concepts are **summarized** in best possible manner (**Approx 300 pages**) + Questions = 380 pages
- 4) **All ICAI RTP/MTP/SM/PAST PAPER Questions are covered**
[All ICAI SM/RTP/MTP Questions till MTP'25 - Except May'25 Paper]
- 5) **Old course Qns are also covered** marked as "Old"
- 6) **Tricks & mnemonics** to remember topics are given
- 7) Its Fully in **Tabular & Chart format**
- 8) Fully **Highlighted & Bold**
- 9) Completely as per **ICAI language**
- 10) Concepts are marked as **"Less Important" / "Only for MCQ"** etc

IMPORTANT NOTE:

- **One more Question Bank + Additional Topics Book will be Provided Separately →**
Although the Questions are Covered in Main Book, But for some questions Hint is Given, So Some students prefer separate Question bank also, Hence we take care of them Also :-)
This question bank is completely linked with Main Book, Let's say, If In Main Book the Question Number is 23, then in Question bank also It's Qn. No. 23

Further, Regarding Additional Topics, Those topics which generally other authors skips / which are less relevant for exams are included in this, further some extra topics of SA's which are not covered in ICAI SM, but ICAI is asking questions from those topics (Like Topics from CA Inter). We did this to ensure that 100% coverage can be made (Just Read once)

- One Separate booklet of **ICAI MCQ Summary & Numerical limits** is also provided separately

Further to reduce duplicity, I have not covered Concepts for which Question is Given just below, So, when you will read the question, the concept will get covered automatically > That's a main reason of reducing no. of pages > coverage is 100%

It's completely as per **ICAI Language & Coverage**, you can do cross **check from ICAI module** to get Comfort.

Font Color Combination →

- ✓ **Red** → **Very Important Keyword**
- ✓ **Blue** → **Important keyword**
- ✓ **Green** → **Tricks/Memory Techniques**

Highlighter/Shadow Color Combination →

- ✓ **Blue** → **General**
- ✓ **Green** → **Questions**

- Qn on which → "**SM**" word is mentioned is **ICAI SM** Question
- Qn on which → "**Old**" word is mentioned is **Old Course** Question, But still relevant
- Qn on which → Nothing is mentioned is **also ICAI SM Question** (Except Few....)
- Qn on which → "**Hint**" is Given → it means only Hint is covered in Main Book (However, all main key words & Key points are covered in Main book), But For full Qn & Full Answer → refer "Question Bank"
- Question Bank is Fully Linked with the Main Book, For example, In Main Book if Qn. No. is 9, then in Main Books also Qn Number is 9 (Means Same question Sequence/Number is exactly same in Main book & question book, to quickly find that question in Qn Bank)

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*It's completely as per **ICAI Language & Coverage**, you can do cross check from **ICAI module** to get Comfort*

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	Name	ICAI Coverage
SQC-1	Quality control for firms that perform Audits & Review of Historical F.Info. & Other Assurance and related service engagements	Chapter 1

Standard's on Auditing (SA's)		
200	Overall objectives of an independent auditor and conduct of an audit in accordance with SA's	2-CS based only
210	Agreeing to terms of Audit engagement	2-CS based only
220	Quality control for an audit of FS	1
230	Audit documentation	2-CS based only
240	Auditor's responsibility relating to fraud in an audit of FS	2
250	Consideration of laws and regulations in an audit of FS	2
260	Communication with TCWG	2
265	Communicating deficiency in internal control to TCWG and management	4
299	Joint Audit of Financial Statements	2
300	Planning an audit of FS	3-CS based only
315	Identifying and Assessing ROMM by understanding Entity and its environment	4-CS based only
320	Materiality in planning and performing audit	4-CS based only
330	Response to assessed risks	4
402	Auditor considerations relating to an entity using Service Organization	2
450	Evaluation of Misstatements identified during audit	3
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501	Audit evidence Specific considerations for selected items	5-CS based only
505	External Confirmations	5-CS based only
510	Initial Audit Engagement -Opening Balances	5-CS based only
520	Analytical Procedures	3
530	Audit Sampling	5-CS based only
540	Auditing of Accounting Estimates including Fair value accounting estimates and Related Disclosures	3
550	Related Parties	5-CS based only
560	Subsequent Events	6-CS based only
570	Going Concern	6-CS based only
580	Written Representations	6-CS based only
600	Using work of Other Auditor	3
610	Using work of Internal Auditors	3
620	Using work of Auditor's Expert	3
700	Forming an Opinion and Report on FS	7
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705	Modifications to the Opinion in the Independent Auditor's Report	7
706	Emphasis of matter Paragraphs and Other Matter Paragraphs in the Independent Auditors Report	7
710	Comparative information Corresponding figures and Comparative FS	7
720	Auditor's Responsibility in Relation to Other Information in Documents containing Audited FS	7
800	Special consideration - Audits of FS prepared in accordance with Special purpose framework	8
805	Special Considerations-Audits of Single FS and Specific Elements, Accounts or Items of a FS	8
810	Engagements to Report on Summary Financial Statements	8
Standards on Review Engagement:		
SRE 2400	Engagements to Review FS	10
SRE 2410	Review of Interim Financial info. performed by independent auditor of entity	10

Standards on Assurance Engagement:

SAE 3400	The examination of prospective financial information	11
SAE 3402	Assurance reports on control at a service organisation	11
SAE 3420	Assurance engagements to report on a compilation of Proforma Financial information included in Prospectus	11

Standards on Related Service:

SRS 4400	Engagements to perform agreed upon procedures regarding financial info.	9
SRS 4410	Compilation Engagements	9

ABBREVIATIONS:

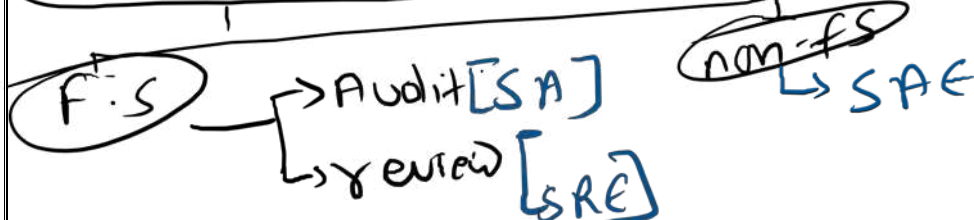
A.Report	Audit Report
AD	Audit Documentation
AE	Accounting Estimates
AUP	Agreed Upon Procedure
B/S	Balance Sheet
BOA	Books of A/c's
BOA	Books of A/C's
BOD	Board of Directors
CAip	CA In Practice
C/A/D/S	Class of transaction, account balance or disclosure
CFI	Consolidated Fund of India
CC	Cash Credit
CG	Central Govt.
CIA	Chief Internal Auditor
CL	Contingent Liability
COE	Code of Ethics
CR	Control Risk
Cr	Crores
Co. Act	Companies Act
D.A	Direct Assistance
DP	Drawing Power
DR	Detection Risk
EA	External Auditor
Engmnt/Egmt	Engagement
EOM	Emphasis of Matter
EQCR	Engagement Quality control reviewer /review
ET	Engagement Team
FAP	Further audit procedure
FI	Financial Information
FR	Financial Reporting
FRF	Financial reporting framework
FS	Financial Statement
Fx	Function (i.e., Used for INTERNAL AUDIT Fx)
GC	Going Concern
G&S	Goods & Services
HFI	Historical Financial Information
I.A.	Internal Auditor
I.auditor	Internal Auditor
IAF	Internal Audit Function
IC	Internal Control
ICFR	Internal Control over financial reporting
IR	Inherent Risk
JA	Joint Auditor's
JV	Journal Voucher / Journal Entries
KAM	Key Audit Matter
L&R	Law & Regulations
M.U	Material Uncertainty
MMS	Material Misstatement
Mngt	Management
MSCS	Multi-State Co-operative society
NFRA	National Financial Reporting Authority
NOC	No objection certificate

NTE	Nature, Timing & Extent of Audit procedure
O.A	Other Auditor
OM	Other Matter
PA	Principal Auditor
P&D	Presentation & Disclosure
P&P	Policies & Procedure
PAC	Public account committee
QC	Quality control
RAP	Risk assessment procedure
ROMM	Risk of material misstatement
RPR	Related Party Relationship
RPT	Related Party Transaction
RRB	Regional Rural Bank
S.E.	Subsequent event
SAAE	Sufficient & Appropriate Audit Evidence
SAP	Substantive analytical procedure
Sig. Deficiency	Significant Deficiency
SO	Service Organisation
SOD	Segregation of Duties
TOC	Test of controls
TOD	Test of Details
UE	User Entity
UN	United Nations
W.C	Working Capital
WR	Written Representation

BASICS OF QUALITY CONTROL & ENGAGEMENT STANDARDS:

Intro	Auditing Standards represent guidance & procedures for professionals to conduct audit.	
AASB	Auditing Standards in India are formulated by Auditing & assurance stand. Boards. (AASB)	
Engagement Standards	<i>Engagement based on the nature of services provided by a member:</i>	
	Standards on Auditing (SA's)	are applied in the audit of historical financial information.
	Standards on Review Engag. (SRE's)	are applied in the review of historical financial information.
	Standards on Assurance Engag. (SAE's)	are applied in assurance engagements, dealing with subject matters other than historical financial information.
	Standards on Related Services. (SRS's)	are applied to engagements involving application of agreed-upon procedures to information, compilation engagements , and other related services engagements, as may be specified by the ICAI.
	Standard on Quality Control (SQC)	contains extensive requirements in relation to establishment and maintenance of a system of quality control in the audit firms as well as even for sole practitioners.

Assurance Service



Non-Assurance

Handwritten note: SRS (circled).

➤ Some Terms that we should understand before starting Audit:

Management:	Management means the person(s) who have executive responsibility for the conduct of the entity's operations (<i>Managing day to day operation</i>)
Those charged with governance (TCWG):	TCWG means the person(s) responsible for the supervision, control and direction of an entity who are accountable for ensuring that the entity achieves its objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, compliance with applicable laws and reporting to interested parties. e.g., Audit Committee, where there is one; else BOD (<i>Responsible for making long term plans, strategy</i>)

Independence:	Judgement of a person is > not subordinate to the wishes or direction of another person > who might have engaged him, Includes: 1) Independence of mind (exist in facts) 2) Independence in appearance (also appear to so exist)

Types of Opinion:			
SA 700	SA 705: 3 Type of Modification		
Unmodified Opinion	Qualified Opinion (3 types)		
	Qualified Opinion	Adverse Opinion	Disclaimer of Opinion

Types of modifications		Pervasive	Not Pervasive
	Material Misstatement	ADVERSE	QUALIFIED
	SAAE not obtained	DISCLAIMER	QUALIFIED

Financial Reporting Framework (FRF):	In easy language, its set of standards use to prepare FS (i.e., accounting standards or Ind-AS), i.e., Prescribe the manner to prepare & present F.Info. of an entity It can be of two types: - In Compliance with Law & Regulation - True & Fair Financial reporting

fair presentation framework:	FRF that requires compliance with the requirements of the framework and : 1) Acknowledges explicitly or implicitly that, to achieve fair presentation of FS, it may be necessary for mgt to provide disclosures beyond those specifically required by the framework; or 2) Acknowledges explicitly that it may be necessary for mgt to depart from a requirement of the framework to achieve fair presentation of the FS. Such departures are expected to be necessary only in extremely rare circumstances .

Compliance framework:	Refer to a FRF that requires compliance with the requirements of the framework, but does not contain the acknowledgements above

Applicable FRF:	FRF: 1) Required by the L&R, OR, 2) Adopted by Mngt/TCWG & ACCEPTABLE as per nature of entity & FS objective

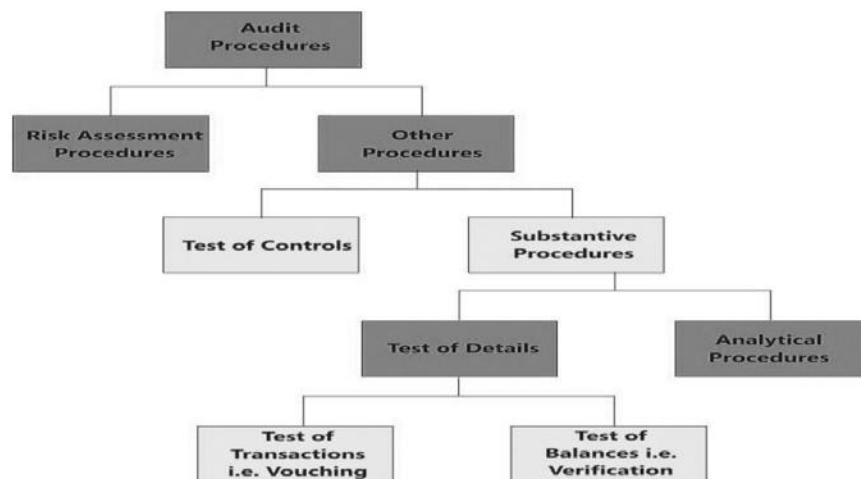
Misstatement: (SA 200/450)	Misstatement occurs when something has not been treated correctly in the financial statements as per FRF i.e., Difference between : 1) amount, classification, presentation, or disclosure (ACPD) reported in FS Vs. 2) ACPD Required by FRF (Can be error or fraud)

Material Misstatement:	Material misstatement is information in the financial statements that is sufficiently incorrect that it may impact the economic decisions of someone relying on those statement

(SA 320)

Reasonable Assurance:	High but not absolute (100%) level of assurance (Inherent limitation of Audit)
Absolute Assurance:	100% Assurance
Guilty ?	Auditor performed audit as per SA's, due diligence, Care → still after issuing clean audit report → some MMS left → Is auditor Guilty ? → Not guilty, provided he kept due diligence, Skill, care (As there are INHERENT LIMITATIONS of AUDIT... it's Not an GURANTEEE)

SAAE:	Reasonable assurance kese milega ?? --? Sufficient & Appropriate Audit evidence leke ... • Sufficient → Quantity, depends upon 2 factors, ✓ ROMM in F.S → if high risk... high SAAE needed ✓ Quality of A.E. → If good quality .. less SAAE needed • Appropriateness → Quality, Depends upon 2 factor: ✓ Relevance (eg., to test A/C payable→ Assertion of "Completeness" also needs to be check → to check completeness .. auditor is checking only Account payable RECORDED in Books .. is wrong Auditor can check Subsequent bank payments & other Correspondences) ✓ Reliable → (External generated, Internal generated ... etc...)
	Always Need Persuasive Audit Evidence



- **Risk assessment procedures** are the audit procedures performed to obtain an understanding of the entity and its environment to identify and assess the risks of material misstatement, at the financial statement and assertion levels.
- **Further audit procedures:** Further Audit Procedures comprise of:
 - (i) **Tests of controls:** Test of controls may be defined as an audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at **assertion level**.
 - (ii) **Substantive procedures:** Substantive procedures are designed to detect material misstatements at the **assertion level**. They comprise:
 - (a) Tests of details: (of classes of transactions, account balances, and disclosures),
 - (b) Substantive analytical procedures:

CHAPTER 1- Quality Control (SQC 1 & SA 220)

Audit Quality

- **Why:** It helps in creating trust in users of financial information. Industry, government and public at large who are the stake holders who relies upon assurance given by auditors. So, necessary to ensure high audit quality throughout the audit process.
- **Meaning:** Audit quality involves application of a rigorous audit process by auditors and quality control procedures that comply with L&R and applicable professional standards.
- **SQC 1 & SA-220:** deal Quality control systems & responsibilities of auditors in this regard. Both the standards deal with audit quality.

SQC 1:	Quality Control for firms that perform audits and reviews of historical financial information, and other assurance and related services engagements (i.e., Deals with quality at level of firm, even for Non-audit engmnt also)

SA 220:	Quality Control for an audit of financial statements (i.e., Deals with audit quality at individual audit engagement level)

- Besides above two standards, other SA's, code of ethics by ICAI and certain provisions of Co. Act, 2013 facilitate quality control process.
- There also exists mechanism for review of quality control through Peer review Board, Quality review Board and NFRA (National financial reporting authority).

❖ SQC 1- Quality Control For Firms That Perform Audits And Reviews Of Historical Financial Information, And Other Assurance And Related Services Engagements

System of Quality Control

- Firm should establish System of Quality Control to provide Reasonable Assurance that: -
- Firm & personnel comply to Professional Standard, Regulatory & Legal Requirements
 - Reports issued by Firm or Engagement Partners are appropriate in circumstances.
- This quality control standard applies to all firms irrespective of their constitution.

Q1. Assignment For Preparation of FS & issue compilation report → SQC 1 is applicable → → "Related Service"

Elements of System of Quality Control:

- (i) Leadership responsibilities for quality within the firm (ii) Ethical requirements (iii) Human resources (iv) Engagement performance (v) Monitoring (vi) Acceptance and continuance of client relationships & engmntg.

[Quality control policies should be documented and communicated to the firm's personnel → Feedback to encourage from personnel on Quality control system, to communicate there views on QC matters)

1) Leadership responsibility for quality of firm: "Qn"

- Policies and procedures to promote quality → firm's CEO or managing partners are responsible for firm's SQC
- Delegation of operational responsibility by CEO/MP for SQC should be assigned to experienced & able person
- Establish policies and procedures to promote good internal culture

Firm's business strategy is subject to the overriding requirement for the firm to achieve quality in all the engagements, It's non-negotiable, should be ensured that (i.e., QC policy will override Firm business strategy):

[Trick: client ko jaano ... fir "Fees" quote karo, uss hisaab se "Salary" wale person "devote" karo]

- 1) Firm before accepting an engagement should acquire vital information about the client. Such an info. should help firm to decide about integrity of Client, promoters and KMP, competence (including capabilities, time and resources) to perform engagement and compliance with ethical requirements (independence)



- 2) Firm assigns its mngt responsibilities so that **commercial considerations (Money)** do not override the quality of work performed.
- 3) Firm **policies & procedures** addressing performance **evaluation, compensation** & promotion (including incentive systems) w.r.t its personnel are designed to demonstrate the firm's overriding commitment to quality
- 4) Firm **devotes sufficient resources** for development, documentation and support of its QC policies & procedr.

Q2. Even after below issues, Mr. A want to accept the audit, → it reflects **poor Quality control**, SQC 1 requires that firm's business strategy is subject to overriding requirement of firm to achieve quality.
 → Partner of firm is close friend of Promoter (**issue of Independence**)
 → inquiries made from Promoters by Regulatory authorities & Last auditor resigned (**issue of Integrity of Client**)
 ("Now mention above 4 points of QC policy will override business strategy")

2) Ethical Requirements

Policies and procedures (**P&P**) → provide reasonable assurance → that the firm and its **personnel comply with relevant ethical requirements** contained in the Code of ethics (COE) issued by ICAI.

Fundamental Principles:	P&P to comply with: Integrity, Professional behavior, confidentiality, Objectivity, Professional competence& Due Care]		
Independence:	Firm should establish P&P designed to provide it with reasonable assurance that the firm, its personnel & (including experts contracted by the firm and network firm personnel) maintain independence where required by the Code. Such P&P should enable the firm to:		
	a) Communicate its independence requirements to its personnel		
	b) Identify circumstances and relationships that create threats to independence, and		
	c) Take appropriate action to eliminate threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, withdraw from the engagement.		
	Engt. partner to notify the firm & it's personnel → about client, it's relationship that may cause threat → if any breach → notify to take appropriate action		
	Annual Confirmation:	At least annually, the firm should obtain written confirmation of compliance with its P&P on independence from all firm personnel.	
	Familiarity threat:	Using the same senior personnel on assurance engagements over a prolonged period may impair the quality of performance, need safeguard. For that Considers matters such as:	
		- Nature of the engagement (extent of involve of public interest) - length of service of senior personnel on engmnt.	
		Safeguard for Above: Example: - rotating the senior personnel or - requiring an engagement quality control review.	
	For Listed Entities:	Engt. partner should be rotated atleast once in 7 yrs. (except, where audit is conducted by a sole practitioner), However Mandatory peer review of such firms	

➤ Review of Audit Work: (Qn)

As per SQC 1, an EQCR/Partner for audits of FS of listed entities includes considering following: (**R-SOCCER**)

- (i) The work has been performed as per professional standards & **Regulatory & legal requirements**;
- (ii) **Significant matters** have been raised for further consideration;
- (iii) The **Objectives of the engagement** procedures have been **achieved**



- (iv) **Appropriate Consultations** have taken place & the resulting conclusions is documented & implemented;
- (v) The **work performed supports the Conclusions** reached and is appropriately **documented**;
- (vi) The **Evidence obtained is sufficient and appropriate** to support the report;
- (vii) There is a need to **Revise the nature, timing** and extent of work performed;

Q3. CA was doing stock audit of P Ltd, he leverage opportunity & ask P Ltd to get Full accounts audited by Him, he will issue Clean stock audit report → **It Violate Code of Ethics & it's spirit** → **poor quality control (SQC-1)**

Q4. Senior partner want to **review the work** of Audit done by Another partner of **Listed Co.** (CA H : Doing from last 8 Yrs): Refer Above topic "**Review of Audit work**" → [Further, **(a)** Apply **safeguard to Reduce Familiarity threat** **(b)** Require **rotation of Engmt Partner**] → **Not complying with SQC 1, Doing audit for more than 7 Yrs)**

Q5. A Partner while going to sign audit report, **met road accident & died** → so, another partner signed **without reviewing work** : **SA 220** → **Apply "review Procedure"** (**Mention above notes**) → When Auditor delegates work to assistant/other auditor, he will be continue to responsible → However, He **can rely on work perform** by others (**Sign report**), **but Exercise Adequate Skill & Care, Fundamental Principle, Carefully direct, supervise, review the work delegated.**

3) Acceptance and Continuance of Client Relationships and Specific Engagements

Before accepting engagement:	Q6. CA accepted the Audit assignment without considering information regarding acceptance & continuance of client relationships and audit engagements are appropriate. Before accepting an engagement should acquire vital information about the client: 1) Integrity of Client, promoters and key managerial personnel. 2) Competence (including capabilities, time and resources) to perform engagement 3) Compliance with ethical requirements. Obtain info to accept engmt & to continue existing one → if issues identified & still accept/continue engmt → it should document how the issues were resolved.
Continuation of Engmt: Information obtained after:	• If is any conflict of interest between the firm and client → Should be properly resolved • If firm obtains any information later → in case it would have obtained it before, → then he may not have accepted the engagement <u>Policies and procedures on the continuance of the engagement and the client relationship should include consideration of:</u> a) The professional and legal responsibilities that apply to the circumstances, including whether there is requirement to report to the person who made the appointment or, in some cases, to regulatory authorities; and b) The possibility of withdrawing from engmt or from both engagement & client relationship
P&P on withdrawal:	Q7. "CA Firm do not have necessary expertise to do audit, wishes to withdraw from engagement . Discuss issues that need to be addressed before deciding to withdraw Policies and procedures on withdrawal from an engagement or from both the engagement and the client relationship address issues that include the following: a) Discussing with appropriate level of client's mngt & TCWG regarding the appropriate action b) If firm determines that it is appropriate to withdraw → Discussing with appropriate level of client's mngt and TCWG withdrawal from the engmt or from engagement + client relationship, and the reasons of withdrawal. c) Report to L&R → Whether there is professional, regulatory or legal requirement for firm to • Remain in place, or • If Withdraw possible → report the withdrawal from engt, or from both engmt + client relationship, together with the reasons for the withdrawal, to regulatory authorities. d) Documenting significant issues, consultations, conclusions and the basis for the conclusions.



➤ How to Evaluate Integrity of Client (Qn)

Q8. W.r.t Integrity of Clients, give some matters which required to be considered by CA firm as per SQC 1

As per SQC 1, 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 mngt**, related parties and TCWG.
- The **nature of the client's operations**, including its business practices.
- Indications that client might be involved in **money laundering** or other criminal activities.
- Whether client is aggressively concerned with **maintaining firm's fees as low** as possible.
- Indications of an **inappropriate limitation** in the scope of work.
- The reasons for proposed appointment of firm and **non-reappointment of previous firm**.
- Information concerning the attitude of the client's principal owners, key management and TCWG towards such matters as **aggressive interpretation of accounting standards** and the IC environment.
- The extent of knowledge a firm will have regarding the integrity of a client will generally grow within the context of an **ongoing relationship with that client**.

➤ Whether firm has the capabilities, competence, time & resources to undertake an Engt:

1. Firm personnel have **knowledge** of relevant industries or subject matters; (*Capability & Competence*)
2. Firm personnel have **experience** with relevant regulatory or reporting requirements, or the ability to gain the necessary skills and knowledge effectively (*Capability & Competence*)
3. Firm would be able to complete the engagement within the **reporting deadline**. (*Time*)
4. The firm has **sufficient personnel** with the necessary **capabilities and competence** (*Resources*)
5. **Experts** are available, if needed; (*Resources*)
6. Individuals meeting the criteria and eligibility requirements to perform engmt quality control review (EQCR) **are available**, where applicable;

Q9. XYZ Ltd approached us to appoint tax auditor, But on XYZ, Search done by ED of Income tax, Huge Cash recovered (can he accept audit): **SQC 1, before accepting a new engagement, "integrity of client", might be involved in money laundering activities. Therefore, offer should not be accepted.**

Q10. on Company → Search by IT authority, Promoter's brother is contesting Election. → In CA Firm one expertise senior member left...& he is planning to provide a/cing service to one of associate co. (can accept audit ?) :

Hint: SQC 1 requires (a) Integrity of Client, (b) Competence, (c) Ethical req.) &

SA 220 requires Independence (in doing so → Obtain relevant info from firm, Identify threat to Independence):

→ **Political Party engagement** (Integrity issue of Funding routing threat), → **income tax search** (ROMM & non-disclosure of tax liability) & → **Senior member left** (lack of competence and resources), → Further that **Senior member planning to provide a/cing service to associate co.** (can be Independence & Objectivity issue)

4) Human Resources

About:	Policies and procedures designed to provide reasonable assurance that: • it has sufficient personnel with the capabilities, competence, and commitment to perform its engagements in accordance with professional • to issue reports that are appropriate in the circumstances. Such P&P also deals: HR issues, Compensation, training, development etc. Engmt Team → should able to carry out its responsibility with necessary competence and skill.
Responsible:	The firm should assign responsibility for each engagement to an engagement partner .
P&P require: (Khud, KMP, capable)	<u>The firm should establish policies and procedures requiring that:</u> a) The responsibility of engmt partner are clearly defined & communicated to that partner b) Identity and role of the engmt partner are communicated to KMP of client's & TCWG c) The engmt partner has the appropriate capabilities, competence, authority and time to perform the role; and



5) Engagement Performance

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

- Consultation in difficult or contentious matters:**
- Consultation needed for **difficult or contentious matters** pertaining to an engagement.
 - It includes **discussion, at an appropriate professional level**, with individuals **within or outside** the firm who have **specialized expertise**, to resolve a difficult or contentious matter.
 - It promotes quality and improves the application of professional judgment. Consultation procedures require consultation with those having appropriate knowledge and **appropriate documentation and implementation of conclusions** resulting from consultations
 - Consult externally when lack of required internal resources (Advisory services)

Engagement quality control review (EQCR)	Applicable:	• Listed entities audits of FS of → Mandatory • Other Engagements → devise criteria
	About:	• EQC Reviewer will review Significant judgments made in an engagement before the report is issued (i.e., do not issue report before EQCR review) • extent of the review depends on the complexity of engagement & risk • review does not reduce the responsibilities of the engagement partner.
	EQCR:	Should be member of ICAI + suitably qualified external person (Partner or employee), <u>or</u> Team of individuals <u>or</u> can be from another firm with similar background → sufficient and appropriate experience and authority
	EQCR Objectivity: [EQCR can consult Engmt. Partner provided it does not compromise objectivity]	• EQCR Objectivity require: <u>participation in engagement</u> or making <u>decisions</u> for engmnt team is to be avoided • However, engmnt partner may consult engagement EQCR during engmnt so as not to compromise his objectivity & eligibility to perform role. • Significant Consultation: Where the nature & extent of consultations become significant, however, care is taken by both the engmnt team and the reviewer to maintain the reviewer's objectivity. ✓ Where this is not possible → another individual within the firm or a suitably qualified external person is appointed: ❖ As EQCR or ❖ person to be consulted on the engagement. • The firm's policies should provide for replacement of EQCR where the ability to perform an objective review may be impaired
	(Special Trick :-) EQC Review for Audit of Listed FS includes considering the following: [Matters evaluated by EQCR]	[Trick: ha me "independent" hu, "Risk" mili to mera "judgement" bhi lagaya, dusro se "consultation" bhi lii > "Misstatement" "mngt ko communicate" kara > "working paper" k hisaab se "report" issue kar dii ...] 1) Engmnt team's evaluation of firm's independence i.r.t specific engmnt 2) Significant risks identified during the engmt & responses to those risks. 3) Judgments made, particularly w.r.t materiality and significant risks. 4) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations 5) The significance and disposition of corrected and uncorrected misstatements identified during the engagement 6) The matters to be communicated to mngt and TCWG and, where applicable, other parties such as regulatory bodies.



	7) Whether working papers selected for review reflect the work performed i.r.t the significant judgments and support the conclusions reached 8) The appropriateness of the report to be issued.		
	MCQ: <u>If EQCR is selected by Engagement Partner + EQCR made decision for Engt Team</u> → SO EQCR Objectivity can not be maintained		
Differences of Opinion:	Q11. During audit, Engagement partner is not willing to accept recommendations of EQCR. - Between Engmnt Team or those consulted & Engmnt partner & EQCR → report should only be issued after resolution of such differences - If recommendations of EQCR are not accepted by engmnt partner & 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:	Time limit Assembly	P&P	P&P for engmnt teams to complete the assembly of engmnt files on a timely basis after the engagement reports have been finalized.
		Audit engmnt:	Files should be completed in not more than 60 days after date of auditor's report
		Other:	Other engmnt files within the limits appropriate to engagements. (timely basis after engmnt report)
		2 or more different report	- Where 2 or more different reports are issued i.r.t. same subject matter information of entity, the firm's P&P relating to time limits for assembly of final engmnt files should be considered for each report as if it were for separate engmnt. <u>Example</u>, be the case when the firm issues an <u>auditor's report</u> on a <u>component's financial info for group consolidation purposes</u> and, at a subsequent date, an auditor's report on the <u>same financial information for statutory purposes</u>.
	Time limit for retention	Engmnt documentation → retained for period of time sufficient to permit those performing monitoring procedures to evaluate the firm's compliance with its system of QC, or for a longer period if required by law or regulation Audit Engagements: minimum 7 years from the ✓ date of the auditor's report, or, ✓ if later, the date of the group auditor's report	
	Safety:	P&P should be designed to maintain the confidentiality, safe custody, Integrity, Accessibility and Retrievability (IAR) of engagement documentation	
	Property of Auditor:	- Unless otherwise specified by L&R, E.D is the property of 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.	
	EQCR review Doc:	Care should be taken that P&P on documentation of the engagement quality control review should <u>require documentation that</u> : - Procedures required by the firm's policies on engagement QC review have been performed. - engagement QC review has been completed before the report is issued - The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the Engmnt team made and the conclusions they reached were not appropriate	

1.6 | Page

Chp 1: SQC 1 & SA 220



➤ Procedure for Electronic / Scanned Engagement Documentation

If For Practical reason, Physical Docs may be needed to Electronically scanned for inclusion in Engmnt file, In that case, Firm to Implement Appropriate Procedure, requiring engmnt team to:

- a) **Generate scanned copies** (including manual signature. Cross-reference)
- b) **Integrate the scanned copies into the engagement files**, including **indexing & signing** off
- c) Enable the scanned copies to be **retrieved and printed** as necessary

Further, It's **important to identify source of document & information used** (Client obtained or team prepared)

Q12. Engmt Partner is of **View that After Review by EQCR** → Engmt partner responsibility will be Reduced: It's **Wrong** (Now mention above Notes "Matters evaluated by EQCR")

Q13. Can EP consult EQCR? → EQCR require to maintain Objectivity (so his participation for decision in Engmnt is to be avoided) → however He can consult EQCR → Provided it do not Compromise his "Objectivity"

Q14. engmt file needs to be **Assembled AFTER** engmt reports finalised (60 days), **Not PRIOR** to issue report

Q15. CA Firm maintaining Audit Documentation **Electronically & Physical Form**. (Physical File neither scanned & incorporated into electronic files, Nor Cross-referenced to Electronic File), and Documentation do not contain detail whether information obtained from Client or prepared by Engmt team (SM)

Hint: SQC 1 → **SQC 1** → establish **P&P** designed to maintain confidentiality, safe custody, Integrity, Accessibility and **Retrievability (IAR)** of engagement documentation.

→ physical files Not Scanned, nor-cross check → difficult to check whether A.File assembled in 60 days or not.

→ integrity, accessibility or retrievability of the underlying data may be compromised if the documentation could be altered, added to or deleted without the firm's knowledge. → so control needed to protect integrity of info.

(Now refer Above Topic: "Procedure for Electronic/Scanned Engagement Documentation")

6) Monitoring:

About:	- The firm should ensure that P&P relating to the system of QC are relevant, adequate, operating effectively and complied with in practice. - Such P&P should include an ongoing consideration and evaluation of the firm's QC system, including a periodic inspection of a selection of completed engagements.
Monitoring Factors: (Nov'24) <i>(Special Trick :-)</i>	Q16. Discuss the factors considered by CA T for monitoring the quality control in firm. Quality control of engagements has to be monitored taking into account following factors: <i>[Trick: QC policy "appropriate hai" ? "kisne lagai" ? par uske against to "complaint" aai thi ki "New L&R" ka knowledge hi nii hai usko > ohh accha aisa .. to fir "action lete h" uspe .. + khoo "firm deficiency" bhi shii karte h]</i> - Decide whether QC system of firm is appropriately designed & effectively implemented - 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 & allegations against firm or any employees of non - compliance with professional standards or regulatory requirements by person within or outside firm. - Examining whether new developments in the professional standards, legal and regulatory requirements have been reflected in the quality control policies. - Taking appropriate remedial actions against the personnel who did not conform to QC policies. - Taking action when deficiencies in the design or operation of firm's QC policies and procedures, or non-compliance with the firm's system of QC are identified.

❖ SA 220 – QUALITY CONTROL FOR AN AUDIT OF FS

About:	Based on QC policies → Engagement partner of a team is responsible for quality control



	procedures of a particular audit engagement as per SA 220 - Therefore, SA-220 is premised on the basis that the firm is subject to SQC 1 - Within the context of firm's system of QC, Engmnt teams have a responsibility to implement QC procedures that are applicable to the audit engagement - Engagement teams are entitled to rely on the firm's system of QC, unless information provided by the firm or other parties suggests otherwise				
SA 220 describes responsibilities of engagement partner in relation to following matters:	Elements of System of Quality control:				
a) Leadership responsibilities for quality on audits. b) Relevant ethical requirements c) Acceptance and continuance of client relationships and audit engagements . d) Assignment of engagement teams. e) Engagement performance. f) Monitoring.	a) Leadership responsibilities for quality within firm b) Ethical requirements c) Acceptance and continuance of client relationships & engmnt. d) Human resources e) Engagement performance f) Monitoring				
Objective:	a) audit complies with professional standards and regulatory and legal requirements b) auditor's report issued is appropriate in the circumstances.				
Leadership Responsibilities for Quality on Audits: <i>[team ne Standard, L&R, QC follow krke report issue ki]</i>	Engagement partner is to take responsibility - Leadership responsibilities for quality on audits: <table border="1"> <tr> <td>a) Importance to audit quality of:</td> <td> 1) Engmnt team's ability to raise concerns without reprisals fear 2) Performing work that complies with professional standards and regulatory and legal requirements; 3) Complying with firm's QC policies and procedures as applicable 4) Issuing auditor's reports that are appropriate in circumstances </td> </tr> </table> b) The fact that quality is essential in performing audit engagements.	a) Importance to audit quality of:	1) Engmnt team's ability to raise concerns without reprisals fear 2) Performing work that complies with professional standards and regulatory and legal requirements; 3) Complying with firm's QC policies and procedures as applicable 4) Issuing auditor's reports that are appropriate in circumstances		
a) Importance to audit quality of:	1) Engmnt team's ability to raise concerns without reprisals fear 2) Performing work that complies with professional standards and regulatory and legal requirements; 3) Complying with firm's QC policies and procedures as applicable 4) Issuing auditor's reports that are appropriate in circumstances				
Relevant Ethical Requirement:	- 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 engmnt partner to relevant persons within the firm to determine appropriate action, which may include eliminating the activity or interest that creates the threat, or withdrawing from audit engmnt, where withdrawal is legally permitted. <table border="1"> <tr> <th colspan="2">Independence (SA 220)</th></tr> <tr> <td colspan="2"> EP shall form a conclusion on compliance with independence requirements w.r.t audit engt: (i) Obtain relevant information from the firm and, network firms, to identify and evaluate circumstances and relationships that create threats to independence; (ii) Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for engmt; (iii) Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit. </td></tr> </table>	Independence (SA 220)		EP shall form a conclusion on compliance with independence requirements w.r.t audit engt: (i) Obtain relevant information from the firm and, network firms, to identify and evaluate circumstances and relationships that create threats to independence; (ii) Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for engmt; (iii) Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit.	
Independence (SA 220)					
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Acceptance & Continuance:	Same as SQC 1, obtain such information (Information like integrity of principal owners, competence of engmnt team & capabilities including time and resources, Ethical requirement + Significant matter arisen during current & previous audit engmnt)				
Assignment of Engagement	Engmnt team and any auditor's experts who are not part of the enmnt team, collectively have the appropriate competence and capabilities to perform the engagement in accordance with professional standards and regulatory and legal requirements.				



Teams:	
Monitoring:	system of quality control includes a monitoring process → Engagement partner shall consider the results of the firm's monitoring process
Engagement Performance:	
Enmngt partner has responsibility for: • Direction, supervision and performance of audit engmnt. • Review of audit documentation <u>before issue of audit report</u> is his responsibility. • SAAE Obtained for Conclusion: It has to be ensured that SAAE has been obtained to support the conclusions reached and for issuance of auditor's report. • Consultation: Engagement partner is also responsible for ensuring undertaking appropriate consultation on difficult or contentious matters.	
(Special Trick :-)	EQCR: <u>Engagement Partner Responsibility for EQCR:</u> - Determine that an EQCR has been appointed Discuss significant matters arising during the audit engagement, including those identified during the EQC Review, with the engagement quality control reviewer Not date the auditor's report until the completion of the engagement QC review. EQCR shall perform an objective evaluation of the <u>significant judgments</u> made by the engagement team, and the <u>conclusions reached</u> in formulating the auditor's report. This evaluation shall involve: [Trick: "Significant matter" resolve karke > "document" kara usko > "conclusion" > "audit report" me likha] - Discussion of significant matters with the engagement partner - Review of selected audit documentation w.r.t significant judgments the engagement team made and the conclusions it reached and - Evaluation of the conclusions reached in formulating the auditor's report and consideration of whether the proposed auditor's report is appropriate - Review of the financial statements and the proposed auditor's report
	Q17. EQCR for an audit engmnt of a listed company. What aspects, which would be looked? Answer: For <u>audits of FS of listed entities</u>, the <u>EQCR</u>, on performing an engagement quality control review, shall also consider the following: - The engagement team's evaluation of independence i.r.t the audit engagement; - Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; - 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: Engagement team shall follow the firm's policies and procedures for dealing with and resolving differences of opinion.
	Documentation: <u>Refer "Additional Booklet PDF"</u>
	Q18. in CARO 2020 Clause vii, Auditor commented "that company is "generally regular" in depositing statutory dues" → This reporting is Not Qualitative as per SA 220 (Quality control should provide auditor with reasonable assurance that audit complies with professional standards & regulatory and legal requirements)
	Q19. Even if Listed company took Expert opinion of ICAI on Ind AS issue, still EQCR is mandatory to appoint.



Q20. Listed company Audit (FY 31/03/18), Completed on 01/05/18 → Audit report dated 12/05/18 → However Q.C review completed on 15th May 2018. → (a) (Refer above Notes "Engagement Partner Responsibility for EQCR") → (b) Further SA 700: auditor's report to be dated no earlier than the date on which obtained SAAE, in Given case → Hence, Auditor report is dated before completion of review of EQCR (not in order)

Q21. "EQCR" also require to Evaluate firm's Independence, As well as Engagement Partner shall also:
 (a) Obtain relevant info from firm (to identify, evaluate circumstances/relationship create threat of indepdnce)
 (b) Evaluate info. On identified Breach, whether it create threat (c) Take appropriate action to eliminate threat

Q22. What steps should Partner take to ensure compliance with independence requirements for audit engt? Why is it necessary for an audit firm to have well-documented policies and procedures to maintain independence.
Hint: Refer both the Independence topics i.e., Given in SQC 1, as well as Given in SA 220

➤ SQC 1 VS. SA 220- KEY DIFFERENCE IN NATURE, SCOPE & APPLICABILITY:

	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 same.
2	It is applicable to (All) 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 QC 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 QC 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.

Q23. CA Ragini EQCR never done listed company audit, he done review just by ticking Yes/No on checklist (there is no other Working Docs):
SQC 1 → (first Write "Definition of EQCR") → then, EQCR should have sufficient & appropriate experience and authority, should have requisite technical expertise and experience. → CA Ragini not appropriate to accept ECQR.
SA 220 → EQCR shall document → that 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.

In the instant case, there are no working papers to show that evaluation has been done by EQCR, Mere ticking of a Yes/No checklist shows that no such evaluation and review made by EQCR → Wrong Approach by EQCR.

➤ MECHANISMS FOR REVIEW OF QUALITY CONTROL:

Peer Review Board	
Constituted:	Peer review Board is constituted by Council of ICAI
Objective of PRB:	Main objective of Peer review Board is to ensure that, in carrying out assurance assignments: a) Technical, professional and ethical standards (TPE) including regulatory requirements are complied with by members of ICAI. b) Proper systems are in place including documentation thereof which amply demonstrate quality of assurance services provided by members
Purpose:	It meant for purpose of enhancing quality of professional work resulting in more reliable and useful audit reports.



Review of the systems and procedures:	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.
Brief Process:	- Once a Practice Unit is subjected to Peer review, - its assurance engagement records pertaining to the Peer review period are subject to examination and review by the Peer Reviewer. If Unqualified report → 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

Quality Review Board	
Set up by:	Central government
Members	It consists of members nominated by Central govt and Council of ICAI.
Functions of QRB are:	a) To make recommendations to Council regarding quality of services provided by ICAI Member; b) To review the quality of services provided by ICAI Member including audit services & c) To guide the members of the Institute to improve the quality of services and adherence to the various statutory and other regulatory requirements;
Company select:	The statutory auditors i.r.o companies are identified for their audit quality review based upon risk-based approach
Carried by:	review is carried out by technical reviewers who are empanelled by QRB on engagement basis from across the country.

National Financial Reporting Authority (NFRA)	
Sec 132(1)	NFRA has been constituted in terms of Section 132(1) of Companies Act, 2013
Duties of NFRA:	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
Power:	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.
Companies:	Such companies include listed companies, insurance companies, banking companies & other companies as provided for in rule 3 of NFRA Rules, 2018
QRB vs NFRA:	- Overseeing quality of audit services of listed companies falls under 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



CHAPTER 2- General Auditing Principles & Auditor's Responsibilities

(SA 200, 210, 230, 240, 250, 260, 299, 402)

SA 240 – AUDITOR'S RESPONSIBILITY RELATING TO FRAUD IN AN AUDIT OF FS

Fraud:	An Intentional act by one or more individuals in an organisation with an intention to obtain unjust or illegal advantage
Misstatement:	Misstatements in the financial statements can arise from either fraud or error
Error:	Misstatement of the financial statements is unintentional .
Primary Responsibility:	- Primary responsibility for the prevention and detection of fraud rests with both TCWG and Mngt (Not with Auditor, provided he applied professional skepticism). - Mngt & TCWG should place a strong emphasis on fraud prevention & fraud deterrence (punishment for fraud), creating a culture of honesty and ethical behaviour
Objective of auditor:	- To identify & assess the ROMM in FS due to fraud - To obtain SAAE about the assessed ROMM due to fraud, implement response - To respond appropriately to identified or suspected fraud
No Legal determination:	Although the auditor may suspect or, in rare cases, identify the occurrence of fraud , the auditor does not make legal determinations of whether fraud has actually occurred .

Two types of intentional misstatement:

Fraudulent Financial reporting:	Misappropriation of assets:
- Fraudulent FR involves intentional misstatements including omissions of amounts or disclosures in FS to deceive FS users. It can be caused by the efforts of management to manage earnings in order to deceive FS users by influencing their perceptions as to the entity's performance and profitability Inappropriate adjustment of assumptions & changes in judgments by mngt - Pressures and incentives to meet market expectations Trick: [Manipulate kara by > Omit, Advance, delay or Alter the JV > Because of Wrong Accounting / Assumption] Ya fir, Complex transaction Conceal kara]	Misappropriation of assets involves the theft of an entity's assets and is often perpetrated by employees in relatively small and immaterial amounts. However, it can also involve management who are usually more able to disguise or conceal misappropriations in ways that are difficult to detect.
Fraudulent FRF may be accomplished by: (Man, Mis Mis)	It can be accomplished in a variety of ways including:
Manipulation, falsification (including forgery), or alteration of A/cing records or supporting documentation from which the FS are prepared Misrepresentation in or intentional omission from, the FS of events, transactions or other significant information. - Intentional misapplication of a/cing principles relating to amounts, classification, manner of presentation, or disclosure.	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, colluding with a competitor by disclosing technological data in return for payment). - Causing an entity to pay for goods
It can be committed by management overriding controls using such techniques as: - (Alter, Omit, Conceal + FICtitious)	
Altering records & terms related to significant & unusual transaction Omitting, advancing or delaying recognition in the FS of events and transactions that have occurred during the reporting period. Concealing, or not disclosing, facts that could affect the amounts	



recorded in the FS. (i.e., Hiding Legal case) iv. Recording Fictitious JV, particularly close to end of an A/cing period, to manipulate operating results or achieve other objectives. v. Inappropriately adjusting assumptions and changing judgments used to estimate a/c balances. (i.e., Provision for warranty) vi. Engaging in Complex transactions that are structured to misrepresent the financial position or financial performance. (i.e., Sale of M/c to R.P at high price to increase profit, then again taken on lease back)	and services not received (Eg, payments to fictitious vendors, kickbacks paid by vendors to the entity's purchasing agents in return for inflating prices, payments to fictitious employees). 4) Using an entity's assets for personal use (Eg, using the entity's assets as collateral for a personal loan).

Q1. Source of such **fraudulent FR**. Or, how **fraudulent FR** may be accomplished and discuss the **techniques of committing fraud by management overriding controls**: [Refer Above Notes : "Fraudulent FRF may be accomplished by" & "It can be committed by management overriding controls using such techniques as"]

Fraud, involves **incentive or pressure** to commit fraud, a **perceived opportunity** to do so and **some rationalization** of the act. **For example**:-

- 1) **Incentive or pressure** to commit fraudulent FR may exist when **mngt is under pressure**, from sources outside or inside the entity, to **achieve an expected (and perhaps unrealistic) earnings target** or financial outcome - particularly since the consequences to mngt for failing to meet financial goals can be significant.
- 2) Individuals have an **incentive** to misappropriate assets, Eg, **individuals are living beyond their means**
- 3) A **perceived opportunity** to commit fraud may exist when an **individual believes internal control can be overridden**, for Eg, individual is in a position of trust or has knowledge of specific deficiencies in IC.
- 4) Individuals may be able to **rationalize committing a fraudulent** act. Some individuals **possess an attitude**, character or set of ethical values that allow them knowingly & **intentionally to commit a dishonest act**. However, even honest person can commit fraud in an environment that imposes sufficient pressure on them.

➤ **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. For example:-

Relates to: Fraudulent Financial Reporting:	Relates: Misappropriation of Assets:
A) Incentives/Pressure: Excessive pressure exists for management to meet the requirements or expectations of 3rd parties due to the following: 1) Profitability or trend level expectations of investment analysts, institutional investors, significant creditors, or external parties (<i>Investor already hai ...</i>) 2) Need to obtain additional debt or equity financing to stay competitive (<i>Ya laana hai ...</i>) 3) Marginal ability to meet exchange listing requirements or debt repayment or other debt covenant requirements 4) 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 TCWG is threatened by the entity's financial performance arising from the following:- <i>Trick: mngt ka personal interest hai company me ...ESOP/Bonus /Gurantee etc. y sab tab hi milega jab profit accha hoga.. yaa usse Maar rhe hai</i> 1) Significant financial interests in entity.	A) 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: <i>[Trick: Employee ko tum Nikaal rahe ho, Binaa Paise diye]</i> 1. Known or anticipated future employee layoffs. 2. Recent or anticipated changes to employee compensation or benefit plans. 3. Promotions, compensation or other rewards inconsistent with expectations.



2) 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. 3) Personal guarantees of debts of the entity. 4) There is excessive pressure on management or operating personnel to meet financial targets established by TCWG, including sales or profitability incentive goals	
B) 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: - <i>RP ke saath Complex Transaction karna .. dusri jurisdiction wali ... to save tax</i> 1. Significant RPT not in the ordinary course of business or with <u>related entities not audited</u> / audited by another firm. 2. 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 that may result in inappropriate or non-arm's-length transactions. 3. <u>Assets, liabilities, revenues, or expenses</u> based on significant estimates that involve subjective judgments or uncertainties that are difficult to corroborate. 4. Significant, unusual, or highly complex transactions, especially those <u>close to period end</u> that pose difficult "substance over form" questions. 5. Significant operations located or conducted across international borders in jurisdictions where differing business environments and cultures exist. 6. Use of business intermediaries for which there appears to be no clear business justification 7. Significant bank accounts or subsidiary or branch operations in tax-haven jurisdictions for which there appears to be no clear business justification	B) 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: <i>[Trick: Chote chote SMALL items pe INTERNAL CONTROL accha nahi rakhte]</i> 1. Large amounts of <u>cash on hand</u> 2. <u>Inventory items that are small in size</u>, of high value, or in high demand 3. <u>Easily convertible assets</u>, such as bearer bonds, diamonds, or computer chips. 4. <u>Fixed assets which are small in size</u>, marketable, or lacking observable identification of ownership. <u>Inadequate I.C over assets may increase susceptibility of Missappropriation of those assets:</u> 1) Lack of <u>SOD</u> 2) Inadequate <u>records of assets</u> 3) Inadequate <u>physical safeguard</u> over cash, investment, inventory 4) Lack of <u>timely Reco. Of assets</u> 5) Lack of <u>mandatory vacation</u> of employees
C) Attitudes/Rationalizations: <i>Bekaar entity hai .. koi values nii.. koi morale nii ... Non-Finance ke bande hai... wo gadhe kese Law & IC banaenge ...</i> <i>Bas fraud karwa lo unse .. stock price manipulation tax fraud</i> 1) Communication, enforcement of the entity's values or ethical standards by mngt, or communication of inappropriate values/ethics, that are <u>not effective</u> 2) Low morale among senior management. 3) Non-financial management's excessive participation in or preoccupation with the selection of accounting policies or the determination of significant estimates 4) Known history of violations of securities laws or other laws and regulations, or claims against the entity 5) Management failing to remedy known significant	C) Attitudes/Rationalizations: <i>[Trick: naa to company wale ASSETS ka dyaan rkhte h, naa EMPLOYEES ka]</i> 1. <u>Disregard for the need for monitoring or reducing risks</u> related to <u>misappropriations of assets</u>. 2. <u>Disregard for internal control over misappropriation of assets</u> by overriding existing controls or by failing to take appropriate remedial action on <u>known deficiencies in internal control</u>. 3. Behavior indicating displeasure or dissatisfaction with the entity or its treatment of the employee. 4. Changes in behavior or lifestyle that may



deficiencies in **internal control** on a timely basis.

- 6) Excessive **interest by management in maintaining** or increasing the entity's **stock price** or earnings trend.
- 7) An interest by mngt in employing inappropriate means to **minimize reported earnings for tax-motivated reasons**.
- 8) The owner-manager makes no distinction between **personal and business transactions**
- 9) The **relationship between management** and the current or predecessor **auditor** is **strained**,

indicate assets have been misappropriated.

5. Tolerance of **petty theft**.

The **relationship between Mngt and the current or predecessor auditor is strained**, as exhibited by the following: - *[trick: aae deen lad raha h .. data dera ni h .. restriction lagara h ... fir bolra h jldi audit karo]*

- 1) **Frequent disputes** with the current or predecessor auditor on **accounting, auditing, or reporting matters**
- 2) **Restrictions on the auditor** that inappropriately limit access to people or information or the ability to communicate effectively with those charged with governance.
- 3) **Domineering management behaviour** in dealing with the auditor, **especially involving attempts to influence the scope of the auditor's work** or the selection or continuance of personnel assigned on audit engagement.
- 4) Unreasonable demands on the auditor, such as unrealistic **time constraints regarding the completion** of the audit or the issuance of the auditor's report

Why evaluation of fraud risk factors by auditor is necessary?

- Evaluate whether 1 or more FRF are present → **not necessarily indicate the existence of fraud**
- The fact that fraud is usually concealed can make it very difficult to detect.
- Fraud risk factors **cannot easily be ranked in order of importance**. significance of Fraud RF varies widely
- Accordingly, the **determination of whether a fraud risk factor is present and whether it is to be considered in assessing the ROMM of the FS due to fraud** requires the **exercise of professional judgment**.

Q2. Risk Factor related to misstatement arising from Misappropriation of Assets: Refer above notes "**Fraud Risk factor - Relates to misappropriation of Assets**"

Q3. Manufacturer of Fabrics, want to install new plant (need huge capital) → auditor finds that **revenue increase from Rs. 750 Crore to 1000 Cr** this year (no change in plant capacity) → any ROMM due to Fraudulent FR ?

Hint: Given case, **Excessive pressure exist for mngt for Fraudulent FR** (tempted to inflate revenue → it's Fraud risk factor) → audit procedure to assess ROMM due to fraudulent FR → Substantive analytical procedure (For revenue), CAAT's to identify **Unusual revenue**, testing control relating to revenue transaction

Q4. Stat. auditor found → I.Auditor report pointed out Following deficiencies in I.C., But Mngt didn't corrected:
(a) **Receivable Not reconciled on periodical basis** (b) **Customer Credit limit not reviewed**.

Hint: Its **Fraud Risk Factor of Fraudulent FR** (as **mngt failure to correct KNOWN Sig. Deficiency in I.C on timely**, it reflects **Attitude/Character/ethical values Intentionally allow to allow commit Dishonest Act**)

→ Failure to rectify known control deficiency as given above (a) & (b) : **Its' a Intentional Misstatement**

→ Further, non-review of Limit may cause grant of credit beyond creditworthiness:

➤ Auditor's Duty/Responsibility i.r.t Fraud in an Audit of FS:

Responsibilities of the Auditor:

[Read only]

- Obtain as **reasonable assurance that the FS** taken as a whole are free from MMS, whether caused by fraud or error.
- Owing to the **inherent limitations** of an audit, there is an **unavoidable risk that some MMS of the FS may not be detected**, even though audit is properly planned as per SA
- **Fraud > Error:** The risk of not detecting a MMS resulting from fraud is higher than the risk of not detecting one resulting from error (as Fraud organised & Sophisticated)
- Risk of not detecting MMS due to **Mngt Fraud is higher than Employee fraud** (as mngt is at position to directly manipulate accounts)

	auditor is responsible for maintaining professional skepticism
Some Common Points to Quote in answer: [Read only]	- Obtain Reasonable Assurance that FS as a whole are free from MMS due to fraud. - Maintaining Professional Skepticism throughout Audit. - Not Expect to detect fraud unless suspicion arises. Whether the FS is materially misstated due to fraud - Consider Impact of fraud on financial statements. - Consider Reliability of Written Representation if mgt. fraud found - Obtain Written Representation - Communicate to Chairman & BODs - if conditions are like documents not authentic/modified then Investigate. - Investigate if Inconsistent Responses of Mgt./ TCWG. Section 143(12)- Fraud reporting: Auditor has reason to believe that an offence involving fraud is being or has been committed against company by officers /employees of company - Immediately report matter to Audit Committee in 2 days of knowledge (as amount < ₹1Crore) mentioning - Nature of Fraud & Description - Approximate amount involved - Parties involved -Immediately report matter to CG in time & manner prescribed in Rule 13 if amount > ₹1 Crore. - Reporting responsibility in CARO & Section 447 person committing fraud liable.
Maintain Professional Skepticism: [Read only]	- Shall maintain professional skepticism throughout the audit for MMS due to fraud (Notwithstanding auditor's past experience of honesty & integrity of mngt & TCWG) <u>Unless auditor has reason to believe contrary</u>→Auditor may accept record & docs as genuine. <u>If conditions identified</u> during audit cause auditor to believe <u>that docs not authentic</u> or that terms in a document have been modified but not disclosed→auditor shall investigate further - Where <u>responses to inquiries</u> of mngt / TCWG is <u>inconsistent</u> → investigate inconsistencies.
If auditor is unable to continue performing: (Special Trick ;-)	Then auditor shall: Determine professional and legal responsibilities including whether there is requirement to report to person who made appointment or regulatory authority [Section 143(12)] - Consider appropriateness of withdrawal, where legally permitted If Auditor withdraw: Discuss with the appropriate level of Mngt & TCWG, the auditor's withdrawal from the engagement and the reasons for the withdrawal and - 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, the auditor's withdrawal from the engagement and the reasons for the withdrawal. - Where withdraw is not appropriate, auditor needs to express modified opinion (also mention the reasons for same) - Where withdraw is legally permitted, communicate with TCWG and other regulatory authorities required u/s 140 - Resignation
Communicate to TCWG:	Appropriate Mngt: If identified /suspect Fraud → communicate to appropriate level of mngt (Whose primary responsibility to prevent detect fraud) → on Timely basis TCWG: <u>Unless all TCWG involved in managing entity</u> → identified or suspects Fraud done by mngt, employees have significant role in IC →communicate matters to TCWG on timely basis If suspects that fraud involving mngt: <u>Communicate suspicion to TCWG & Discuss NTE</u> of audit procedures necessary to complete the audit. - Also communicate other matters to TCWG relevant in the auditor's judgment



Communicate to Regulatory & Enforcement Authorities:

- **Report to Outside Party:** If auditor identified or suspects fraud → determine whether there is responsibility to report the occurrence or suspicion to a party outside the entity.
- **L&R override Confidentiality:** Although auditor's professional duty is to maintain confidentiality of client information → auditor's legal responsibilities may override the duty of confidentiality in some circumstances. Eg., in case of audit of banks, the auditor has a statutory duty to report the occurrence of fraud to the supervisory authorities, i.e. RBI.
 - ✓ Also, in some entities the auditor may have a duty to report misstatements to authorities in those cases where mngt and TCWG fail to take corrective action.
 - ✓ In some clients, requirements for reporting fraud, whether or not discovered through the audit process, may be subject to specific provisions of audit mandate or related L&R

Q5. Company entered into transaction on 25/02/2028 (near yr end), to pay 60 lacs to engineer consultant → No amount was paid actually, but expense booked in Books (No docs/evidence) → what should auditor approach ?
Hint: SA 240 → Fraud can be done by Mngt overriding controls (like Fictitious JV), mainly near Year End. → If misstatement is result of fraud/suspected fraud, (Withdraw) → Refer Above Notes "If auditor is unable to continue performing" + Mention Sec 143(12) Fraud report to CG if ≥ 1 Crore + Clause 11 of CARO

Q6. Misstatement resulting from fraud or suspected fraud during the audit → not possible to continue audit.
Hint: SA 240 → [Explain the Withdraw Process + Sec 143(12) reporting, CARO 2020 reporting]

Q7. A special audit was conducted on company related to Fraud → but mngt is not giving report copy to Stat Auditor (neither providing W.R i.r.t Fraud)
Hint: "SA 240" (auditor to obtain reasonable assurance the FS free from MMS due to fraud/error & "SA 580" → Not provide W.R, alert for significant issue may exist (Re- evaluate Integrity of Mngt & effect on reliability of representation/evidence & Effect on A.Report. → Now explain Withdraw Process + Sec 143(12) + CARO 2020

➤ **ROMM & Fraud:**

Discussion among E.Team:	Discussion among the engmnt team shall place particular emphasis on how and where the entity's FS may be susceptible to MMS due to fraud, including how fraud might occur. [Discussion Points are mentioned in "Additional PDF in addition to Main book]
Risk of Non-Detection of MMS:	Obtain reasonable assurance that FS is free from MMS whether due to fraud or error: • Due to inherent limitation of audit (SA 200) → Some MMS of FS not detected • Risk of not detecting MMS due to Fraud is higher than Error (as Fraud organised & Sophisticated) • Risk of not detecting MMS due to Mngt Fraud is higher than Employee fraud (as mngt is at position to directly manipulate accounts)
Risk Assessment Procedures to obtain info for use in identifying ROMM due to fraud:	When performing RAP and related activities to obtain an understanding of the entity & its environment, including the entity's IC or shall perform the procedures to obtain information for use in identifying the ROMMs due to fraud like: 1) Inquiries of management & others within the entity, 2) Obtaining understanding as to how TCWG exercise oversight of mngt's processes for identifying and responding to the risks of fraud in the entity & the IC that mngt has established to mitigate these risks and 3) Evaluation of unexpected relationships identified in performing analytical procedures which may indicate ROMM due to fraud. Evaluate whether the info obtained from the other RAP and related activities performed indicates that one or more fraud risk factors are present.
SA 315: Identifying &	SA 315, Auditor shall identify & assess ROMM due to fraud at FS level, & assertion level: When identifying and assessing the ROMM due to fraud, based on below assumption.



Assessing ROMM due to Fraud [Presumed/Deemed Risk]	<u>Following area are presumed to be high risk:</u> - Revenue Recognition - Mgt Override Control The auditor shall treat those assessed ROMM due to fraud as significant risks and accordingly, to the extent not already done so, the auditor shall obtain an understanding of the entity's related controls, including control activities, relevant to such risks. <u>Pre-assumption of Fraud risk may be Rebutted (ignored) i.e., No ROMM due to Fraud:</u> → If only Single type of Simple revenue structure (eg., Single Rental property) <u>Pre-assumption of Fraud MUST be Considered i.e., High chances of ROMM due to Fraud:</u> → Complex revenue structure or Lack of Control
Document:	When auditor has concluded that the presumption that there is a ROMM due to fraud related to revenue recognition is not applicable in the circumstances of the engagement, the auditor shall document the reasons for that conclusion

➤ **Responses to the Assessed Risks of Material Misstatement Due to Fraud:**

Overall Responses (At FS Level)	Response of assessed ROMM due to Fraud at Assertion Level	Response to Risks Related to Management Override of Control
[Trick: "PAU"] Person: Assign & supervise <u>personnel of Skill knowledge</u>, and Individuals ability to assess the ROMM due to fraud for engmnt A/cing Policies: Evaluate selection & application of <u>a/cing policies relates to subjective measurement</u> may be fraudulent FR from mngt Unpredictability: Incorporate unpredictability in selection of NTE of audit procedures	- Auditor shall design & perform further audit procedures (FAP) whose NTE are responsive to the assessed ROMM due to fraud at the assertion level. - Auditor may change NTE of audit procedures to obtain <u>audit evidence that is more reliable</u> & relevant or to obtain additional corroborative Info. Example: if <u>mngt under pressure to meet earning target</u> → mngt may enter sales agreement (prepone) or invoicing sales before delivery: ✓ So AUDITOR shall <u>Not only use E.confirmation to Confirm O/s amt but Also confirm the details of the sales agreements</u> (including date, any rights of return, delivery terms) ✓ Further auditor might do <u>Inquiry of Non-financial Personnel</u> (i.e., sales) reg. any changes in sales agreement.	Mngt is in unique position to perpetrate fraud because of mngt's ability to manipulate A/cing records & fraudulent FS by overriding controls that otherwise appear to be operating effectively. This risk is present in all entities. Mngt is Unpredictable in how override could occur so it is a significant fraud risk. <u>Irrespective of the auditor's assessment of the risks of mgt override of controls, the auditor shall design and perform audit procedures to:</u> - Test <u>appropriateness</u> of journal entries recorded & Yr end adjustment in FS - Review A/cing estimates, Bias if any. - Significant transactions that are outside normal course of business, appear Unusual → <u>evaluate whether the business rationale</u> or it's fraudulent FR / Misappropriation ins asset

➤ **Some Other Topics (Based on Question Asked)**

DEEMED/PRE-ASSUMED RISK:

Q8. Hotel Audit → risk of Improper revenue recognition (not treated as Fraud Risk), IC not designed to mitigate risk of revenue recognition, Not account revenue of 35 Cr, & some amt receive in CFO personal A/C.

- Auditor Responsibility is w.r.t Fraud is → **SA 240 & 315** (identify & assess ROMM due to fraud FS & assertion)
- SA 240 & 330** → determine overall responses to address the assessed ROMM due to fraud
- Presumption** → that there are risk of fraud in revenue recognition (Eg. Where single type of simple revenue



transaction → Auditor May conclude that there is No ROMM, However, For complex revenue structure Or Lack of control on revenue recognition → High Probability of fraud risk in revenue recognition)
Now Explain Given Case Issues (same as Qns) → So while performing RAP → Consider complexity & nature of revenue for determining fraud risk, Further Deficiency in I.C / IC Not exist → as Risk if improper revenue recognition is **significant risk**, + fraud reporting to CG as per **Sec 143(12)** if fraud amount exceed Rs. 1 Crore.

MANAGEMENT FRAUD:

Q9. Explain Duties & Responsibilities of Auditor for MMS resulting from Management Fraud

- Misstatement in FS can arise from Fraud/Error, "**Fraud**" means → 'Intentional Act' by one or more individuals among mngt, TCWG, employees, or 3rd parties, involving use of deception to obtain an unjust or illegal advantage.
- **SA 240** → **Primary responsibility for prevention** & detection of fraud rests with both **TWCG & Mngt** → Auditor is responsible for obtaining reasonable assurance that FS as whole free from MMS, whether by fraud or error.
- **SA 200** → **Inherent Limitation** is significant in case of misstatement from Fraud → **Risk of not detecting MMS from fraud** is higher than not detecting Error (Fraud is Sophisticated than Error). Further, risk of the auditor not detecting a MMS resulting from Mngt fraud is greater than for employee fraud. → Further, to obtain reasonable assurance, auditor to Maintain **Professional Skepticism** throughout the audit
- **Sec 143(12)** → Explain Fraud Reporting (if amount is Less than 1 Crore & Exceed 1 Crore)
- **Clause 11 of CARO 2020** → Explain this clause

Q10. Director has committed **Teeming & Lading** fraud (subsequently deposited) → Responsibilities of Auditor

- **Firstly**, SA 240 → auditor needs to perform procedures whether FS are materially misstated.
- **Secondly**, the auditor needs to consider the impact of fraud on F.S. and its disclosure in the audit report.
- **Thirdly**, the auditor should communicate the matter to the Chairman and Board of Directors.
- **Finally**, in view of the fact that the fraud has been committed at the highest level of mngt, it affects reliability of audit evidence previously obtained since there is a genuine doubt about W.R. [*now Explain* → **section 143(12)**]

➤ **Other Integrated Qns & Specific Frauds**

Q11. During Audit you found → cash balance in books ₹ 2.10 crores. But only, small amounts of ₹ 50K withdrawn to meet day-to-day expenses: = SA 240 → If circumstances indicate misstatement from Fraud → consider **Impact of Fraud on FS**. (For Cash & Bank → carry out **surprise verification** of cash more frequently, If Cash not agreed with Book, Seek Explanation, otherwise state fact in A.Report)

Q12. During Audit → Found Error in Inventory Valuation (Affect FS materially): = SA 240

- If Circumstances indicate Possible Fraud → (a) Consider Effect of Suspected Fraud/Error on Financial Info.
(b) If Have material effect on Financial Info → Perform **Modified/Additional procedure**
- If Auditor Identified Misstatement, EVALUATE → (a) Whether misstatement is indicative of Fraud
(b) evaluate it's implication on Other aspects of Audit (like W.R)
- Further SA 320 → Request mngt to Adjust Financial Info → if Refused (express **Qualified / Adverse**)

SA 250 - CONSIDERATION OF LAWS AND REGULATIONS AN AUDIT OF FS

Introduction:	Auditor should check whether client has followed all the applicable laws & regulation or not because non-Compliance of them may attract penalties & disclosure [AUDIT of FS]
Not apply:	not apply to other assurance engagements in which the auditor is specifically engaged to test and report separately on compliance with specific L&R .
Effect of L&R on FS:	Effect on the FS of L&R varies considerably → some have direct effect on FS (reported amounts and disclosures) → Other L&R not have a direct effect Some entities operate in heavily regulated industries (such as banks and chemical) → non-compliance have result in fines, litigation → material effect on FS



Responsibility of the Auditor

Consider L&R in audit:	Auditor is responsible for obtaining reasonable assurance that the FS, taken as a whole, are free from MMS, whether caused by fraud or error. In conducting an audit of FS, the auditor takes into account the applicable legal and regulatory framework.		
Auditor NOT responsible:	The auditor is not responsible for preventing non-compliance and cannot be expected to detect noncompliance with all L&R. [It's primary responsibility of Mngt]		
Inherent Limitation: [Trick: Fraud "deliberately chupaya" ... "FS ko affect" kar ra h to bhi ,mgt bolra h ki nhi .. "court" wala bolega to hi mangenge]	Q13. Why effects of inherent limitations as in SA 200, are greater i.r.o non-compliance of L&R? Due to inherent limitations, there is unavoidable risk that some MMS in FS may not be detected, even though the audit is properly planned and performed as per SA's, due to: a) 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. b) Many L&R, principally to the operating aspects of an entity that typically do not affect FS and are not captured by the entity's info. systems relevant to financial reporting. c) Whether a act is non-compliance is ultimately a matter for legal determination by court of law.		
Documentation:	Auditor shall document identified or suspected non-compliance with L&R and results of discussion with mngt and, where applicable, TCWG and other parties outside the entity.		
Responsibility of the Auditor : [2 different category of Law] [Auditor consideration of compliance with L&R]	a)	Laws which have Direct Effect on F.S Amount or Disclosure:	<u>[Eg, Tax (i.e, GST Payable, Income tax)]</u> Auditor should obtain SAAE w.r.t compliance of L&R
	b)	Law which does not have direct effect on F.S Amount or Presentation:	But compliance is fundamental effect on the operations of the entity → may Go concern issue → to Avoid Penalties or Continue the business (Eg., Labour laws, Environmental Laws, non-comply operating license, regulatory solvency requirements, For Bank capital or investment requirements, NBFC not get certificate if net owned fund is less): Such Non-compliance may have material effect on the FS Auditor should perform <u>limited specified procedure</u> on other L&R that may have material effect on FS: • Inquire with management, whether entity comply such L&R • Inspecting correspondence with regulatory authorities

Q14. Roles and responsibilities of statutory auditors i.r.t compliance with L&R by the entity? [OLD]

- Obtain General Understanding of:
 - a) legal and regulatory framework applicable to entity & Industry or Sector in which entity operates
 - b) How the entity is complying with that framework.
- Obtain SAAE regarding compliance of L&R having for Direct effect FS (Material amount or Disclosure)
- To identify non-compliance of other L&R, that may have material effect on FS,
 - a) Inquire of management &
 - b) Inspecting Correspondence
- Auditor shall remain Alert possibility of non-compliance of L&R → Professional skepticism
- Obtain written representations (That known /suspected Non-compliance are disclosed)

Q15. Management is Saying that Child Labour Employed (Compliance with other L&R) is outside Scope of Auditor
Hint: SA 250 → Auditor not responsible for preventing Non-Compliance (But he have to obtain reasonable



assurance that FS is Free from Material FS, so take into account applicable L&R)

(a) For L&R have direct effect on FS → Obtain SAAE, (b) other L&R having material effect on FS → Specified Procedure. (as Other L&R Non compliance lead to fines, litigation or other consequences → may need to be provided for in the FS, Like Child Labour Employed can have Material effect on FS)

→ Ensure that disclosure of above fact & provision for the cost of fines, litigation → if Non-Compliance have material effect on FS & not been adequately reflected in FS → Express qualified or adverse opinion (SA-705)

➤ Indicator of Non-Compliance & Management responsibility to Comply L&R:

Indicators of Non-Compliance of L&R : (Special Trick;-)	Q16. Indications of non-compliance with L&R Or for non-compliance Indicate possible areas • Unusual payments in cash, purchases in the form of cashiers' cheques payable to bearer or transfers to numbered bank accounts. • Unusual payments towards legal and retainership fees. • Payments for unspecified services or loans to consultants, related parties, employees or government employees. • Sales commissions or agent's fees that appear excessive in relation to those ordinarily paid entity or in its industry or to the services actually received. • Purchasing at prices significantly above or below market price • Payments without proper exchange control documentation • Unusual transactions with companies registered in tax havens. • Investigations by regulatory organisations & Govt departments or payment of fines, penalty. • Payments for G&S made other than to the country from which the G&S originated. • Existence of an information system which fails, whether by design or by accident, to provide an adequate audit trail or sufficient evidence. • Unauthorised transactions or improperly recorded transactions. • Adverse media comment.
Responsibility of Mngt for Compliance of L&R: [Policies & Procedures to Prevent/Detect Non-Compliance]	It is the responsibility of mngt, with the oversight of TCWG, to ensure that the entity's operations are conducted as per provisions of L&R, including compliance with the L&R. Q17. Example of Policies & procedure for prevention & detection of Non-Compliance [Trick: "IC" & "COC" > "Employee" ko samjao > "Monitor" karo > in case of Non-compliance, "Disciplinary action" lo] • 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 legal requirements and ensuring that operating procedures are designed to meet these requirements. • 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 to comply within its particular industry and a record of complaints. [In larger entities, these policies & procedures may be supplemented by assigning appropriate responsibilities to internal audit f(x), audit committee, compliance function]

Q18. Social media company → Govt bringing new Strict Laws for them: =

So Verify whether has System & Procedures (to meet new Laws requirement) Like Policies & procedure (I.C, Sensitizing Employees reg. new L&R, Engage Legal advisor). → Further, Financial stability of company may be threatened due to New Regulatory requirement (Mngt is under Pressure → so evaluate Fraud risk Factor)



➤ Audit procedure when Non-Compliance is Identified:

1. Auditor shall obtain an understanding of nature & Circumstances in which it occurs
2. Evaluate possible effect on FS. (Fines, Going concern, True & Fair view, Disclosure)
3. Discuss with Mngt/TCWG
4. If Mngt/TCWG not give info & have material effect on FS → take legal advice
5. If sufficient info about Non-compliance cannot be obtained i.e., Lack of SAAE → Affect auditor's opinion
6. Evaluate non-Compliance implication i.r.t Other aspect → i.e., Auditor Risk Assessment & Reliability of W.R, Appropriate action
7. Reporting of non-compliance
 - (a) Reporting to management/TCWG
 - (b) Reporting to users of auditor's report of FS
 - (c) Reporting to regulations

Q19. For Insurance Company → Following are Indication of Non-Compliance of L&R: (SM Qn)

- (1) GST Dept issued notice for creating Fictitious invoices of sales (Involve penalty, have Direct effect on FS)
 - (2) IRADAI was also informed by GST dept → IRDAI may also levy Fine & Litigation (Material effect on FS)
- (Now refer Above procedure "Audit Procedure when Non-Compliance is Identified") (Answer Ends)

➤ REPORTING RESPONSIBILITY of Auditor i.r.t Non-Compliance of L&R:

Q20. State Auditor's responsibility for Non-Compliance of L&R i.r.t audit of FS

- 1) Reporting Non-Compliance to TCWG: (Unless all TCWG involved in mngt, and mngt aware of this matter)

If non-compliance is believed to be intentional & material:	communicate matter → as soon as practicable.
If suspects that management or TCWG are involved in non-compliance:	communicate to → next higher level of authority (like audit committee or supervisory board)
Where no higher authority exists, or if auditor believes that the communication may not be acted upon or is unsure about person to whom to report:	consider the need to obtain legal advice.

- 2) Reporting Non-Compliance in the Auditor's Report on the FS:

If concludes that non-compliance has material effect on FS, & has not been adequately reflected in FS:	As per SA 705 express a qualified or adverse opinion
If auditor is precluded by mngt or TCWG from obtaining SAAE to evaluate whether non-compliance that may be material:	express a qualified opinion or disclaim as per SA 705.
If auditor is unable to determine whether non-compliance has occurred because of limitations imposed by the circumstances rather than by mngt or TCWG:	evaluate the effect on the auditor's opinion as per SA 705.

- 3) Reporting Non-Compliance to Regulatory & Enforcement Authorities: If auditor identified or suspects non-compliance → determine whether auditor has a responsibility to report to parties outside the entity.

SA 260 – Communication with Those Charged with Governance

TCWG means:

[Read only]

- TCWG denotes the person(s) or organization(s) (e.g., a corporate trustee) responsibility for overseeing the strategic direction of the entity and includes those overseeing the FR process.
 - For some entities, TCWG 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.



	➤ In some cases, some, or all of TCWG are involved in managing the entity. In others, TCWG and management comprise different persons. (it can be collective responsibility of BOD, Supervisor board, partners, etc) ➤ In smaller entities, however, one person may be charged with governance (owner/mngr) ➤ Appropriate TCWG: <u>Due to diversity</u> → auditor <u>can-not determine specific person to communicate particular matters</u> → <u>Not be clearly identifiable</u> from the applicable legal framework → not formally defined, such as some family-owned entities & NPO, • In Such case, auditor may need to discuss and agree with the engaging party the relevant persons with whom to communicate. • In deciding with whom to communicate, auditor's understanding of an entity's governance structure & processes obtained in accordance with SA 315 is relevant. • The appropriate persons with whom to communicate → may vary depending on matter to be communicated.
The Auditor's Responsibilities:	The auditor shall communicate his responsibilities & some other matters to TCWG i.e., e auditor is responsible for forming and expressing an opinion on the FS.
Appropriate Person:	The auditor shall determine the appropriate person(s) within the entity's governance structure with whom to communicate <u>Sub Group of TCWG (Eg. Audit Committee) : If the auditor communicates with a subgroup of TCWG, for example, an audit committee, or an individual, auditor shall determine whether the auditor also needs to communicate with the governing body.</u>
When All of TCWG Are Managing Entity:	Eg. small business where a single owner manages, matters need not be communicated again with those same people(s) in their governance role
Form/ Process of Communication: [Depend: Oral/Writing]	• In writing with TCWG for significant findings of audit, if in auditor's judgement, oral communication would not be adequate • Written communications need not include all matters arose during the course of audit. • The auditor shall communicate in writing to TCWG regarding auditor independence. In case of Listed entities
Timing	The auditor shall communicate with TCWG on a timely basis .
Adequacy of Communication:	evaluate whether the two-way communication (between Auditor & TCWG) is adequate for audit → if not adequate → auditor shall evaluate auditors assessment of ROMM & ability to obtain SAAE

➤ Matters to be included in Communication

Matters to be included in Communication:	Q21. Auditor should communicate audit matters arising from FS audit with TCWG". state the matters to be included in such Communication. [Significant Findings from audit] As per SA 260 "Communication with TCWG", the auditor shall communicate with TCWG, I] Responsibilities of the auditor in relation to the FS audit, including that: (a) The auditor is responsible for forming and expressing an opinion on the FS that have been prepared by management with the oversight of TCWG; & (b) The audit of the FS does not relieve management or TCWG of their responsibilities. [Generally above is included in engmnt letter or other suitable form of written agreement] II] Planned scope & timing of audit: • Assist TCWG to understand better consequences of auditor work, discuss risk & materiality & identify areas where auditor should undertake additional procedure • Assist auditor in understanding better the entity and its environment

	- communicate OVERVIEW of scope/ timing of audit (including significant risk identified) Care is necessary when communicating with TCWG about the planned scope and timing of the audit so as not to compromise the effectiveness of the audit, particularly where some or all TCWG are involved in managing the entity. may reduce the effectiveness of those procedures by making them too predictable. III] Auditor shall communicate with TCWG, following <u>Significant Findings from Audit</u>: (a) The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and FS disclosures. When applicable, → explain to TCWG → why auditor considers, that a significant a/cing practice as per applicable FRF → is not to be most appropriate to the particular circumstances of the entity; (b) Significant difficulties, if any, encountered during the audit; (c) Unless all of TCWG are involved in managing the entity: Significant matters, if any, arising from the audit that were discussed, or subject to correspondence with management; and Written representations the auditor is requesting; and (d) Other matters, if any, arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process. (e) Circumstances that affect the form and content of the auditor's report, if any and The communication of findings from the audit may include requesting further information from TCWG in order to complete the audit evidence obtained.
Significant Difficulties: <i>(Special Trick :-)</i>	Q22. which matters can be considered as significant difficulties as per SA 260. [OLD] SA 260, significant difficulties encountered during the audit may include such matters as: - An unreasonably brief time within which to complete the audit. - The unavailability of expected information Significant delays by mngt, the unavailability of entity personnel, or an unwillingness by mngt to provide info necessary for the auditor to perform the auditor's procedures. - Extensive unexpected effort required to obtain SAAE audit evidence. Restrictions imposed on the auditor by management. Mngt'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.as per SA 705 (Revised), Modifications to the Opinion
Communication to TCWG, When Additional Info is included in Auditor's report:	- The auditor expects to modify the opinion in 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 necessary to include EOM or OM para as per SA 706 or other Sas - The auditor has concluded that there is an uncorrected material misstatement of the other information in accordance with SA 720. In such circumstances, Auditor may provide TCWG with a draft of the auditor's report to facilitate a discussion of how such matters will be addressed in the auditor's report.
Auditor Independence (Listed Entities): <i>(bhai dekho)</i>	Q23. CA. Shelly Goel is offered a listed company audit. The audit committee of company wants her to justify independence i.r.t company through proper communication? In the case of listed entities, the auditor shall communicate with TCWG: ➤ All relationships and other matters between the firm, network firms, and the entity that may reasonably be Impact independence. This shall include total fees charged by firm /



...Apni ye ye
Relationship hai
.. uspe mene ye-
ye Safeguard
laga diye .. to Me
independent hu)

network firm during the period for audit and non-audit services

- The related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level.
- A statement that the ET and others in the firm as appropriate, network firms have complied with relevant ethical requirements regarding independence; and

Further, as per Co. Act, 13 requires audit committee to review and monitor auditor's independence. Therefore, audit committee requiring auditor to justify her independence

Q24. Auditor communicated Following matters to TCWG (a) Auditor's responsibility for FS Audit (b) Planned Scope & Timing of Audit (c) Auditor's independence → which Matters Not Included ?
Hint: Refer above Notes & explain "Significant Findings from the Audit" (under Matter's to communicate TCWG)

➤ Why it is Important to Communicate KAM to TCWG [Old Qn - Not in SM]

Q25. When to communicate "KAM"? What are relevant considerations in this regard and their usefulness?

- SA 260 (Revised) requires the auditor to communicate with TCWG on a timely basis.
- SA 701 The appropriate timing for communications about KAM will vary with the circumstances of engmnt.

However, the auditor may communicate preliminary views about KAM when discussing the planned scope and timing of the audit, and may further discuss such matters when communicating about audit findings.

Communicating to TCWG enables them to be made aware of the KAM that the auditor intends to communicate in the auditor's report, & provides them with an opportunity to obtain further clarification where necessary.

Auditor may consider it useful to provide TCWG with a draft of auditor's report to facilitate this discussion.

Communication with TCWG recognizes their important role in overseeing the FR process, and provides the opportunity for TCWG to understand the basis for the auditor's decisions i.r.t KAM & how these matters will be described in the auditor's report.

It also enables TCWG to consider whether new or enhanced disclosures may be useful in light of the fact that these matters will be communicated in the auditor's report.

SA 299 - JOINT AUDIT OF FINANCIAL STATEMENTS

Meaning:	A joint audit is an audit of FS of an entity by 2 or more auditors appointed with the objective of issuing the audit report. [Generally, for larger entities, sometime requires by Law]
Not applicable:	Relationship between Principal audit & Subsidiary/branch/JV/Ass/other Auditor (SA-600)
Audit planning, Risk Assessment and Allocation of Work:	• The engagement partner and other key members of the engagement team from each of the joint auditors shall be involved in planning the audit. • The joint auditors shall jointly establish an overall audit strategy that sets the scope, timing and direction of the audit. [In Developing Audit Plan Joint Audit Shall Consider → "Refer Additional PDF"] • ROMM need to be considered and assessed by each of the joint auditors and shall be communicated to other joint auditors • Discuss & document the NTE of audit procedures for common and specific allotted areas, same shall be discuss & Communicated to TCWG • Joint auditors shall obtain common engagement letter & common Mngt representation letter. • Work allocation & Specific Allotted areas shall be Documented & shall be signed by all the joint auditors & same shall be communicated to TCWG. [Documentation of allocation of work helps in avoiding any dispute or confusion among the joint auditors regarding scope of work]



Each JA is entitled to Assume:	a) The other joint auditors have carried out their part of the audit work and the work has actually been performed in accordance with the SA's issued by ICAI. It is not necessary for a joint auditor to review the work performed by other joint auditors. b) The other joint auditors have brought to said joint auditor's notice any departure from applicable FRF or significant observations that are relevant to their responsibilities noticed in the course of the audit. <u>Where FS of a division/branch are audited by one of JA's</u> → the other JA are entitled to proceed on the basis that such FS comply with all L&R requirements and present a true & fair view of the state of affairs and of the results of operations of the division/branch concerned.
➤ Feature of SA's	
Division of Work	Where joint auditors are appointed, by mutual discussion, Divide audit of (i) Identifiable units or specified areas. (ii) Where above 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. ➤ Not divided: Certain areas of work, owing to their importance or owing to the nature of work involved would not be divided and would be covered by all the joint auditors. ➤ Documented: Such a division affected by the joint auditors should be adequately documented and preferably communicated to TCWG. (Mention in other matter para, SA 706 → Specific responsibility of JA)
Coordination	Where in the course of his work, a joint auditor comes across matters which are relevant to the areas of other joint auditors and which require joint discussion, he should communicate the same to all the other joint auditors in writing before the finalization of audit and preparation of audit report.
➤ RESPONSIBILITY:	
Join Auditors are Specifically responsible for:	Joint Responsibilities, All the joint auditors shall be jointly and severally responsible:
(a) Audit work divided among the JA's; each JA shall be responsible only for the work allocated to such JA including proper execution of the audit procedures. (b) It shall be the responsibility of each auditor separately to determine the: • NTE of audit procedures to applied i.r.t areas of work allocated to JA. • to study and evaluate the prevailing system of internal control relating to work allocated to him • Assessment of risk relating to areas of work allocated to said joint auditor (c) each JA is entitled to assure that the other joint auditors have <u>carried out their part of work in accordance with the generally accepted audit procedures</u> and therefore it would not be necessary for joint auditor to review the work (d) specific responsibility of each JA to <u>obtain info & explanations from the mngt i.r.t. such divisions /zones/units</u> and <u>to evaluate</u> the info & explanations	(a) Audit work which is not divided among the joint auditors & is carried out by all JA's; (b) Decisions taken by all the joint auditors under audit planning phase concerning the NTE of the audit procedure to be performed by each of the auditor; (c) Matters which are brought to the notice of the joint auditors by any one of them and on which there is an agreement among the joint auditors; (d) examining that the FS comply with requirements of relevant statutes; (e) Presentation and disclosure of the FS as required by the applicable FRF. (f) Ensuring that the audit report complies with requirements of relevant statutes. (g) the responsibility of <u>obtaining and evaluating information and explanation from the mngt</u> is generally a joint responsibility of all the auditors, <u>Unless agreed on specific pattern of distribution of this responsibility</u>
Reporting	Q26. A, B and C are joint auditors of a company. A&C are agreed on some matter, But B is not.



Responsibility:	Is B required to go by majority opinion of 2-1 <u>B is not required to go by majority opinion of 2-1.</u> ➤ Usually, Joint auditor is required to issue common audit report (unanimous opinion) ➤ If, however, where the joint auditors are in disagreement with regard to the opinion or any matters to be covered by the audit report, → express opinion in separate audit report ➤ If Joint Auditor Disagree to Majority Joint Auditors such Joint Auditor is not bound by the views of majority & can issue Separate Report in case of disagreement ➤ Further such separate audit reports shall also make reference to the audit report issued by other Joint Auditors under heading "Other Matter Paragraph" (SA 706) ➤ Before finalizing their audit report, the joint auditors shall discuss and communicate with each other their respective conclusions that would form the content of the audit report.
Communication with TCWG:	➤ When JA expect to modify opinion in report → communicate with TCWG the circumstances that led to the expected modification and proposed wording of modification. (SA 705) ➤ If the JA expect to include an EOM or OM para report → communicate to TCWG reg. this expectation & the proposed wording of this paragraph to ensure compliance with SA 706
Point to Note:	Even Though the Area is planned by all J.A commonly, planning was correct → but performed by Specific Auditor not professionally (mistake in execution) → then He will only be responsible

Q27. (SM) Joint Auditors (X,Y,Z) → IT System Control was **PLANNED as **Common Area**. → However **ACTUAL audit procedure** was performed by "**CA Y**" only (**Not Performed Professionally**) :: → So "**CA Y**" would be **Only Responsible** for It (As J.A was responsible for Appropriateness of NTE of Planning, However Execution Lies with Concerned auditor, so that individual concerned Auditor will be responsible)**

Q28. 2 joint auditor's → Divided activities into 4 geographics region → Explain the JA's responsibilities.
Hint: SA 299: i.r.o audit work divided among the joint auditors, **each joint auditor shall be responsible ONLY** for the work allocated to such joint auditor including proper execution. (also reg. Obtaining Information & explanation i.r.t to Such Division allotted to him) → [Refer & Explain Above Notes (1) Responsibility → Joint Responsibility" (2) Coordination (3) Join Auditors are Specifically responsible for]

Q29. Write Short Note on "Responsibility of JA's" Or Relationship among J.A's. (Old)

Hint: Refer Above Notes → "**Division of work**" & "**Coordination**", "**Responsibility**" "**Reporting responsibility**"

Q30. (MTP Nov'24) → Joint auditor → **Major Understatement in Value of Inventory (Inventory was checked by MN&Co), But **No documentation** for division of work.**

Hint: Refer Above Notes: "**Division of work**", "**Joint Responsibility**"

(Further **Document** the NTE of Audit procedure/ Work allocation for Common & Specific divided area → should be **signed** by all JA's → **communicate** to TCWG) →

(a) MN& Co is only responsible for Inventory **(b) there is violation of SA 299** (As work division not documented)

Q31. (Old) → Joint auditor → **Whether or not a Separate Report is require in case of Disagreement?**

Hint: → require to issue common report (However, If disagreement → issue separate report) → **Make reference** in Separate A.report "SA 706 → Other matter para) → Refer Above Notes "**Each JA is Entitled to Assume**"

Q32. (Old) → Mr. X, Y, Z are J.A → Mr. X & Y are agreed on same actuary report, However Z did not. Explain (a) Joint & Several responsibilities of Auditor (b) Responsibility of J.A, if Mr. Y Actuary report found faulty.

Hint: (a) Refer Notes "**Joint Responsibility**" & "**Reporting Responsibility**" i.e., Mr. Z can issue separate report, not bound by Majority & OM para

(b) SA 620 → Auditor responsibility not reduced by use of A.expert's work.

- Evaluate **Expert Work Adequacy** (relevance and reasonableness of expert Finding & Conclusion, it's consistency)
- **relevance & reasonableness of assumptions & methods**, → relevance, completeness, & accuracy of source data
- (Now Explain Qn Info.) → X & Y held responsible for Gross negligence, Not Mr. Z (As separate report issued)



SA 402 – Audit Considerations Relating to an Entity Using a Service Organization

Brief about this SA	- PwC (User auditor) is an auditor of XYZ Ltd (User entity), - XYZ Ltd outsourced its any part of business, which affect FS (Let's say Accounting is outsourced) to ABC Ltd (Service organization) (SO) - So PwC also need to check controls of ABC Ltd, Because if ABC Ltd control is weak, then it will impact XYZ Ltd FS also. - If ABC also outsourced its some part to CC Ltd, Then PwC also need to Check control of CC Ltd (Sub-service organization) - PwC have many methods to test control of ABC & CC Ltd, one of them is, they request ABC Ltd auditor's (KPMG- Service Auditor), to provide report on ABC Ltd controls. - If above report does not contain any info regarding CC Ltd control, then it will be known as CARVE OUT METHOD, - If that report contains info about CC Ltd control also, then known as INCLUSIVE METHOD - Further this report have 2 type. TYPE 1 & TYPE 2 (will Discuss later)
Scope of SA	User auditor's responsibility to obtain SAAE when a user entity uses the services of one or more service organisation (S.O) [Expand → how user auditor applies SA 315 and SA 330 in obtaining an understanding of the user entity, including IC relevant to audit, assess ROMM]
User entity:	is an entity that uses a S.O. & whose FS are being audited.
User auditor	is an auditor who audits and reports on the FS of a user entity
Service Organisation:	S.O. is a 3rd party organisation (or segment of a 3 rd party organisation) that provides services to user entities that are part of <u>those entities' info. systems relevant to financial reporting.</u>
Service auditor	auditor who, at the request of the S.O, provides an assurance report on the controls of a SO.

➤ When services provided by a S.O. are relevant to the audit of a user entity's FS?

Not relevant:	All outsource Service are not relevant for audit i.e., Outsource tax compliance function
Relevant Services for audit:	when those services which are provide by SO, and the controls over them, are part of the user entity's information system , including related business processes, relevant to financial reporting → Some other control are also relevant i.e., controls over safeguarding of assets.
➤ Relevant to financial reporting if these services affect any of: A SO's services are part of a user entity's information system, including related business processes, relevant to financial reporting if these services affect any of the following: - The classes of transactions in the user entity's operations that are significant to the user entity's FS; - How the user entity's information system captures <u>events and conditions</u>, other than transactions, that are significant to the financial statements; Controls surrounding journal entries, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments. - The procedures, within both info technology (IT) & manual systems, by which the user entity's transactions are initiated, recorded, processed, corrected as necessary, transferred to general ledger & reported in FS; - The related accounting records, either in electronic or manual form, supporting information and specific accounts in the user entity's FS that are used to initiate, record, process and report the user entity's transactions; this includes the correction of incorrect info & how info is transferred to the general ledger; - The financial reporting process used to prepare the user entity's FS, including significant accounting estimates and disclosures	

Q33. Outsourced Accounting Function → As an Auditor Enumerate Factors to be consider related to it F.R.

Hint: Refer notes : "Not relevant", "Relevant Services for audit", "Relevant to FR if these services affect any of"



➤ Obtain Understanding of services provided by S.O:

Obtain Understanding of services provided by S.O: <i>(Special Trick :-)</i>	The user auditor shall obtain an understanding of how a user entity uses the services of a service organisation in the user entity's operations, including: (i) The nature of the services provided by the SO and the significance of those services to the user entity, including the effect thereof on the user entity's internal control: [Available sources: user manuals, contract between user entity and SO etc.] (ii) The nature and materiality of the transactions processed or accounts or financial reporting processes affected by the service organisation; [sometimes transactions processed by SO, not appear to be material to FS, but nature of transaction process can be significant → so auditor should understand that control] (iii) The degree of interaction between the activities of the SO & of the UE; [It means, extent to which a user entity is able to and elects to implement effective controls over the processing performed by the SO. For example, a high degree of interaction exists between the activities of the U.E & those at the S.O when the U.E authorizes transactions and the S.O. processes and does the accounting for those transactions] (iv) The nature of the relationship between the user entity and the service organisation, including the relevant contractual terms for the activities undertaken by the S.O.
Understand IC & Significance of service: <u>[Read Only]</u>	• When obtaining understating of IC as per SA 315 → auditor also evaluate relevant controls at user entity that relate to services provided by S.O. • Determine whether a sufficient understanding of the nature and significance of the services provided by SO and their effect on the user entity's IC has been obtained
Further procedures if Sufficient understanding not obtained	<u>Further procedures if Sufficient understanding of UE not obtained by above methods:</u> • Obtaining Type 1 or Type 2 report (if available) • Contacting Service Organization, through user entity to obtain specific info. • Visiting Service organization & performing procedures to get info about controls at SO. • Use another auditor to perform procedures to get info on relevant control at SO.

Q34. G Ltd outsourced Payroll, Accounting → how auditor can obtain understanding of Services, Or
As auditor, what would be your considerations regarding the nature & extent of activities undertaken by S.O.
Hint: SA 402 & 315 → Refer above notes "Obtain Understanding of services provided by S.O"

➤ About Type 1 & Type 2 Report:

Obtaining Type 1 or Type 2 Report	<u>Type 1 Report:</u> [DD - Description & Design of Control]	• A description, prepared by mgt of the SO, → of the SO system, control objectives and related controls that have been designed and implemented as at a specified date; and • A report by the service auditor with the objective of conveying reasonable assurance that includes the service auditor's opinion on the description of the SO system, control objectives and related controls and the suitability of the design of the controls to achieve the specified control objectives.
	<u>Type 2 Report</u> [DDO- Description, Design & Operating effectiveness of Control]	• A description, prepared by mgt of the SO, of the SO system, control objectives and related controls, their design and implementation as at a specified date or throughout a specified period and, in some cases, their operating effectiveness throughout a specified period; and • A report by the service auditor with the objective of conveying reasonable assurance that includes: ✓ The service auditor's opinion on the description of SO system, control objectives & related controls, suitability of the design of controls to achieve the specified control objectives, and operating effectiveness of controls; &



	✓ A description of <u>service auditor's tests of controls & results thereof.</u> Q35. How does an auditor report on the <u>description, design and operating effectiveness</u> of controls at a S.O? =: <u>Explain about "Type 2 Report" (as it's asking about DD"O")</u>
Using Type 1 & Type 2 Report:	When user auditor is using type 1 or 2 report to understand I.C. and SO: In determining the SAAE provided by Type 1 or 2 report, user auditor shall satisfied as to: - The <u>service auditor's professional competence</u> (except where service auditor is a member of ICAI) and <u>independence</u> from the service organisation; and <u>Adequacy of the standards</u> under which the Type 1 or Type 2 report was issued. If user auditor plans to use Type 1 or 2 report as audit evidence to support user auditor's understanding about design & implementation of controls at SO, the user auditor shall: - Evaluate whether the Description and Design of controls [DD] at the <u>SO</u> is at a <u>date</u> or for a period that is <u>appropriate for the user auditor's purposes</u>; - Evaluate <u>Sufficiency & appropriateness</u> provided by the report for the understanding of the <u>user entity's I.C</u> relevant to the audit; (i.e, in general User entity ke kya control hai uss work pe) - Determine <u>whether complementary user entity controls</u> identified by SO are relevant to the user entity and, if so, obtain an understanding of <u>whether the user entity has designed and implemented such controls</u>. (i.e, SO ye soch ke kaam kar rha hai ki, U.E ne kuch specific control to lagaae hi honge uss kaam k liye, to as an Auditor apan ko y dkhna h ki Wo Control UE me shii hai yaa nii) [<u>Complementary user entity controls</u> refer to <u>controls that the service organisation assumes</u>, in the design of its service, <u>will be implemented by user entities</u>, and which, if necessary to achieve control objectives, are identified in the description of its system.]
Test of Control:	<u>When User auditor's initial risk assessment includes an expectation that controls at SO are operating effectively</u>, the user auditor shall <u>obtain audit evidence about the operating effectiveness</u> of those controls <u>from one or more of the following procedures</u>: - - Obtaining a <u>Type 2 report</u>, if available - Performing appropriate <u>TOC at the S.O</u> <u>Using another auditor to perform TOC at the SO</u> on behalf of the user auditor Q36. U.E. Auditor demanded from S.O. → <u>description</u> of SO & <u>effectiveness</u> of the control. Which type of report? What aspects to be considered by U.E. Auditor in using such assurance report as audit evidence that controls at S.O are operating effectively? (MAY'24) Answer: SA 402: Using <u>Type 2</u> report as A.evidence that controls at SO are operating effectively Using a Type 2 report as audit evidence that controls at SO are operating effectively, user auditor shall determine whether the service auditor's report provides SAAE about the effectiveness of the controls to support the user auditor's risk assessment by: - Evaluating whether the Description, Design & Operating effectiveness [DDO] of controls at the <u>S.O</u> is at a <u>date</u> or for period <u>that is appropriate for the user auditor's purposes</u> - Determine <u>whether complementary user entity controls</u> identified by SO are relevant to the user entity &, if so, obtain an understanding of <u>whether the user entity has designed and implemented such controls</u>., if so, testing their operating effectiveness; - Evaluating the <u>adequacy of the time period covered by the TOC</u> and the time elapsed since the performance of the tests of controls; and - Evaluating whether the <u>TOC performed by the service auditor and the results</u> thereof, as described in the service auditor's report, are relevant to the assertions in the user entity's FS and <u>provide SAAE to support the user auditor's risk assessment</u>

➤ Sub-Service Organisation (Inclusive & Carve Out Method)

Q37. When S.O. uses Sub-S.O. → what 2 alternative method of presenting controls description. As a user auditor what information would you obtain about controls at a sub-service organization? (Old)

SA 402 → a U.E may use S.O → S.O uses Sub-S.O., that service affect part of U.E info system relevant to FR.

- A user auditor may need to consider controls at the sub-service organisation:
 - ✓ **interaction between** the **user entity, the SO and Sub-SO**
 - ✓ The **degree of this interaction**, as well as the **nature and materiality of the transactions** processed by S.O & Sub-S.O → determining the significance of the **S.O & sub-S.O controls to the user entity's controls.**
- User auditor shall determine whether a sufficient understanding of the **nature & significance of services provided** by the S.O & their effect on the U.E. internal control relevant to the audit.
- If the user auditor is unable to obtain a sufficient understanding from the UE, the user auditor shall obtain that understanding by application of the following 2 methods of presenting description of I.C i.e.
 - (i) Type 1 report; or (ii) Type 2 report.
- If a S.O uses a Sub- S.O, the **service auditor's report** may **either include or exclude** the **subservice organisation's relevant control** objectives and related controls in the S.O description of its system and in the scope of the service auditor's engagement. → These two methods of reporting are known as the **inclusive method** and the **carve-out method** respectively.
- But Either method, S.O includes → **description of functions & nature of processing performed by the Sub-S.O**
- If Report (Type-1 / Type-2) Excludes Control of Sub-S.O → & if Sub-SO are relevant to User Entity FS → **User Auditor is required to apply requirement of SA 402 i.r.t. Sub-SO also**
- How much Work to be Performed by User Auditor Reg. Sub-SO ? → Nature & extent of work (to be performed BY the "User Auditor" regarding the Sub-SO), **depend on** → **nature & significance of those services to the U.E and relevance of those services to the audit.**

(Above Answer Ends)

Fraud / non-comply L&R at SO:

User auditor shall inquire user entity mngt → whether he is aware of **any fraud / non-compliance of L&R or uncorrected misstatement** affecting FS of user entity → **if Yes** → **evaluate how such matters affect the NTE of the user auditor's FAP**, including the effect on the user auditor's **conclusions** and user auditor's report.

➤ Reporting by User Auditor (Reference in User Auditor's Report)

- **If user auditor is unable to obtain SAAE** regarding the services provided by the service organisation relevant to the audit of the user entity's financial statements → **MODIFY** the Opinion
- **Unmodified Opinion:** The **user auditor shall NOT refer to the work of a service auditor** in the user 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 user auditor's report shall indicate that the reference **does not diminish the user auditor's responsibility for the audit opinion.**
- **Modified Opinion:** If reference to the work of a service auditor is **relevant to an understanding of a modification to the user auditor's opinion**, the user auditor's report shall indicate that such reference **does not diminish the user auditor's responsibility for that opinion.**

Q38. CA Raman → issued Unmodified A.report → his assistant made reference of work done by Service Auditor.

Hint: Refer & Explain Above Notes → "Reporting by User Auditor" → so CA Raman should remove the reference

ADDITIONAL SA's

(ICAI has NOT given them in MODULE, But Mentioned that these are discussed in CA Inter, So



CHAPTER 2: SA 200, 210, 230

SA 200 - OVERALL OBJECTIVES OF AN INDEPENDENT AUDITOR AND CONDUCT OF AN AUDIT IN ACCORDANCE WITH STANDARDS ON AUDITING

Objective	To obtain reasonable assurance about whether FS as a whole are free from MMS , whether due to fraud or error , thereby enabling Auditor to express an opinion on whether FS are prepared, in all material respects, in accordance with applicable FRF . And to report on FS & Communicate as per SA's.
SOME IMPORTANT REQUIREMENTS OF SA 200 :	
Professional Skepticism: (Bank statement vs Bank Confirmation.. bank statement alone is not sufficient)	An attitude that involves questioning mind being alert to the conditions which may indicate possible misstatement due to error or fraud and requires critical assessment of audit evidence . Professional skepticism includes being alert to the following situations: 1. Contradictory audit evidence 2. Reliability of documents 3. Conditions that may indicate possible fraud 4. Circumstances suggest need for audit procedure in addition to those required by the SA's Profession skepticism reduces risk of: (OOI) 1. Overlooking unusual circumstances 2. Over generalizing conclusions from audit observations 3. Using Inappropriate audit assumptions in determining NTE of audit procedures
Ethical Requirement :	1. Confidentiality 2. Integrity 3. Objectivity 4. Professional behavior 5. Professional competence and due care
Professional Judgement: (A.P. → SAAE → Conclusion)	Application of relevant knowledge, training and experience within the context of auditing, accounting and ethical standards to make an informed decision. It requires to decide about: (1) Materiality & Audit risk (2) Audit Procedures NTE, (3) Evaluating SAAE (4) Evaluating mngt judgement in applying FRF (5) Drawing conclusion
SAAE	To obtain reasonable assurance, the auditor shall obtain SAAE to reduce audit risk to acceptably low level (SAAE = Sufficient & appropriate audit evidence) 1. Sufficiency = Quantum of Evidence 2. Appropriateness = Quality of Evidence
Inherent limitation of Audit: [1,2, & FLIRT - G]	1. Nature of Financial reporting: - Preparation of Financial Statements involves Judgment by management, this gives rise to Inherent Risk which cannot be eliminated. 2. Nature of Audit Procedure - Audit procedure give reasonable assurance only rather than absolute assurance (i.e involve SAMPLING rather than 100% testing, etc.) - Audit is not an official Investigation so no power of search & seizure. 3. Frauds , particularly involving senior management (or Collusion) 4. Non-Compliance with Laws & Regulations 5. Non-disclosure of Related Parties

	6. Timeliness of Info (Relevance of info, Value diminishes over time), 7. Audit to be conducted within a reasonable period of time and at a reasonable cost . 8. Future events or conditions that may cause an entity to cease to continue as a going concern 9. Information not provided by management	
Audit Risk: (Refer Chp 3)	Risk that auditor may give inappropriate opinion on FS which are materially misstated - Audit risk = Risk of material misstatement (ROMM) X Detection Risk (DR) - ROMM = Inherent risk (IR) X Control risk (CR)	
Independence	- It comprises both independence of mind & appearance - Engagement team to be independent	
Compliance with SA's Relevant requirements	The auditor shall comply with each requirement of an SA unless : • Entire SA is not relevant; [eg, SA 299 Not applicable in case of single auditor], or • Requirement is not relevant because it is conditional and condition not exist. In exceptional circumstances , where the auditor decides to depart from a relevant requirement then the auditor needs to perform alternative procedures to achieve aim of that requirement	
Mind Booster Points	Follow all SA's →	Auditor shall follow all the SA's relevant for audit, however if Entire SA is not relevant. Follow only relevant portions of the SA
	If Objective of SA not achieved →	Modify the auditor's opinion or withdraw
	Responsibility of TCWG & Mngt →	• To Select FRF, • Prepare FS as per applicable FRF • Maintain IC relevant for preparation of FS
	Reasonable assurance →	Due to inherent limitation audit, Auditor expresses Reasonable assurance (Not Absolute)
	Not Future guarantee →	The Auditor's Opinion Does Not Assure , The Future Viability of the entity Nor the Efficiency Or Effectiveness
	A.Evidence →	Due to inherent limitation → Audit evidence are persuasive rather than conclusive (But he can't take Less than Persuasive evidence)

Q39. Analyse ROMM & Overall audit risk → Chances that 40% Bills deflected, IC can prevent it at 75%, Audit gives satisfaction of detection of Fraud & error to 60%

Hint: SA 200 → Define "Audit Risk", it's 2 Components & there definition (A. Risk = ROMM x Detection risk) → (ROMM = Inherent Risk x Control risk) So,

Inherent R. = 40%, Control R. = 25% (100-75), ROMM = 40% * 25% = 10%, Detection R. = 40% (100-60), A.Risk = 4%

Q40. SA's also applied to NPO's → as Audit is independent examination of FS/info. of any entity; **whether profit-oriented or not** and irrespective of its size, or legal form (unless specified otherwise) when such an examination is conducted with a view to expressing an opinion thereon.

Q41. Whether an auditor due to Inherent Limitation of Audit → Not Able to Get Persuasive Evidence ? Further, Discuss Certain Matters/Assertion where it's difficult to detect MMS due to Inherent Limitation. (OLD)

Hint: SA 200 & SQC 1 → Because of I.Limitation → unavoidable risk that MMS may not be detected.

Subsequent discovery of MMS due fraud/error does not by itself indicate a failure to conduct audit as per SAs.

However, I.Limitation of audit is Not a justification for auditor to get less-than-persuasive audit evidence.

So Auditor is INCORRECT . → Now refer Notes "Inherent Limitation of Audit" (Point 3,4,5,8) → Fraud, RP, L&R, G.C

Q42. Meaning of Reasonable Assurance ? Can get Absolute Assurance ? . (OLD - May'21)

Hint: SA 200: **Reasonable assurance** is **high level of assurance** & is **less than absolute assurance**. → Obtained when auditor obtained SAAE to reduce risk to acceptable risk. **Can't reduce risk to zero so, can't do absolute assurance.**

This is due to I.Limitation of Audit → (a) Nature of F.Reporting (b) Nature of A.procedure (c) Time & Cost



SA 210 - AGREEING TO TERMS OF AUDIT ENGAGEMENT

Basis/ Objective:	<u>While accepting or continuing audit engagement, two conditions must be satisfy:</u> • Common understanding between Auditor & management/TCWG • Preconditions must be satisfied
Do not accept Audit if:	• Pre-conditions are not present • Prior to acceptance management imposes limitations (Do not accept audit, unless require by law, Or Issue disclaimer)
Pre- Condition for Audit:	Defined as the use by management of an acceptable FRF in the preparation of the FS and the agreement of mngt and, where appropriate, TCWG to the premise on which an audit is conducted. In order to establish whether the preconditions for an audit are present, the auditor shall: b) Determine whether the FRF to be applied in the preparation of FS is acceptable; & (Refer <i>Additional PDF for Acceptability of FRF</i>) c) Obtain the <u>agreement of mngt that it acknowledges and understands its responsibility:</u> i) For the preparation of FS as per applicable FRF, including where relevant their fair presentation ii) For such internal control as mngt determines is necessary to enable the preparation of FS that are free from MMS, whether due to fraud or error; and iii) <u>To provide the auditor with:</u> • Access to all information of which mngt is aware that is relevant to the preparation of the FS such as records, documentation and other matters; • Additional information that the auditor may request from mngt for the purpose of audit • Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

Q43. Company mentioned in **Audit terms** that they will not provide **Internal Audit report** to Stat. Auditor (& some other Limitation) → What **Precondition Auditor** to see before **Accepting/Refusing**. (Old)

Hint → Refer Above "**Pre-Conditions for Audit**", If auditor believe **Limitation** will result Auditor in **Disclaiming** an Opinion → **Don't Accept such engmnt** (unless L&R require) → So in given case, Do Not Accept.

➤ Content of Engagement Letter

Mngt/Tcw:	Auditor shall agree the terms of the audit engagement with mngt or TCWG , → as appropriate .
Content of Engt Letter Include: <i>[Mera kaam, aapka kaam, meri respons., aapki respons.]</i>	The agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include: Identification of the applicable FRF for the preparation of the FS; and - The objective and scope of the audit of the financial statements; - The responsibilities of the auditor; - The responsibilities of management; Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content
If L&R prescribe terms:	If L&R prescribes in sufficient detail the terms of the audit engagement, the auditor need not record them in a written agreement , except for the fact that such law or regulation applies and that management acknowledges and understands its responsibilities.

Q44. In Qn, few matters of Engmnt Letter were Mentioned, and matter of "mngt responsibility" was missing → Find discrepancy in Audit engagement letter:: → Refer Above notes: "Content of Engt Letter Include"



➤ Recurring Audit

Q45. Elucidate Circumstances that may warrant the Revision in Terms of Emnt ? or New Emnt letter to be Sent

Trick: mera padosi bahar jaara tha tab uski gaadi muje deke chale gya > mene galti se "L&R" toda gaadi chalte wqt, gaadi ki "Ownership" bhi mre pass nhi thi, me to bas uss gaadi ko mere padosi k liye "manage" kar rha tha > par Police ko to "misunderstanding" ho gyi unko laga mera "Nature" hi chori karna h > fir unhone mujse "Special" tarike se "Finance" Maanga

SA 210 → Auditor may decide not to send a new audit Emnt letter each period. However, following factors may make it appropriate to revise the terms of the audit engagement or to remind the entity of existing terms:

- 1) Change in **legal or regulatory** requirements.
- 2) Significant change in **ownership**.
- 3) Recent change of senior **management**.
- 4) Any indication that the entity **misunderstands** the objective and scope of the audit.
- 5) Significant change in **nature or size** of the entity's business.
- 6) Any **revised or special** terms of the audit engagement.
- 7) Change in the **financial reporting framework** adopted in the preparation of the financial statements
- 8) Change in **other** reporting requirements. (Eg. CARO)

➤ Limitation on scope / Change in Terms:

Reason for change request:	<u>Trick: R .. u ..MC</u> 1) a Change in circumstances affecting the need for service, 2) a misUnderstanding as to the nature of an audit or related service originally requested. 3) a Restriction on the scope of the engmnt, whether imposed by Mngt or circumstances														
Changes in term of Audit Engagement: (Eg., Audit to Review proposed by Client)	Q46. Before engmnt completion, mngt requested to change Terms lead to lower level of assurance Before completion of the engagement → mngt request to change the engagement to one which provides a lower level of assurance → auditor should consider the appropriateness of doing so. <table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 20%;">Reason & Implication:</td><td> - Auditor would consider carefully the reason & Justification given for request implications of a restriction on the scope Example: ✓ Reasonable change → Change in circumstances that affects the entity's requirements, misunderstanding nature of service ✓ Unreasonable change → change not reasonable if it relates to info that is incorrect, incomplete (i.e., Unable to obtain SAAE) </td></tr> <tr> <td colspan="2" style="text-align: center;">If Reasonable Justification of Doing so:</td></tr> <tr> <td>Not include old Engmnt terms:</td><td> If the auditor concludes that there is reasonable justification to change the engagement → Audit work will comply to SA's → report issued would be appropriate in revised terms. So, to avoid Confusion → report would NOT include: a) the original engagement; or b) any procedures that may have been performed in original engagement </td></tr> <tr> <td>If terms changed:</td><td> - Auditor and mngt shall agree on and record the new terms in engagement letter or other suitable form of written agreement </td></tr> <tr> <td colspan="2" style="text-align: center;">If No Reasonable Justification of Doing so:</td></tr> <tr> <td>Don't agree</td><td>Should Not agree to a change of engt when no reasonable justification.</td></tr> <tr> <td>If mngt not</td><td>If the auditor is unable to agree to a change and is not permitted by management</td></tr> </table>	Reason & Implication:	- Auditor would consider carefully the reason & Justification given for request implications of a restriction on the scope Example: ✓ Reasonable change → Change in circumstances that affects the entity's requirements, misunderstanding nature of service ✓ Unreasonable change → change not reasonable if it relates to info that is incorrect, incomplete (i.e., Unable to obtain SAAE)	If Reasonable Justification of Doing so:		Not include old Engmnt terms:	If the auditor concludes that there is reasonable justification to change the engagement → Audit work will comply to SA's → report issued would be appropriate in revised terms. So, to avoid Confusion → report would NOT include: a) the original engagement; or b) any procedures that may have been performed in original engagement	If terms changed:	Auditor and mngt shall agree on and record the new terms in engagement letter or other suitable form of written agreement	If No Reasonable Justification of Doing so:		Don't agree	Should Not agree to a change of engt when no reasonable justification.	If mngt not	If the auditor is unable to agree to a change and is not permitted by management
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	permit to continue audit: to continue the original audit engagement, the auditor shall: Withdraw from audit engt, where possible under applicable L&R; and Determine whether there is any obligation, contractual or otherwise, to report the circumstances to other parties, such as TCWG, owner or regulator.
Limitation of Scope:	<u>If scope restricted:</u> <u>Before accepting Engagement</u> → Not to accept <u>After accepting engagement</u> → - Request MGT not to restrict <u>If management refuses to remove such restriction:</u> ✓ Withdraw from engagement if allowed under law (or) Express disclaimed opinion
FRF Prescribed by L&R is Unacceptable	If L&R prescribed FRF is unacceptable, Not accept audit, Unless: - Mngt Agrees to provide additional disclosures to avoid misleading - Write in Terms of engagement that - report will include EOM para to draw user attention to additional disclosure - Unless require by L&R do not use "True & Fair view, fair in all material aspect"
Auditor report format by L&R	Applicable L&R prescribed wording & layout of Audit report, which is different from SA's, Provide Additional explanation to mitigate users understanding, if additional explanation is not enough, Not accept audit unless require by L&R (AR can-not state that audit is conducted in acc. To SA's if SA not complied)

SA 230 - AUDIT DOCUMENTATION

Define:	Audit Documentation refers to the record of: - audit procedures performed, - relevant audit evidence obtained, and conclusions the auditor reached. <u>Point to Note:</u> The standard does not limit the specific documentation i.e., if other SAs prescribe more documentation requirements, those documentations are also to be maintained.
Nature of AD:	Audit Documentation provides: evidence of auditor's basis for a conclusion about achievement of objectives of auditor, - evidence that audit was planned and performed in accordance with SAs & applicable L&R
Purpose/ Importance of A.D:	<u>Help Engt Team:</u> - Assisting the engagement team to plan and perform the audit. - Assisting members of the engt team to direct and supervise the audit work <u>Accountability:</u> - Enabling the engagement team to be accountable for its work. - Retaining a record of matters of continuing significance to future audits. <u>External & Internal Inspection:</u> - Enabling conduct of quality control reviews and inspections in accordance with SQC 1. - Enabling conduct of external inspections as per applicable legal, regulatory or other req.
Factors affecting Form, Content & Extent of AD:	Q47. What factors would influence the amount of working papers required for Audit [Old] SA 230 → "Audit Documentation" means record of A.procedures performed, A.evidence obtained & conclusions reached, the amount of audit working papers depend on factors such as- - The nature of the audit procedures to be performed. - The significance of the audit evidence obtained



	c) The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained. [Trick: Jis "Entity" ki Audit kar rahe h > Usme kitni "Risk" hai > uss hisaab se "Audit method" lgao] d) The size and complexity of the entity. e) The identified risks of material misstatement. f) The nature and extent of exceptions identified. g) The audit methodology and tools used. h) Timely preparation of audit documentations
Ownership of A.D	- Working papers are property of auditor - He can make available copy of working paper to client on request at this discretion
In case of any modification of AD	In exception circumstances, He can modify existing AD or add new AD, but he should: Explain reason for modification, When and by whom they were made or reviewed
Matters After due date of Auditor's report	If under Exceptional circumstances, Auditor performs Additional Audit Procedures / Draws new conclusions, Auditor shall document - The Circumstances encountered. - New or Additional Audit Procedures performed, Audit Evidence obtained & conclusions reached. When & by whom resulting changes to Audit documentation were made & reviewed.
Matters definitely documented:	What are the matters that should be definitely documented: Significant risks identified - Significant uncertainties noticed - Findings resulting to modifications - Limitation and difficulties in auditing Professional judgment w.r.t subjective areas like estimates, uncertainties associated with client
Audit File:	Physical or electronical → 1 or more folder → Audit documentation for a specific engagement .
Administrative process:	Assembling of audit file is just an administrative process → does <u>not involve the performance of new audit procedures</u> or the drawing of new conclusions
Timely Prepare:	The auditor shall prepare audit documentation on a timely basis

Q48. Discuss Auditor's responsibility to **provide access of audit working papers** to Regulators & 3rd parties. [Old]

Hint: Auditor should not provide access of working papers to any 3rd party **without authority** or **unless L&R duty**:

- Clause 1 (P-1, S-II of CA Act 1949)** → CAip shall be guilty if he discloses info. without client consent.
- SA 200** → Auditor should **respect confidentiality** & not disclose info to 3rd party without authority or L&R duty.
- SQC 1** → audit documentation is the **property of auditor**. He may at his discretion, make portions of, or extracts from, documentation available to clients, provided such disclosure not undermine the validity of work
- SQC 230** → A.docs **serves number of additional purposes**, including external inspections as per applicable L&R

Q49. Every matter can't be Documented, make **professional Judgement**, auditor should **not document separately** with matters, for which **compliance is demonstrated by documents included within the audit file** [Old]

Hint: SA 230 → **neither necessary nor practicable** for the auditor to **document every matter**.

[Trick: Eng Letter > Audit Plan > Perform audit by **Professional skep & Direction/supervision** > Then issue **Qualified Opinion**]

For example,

- signed Engmt letter** in audit file **demonstrates** that → the **auditor has agreed the terms** of audit with mngr
- existence of an adequately documented audit plan** **demonstrates** that the **auditor has planned the audit**.

- (iii) Report containing **qualified opinion** demonstrates → auditor complied SA's requirement to express qualified.
- (iv) i.r.t requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file:
- Eg., No single way in which auditor's **professional skepticism** is documented. But A.Docs may provide evidence of that. Like it include specific procedures performed to corroborate mngt's responses to auditor's inquiries.
 - Eg, Engt partner has taken responsibility for **direction, supervision & performance of audit** may include Docs of partner's timely involvement in audit, Like Participating in SA 315 team discussion, "Identifying & Assessing ROMM"

CHAPTER 3- Audit planning, Strategy, and execution

SA 300, 450, 520, 540, 600, 610, 620

SA 300 – Planning an Audit of Financial Statements

Objective

Strategy

Plan

Program

Execution

➤ Audit Strategy

Means:	An audit strategy sets Direction, Timing, & Scope of audit → used as guideline when developing plan
	Author's Note: Strategy means What is his Aim & Decision ?

Q1. Enumerate factors to be considered while establishing an overall audit strategy and its benefits [OLD]

Factors: (Trick: CEO-RP)	<u>Factors while establishing Overall Audit Strategy:</u> 1. <u>Characteristics of Audit / Scope</u> : Identify the characteristics of the engagement i.e. <u>Scope</u> 2. <u>Team's Efforts</u>: Consider factors that are significant in directing engagement team effort. 3. <u>Reporting Objectives</u>: Ascertain the reporting objectives of the engagement to plan audit 4. <u>NTE of Resources</u>: Ascertain the NTE of resources necessary to perform the engagement. 5. <u>Preliminary Work</u>: Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed
Benefits: Resources ko: Employ, allocate, timing & manage	1. <u>Employment of Qualitative Resources</u>: The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas / experts 2. <u>Allocation of Quantity of Resources</u>: 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, or the audit budget in hours to allocate to high risk areas. 3. <u>Time of Deployment of Resources</u>: When to deployed [interim audit stage or key cutoff date] 4. <u>Management of Resources</u>: How such resources are managed, directed & supervised, how engagement partner and manager reviews are expected to take place

Q2. new venture of online shopping. What factors would be considered in formulating audit strategy of company?

General Factors	<u>Refer above answer "Factors" Topic</u>
Specific Factors for Online Shopping Trick: Transaction, Then Pass JV, report to FS	The auditor shall also obtain an understanding of the information system including the related business processes due to new venture of online shopping in the following areas: (i) The <u>classes of transactions</u> in the entity's operations <u>that are significant to the FS</u>; (ii) How the <u>Info system captures events & conditions</u>, other than transactions, that are <u>significant to the F.S.</u> (iii) <u>Controls surrounding journal entries</u>, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments. (iv) The procedures, within <u>both information technology (IT) and manual systems</u>, by which those <u>transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements</u> (v) The related <u>accounting records</u>, supporting information and specific accounts in the financial statements that are <u>used to initiate, record, process and report transactions</u>; this includes the correction of incorrect information and how information is transferred to the general ledger. The records may be in either manual or electronic form;

➤ Audit Plan



Means:	It's a road map to conduct an audit. Much more detailed than audit strategy. The audit planning is necessary to conduct an effective audit, in an efficient & timely manner.								
Planning is Continuous Process: (SA-300) (MALE-O..) (Special Trick;-)	Q3. "Planning is not a discrete phase of an audit but rather a continual & iterative process." [OLD] Planning is not a discrete phase of an audit but rather a continual and iterative process. It often begins shortly after the completion of previous audit & continues until the completion of current A.Engmnt. Planning includes consideration of the timing of certain activities and audit procedures. For example, <u>planning includes the need to consider such matters as:</u> ✓ The determination of materiality ✓ 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 involvement of experts. ✓ The performance of other risk assessment procedures.								
Responsibility of Auditor:	Auditor can discuss planning with mngt, however, Overall Audit Strategy & Audit Plan - Responsibility of the Auditor, to not compromise audit effectiveness.								
Contents of an Audit Plan: (SA-300)	Q4. Write a short note on Contents of an audit plan [OLD] The auditor shall develop an audit plan that shall include a description of: <table border="1"> <tr> <td>RAP</td><td>(i) The NTE of planned RAP, as determined under SA 315 "Identifying & Assessing the ROMM through Understanding the Entity and Its Environment".</td></tr> <tr> <td>FAP</td><td>(ii) The NTE of planned FAP at assertion level, as determined under SA 330 "The Auditor's Responses to Assessed Risks".</td></tr> <tr> <td>OAP</td><td>(iii) Other planned audit procedures that are required to be carried out so that the engagement complies with SAs</td></tr> </table> Audit plan is more detailed than the overall audit strategy (includes NTE of audit procedures)	RAP	(i) The NTE of planned RAP , as determined under SA 315 "Identifying & Assessing the ROMM through Understanding the Entity and Its Environment".	FAP	(ii) The NTE of planned FAP at assertion level, as determined under SA 330 "The Auditor's Responses to Assessed Risks".	OAP	(iii) Other planned audit procedures that are required to be carried out so that the engagement complies with SAs		
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OAP	(iii) Other planned audit procedures that are required to be carried out so that the engagement complies with SAs								
Relationship Between Audit Plan & Strategy: (SA-300)	Q5. Discuss the relationship between overall audit strategy and audit plan. [OLD] <table border="1"> <tr> <td>Strategy</td><td>(i) The audit strategy is prepared before the audit plan.</td></tr> <tr> <td>Plan</td><td>(ii) Strategy provides the guidelines for developing the plan. It establishes the scope & conduct of A. procedures & works as basis for developing detailed plan</td></tr> <tr> <td>Plan is detailed</td><td>(iii) The audit plan contains more details than the overall audit strategy (iv) Detailed audit plan would include the NTE of A.procedures to obtain SAAE.</td></tr> <tr> <td>Inter-Related</td><td>(v) Audit strategy & plan are inter-related, because change in one would result into change in the other.</td></tr> </table>	Strategy	(i) The audit strategy is prepared before the audit plan .	Plan	(ii) Strategy provides the guidelines for developing the plan . It establishes the scope & conduct of A. procedures & works as basis for developing detailed plan	Plan is detailed	(iii) The audit plan contains more details than the overall audit strategy (iv) Detailed audit plan would include the NTE of A.procedures to obtain SAAE.	Inter-Related	(v) Audit strategy & plan are inter-related , because change in one would result into change in the other.
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Inter-Related	(v) Audit strategy & plan are inter-related , because change in one would result into change in the other.								
Benefits: (SA-300) Trick: "Engagement team" ko "Important" torr pe & "manage" karta h	Q6. you are required to analyse & explain the benefits of Planning in an Audit of FS [OLD] SA 200 → to achieve the overall objectives of auditor, audit planning is necessary to conduct an effective audit in an efficient and timely manner. Benefits/Advantages of Planning in an Audit of Financial Statements <table border="1"> <tr> <td>Select, Coordinate, Direct & Supervise</td><td>1. Proper Selection of Engagement Team 2. Easy Coordination in work done by auditors of components and experts 3. Direction and Supervision of Engagement Team</td></tr> <tr> <td>Important Area</td><td>4. Attention to Important areas 5. Timely resolution of Potential Problems</td></tr> <tr> <td>Manage Audit</td><td>6. Proper Organisation and Management of Audit Engagement</td></tr> </table>	Select, Coordinate, Direct & Supervise	1. Proper Selection of Engagement Team 2. Easy Coordination in work done by auditors of components and experts 3. Direction and Supervision of Engagement Team	Important Area	4. Attention to Important areas 5. Timely resolution of Potential Problems	Manage Audit	6. Proper Organisation and Management of Audit Engagement		
Select, Coordinate, Direct & Supervise	1. Proper Selection of Engagement Team 2. Easy Coordination in work done by auditors of components and experts 3. Direction and Supervision of Engagement Team								
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Manage Audit	6. Proper Organisation and Management of Audit Engagement								
Change in Audit Plan & Strategy: [Factors on which NTE of	Q7. During audit, certain events took place, when would an audit plan require a change. [OLD] SA 200 → Without a careful plan, the overall objective of an audit may not be achieved. Changes to Audit Planning: Auditor should update & change the overall audit strategy & audit plan as necessary during audit. The auditor may need to modify them due to factors Like: • Result of unexpected events								

Q10. Explain planning activities → it includes

- (1) Establishing Overall A.Strategy (Explain Factors for establishing Audit strategy)
- (2) Development of A.plan (Explain Factors for development of audit plan)

Q11. Auditor not visited company even once & failed to understand nature of business. → also included in his working papers checklists of test checking of cost of raw material. What it reflect upon planning audit? (SM)

Hint: SA 300→ Plan audit to perform effectively, & Establish Audit Strategy → Following are violation of SA 300:

(a) Document Strategy, Plan & Changes (b) Not visited company, failed to understand business, & nature of business to identify & assess ROMM (c) Working paper not show business understanding, Failed to document Strategy, plan, chng
There was only checklist in Docs, to support test check of Cost of Raw Material (it's just a general Checklist) → Audit was not planned in Effective manner as per SA 300

Q12. Sample Size needs to be decided in Planning stage (Not at PERFORMING stage) → as Plan include NTE (Extent) of Audit procedure → Extent include Sample Size

Q13. CA Nikita, During Audit, She Embarked Extensive Procedure to verify Foreign Contribution (extensive then what she planned earlier), So She Need to Document Relevant Findings, as well as How she planned Whole exercise
⇒ As SA 300 requires to document Plan & Significant Changes with Reason. (i.e., record NTE of RAP & FAP)
⇒ Further Document the Changes in Plan (with Reason), of doing extensive testing on foreign contribution. (Failure to Document plan, is risk of not conducting audit as per SA's in Qualitative manner)

➤ Audit Programme:

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

Matter to Consider While Formulating Audit Programme: (Less Imp)	1. <u>Nature of business in which the organization is engaged:</u> Visit the client's office, Observe different stages , How record is kept & titles of books in which it is kept, Also consider technical, financial & accounting set-up of company. 2. <u>Overall plan:</u> If there is any <u>change</u> in overall plan, modify audit program accordingly. <u>Adherence to framework</u> - Frame provided by overall plan should be <u>strictly adhered to</u>. 3. Study System of <u>internal control</u> and accounting procedures: 4. <u>Size of the organization and structure</u> of its management 5. <u>Information as regards organization of the business:</u> Auditor should obtain information from his client regarding (i) Client's history & business, (ii) Purpose & nature of engagement & (iii) Time schedule for the completion of audit. 6. <u>Accounting & Mngt policies:</u> Review FS of past years, audited by his predecessors to know info. regarding accounting & management policies which have been followed consistently.
Review & Modification of Audit Program: (Special Trick :-)	Q14. few circumstances where the audit programme to be suitably altered by auditor. [OLD] At each subsequent Engmnt, review the programme and, if necessary, modify it on account of: a) <u>experience</u> gained during the previous audits; b) important <u>changes</u> taken place in business specially in the <u>system of IC</u>, A/cing procedures or in the structure of management or of the scope of business; and c) <u>evaluation of IC</u> made for the current year. <u>Circumstances where audit programme would have to be suitably altered</u> • Designed for <u>volume of turnover</u> & subsequently it has substantially increased. • Discovered that <u>internal control</u> procedures were not as effective as assumed. • Extraordinary <u>increase</u> in amount of <u>book debts or stocks</u> as compared to P.Y. • Suspicion is aroused that <u>assets</u> of company have been <u>misappropriated</u>



Q15. Draw **Audit Program** i.r.t **Revenue & Expenses** of → a **movie theatre complex**. → sale of tickets over **counter & online booking**, income from **cafe, shops, pubs** etc. → other income includes **advertisements** within/outside premises (banners). → **parking of vehicles** (SM)

Answer:

- (i) Peruse the **MOA** and **AOA** of the entity.
- (ii) Ensure the **object clause** permits the entity to engage in this type of business.

(POINTS RELATED TO: INCOME)

- (iii) In the case of income from sale of tickets:
 1. Verify **control system** as to how it ensured that the **collections on sale of tickets** are properly accounted.
 2. Verify the system of relating to **online booking** of various shows and the system of realization of money.
 3. Check that there is **overall system of reconciliation of collections** with No. of seats available on a day.
- (iv) Verify the **I.C. system** and its effectiveness relating to the **income from café, shops, pubs, game zone** etc.
- (v) Verify the system of control exercised relating to the **income receivable from advertisements** exhibited.
- (vi) Verify the system of collection from the **parking areas** in respect of the vehicles parked by the customers.

(POINTS RELATED TO: EXPENSES)

- (vii) In the case of **payment to the distributors** verify the system of payment which may be either through out right payment or percentage of collection or a combination of both. Ensure at the time of settlement any payment of advance made to the distributor is also adjusted against the amount due
- (viii) Verify system of **payment of salaries & benefits to employees** & ensure statutory requirements are complied.
- (ix) Verify the payments effected in respect of **maintenance of building** and ensure the same is in order.
- (x) Verify the **insurance premium paid** and ensure it covers the entire assets

➤ **Audit Execution**

Q16. Key phases in audit execution are Execution Planning, Risk Control Evaluation, Testing and Reporting. Explain

Answer: (OLD COURSE RTP QN)

1. Execution Planning:	Prior to commencement of an audit engagement, → lay down the roadmap for audit execution. • Auditors need to plan their work to carry out audit in an effective, efficient and timely manner. A detailed audit program is prepared laying down the audit objectives, scope & audit approach. • consider manpower requirement, audit team qualifications, and the time element, etc.
2 Risk and Control Evaluation	For each segment of audit, <u>auditors should conduct a detailed risk and control assessment i.e.</u> • List the risks that must be reviewed in that segment, capture for each risk the controls that exist or needed against the risk and the work steps required to test effectiveness of controls. While making Risk & Control assessment it is necessary to borne in mind Materiality levels.
3 Testing	Once a comprehensive understanding is gained of the key risks & the controls to be evaluated in a given audit area , the auditors should test the operating effectiveness of the controls .
4 Reporting	SA 700 → establishes standards on form & content of auditor's report. The auditor should review & assess the conclusions drawn from audit evidence obtained as the basis for the expression of an opinion on FS. Consider whether FS comply with relevant statutory requirements (i.e., Company Law, AS of ICAI, latest Guidelines etc.)
5 Other Considerations	In addition to above, there are certain other consideration which auditor is required to take care while executing the audit such as using the work of other auditor, using the work of an auditor's expert etc.

SA 450 – Evaluation of Misstatements Identified during the Audits

Meaning of	Difference between



misstatement	Amounts, classification, presentation or disclosure of a reported FS item (<i>ACPD</i>) <u>and</u> amount, classification, presentation or disclosure (<i>ACPD</i>) that is required for the item to be in accordance of FRF.	
Objective:	The <i>effect of identified misstatements on the audit</i> & <i>effect of uncorrected misstatements</i> , if any, on the financial statements	
Accumulated Misstatement:	auditor shall accumulate misstatements identified during the audit, <i>other than those that are clearly trivial</i> . → (The auditor may designate an amount below which misstatements would be clearly trivial and would not need to be accumulated because the auditor expects that the accumulation of such amounts clearly would not have a material effect on the FS)	
Some Definitions	Factual misstatements	misstatements about which there is no doubt
	Judgmental misstatements	differences arising from the judgments of management concerning <i>A/cing estimates</i> Or, or selection or application of <i>A/cing policies</i> that the auditor considers unreasonable / inappropriate
	Projected misstatements	the auditor's <i>best estimate of misstatements in populations</i> , involving the <i>projection of misstatements identified in audit samples</i> → to the <i>entire populations</i> from which the samples were drawn.
Documentation <i>(MCQ Asked)</i>	Documentation regarding misstatements identified during audit: a) The <i>amount below which</i> misstatements would be regarded as <i>clearly trivial</i> ; b) All <i>misstatements accumulated</i> during the audit <i>and whether</i> they have been <i>corrected</i> ; c) The auditor's conclusion as to <i>whether uncorrected misstatements are material</i> , individually or in aggregate, and the basis for that conclusion	
Sources of Misstatement:	Q17. Identify the sources of misstatements, Other than Fraud. [Old] following are the sources of misstatements arising from other than fraud (i) <i>Inaccuracy</i> in <i>gathering or processing data</i> from which the FS are prepared; (ii) <i>Omission</i> of an <i>amount or disclosure</i> ; (iii) <i>Incorrect</i> <i>A/cing estimate</i> arising from overlooking, or clear misinterpretation of facts; (iv) <i>Judgments of mngt</i> concerning <i>a/cing estimates</i> that the auditor considers <i>unreasonable</i> or the selection and application of <i>a/cing policies</i> that the auditor considers <i>inappropriate</i>	
Consideration of Identified Misstatements as the Audit Progresses	Determine whether the overall <i>audit strategy and audit plan need revision if</i> : - Nature & circumstances of identified misstatements, <i>indicate that other misstatements may exist</i>, when aggregated misstatements could be <i>material</i>. <i>aggregate of misstatements</i> accumulated <i>approaches materiality</i> as per SA320 <i>Request mngt</i> to procedures to determine the amount of the actual misstatement and to make appropriate <i>adjustments to the FS</i> . <i>If Corrected by mngt</i> → perform <i>additional audit procedures</i> to determine whether misstatements remain.	
Communication & Correction of Misstatements	- Auditor shall <i>communicate on a timely basis</i> all misstatements accumulated during the audit with the appropriate level of mngt, unless prohibited by L&R. - The auditor shall <i>request management to correct</i> those misstatements. <i>If mngt refuses to correct</i> some or all of the misstatements communicated by the auditor, the auditor shall <i>obtain an understanding of management's reasons for not making the corrections</i> and shall take that understanding into account when <i>evaluating whether the FS as a whole are free from MMS</i>.	
Auditor's Procedures if	<u>Whether uncorrected misstatement are Material</u> individually or aggregate (<u>Current Misstatement + Uncorrected</u> of prior period)	

Misstatements identified	<u>Communicate to management /TCWG & request them to correct:</u> a. <u>If mngt corrects</u>: Perform Additional Procedures to determine whether misstatmnt remain. b. <u>If Management refuses</u>: - Reason for refusal? - Re-assess the materiality - If material, communicate uncorrected misstatement and their effect on his opinion to TCWG with a request that uncorrected misstatements be corrected. - If not corrected: Obtain a written representation from management/TCWG w.r.t their believing that effect of uncorrected misstatements is immaterial.

➤ Evaluate Effect of Uncorrected Misstatement:

Q18. Discuss impact of uncorrected misstatements & auditor's response to the same. Or, auditor has intimated the mngt those certain misstatements need to be corrected. Discuss impact of such, if mngt not correct.

Reassess Materiality:	Prior to evaluating the effect of uncorrected misstatements, the auditor shall reassess materiality determined in accordance with SA 320 to confirm whether it remains appropriate.
Whether Uncorrected mistatmnt is Material?	SA 450 → auditor shall <u>determine whether uncorrected misstatements are material, individually or in aggregate</u>. In making this determination, the auditor shall consider- (i) The <u>size and nature of the misstatements</u>, both in relation to particular C/A/DS and the FS <u>as a whole</u>, and the particular circumstances of their occurrence; and (ii) The <u>effect of uncorrected misstatements</u> related to <u>prior periods</u> on the relevant C/A/DS, and the financial statements as a whole.
Communicate to TWCG (Request to correct):	The auditor shall <u>communicate this with TCWG</u> uncorrected misstatements and the effect that they, individually or in aggregate, may have on the opinion in the auditor's report. The auditor's communication shall identify material uncorrected misstatements <u>individually</u>. The auditor shall <u>request that uncorrected misstatements be corrected</u>.
If mngt refuse:	If <u>mngt refuses to adjust financial info & extended audit procedures</u> do not enable the auditor to conclude that aggregate uncorrected misstatements is not material, → <u>report accordingly</u> .
Written Represen. If Immaterial	<u>As per mngt, if effect</u> of such uncorrected misstatement is <u>immaterial</u> then the auditor shall request for a <u>written representation</u> from mngt and, where appropriate, TCWG that whether they believe the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the FS as a whole. Summary of such items shall be included in W.R.

➤ Other Integrated Qns:

Q19. Test checked a sample of 5% of sales, found understatement of Rs. 24 lakhs. he gave a clean report [Old]
Hint: It's Violation of SA-315 → As He should consider Materiality (at both → FS level & Assertion level),
 SA 450 → consider whether effect of Aggregate Uncorrected Mistmt is Material → if Yes → Qualifies/Adverse

Q20. For assessing impact of uncorrected misstatement, Materiality was calculated based on 12 Month sales (12th Month sales was estimated), however later on, Actual 12th month sales was very Less than estimated). [SM]
Hint: SA 450 → required to reassess the materiality, as per SA 320, before evaluating uncorrected misstatements impact (adjust the materiality based on the now available actual financial results)
 SA 320 → audit progresses → materiality may be revised for FS Or specific C/A/DS. → (Explain given Case)
 the auditor, must review and re-assess the materiality → If the re-assessed materiality is lower than the previously calculated amount, → reconsider performance materiality & appropriateness of the NTE of FAP.

SA 520 – Analytical Procedures

Scope:	- Perform Substantive analytical procedure near end of audit when forming conclusion on FS - use of analytical procedures as risk assessment procedures is dealt with in SA 315 - SA 330 include guidance for NTE of A.procedure in response to assessed risk, include SAP.
Meaning:	- Evaluations of financial information - Through analysis of plausible relationships among both financial and non-financial data. - Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.
Considered Factors while performing SAP: Comparison & Relationship with (Nature of SAP):	Analytical procedures include the consideration of: - Comparisons of the entity's financial info. with as well as - Consideration of relationships: ➤ Examples of consideration of comparisons of the entity's financial information are: - Comparable information for prior periods. Anticipated result [budgets/ forecasts] Inc. Auditor's estimation [estimated depreciate] Similar industry information, such as a comparison of entity's ratio of sales to accounts receivable with industry averages or other entities of comparable size same industry. ➤ Examples of Analytical Procedures having consideration of relationships are: - Among elements of financial Info that expected to conform predictable pattern i.e., GP margin % (Sales & Profit) - Between financial info. & relevant non-financial info (payroll costs to no. of employees)

Substantive Analytical Procedure (Steps):

Q21. Considerations to be kept in mind while performing analytical procedures on data prepared by client? (OLD)

When auditor intends to perform analytical procedures on data prepared by the client, he should consider the following: *[Trick: mummy wo ladka mere liye "suitable" nahi hai, bilkul "reliable" nahi h, meri "expectation" se bilkul "different" h, me thoda orr "investigate" karungi]*

- (i) **Determine the suitability** of particular substantive analytical procedures for given assertions, taking account of the assessed ROMM and tests of details, if any, for these assertions;
- (ii) **Evaluate the reliability of data** from which the auditor's expectation of recorded amt or ratios is developed, taking account of source, comparability, & nature and relevance of Info available, & IC over preparation;
- (iii) **Develop an expectation of recorded amounts** or ratios & evaluate whether the expectation is sufficiently precise to identify a misstatement that, individually or when aggregated with other misstatements, may cause the FS to be materially misstated; and
- (iv) **Determine the amount of any difference of recorded amounts from expected values** that is acceptable without further investigation and if analytical procedures performed in accordance with this SA 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:
 - ✓ **Inquiring of Mngt** and obtaining appropriate audit evidence relevant to management's responses; &
 - ✓ **Performing other audit procedures** as necessary in the circumstances.

Suitability of SAP	Depend upon following factors: - SAPs more suitable to large volumes of transactions tending to be predictable over time. - But suitability of AP influenced by: Nature of assertion. & Auditor's assessment of APs effectiveness to identify MMS.



	[Eg, If control over sales process order is weak, then for Receivable assertion → TOD is more reliable rather than SAP] 3) In some cases, unsophisticated predictive models may be useful. [eg. Fixed Salary x No. of employees = Employee cost can be predicted by that, reducing need to perform TOD] 4) Different types of Analytical procedures provide different levels of assurance. [eg. To predict Total rental income = No. of apartment * rent per aptmnt * reduce vacancy rate → It will be reliable & provide more persuasive evidence But, Confirming sales amount by considering normal GP margin rate → Less persuasive evidence, but will help if collaborate with other procedures] 5) Particular SAP may be considered suitable when Tests of Details are performed on same assertion. [eg. For Account receivable assertion → Apply SAP by checking Customer ageing & Apply TOD by checking Subsequent amt received/sales invoice]
Criteria to check Reliability of Data: [SC-NC]	Q22. criteria to determine whether data is reliable for designing substantive analytical P.? Source of the information available. [Eg, Info. Is more reliable when obtained independent sources outside the entity] Comparability of the information available. [Eg, broad industry data may need to be comparable to that of an entity that produces and sells specialised products] Nature and relevance of the information available. [Eg, whether budgets have been established as results to be expected rather than as goals to be achieved] Controls over the preparation of the information that are designed to ensure its completeness, accuracy and validity. [Eg, controls over preparation & review of budgets] Auditor may consider testing the operating effectiveness of controls, if any, over the entity's preparation of information used by the auditor in performing SAP in response to assessed risks. When such controls are effective, the auditor generally has greater confidence in the reliability of the information and, therefore, in the results of analytical procedures.
Difference & Investigation:	If there is Difference in Expected Amt & Actual: If Difference in Acceptable: No Further Investigation require [It's determined by considering materiality, desired level of assurance, possibility that a misstatement may cause the FS to be materially misstated] Q23. analytical procedures showed inconsistencies with other relevant info. State Action. Investigating Results of Analytical Procedures: As per SA 520, "Analytical Procedures": Not Acceptable: Inconsistent with other relevant info. or that differ from expected values by a significant amount, the auditor shall <u>investigate such differences by:</u> Inquiring of management & obtaining evidence relevant to mngt's responses Performing other audit procedures as necessary in the circumstances [Eg. Need to perform other procedure arise when → Mngt unable to provide Explanation Or, Explanation along with audit evidence not adequate]
Timing of AP	Planning Phase → Understanding client business & area of Risk Testing Phase → to obtain Audit evidence Completion Phase: → Assist auditor in forming Conclusion → whether FS are consistent with auditor's understating of entity
Near Audit End for Conclusion:	To design & perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether FS are consistent with the auditor's understanding of the entity. (It will also <u>verify conclusion</u> formed during audit of individual components or elements of FS) (If as a result of A.P. → <u>identified previously unrecognized ROMM</u> → auditor to <u>revise auditor's</u>



assessment of ROMM as per SA 315 & modify further planned audit procedures accordingly)

Q24. Analytical Procedures for Payroll Cost & Hotel room rent Income

- 1) In some cases, even unsophisticated predictive model may be effective as analytical procedure. (Payroll Cost)
→ when Know No. of Employees * Fixed rate of Pay = Total Payroll cost (estimated), Hence need of TOD reduced
- 2) Different types of analytical procedures provide different levels of assurance (Hotel Room rental Income) → Room tariff rate * No. of rooms * Occupancy rate → Provide persuasive evidence of Income, TOD need reduced

SA 540: AUDITING & ACCOUNTING ESTIMATES, INCLUDING FAIR VALUE ACCOUNTING ESTIMATES AND RELATED DISCLOSURES

Brief: (Eg. Suit Provision estimation)	Because of the uncertainties inherent in business activities → Some FS items cannot be measured precisely, but can only be estimated, The measurement objective of a/cing estimates can vary depending on the applicable FRF and the financial item being reported <u>Because of Available data → some Estimation have uncertainty → give rise to ROMM</u>
Scope:	auditor's responsibilities regarding: - A/cing estimates, including fair value accounting estimates and, - Related disclosures in an audit of FS
Objective:	Obtain SAAE w.r.t FRF → - a/cing estimates in FS Recognized is Reasonable & - Completely disclosed (Adequate)
Disclosure related to A/cing estimates:	- The auditor shall obtain SAAE about whether the disclosures in the FS related to accounting estimates are in accordance with the requirements of the applicable FRF - For accounting estimates that give rise to significant risks, the auditor shall also evaluate the adequacy of the disclosure of their estimation uncertainty in the FS as per FRF
Estimation uncertainty:	- Not all FS items, which require Fair value measurement have estimation uncertainty [active and open market that provides readily available and reliable information, valuation of securities quoted on an active and open market at listed price] - Estimation involves judgments based on info. Available when FS are prepared → auditor is not responsible for predicting future conditions
Mngt Bias (neutrality) [MCQ Purpose]	➤ Management bias can be difficult to detect at "ACCOUNT LEVEL". - It may only be identified when considered in aggregate of groups of a/c estimates. Or - all accounting estimates, or - when observed over a number of a/cing periods ➤ Some form of mngt bias is inherent in subjective decisions (no intention of mngt to mislead user) ➤ however, there is intention to mislead, management bias is fraudulent in nature. Q25. Explain some indicators of possible management bias to accounting estimates. [Old] Such judgment may involve unintentional or intentional management bias (for example, as a result of motivation to achieve a desired result). - Changes in a/cing estimate / method → where mngt has made subjective assessment. - Entity's use own assumptions for Fair Value A/c estimate inconsistent with market assumptions - Selection of a point estimate that may indicate a pattern of optimism or pessimism.

Q26. Give any five examples of accounting estimates & Fair value accounting estimates given in SA 540 [Old]

Example of A/cing	Allowance for doubtful accounts. [Current asset]

Estimates:	• Inventory obsolescence. <u>[Current asset]</u> • Depreciation method or asset useful life. <u>[Fixed asset]</u> • Financial Obligations / Costs arising from litigation settlements and judgments. <u>[Loan]</u> • Provision against carrying amount of Investment, when uncertainty of recoverability. <u>[Provision]</u> • Warranty obligations. • Outcome of long-term contracts.
Example of Fair Value A/cing estimates:	• Share-based payments. <u>[Ind AS-102]</u> • Assets/Liabilities acquired in business combination including goodwill & intangible assets. <u>[103]</u> • Asset held for disposal. <u>[Ind AS-105]</u> • Complex financial instruments, which are not traded in an active & open market. <u>[Ind AS-109]</u> • Exchange of assets/liabilities btwn independent parties without monetary consideration. <u>[115]</u> • Estimates where current transaction cost basis is used or based on condition prevailing in market.
Risk Assessment Procedure for A/cing Estimates: (How Auditor reduce ROMM of estimates)	Q27. Risk Assessment Procedure for A.E. Or How auditor can reduce ROMM of Estimates Obtain understanding of entity & its environment, including entity's I.C, as required by SA 315, (i) The requirements of the applicable FRF relevant to a/cing estimates, including disclosures. (ii) <u>How Management identifies those Transactions, Events and Conditions (TEC) that may give rise to the need for accounting estimates to be recognised or disclosed, in the FS.</u> (iii) In obtaining this understanding, the auditor shall <u>make inquiries of mngt about changes in circumstances</u> that may give rise to new, or the need to revise existing, a/cing estimates. (iv) <u>How mngt makes a/cing estimates, estimation making process of management including:</u> (1) The method, including where applicable the model, used in making the a/cing estimates. (2) Whether management has used an expert? (3) The assumption underlying the accounting estimates. (4) Whether and, if so, how the mngt has assessed the effect of estimation uncertainty (5) 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 (6) Relevant controls.
Inquiries from Mngt for Change in Circumstances:	Q28. List down some circumstances, change of will results in Inquiries from the mngt.(Old) <u>[New Transaction or Event / Change in Transction → Acc. Policy Mngt k haath h, par Govt regulation nahi]</u> • The entity has engaged in New types of transactions may give rise to a/cing estimates • Terms of transactions that gave rise to AE have changed. • New conditions or events have occurred • Accounting policies relating to AE have changed as a result of changes in the applicable FRF. • Regulatory or other changes outside the control of management have occurred that may require management to revise, or make new, accounting estimates During the audit, the <u>auditor may identify transactions, events & conditions that give rise to the need for A/cing estimates that mngt failed to identify.</u> → SA 315 deals with circumstances where the auditor identifies ROMM that management failed to identify.
Auditor' Response to the assessed ROMM: (Further Audit Procedure)	Q29. Auditor, found that the entities RAP has some loopholes →, a ROMM due to these fair value estimation. Suggest him as to how he should deal with such risk. (Old - Nov23) while responding to the assessed ROMM, auditor shall determine whether, in auditor's judgement any of those a/cing estimates have been identified as high estimation uncertainty giving rise to significant risk Based on the assessed ROMM , the auditor shall determine: • Whether management has appropriately applied requirements of applicable FRF • Whether methods are appropriate and have been applied consistently, and whether changes, if any, in AE or in method for making them from prior period are appropriate



(Less Important) Subs. Event, Method/assump, TOC & Subs., Range	- If there are changes in a/cing estimates or in the method used for making those from prior period, are those appropriate in the present circumstances. 2) In response to the assessed ROMM, 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 SAAE regarding the 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. - Test checks the effectiveness of the controls over the estimates used by the management together with appropriate substantive procedure (ie., do TOC & Substantive) - Develop a Point estimate Or Range to evaluate management's point estimate, for this purpose: a) When the auditor uses Assumption or Method → which is different from Mngt's, auditor shall obtain understanding of mngt's assumption or Method. b) When auditor is using Range, auditor shall Narrow the range based on audit evidence (Not wide), until all outcomes within the range are considered reasonable.
Estimation Uncertainty: Evaluate A/cing Estimate which involve SIGNIFICANT RISK: [SA 330]	[Trick: Jab itne saare Alternative Assumption the > to bhi ye hi Assumption kyu use Lia ? > kya ye Reasonable h ?.. isme "Uncertainty" nii h? > muje to iska "intent" lagta hi nii hai aisa karne ka .. pagal bna ra] (i) How mngt has considered alternative assumptions or outcomes, & why it has rejected them, or how mngt has otherwise addressed estimation uncertainty in making the a/cing estimate. (ii) Whether the significant assumptions used by management are reasonable. (iii) If, in the auditor's judgment, Mngt has not adequately addressed the effects of estimation uncertainty on the A/cing estimates that give rise to significant risks, the auditor shall, if necessary, develop a range with which to evaluate the reasonableness of the a/cing estimate. (iv) Where relevant to the reasonableness of significant assumptions used by mngt or the appropriate application of the applicable FRF, mngt intent to carry out specific courses of action and its ability to do so.

Q30. Auditor is concerned with **identification & assessment of ROMM for A/cing estimates**. Guide him w.r.t to **estimation making process** adopted by mngt (SA's) → **Mention Only 4th Point of "RAP for A/cing Estimates"**

Q31. Provision of Huge amount is on estimated business. How auditor can evaluate this a/cing estimate which **significant risk** & what if mngt has not addressed the effects of estimation uncertainty on provision made? Or **FAP** to respond significant risk " → **[Refer above: "Evaluate A/cing Estimate which involve Significant Risk"]**

➤ Accounting Estimates Give Rise to LOWER ROMM & HIGHER ROMM

Estimates involve relatively LOW estimation uncertainty & may give rise to lower ROMM:

[Trick: "**FRF**" ke hisaab se 1 "**well known model**" software bana rkha h > tumhare pass jo "**Readily available data**" h wo daalo isme bas > koi "**complex**" nii h , "**routine**" me roz karta hu me]

- Fair value accounting estimates where the **method of measurement** prescribed by the **applicable FRF** is **simple** and **applied easily to the asset or liability** requiring measurement at fair value. (i.e., Stock NRV)
- Fair value accounting estimates where the **model used to measure the accounting estimate** is **well-known or generally accepted**, provided that the assumptions or inputs to the model are observable. (i.e., Black Scholes)
- Accounting estimates derived from **data that is readily available**, such as published interest rate data or exchange-traded prices of securities. Such data may be referred to as "observable" in the context of a fair value accounting estimate.
- Accounting estimates arising in entities that engage in business activities that are **not complex**. (i.e., small retail store bad debt provision)
- A/cing estimates that are frequently made & updated because they relate to **routine transactions**. (i.e. Dep Life)

Q32. (Refer Above Notes) areas of A/cing estimates that may give rise to lower level of ROMM . examples. [Old]

Estimates involve relatively HIGH estimation uncertainty & may give rise to HIGHER ROMM:

[Trick: yrr koi "recognised technique" nhii h iske liye, "software model bhi highly specialized" h > isse accha h jo amt tere "judgement" se aara h wo hi le le > wo baad alag h ki "pichli baar ka estimate ka outcome" galat ho gya... eg. "Derivative Financial instrument"]

- Accounting estimates that are **not** calculated using recognised measurement techniques.
- Fair value accounting estimates for which a **highly specialised entity-developed model** is used or for which there are no observable inputs.
- A/cing estimates that are highly dependent upon judgment, Eg., **judgments about outcome of pending** litigation or amount & timing of future cash flows dependent on uncertain events many years in the future.
- A/cing estimates where the results of auditor's review of similar a/cing estimates made in the **prior period** FS indicate a substantial **difference between original accounting estimate & actual outcome**.
- Fair value accounting estimates for **derivative financial instruments not publicly traded**.

Q33. (refer above) → SA's state examples of A/cing estimates that may have high estimation uncertainty. [Old]

➤ Review of Outcome of Prior Accounting Estimates [Not in SM]

Q34. Auditor requested some info from mngt to review Outcome of Prior Period A.E outcome. Mngt Refused

[Trick: yarr bilkul bhi "Effective" nii h tera estimation → pichli baar jo estimate kara wo wapas "Re-estimate" karna pad gaya iss baar.... Bhayankar "Uncertainty" hai]

SA 540 → auditor shall review the outcome of A/cing estimates included in the prior period FS, or their subsequent re-estimation for the purpose of the current period.

The outcome of an accounting estimate will often differ from accounting estimate recognised in the prior period FS. By performing RAP to identify & understand the reasons for such differences, the auditor may obtain:

- Information regarding the **effectiveness of management's prior period estimation** process, from which the auditor can judge the likely effectiveness of management's current process.
- Audit evidence that is pertinent to **re-estimation, in the current period, of prior period a/cing estimates**.
- Audit evidence of matters, such as **estimation uncertainty**, that may be required to be disclosed in the FS.

The review of prior period a/cing estimates may also assist the auditor, in the current period, in identifying circumstances or conditions that increase the susceptibility of accounting estimates to, or indicate the presence of, **possible management bias**. The auditor's **professional skepticism** assists in **identifying such circumstances** or conditions and in determining the nature, timing and extent of **further audit procedures**.

(mngt can-not refuse auditor to provide info. By saying that auditor is not responsible for Prior period data)

SA-600: Using the work of another Auditor

Applicable	In situation where an auditor (principal auditor), reporting on the financial information of an entity, uses the work of another auditor (other auditor) w.r.t. to the financial information of one/more components (Division, Branch subsidiary, Associate, J.V. or other entity whose F.info audited by principal auditor), included in the financial information of the entity. <u>Not applicable:</u> (a) Joint Auditor (b) Predecessor auditor
Not reduce responsibility:	When the auditor delegates work to assistants or uses work performed by other auditors and experts → He will continue to be responsible for forming and expressing his opinion. However, he will be entitled to rely on work performed by others → provided he exercises adequate skill and care and is not aware of any reason to believe that he should not rely.



Reporting Consideration:	Principal auditor to issue a qualified opinion or disclaimer →	In case of a limitation on the scope of audit → When Work of other auditor cannot be used & principal auditor has not been able to perform sufficient additional procedures regarding the financial info. of the component audited by the other auditor.
	If the other auditor issues a Modified Report	Principal auditor should consider whether subject of the modification is of such nature and significance , i.e. the financial info. of the entity on which the principal auditor is reporting that it requires modification of the principal auditor's report.

➤ **DIVISION OF RESPONSIBILITY:**

- Principal Auditor (PA) is not responsible for work carried out by Other Auditor (OA) unless there are circumstances, which should have aroused suspicion about Reliability of work performed by Other Auditor.
- When PA has to base his opinion on financial info. of entity as whole relying on statements & reports of Other Auditor his **report should state clearly Division of Responsibility** for Financial info of entity.
- It should **indicate extent to which financial info of components audited by** the Other Auditor have been included in financial information of Entity.
- However, if the Principal Auditor notices any material discrepancies, the same has to be brought to the knowledge of other Auditor. This should be **incorporated in the Audit Report**

Q35. Bank has 1034 branches (audited by Branch Auditor) → Error in NPA classification of many advances not pointed out by branch auditor → whether Statutory auditor of H.O liable? any reporting precaution?
Hint: Refer above "Division of Work" → In given situation → Nothing has come to light of statutory auditor which would arouse his suspicion about reliability of work performed by branch auditor → So he is Not Liable.
While Reporting, clearly stated in report that 1034 branches of bank have been audited by branch auditors

➤ **ACCEPTANCE AS PRINCIPAL AUDITOR (PA)**

Q36. PQ Ltd has many branches, you got position of PA, What factors to considered in accepting position of PA

Factors to be considered while accepting the position of Principal auditor -

SA 600 - Using the work of Another Auditor - **[MARK]**

- 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 info. of components **audited by the other auditor**;
- the performance of **Additional procedures** as set out in this SA **regarding the components audited by other auditor** resulting in the principal auditor having significant participation in such audit.

➤ **PRINCIPAL AUDITOR PROCEDURE**

Q37. Principal auditor of Conso FS wants to ensure that Branch Auditor work is adequate, so can he ask Working Paper of component auditor?

[Trick: "Component Visit" kake aa > usse "Discuss" kar uski "competency" or usse bol, ki bhai me tujpe "Rely" karta hu > par meri thodi sii "Advise" maan le yarr tri "Significant Finding" mre liye bahot imp. hai, so pls "Time" pe report de dha]

Using the Work of Another Auditor: When Branch A/c's are audited by a person other than company's auditor, there is need for a clear understanding of the role of such auditor and the company's auditor there is great necessity for a proper rapport between these two auditors for the purpose of an effective audit.

1) Right of Principal auditor to VISIT and examine books of accounts of a component

- In certain situations, if he thinks it necessary to do so → he May → **principal auditor have right on the to visit a component & examine the books** and other records of the said component,



- PA would normally be entitled to **RELY** upon the work of Other auditor unless there are special circumstances to make it essential for him to visit component & examine BOA & other records of component.

2) Principal auditor to consider the professional COMPETENCE of other auditor

PA should consider the professional competence of other auditor (if other auditor is not a member of ICAI)

3) Procedures to be performed by principal auditor when using the work of other auditor [ADVISE]

PA procedures to obtain **SAAE, that the work of the other auditor is adequate** for the principal auditor's purposes. When using the work of another auditor, PA should ordinarily perform following procedures:

- 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. The principal auditor would inform the other auditor of matters such as : (IT +SA)
 - Areas requiring Special consideration,
 - procedures for the Identification of inter-component transactions that may require disclosure &
 - the Time-table for completion of audit;
- Advise the other auditor of the Significant a/cing, auditing & reporting requirements and obtain representation as to compliance with them.

4) Principal auditor to DISCUSS (A.Procedure) & review - Written summary of Findings

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

Principal auditor may also wish to visit other auditor → NTE of procedures will depend on → circumstances of engmntn & materiality → & professional competence of other auditor.

5) The principal auditor should consider the SIGNIFICANT FINDING of the other auditor.

Discuss with other auditor and the mngt of component, → the audit findings or other matters affecting the financial info. of components → He may also decide as to application of supplementary procedures that supplement tests of the records or the FS of component (such test will depend upon circumstances)

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

(i.e., Foreign component → other than a professionally qualified auditor)

Further, SA 230 and SQC 1, → Audit documentation is the property of the auditor.

He may at his discretion, make portions of, or extracts from, audit documentation available to clients, provided such disclosure does not undermine the validity of the work performed

Hence Principal auditor approach is wrong in asking working papers.

Q38. The audit reports i.r.t branches have already been sent to the principal auditor. → Principal Auditor, asked the branch auditors to share with him a summary of audit procedures and findings & working paper (SM)
Hint: [Approx same answer as above Qn, Just Don't mention Point no. 3 of above i.e., Procedure to perform by principle auditor while using work of other auditor (advice)]

Q39. Using work of subsidiary auditor → (1) explain procedure to obtain SAAE that work of other auditor is adequate (2) how to document working paper w.r.t Subsidiaries

Hint: (1) Refer above point (3) i.e., Procedure to be perform by P.A (Advise) (2) below Topic of "Documentation"

➤ PRINCIPAL AUDITOR's DOCUMENTATION [Nov'24]

Document in his working papers:

- **Components** whose financial info. audited by other auditors.
- **Procedures performed** and the **conclusions reached**.
- **results of discussions with O.A** & review **written summary** of other auditor's procedure



Not Document:	Reasons of why P.A. limited its procedures → when Previously SAAE was obtained that "other auditor" is complying the acceptable Q.C policies & procedures.
Modified report of Other Auditor:	Where other auditor's report is other than unmodified → principal auditor should also document how he has dealt with the qualifications or adverse remarks contained in the other auditor's report in framing his own report.

➤ **CO-ORDINATION & SUFFICIENT LIASON between Auditor's**

Q40. Role of Subsidiary & Holding Auditor's Or, Sufficient Liaison between PA & OA (& reporting consideration)(Old)

Author's Note: Summary of Below Answer: [ROLE of P.Auditor & O.auditor]

Role of Principal Auditor	Role of Other Auditor
(i) Issue written communication(s) as a principal auditor to the other auditor. (ii) Should advise the other auditor of any matters that come to his attention that he thinks may have an imp. bearing on other auditor's work (iii) May require the other auditor to Answer a detailed questionnaire regarding matters on which the principal auditor requires information for discharging his duties.	(i) Should co-ordinate with the principal auditor. For example, by bringing to the principal auditor's immediate attention to any significant findings requiring to be dealt with at entity level, (ii) Adhering to the time-table for component audit. (iii) He should ensure compliance with the relevant statutory requirements . (iv) should respond to the questionnaire sent by Principal Auditor on a timely basis

(In answer, Also Mention "**Reporting Consideration**" → as given in Above Notes)

SA 610- Using the Work of Internal Auditors (IA's):

Objective	If entity has an IAF & its relevance to the External Auditor's work, then EA should determine: A. If the specific work of the internal Auditor can be used & if so, to what extent B. Whether, such work is adequate for the audit purpose
Coverage in this SA:	1) Using the work of Internal Audit Function (IAF) 2) Using Internal Auditor (IA) to Provide Direct assistance (DA) under D/S/R of Ext. Auditor.
SA Not applicable:	1) Entity does not have IAF or Entity IAF activities are not relevant for Audit, Or 2) Ext Auditor expects not to use IAF based on preliminary understanding
Internal Audit:	An independent mngt function , which involves a continuous & critical appraisal of the functioning of an entity with a view to suggest improvements thereto & add value + strengthen the overall governance mechanism of the entity, including the entity's strategic risk mngt and I.C system ".
Who can be appointed?	As per section 138, Internal auditor can be: Chartered accountant or cost accountant (whether engaged in practice or not), or Any other professional as may be decided by the Board, - The internal auditor may or may not employee of the company

➤ **Using work of Internal Audit Function (IAF)**

Scope & Objective Of IAF:	Activity w.r.t	Description:
(GIR) (IC-FR-O)	Governance :	Assess the governance process in its accomplishment of objectives on ethics & values, performance mgt. & accountability, communicating risk to appropriate areas of organization.
	Internal Control:	Evaluation of Internal control: specific responsibility for reviewing controls, evaluating their operation & recommending improvements



(Special Trick :-)	(eg., Performing 3 Way match → PO, GRN & Invoice) • Review of Compliance with L&R: Review compliance with L&R or other external requirements & with mgt. policies & directives and other internal requirements • Examination of Financial and operating information: Assigned to review means used to identify, recognize, measure, classify & report financial & operating info. & to make specific inquiry into individual items, including detailed testing of transactions, balances & procedures. (Eg. To check sales → check Sales record (financial) & delivery record (operational)) • Review of Operating Activities: Assigned to review economy, efficiency & effectiveness of operating activities, including non-financial activities (Eg., Review Inventory mngt to prevent damages)
Risk Mngt	Assist entity by identifying & evaluating significant exposures to risk & contributing to improvement of risk mgt. & IC (including effectiveness of FR process), Procedure for detection of fraud. (Eg, Evaluate & manage risk exposure of complex financial instrument)
Objective of E.A. when entity has IAF:	• Determine whether work of the IAF or direct assistance from internal auditors can be used • If using work of IAF, to determine whether that work is adequate for purposes of the audit • If using I.A.'s to provide D.A., to appropriately direct, supervise and review their work.
Areas where IAF can be used by External Auditor:	Q41. Mention some areas where work of IAF can be used by External auditor. [Old] Answer: [TOC/Substantive → Inventory count (SA 501) → L&R (SA 250)] • Testing of the operating effectiveness of controls. • Substantive procedures involving limited judgment. • Observations of inventory counts. • Testing of compliance with regulatory requirements. • Tracing transactions through the information system relevant to Financial Reporting. • Audits/Reviews of financial info of subsidiaries that are not significant components to group
Reliance on Internal Auditor work [Whether work of IAF can be used] S&D-COP	➤ <u>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:</u> 1) The extent to which the internal audit function's Organizational status and relevant Policies and procedures support the Objectivity of the internal auditors; 2) The level of Competence of the internal audit function; and 3) Whether IAF applies a Systematic and Disciplined approach, including quality control. ➤ <u>The E.A. shall not use the work of the IAF if the external auditor determines that:</u> 1) The function's organizational status and relevant policies and procedures do not adequately support the objectivity of internal auditors; 2) The function lacks sufficient competence; or 3) The function does not apply a S&D approach, including quality control.
Adequacy Of Work of Internal Auditor:	For evaluating Adequacy of work of IA, Auditor shall evaluate: 1. Objectivity of Internal Audit Function. 2. Technical competence of IA. 3. Whether work of IA is likely to be carried out with due professional care. 4. Whether there is likely to be effective communication in both.
Determine nature & extent of IAF work	1) The external auditor shall consider nature and scope of work performed by IAF and its relevance to external auditor's overall audit strategy and audit plan. 2) Extent of involvement of E.A: Whether using work of IAF to extent planned would still result in EA being sufficiently involved in audit, given EA sole responsibility for audit opinion.



can be used: [ROJ-C]	3) E.A shall make all significant judgments in audit engmt &, to prevent undue use of work of IAF: (i) Higher assessed ROMM at the assertion level (special consideration for significant risk) (ii) The less IAF organizational status and relevant policies and procedures adequately support Objectivity of internal auditors; and (iii) The more Judgment is involved • Planning and performing relevant audit procedures • Evaluating the audit evidence gathered (iv) The lower the level of Competence of IAF 4) The EA shall, in communicating with TCWG planned scope and timing of audit accordance with SA 260, communicate how EA has planned to use work of IAF
Note:	Auditor's responsibility will not reduce even if he use work / D.A. of Internal auditor → He will remain sole responsible for opinion expressed

Q42. Internal auditor attended the Inventory count + Done Inventory valuation also. → But internal auditor failed to report that Some **inventory is held from Long time** → can External auditor rely on Inv Valuation of I.A. ?
Hint: Inventory held from Long time → So, Higher ROMM (involve more Judgement), Further as per SA 200, higher the assessed ROMM, more persuasive evidence required, External auditor (E.A) to perform more work directly → Risk of inventory obsolesce → So external auditor need to perform more work Directly i.e., Compare NRV vs Cost, recompute provision for Stock

Q43. Internal auditor conducted Physical verification of Inventory → can Statutory Auditor rely on such report ?
Hint: [Refer Above Notes: **Reliance on Internal Auditor work**] (i.e.: **S&D -COP**), → Stat Auditor should ascertain I.A. scope of Verification, coverage area. → review report on physical verification → test check few items (If stat Auditor satisfied → he can rely, However, Final responsibility of opinion remain with Stat Auditor)

➤ Using Direct Assistance (DA) of IA:

Determine whether IA direct assistance can be used?	• The EA may be prohibited by L&R from obtaining DA from internal auditors. • Using IA to provide DA is not prohibited: a) The EA shall evaluate existence and significance of threats to objectivity and level of competence of the internal auditors who will be providing such assistance. b) Evaluation of existence & significance of threats shall include inquiry of internal auditors. [Inquiry of the internal auditors regarding interests and relationships that may create a threat to their objectivity]
Determining the Nature and Extent of Work can Assigned to IA: "[dusro ke Judgement se risk jyada hogi, me khud personally involve ho jaata hu, SA bhi ye hi bolta h]"	The external auditor shall consider: [ROJ-C] (1) The amount of Judgment involved in: (a) Planning and performing relevant audit procedures; and (b) Evaluating the audit evidence gathered; (2) The assessed Risk of material misstatement; and (3) The external auditor's evaluation of the existence and significance of threats to the Objectivity and level of Competence of the I.A who will be providing such assistance. • EA shall not use direct assistance in: a) Involve making significant judgments in the audit; b) Relate to higher assessed ROMM where judgment required in • Performing relevant audit procedures or • evaluating audit evidence gathered is more than limited c) Relate to work with which the internal auditors have been involved & which has already been, or will be, reported to mngt or TCWG by the internal audit function; or



	d) Relate to decisions the external auditor makes in accordance with this SA regarding the internal audit function and the use of its work or direct assistance.
Significant Judgement: [DREGS]	Significant judgement includes following: a) Evaluating the adequacy of <u>Disclosures in F.S.</u> & other matters affecting auditor's report. b) Assessing the <u>RMM</u> ; c) Evaluating significant <u>accounting Estimates</u> ; and d) Evaluating the appropriateness of mgnt use of the <u>Going concern</u> assumption; e) Evaluating the <u>Sufficiency of tests</u> performed;
When using the DA of IA (Prior to use)	Q44. what factors he should ensure prior to using him for direct assistance? [MTP'24] 1) Prior to using IA to provide DA for purposes of audit, the external auditor shall <u>Obtain written agreement</u> from: • <u>an authorized representative</u> , That internal auditors will be <u>allowed to follow the external auditor's instructions</u> , and that entity will not intervene • <u>Internal auditors</u> that they will keep <u>confidential</u> & Inform E.A if any threat to objectivity 2) The external auditor shall <u>direct, supervise and review</u> the work performed by internal auditors on engagement in accordance with SA 220. 3) <u>Remain alert</u> for indications that the EA's evaluations are no longer appropriate.
Documentation when E.A. using DA of I.A: (O-WWW)	Q45. CA L (E.A) uses the I.A. as direct assistance → But he is <u>not documenting Working paper prepared by I.A. in D.A</u> ? Guide him as to matters to be included in the Audit docs (N24) <u>Documentation when External Auditor uses I.A to provide Direct Assistance:</u> a) <u>Evaluation of existence</u> & significance of <u>threats to objectivity</u> , & level of <u>competence</u> of IA b) Basis of decision regarding <u>nature & Extent of work performed by internal auditor</u> c) <u>Who reviewed work</u> performed and <u>date & extent</u> of that review as per SA 230 d) <u>Written agreement</u> obtained from authorised representative of entity & internal auditor e) <u>Working paper prepared by I.auditor</u> who provided direct assistance Hence in given case → CA L is not correct (as he is required to document)
Note:	<u>Auditor's responsibility will not reduce</u> even if he uses work of Internal auditor → He will remain sole responsible for opinion expressed - ICAI has also issued <u>13 SIA</u> (Standard on Internal audit), to conduct internal audit with best practices (<u>Currently SIAs are recommendatory</u> in nature, not mandatory)

Q46. State the factors to consider in opting to make use of direct assistance of the I.A [Old]
Hint: Refer Above Notes "Determining Nature & Extent of Work can assign to IA" "[ROJ-C]" Points Only
(Judgment, ROMM, Objectivity, Competence)

If using I.A. for D.A is NOT prohibited by L&R, E.A shall evaluate → objectivity threats & level of competence.
Including inquiry of the internal auditors regarding interests & relationships that may threat to their objectivity

Q47. (Old) → Large balance of Debtors (High risk area) → Using D.A of I.A:

- Checking accuracy of Ageing of Debtors → It can be assigned to I.A
- Creating provision on debtor, based on above Ageing → Can't assign to I.A, it involve more than limited Judgement
(Now explain Above Topic: "Determining the Nature & Extent of Work can Assigned to IA?:)

Q48. (a) Evaluating significant a/cing estimates or Going Concern → D.A can't be used for this (as it's a Significant Judgement (Explain Above "Significant Judgement" i.e., DREGS)

(b) D.A. of I.A. w.r.t External Confirmation Request & Evaluation of E.C. procedure:

- SA 505 require E.A. to maintain control over E.C & Evaluate result of E.C. procedure. → can't assign to I.A.
(However, I.A. may assist in assembling info necessary for E.A. to resolve exceptions in confirmation responses

Q49. Evaluating sufficiency of test performed & adequacy of FS disclosure → D.A can't be used (Explain DREGS)

Q50. SA 610, in determining nature of work to be assigned to the I.A., External Auditor Should be Careful → Not appropriate to take D.A for matters, example → Fraud risk discussion, Unannounced A.Procedure (SA 240)

Those assertion which was Not tested by him in Previous Year (due to less material in last year) → So, this year, to test those assertion, Incorporate Unpredictability (Unpredictability needed so that person within company who are familiar with Normal A.process, Not able to conceal Fraudulent F.R.) → So, In that case, using D.A of I.A can defeat the purpose → Hence, to be Done by External auditor only.

Further, Qn also asked → factors to ensure prior using D.A → refer notes → "When using DA of IA (Prior to use)"

Q51. Exactly same as Above Qn (MTP'25) i.e., Last year Assertion was not tested, so in Current Year D.A. can't be Obtained for that Assertion testing (But Language of Answer is different) → Refer Qn Bank
[i.e., If D.A not prohibited by L&R → Evaluate I.A (a) Objectivity (b) Competence]

SA 620 "Using the Work of Auditor's Expert":

Definitions	Auditor's Expert	An individual or organization possessing <u>expertise</u> in a field <u>other than accounting or auditing</u> , whose work in that field is used by the auditor to assist the auditor <u>in obtaining sufficient appropriate audit evidence</u> . An auditor's expert may be the auditor's internal expert or an external expert
	Management Expert	An individual or organization possessing expertise in a field <u>other than accounting or auditing</u> , whose work in that field is used by the entity to assist the entity <u>in preparing the financial statements</u> . (SA - 500)
Objective	To determine whether to use the work of an auditor's expert & whether that work is adequate for the auditor's purposes.	
Evaluate <u>CCO</u> of that Expert (SA 500)	➤ Competence-Nature & level of Expertise ➤ Capability-Ability to exercise competence ➤ Objectivity- bias, conflict or interest or influence of others [evaluation of objectivity include <u>inquiry regarding interests & relationships</u> → may create a threat to objectivity.] <u>SOURCES FOR OBTAINING INFORMATION OF AN AUDITOR'S EXPERT</u> • Personal experience with previous work of that expert. • Discussions with that expert. • Discussions with others who are familiar with that expert's work. • Knowledge of that expert's qualifications. • Published papers or books written by that expert. • Auditor's firm's Quality Control Policies & Procedures.	

➤ Whether to use an Auditor's Expert

Considerations when deciding whether to use an auditor's expert may include:	<u>[Trick: koi to "significant" ya "Risky" matter hoga → tabhi to koi "experience" "mngt expert" rkha]</u> • The nature and significance of the matter, including its complexity. • The RMM in the matter. • Whether management has used a management's expert in preparing F.S. • 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 mngt has used mngt expert:	Auditor's decision on whether to use auditor's expert may also influenced by such factors as: <u>[trick: mngt ne kis "Kaam" ke liye usse "employ" kara h > maana ki wo "capable/competent h"... uske bhi apne "professional standard" h... par mngt to usse fees dera hai.. to wo usse influence kar dega]</u> • The nature, scope and objectives of the management's expert's work. • Whether mngt expert is employed by entity, or is engaged by it to provide relevant service • Extent to which mngt can exercise control or influence over the work of mngt's expert. • The management's expert's competence and capabilities. • Whether mngt'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

➤ Matters & It's Adequacy (Relevance & Reasonableness)

Areas where Expert can assist auditor (Need of auditor's expert)	<u>An auditor's expert may be needed to assist the auditor in one or more of following:</u> - Identifying & assessing the ROMM → SA 315 - Obtaining an understanding of entity & it's environment (IC) → SA 315 - Implement overall response to assessed risk at FS level → SA 330 - Performing further audit procedure to respond risk at assertion level → SA 330 - Evaluating SAAE in forming opinion on FS → SA 500							
For which matters (Types of Report):	<u>Expertise in a field other than accounting or auditing:</u> (i) The valuation of complex financial instruments, land and buildings, plant and machinery, jewelry, works of art, antiques, intangible assets, assets acquired and liabilities assumed in business combinations and assets that may have been impaired. (ii) The valuation of environmental liabilities, and site clean-up costs. (iii) The actuarial calculation of liabilities associated with insurance contracts or employee benefit plans. (iv) The estimation of oil and gas reserves. (v) The interpretation of contracts, laws and regulations. (vi) The analysis of complex or unusual tax compliance issues.							
Adequacy/ Reasonableness /Extent of reliance on expert work	Auditor should evaluate the adequacy including: <table><tr><td>(i) Relevance and reasonableness of → & its Consistency with →</td><td>Expert finding or conclusion Other audit evidence</td></tr><tr><td>(ii) Relevance and reasonableness of any →</td><td>Significant assumptions or methods used</td></tr><tr><td>(iii) Accuracy, Completeness, & relevance of →</td><td>Source data if any used</td></tr></table>		(i) Relevance and reasonableness of → & its Consistency with →	Expert finding or conclusion Other audit evidence	(ii) Relevance and reasonableness of any →	Significant assumptions or methods used	(iii) Accuracy, Completeness, & relevance of →	Source data if any used
(i) Relevance and reasonableness of → & its Consistency with →	Expert finding or conclusion Other audit evidence							
(ii) Relevance and reasonableness of any →	Significant assumptions or methods used							
(iii) Accuracy, Completeness, & relevance of →	Source data if any used							
Inadequate expert work	<u>If auditor is of the opinion that expert' work is not adequate, then:</u> (i) Determine the nature and extent' of further work to be performed by the expert, Or, (ii) Perform further audit procedures appropriate to the situation <i>If above is not possible → modify opinion as per SA 705</i>							
Review Relevance & reasonableness: (Specific Procedure for Adequacy): [ICA-ORR]	<u>The relevance and reasonableness of that expert's findings or conclusions, and their consistency with other audit evidence:</u> <u>Inquiries</u> of the auditor's expert. <u>Reviewing</u> the auditor's expert's working papers and reports. - Corroborative procedures, such as: ✓ <u>Observing</u> the auditor's expert's work; ✓ Examining published data, i.e., statistical reports from reputable, authoritative source ✓ <u>Confirming</u> relevant matters with third parties; ✓ Performing detailed <u>analytical procedures</u>; and ✓ <u>Re-performing</u> calculations. <u>Discussion with another expert</u> with relevant expertise when, for example, the findings or conclusions of the auditor's expert are not consistent with other audit evidence. <u>Discussing the auditor's expert's report with management.</u>							

Refer SA 500, for Evaluation of Experts "significant assumption/Methods" & "Source data"

Q52. Auditor require report from Expert, What types of report/opinion can be obtain ? & to what extent can rely ?
Hint: "(a) For which matters (Types of Report) (b) Extent of reliance on expert work (c) Inadequate expert work

Q53. Auditor used Engineer consultant → which Specific procedure to follow, to evaluate Adequacy of expert work.

Or, Review procedure to apply to check relevance & reasonableness of A.Expert work.

Hint: Refer above notes: → (a) "Review Relevance & reasonableness (Specific Procedure)"

(b) Extent of reliance on expert work (b) Inadequate expert work

➤ Written Agreement with Auditor's Expert:

Matters in agreement:	Auditor shall agree, in writing when appropriate, following matters with auditor's expert: <u>[Trick: "kaam kya hai", "teri meri responsibility" kya h ... "apne bich me jo bhi baat" ho wo "confidential" honi chahiye]</u>
(Special Trick :-)	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 NTE of communication between the auditor and that expert, including the form of any report to be provided by that expert; and [For <u>significant risk</u>, <u>both</u> a formal <u>written report at the conclusion</u> & <u>oral reports</u> as the <u>work progresses</u>] → MCQ d) The need for the auditor's expert to observe confidentiality requirements.

Q54. Complex derivative valuation, & the expert which auditor has appointed was never used by him earlier, Auditor did not enter into formal agreement with the Auditor's expert.

Need of Detailed Written Agreement:	As per SA 620, some matters may affect the level of detail and formality of the agreement, Like whether it need in writing. Example: following factors may suggest the need for more a detailed agreement in Writing : • The auditor's expert will have access to sensitive or Confidential entity information. • The matter to which the auditor's expert's work relates is highly Complex. • Greater the extent of auditor's expert's work, & its Significance in context of audit. • The auditor has not previously used work performed by that expert. (New) • Multi-jurisdictional Legal or regulatory requirements apply. • The respective roles or responsibilities of the auditor and the auditor's expert are different from those normally expected. In given case, considering complexity in derivatives valuation and also due to the fact that the auditor and auditor's expert were new to each other, auditor should have signed a formal agreement/ engagement letter.

➤ Reference of Expert in Auditors' Report

Reporting:	<u>REFERENCE TO THE AUDITOR'S EXPERT IN THE AUDITOR'S REPORT:</u>	
	Unmodified A.Report →	No reference unless required by L&R → If require by L&R → indicate in auditor's report that reference does not reduce the auditor's responsibility for audit opinion
	Modified report →	Auditor May provide reference of auditor expert in Audit report, when such reference is relevant to an understanding of a modification to the auditor's opinion i.e., to explain the nature of modification. Auditor may need permission of auditor's expert before making such a reference → Not reduce responsibility of A.expert
Note:	• Auditor's responsibility will not reduced even if he use work of Auditor's expert → He will remain sole responsible for opinion expressed • Issue Modified Opinion → When Auditor's expert work is not adequate for auditor's Purpose, and Auditor not able to resolve it through Additional procedure. (not able to obtain SAAE)	

Q55. Auditor's Expert work is Not adequate → so auditor concluded that modified opinion needed, However issued Clean report & included name of expert to reduce his responsibility:: = Refer above notes i.e., If expert work not Adequate, Not able to resolve through Additional procedure → require to issue Modified opinion, and reference do not reduce auditor's responsibility)



➤ Other Integrated Qns:

Q56. Mr. X, Y, Z are J.A → Mr. X & Y are agreed on same actuary report, However Z did not. Explain Responsibility of J.A, if Mr. Y Actuary report found faulty.

Hint: SA 620 → Auditor responsibility not reduced by use of A.expert's work.

- Evaluate Expert Work Adequacy (relevance and reasonableness of expert Finding & Conclusion, it's consistency)
- relevance & reasonableness of assumptions & methods, → relevance, completeness, & accuracy of source data
- (Now Explain Qn Info.) → X & Y held responsible for Gross negligence, Not Mr. Z (As separate report issued)

CHAPTER 4- Materiality, Risk assessment & Internal control

SA 265, 315, 320, 330

➤ Risk Assessment

Define:	- It assesses the level of risk in the various business processes. Focuses on the business environment, regulatory environment, organization structure, organizational & business environmental changes & - specific concerns of management & Audit committee to determine the areas of greatest risk
Audit Risk:	- Risk of expressing an inappropriate audit opinion on F.S. that are materially misstated - It needs to be considered at Overall Level & at Assertion Level. - It is brought about by error & fraud Components: Audit Risk = Risk of material Misstatement (ROMM) X Detection Risk
ROMM:	- An anticipated risk that a Material Misstatement may exist in F.S. before start of Audit Components: ROMM = Inherent Risk X Control Risk
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 F.S. level & at the assertion level - Auditor to consider IR when designing TOC or Substantive procedure to design its extent. Example: Technological developments might make a particular product, Complex calculation could be misstated, High value inventory, A/cing estimate significant uncertainty, lack of W.C.
Control Risk:	Risk that entity's internal control system will not prevent, or detect & correct on a timely basis Misstatement that could be material individually or when aggregated with other misstatement
Detection Risk:	- Risk that the auditor will not detect a misstatement at exists in an assertion that could be material either individually or when aggregated with other misstatement Acceptable level of detection risk for a given level of audit risk audit risk bears an inverse relationship to the ROMM at the assertion level. Example: Selecting an inappropriate audit procedure, misapplying an audit procedure, Misinterpreting the results from an audit procedure

There is INVERSE Relationship Between ROMM & Detection Risk

ROMM	Acceptable Detection Risk
High	Need to be Low
Low	Can Be High

The objective of the audit is to reduce this audit risk to an acceptably low level

Control Risk Assessment:

Auditor assesses control risk as **Rely or Not rely on Controls**. When making control risk assessments → if **deficiency is identified** → **identify the assertion of FS affected, Revise the ROMM & modify NTE of substantive procedure**

Q1. Auditor noticed that Laid down Delegation of Powers has not been followed, earlier auditor assessed ROMM as LOW, describe why above finding will change Auditor's assessment (**HINT** → **Assessing CONTROL Risk**)

Hint: Evaluation of I.C → **Influence** auditor's assessment of ROMM. (ROMM include **Control Risk**). → Above situation shown **controls are not Operating effectively**. So, **Control risk assessment needs to be revised** → lead to **Revision in ROMM Assessment** → lead to **modification of NTE of planned substantive procedures**.



Q2. NGO getting it's A/c's audited for 1st time → Get Substantial Donation incl Foreign Funds (last yr no activities)
 → govt has power to cancel FCRA certificate (working in field of Politics/Social), → how assessing Audit risk ?
Hint: to assess Audit risk → Consider All component of Audit risk. (Inherent Risk -IR) (Control R) (Detection R)
 • NGO field is Politics + Crowdfunding Donation + foreign Fund (integrity of person behind NGO is important, may involve in Money Laundry), last yr a/c unaudited (probable misstatement in last yr) → **Inherent Risk**
 • Last Year NGO Activities were less (may less controls / No formal control), but this year High Funding received, May lead to non-compliance with laws / FCRA → **Control Risk**
 • NGO getting it's a/c's audited 1st time (lack of understanding + inappropriate Sampling Procedure) → **Detection R**

➤ Types of Assertion

Assertion Meaning: Representations by management, explicit or otherwise, that are embodied in the financial statements, as used by the auditor to consider the different types of potential misstatements that may occur.

Q3. as per SA 315, types of assertions used by auditor to consider different types of potential misstatements [Old]

Transactions & events	Assertions about classes of transactions & events FOR THE PERIOD under audit-	
	Classification	Transactions and events have been recorded in the proper accounts
	Occurrence	Transactions & events that are recorded have occurred & pertain to the entity.
	Completeness	All transactions & events that should have been recorded have recorded .
	Accuracy	Amounts & other data have been recorded appropriately
	Cut-off	Transactions & events have been recorded in correct accounting period
Account Balances	Assertions about account balances AT THE PERIOD END-	
	Existence	Assets, liabilities, & equity interests exist
	Rights and obligations	Entity holds or controls rights to assets & liabilities are obligations of entity .
	Completeness	All assets, liabilities & equity interests that should have recorded are recorded
	Valuation and allocation	Assets, liabilities, & equity interests are included in the FS at appropriate amounts & any resulting valuation or allocation adjustments are appropriately recorded
Presentation & Disclosure	Assertions about Presentation & Disclosure-	
	Occurrence & rights & obligations	Disclosed events, transactions, & other matters have occurred & pertain to the entity .
	Completeness	All disclosures that should have been included in FS have been included .
	Classification & understandability	Financial information is appropriately presented & described, & disclosures are clearly expressed .
	Accuracy & valuation	Financial & other info are disclosed fairly & at appropriate amounts

➤ Possible potential misstatements - Indicators

Completeness (Not recorded)	- Transactions not identified <u>Source documents</u> not prepared <u>Source documents</u> not captured. - Rejected <u>source documents</u> not represented
Existence (Dummy recorded)	- Fictitious or unauthorised transactions entered on <u>source documents</u> <u>Source documents</u> overstated. - Transactions duplicated on <u>source documents</u> - Capture of <u>source documents</u> duplicated - Invalid <u>source documents</u> captured on subsidiary ledgers
Recording (Inaccurate)	<u>Source documents</u> captured inaccurately. - Processing of <u>transactions</u> is inaccurate.



	Inaccurate adjustments made in subsidiary ledgers.
Cut-Off Procedures	<u>Transactions</u> occurred in one period are recorded in another period.

➤ Steps for Risk Identification

Q4. Engmnt team is seeks your advice regarding steps for risk identification. Elaborate. **(Imp)**

1. Assess the **significance of the assessed risk**, **impact** of its occurrence and also **revise the materiality** accordingly for the specific account balance
2. Determine the **likelihood for assessed risk** to occur and its impact on our auditing procedures
3. **Document the assertions** that are affected
4. Consider the **impact of the risk** on each of the **assertions**
5. (**Completeness, existence, accuracy, validity, valuation and presentation**) relevant to the account balance, class of transactions, or disclosure
6. Identify the **degree of Significant risks** that would require separate attention and response by the auditor. Planned audit procedures should directly address these risks.
7. **Enquire** and document the **management's response**
8. 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
9. Consider **any unique characteristics** of the risk.
10. 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
 [Examples: High value inventory, complex contractual agreements, absence of a paper trail on certain transaction streams or a large percentage of sales coming from a single customer]

➤ Risk Based Audit (RBA) **(IMP)**

Define:	- Audit should be risk-based or focused on areas of greatest risk to achievement of the audited entity's objectives (as no need to perform all procedures on all area, only require for risky area) - It is an approach to audit that analyses audit risks Sets materiality thresholds based on audit risk analysis & Develops audit programmes that allocate larger portion of audit resources to high-risk areas Focuses primarily on the identification & assessment of the F.S. misstatement risks
Essential element:	Risk Based Audit is an essential element of Financial Audit , both in • Attest audit of the FS & • in the audit of financial systems and transactions including evaluation of IC.
Performance Audit:	In context of performance audit (it is the risk to delivery of an activity or scheme or programme of the entity with economy, efficiency and effectiveness . <u>Awareness of areas that puts the programme or resources at risk</u> from the point of view of EEE helps focus audit attention on them. The risk analysis provides a framework for assurance in performance auditing.
Audit Risk Analysis:	Auditor should perform analysis of audit risks that impact auditee before undertaking specific audit procedures . Risk assessment is subjective process & professional judgment of auditor. The auditor has the responsibility to plan and perform the audit to obtain reasonable assurance about whether the FS are free of MMS , whether caused by error or fraud .



	Audit risks are brought about by error and fraud: <table border="1"> <tr> <td>Error:</td><td>Error is an unintentional mistake (may arise from an <u>error in principle</u>, <u>estimate</u>, <u>critical information processing</u>, <u>FR process</u> or <u>disclosure</u>.)</td></tr> <tr> <td>Fraud:</td><td>It's intentional misstatement (<u>manipulation</u>, <u>falsification</u> of a/cing records, or <u>misrepresentation</u> in the FS of events or <u>misapplication</u> of a/cing principles or funds.</td></tr> </table>	Error:	Error is an unintentional mistake (may arise from an <u>error in principle</u> , <u>estimate</u> , <u>critical information processing</u> , <u>FR process</u> or <u>disclosure</u> .)	Fraud:	It's intentional misstatement (<u>manipulation</u> , <u>falsification</u> of a/cing records, or <u>misrepresentation</u> in the FS of events or <u>misapplication</u> of a/cing principles or funds.		
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General Steps:	Q5. Steps required by statutory audit for risk based and focused on areas of greatest risk to the achievement of company's objectives. <u>Or General Steps for Risk based audit</u> The auditor's objective in a risk-based audit is to obtain reasonable assurance that no material misstatements whether caused by fraud or errors exist in the F.S. This involves the following three key steps: • Assessing the ROMM in the F.S. • Designing and performing further audit procedures that respond to assessed risks and reduce the ROMM 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.						
<u>Distinct phases of RBA:</u>	<table border="1"> <tr> <td data-bbox="305 877 483 1392"> Risk assessment Phase (Less Imp) </td><td data-bbox="483 877 1523 1392"> Q6. Discuss steps to be taken for risk assessment phase of the audit. [Old] <u>Risk assessment phase of the audit involves the following steps:</u> • Performing client acceptance or continuance procedures (SA 220/300) • Planning the overall engagement (SA 300) • Performing risk assessment procedures to understand the business and identify inherent and control risks. (SA 315) • Identifying relevant I.C procedures & assessing their design & implementation (SA 315) • Assessing ROMM in the F.S. (SA 315) • Identifying the significant risks that require special audit consideration and those risks for which substantive procedures alone are not sufficient • Communicating any material weaknesses in the design and implementation of internal control to Mgmt. & TCWG (SA 265) • Making an informed assessment of the ROMM at FS level & at assertion level </td></tr> <tr> <td data-bbox="305 1392 483 1612"> Risk response </td><td data-bbox="483 1392 1523 1612"> Design & perform further audit procedures that respond to assessed ROMM & will provide evidence necessary to support the audit opinion. Audit procedures designed to address the assessed risks could be mixture of: • Tests of the operational effectiveness of internal control • Substantive procedures such as tests of details & analytical procedures. </td></tr> <tr> <td data-bbox="305 1612 483 1824"> Reporting </td><td data-bbox="483 1612 1523 1824"> Assess the audit evidence obtained & determine whether it is sufficient & appropriate to reduce the ROMM in the F.S. to an acceptably low level. <u>When all procedures have been performed and conclusions reached:</u> • Audit findings should be reported to management & TCWG • Audit opinion should be formed </td></tr> </table>	Risk assessment Phase (Less Imp)	Q6. Discuss steps to be taken for risk assessment phase of the audit. [Old] <u>Risk assessment phase of the audit involves the following steps:</u> • Performing client acceptance or continuance procedures (SA 220/300) • Planning the overall engagement (SA 300) • Performing risk assessment procedures to understand the business and identify inherent and control risks. (SA 315) • Identifying relevant I.C procedures & assessing their design & implementation (SA 315) • Assessing ROMM in the F.S. (SA 315) • Identifying the significant risks that require special audit consideration and those risks for which substantive procedures alone are not sufficient • Communicating any material weaknesses in the design and implementation of internal control to Mgmt. & TCWG (SA 265) • Making an informed assessment of the ROMM at FS level & at assertion level	Risk response	Design & perform further audit procedures that respond to assessed ROMM & will provide evidence necessary to support the audit opinion. Audit procedures designed to address the assessed risks could be mixture of: • Tests of the operational effectiveness of internal control • Substantive procedures such as tests of details & analytical procedures.	Reporting	Assess the audit evidence obtained & determine whether it is sufficient & appropriate to reduce the ROMM in the F.S. to an acceptably low level. <u>When all procedures have been performed and conclusions reached:</u> • Audit findings should be reported to management & TCWG • Audit opinion should be formed
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➤ Internal Control System

Definition, Scope & Limitation:



Q7. Prabhu., wants to develop I.C system. Provide to brief about I.C system & inherent limitations of I.C [Old]

IC System:	- All the policies and procedures adopted by the Mgmt of an entity - To assist in achieving management's objective of ensuring, Orderly & efficient conduct of its business, including adherence to Mgmt. policies, safeguarding of assets, prevention & detection of fraud & error, accuracy & completeness of accounting records, & timely preparation of reliable financial information
Internal Control:	SA 315 defines the system of IC as the process Designed, Implemented and Maintained [DIM] by TCWG, mngt and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting , effectiveness and efficiency of operations, safeguarding of assets, and compliance with applicable laws and regulations.
Scope: [FOIA] (Special Trick :-) 	- 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 - Enabling it to provide reasonable assurance reg. risk & to assist in achievement of objectives. - However, in financial audit, Auditor is primarily concerned with policies and procedures having a bearing on the assertions underlying the FS, As given below: <u>Fundamental to a system of internal control is that it is integral to the activities of the company, not something practiced in isolation:</u> - Facilitates effectiveness & efficiency of Operations - Helps to ensure reliability of internal & external Financial reporting - Assists compliance with Laws & regulations - Helps safeguarding the Assets of the entity → evaluate only those administrative controls which have bearing on reliability of financial records
Limitations : CHUMA-C 	I.C., 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: - The possibility of circumvention of internal controls through Collusion with employees or with parties outside the entity. - The potential for Human error, such as, due to carelessness, distraction, mistakes of judgement and misunderstanding of instructions. - The fact that most IC do not tend to be directed at transactions of Unusual nature. - Manipulations by mngt w.r.t transactions or estimates & judgements required in FS preparation - Possibility that a person responsible for exercising an IC could Abuse that responsibility, for eg., a member of management overriding an internal control. - Management's consideration that the Cost of an internal control does not exceed the expected benefits to be derived.

Above Answer Ends

Accounting Control Objectives:	Q8. Objective of I.C w.r.t Accounting system, List down matters to be ensured by A/cing controls Or, What are control objectives you would like the accounting control system?	
	Accounting Control Objectives: which are sought to be achieved by any a/cing control system are:	
	Transactions	1. Transactions are executed through general or specific mngt authorization 2. All transactions are promptly recorded in an appropriate manner to permit the preparation of financial information & to maintain accountability of assets
	Assets	3. Assets & records are safeguarded from unauthorized access or use



Trick: Transaction should be "proper" "Value" pe "record" karo on "Real" "time" basis + "C.D.S."	4. <u>Assets</u> are verified at reasonable intervals and appropriate action is taken with regard to the discrepancies 5. Whether all transactions are properly posted 6. Whether all recorded transactions are properly valued 7. Whether all transactions are recorded 8. Whether recorded transactions are real 9. Whether all transactions are recorded timely 10. Whether all transactions are properly Classified and Disclosed 11. Whether all transactions are properly Summarized If the response to all the above answer is positive, the auditor would be justified in limiting his account balance tests considerably.
Objective of IC:	1. <u>Transaction</u> is authorized 2. <u>Transaction</u> is reported appropriately 3. Safeguarding of assets from unauthorized use 4. There should be I.C to verify assets physically on periodical basis.
Segregation of duties:	<u>The following functions are segregated:</u> a) Authorization of transactions b) Execution of transactions c) Physical custody of related assets & d) Maintenance of records & documents
Auditor Audit Evidence for IC	<u>When obtaining audit evidence about the effective operation of I.C, the auditor considers :</u> • How they were applied, • by whom they were applied. • The consistency with which they were applied during the period and
Manual elements in internal control:	Use of manual or automated element in I.C also affect manner in which transactions are initiated, recorded, processed & reported, even mix of it can be use based on nature & complexity <u>Manual elements in internal control may be more suitable where judgment and discretion are required such as for the following circumstances:</u> • Circumstances where errors are difficult to define, anticipate or predict • Large, unusual or non-recurring transactions • In changing circumstances that require a control response outside the scope of an existing automated control. • In monitoring the effectiveness of automated controls

Components of Internal Controls: **[MICRA]**

Q9. What are the components of Internal control Framework

Answer:

There are five components of an internal control framework. They are as follows:

- **M**onitoring
- **I**nformation & Communication;
- **C**ontrol Environment
- **R**isk Assessment;
- Control **A**ctivities *[Above answer Ends]*

Control Environment

Q10. The effectiveness of controls cannot rise above the integrity and ethical values of the people who create, administer, and monitor them. Explain.

Answer: [Only Point (a) Communication & enforcement of integrity & ethical values]

(a) Communication & enforcement of Integrity & ethical values:



(IPC-SHAP) (Special Trick :-)	• The <u>effectiveness of controls cannot rise above the integrity & ethical values of the people who create, administer, & monitor them.</u> • Integrity and ethical behavior are the <u>product of the entity's ethical and behavioral standards, how they are communicated, & how they are reinforced in practice.</u> • The enforcement of integrity and ethical values includes, for example, <u>management actions to eliminate or mitigate incentives or temptations that might prompt personnel to engage in dishonest, illegal, or unethical acts.</u> • Communication of entity policies on integrity & ethical values may include communication of behavioral standards to personnel through policy statements & codes of conduct & by example. (b) Participation by TCWG: entity's control consciousness is influenced significantly by TCWG. (c) Commitment to competence: Competence is the <u>knowledge & skills</u> necessary to accomplish tasks that define the individual's job (d) Organisational Structure: Establishing a relevant organizational structure includes considering key areas of authority & responsibility & <u>appropriate lines of reporting.</u> (e) Human resource policies & practices: example, standards for recruiting the most qualified individuals, Promotions driven by periodic performance appraisals demonstrate the entity's commitment to the advancement of qualified personnel to higher levels of responsibility. (f) Assignment of Authority & responsibility: The assignment of authority & responsibility may include policies relating to appropriate business practices, <u>knowledge & experience of key personnel</u>, & resources provided for carrying out duties.. (g) Management's Philosophy & operating style: Management's philosophy & operating style encompass a broad range of characteristics.
Risk assessment Process of ENTITY (Not Auditor)	Q11. Briefly describe the various <u>stages of a Risk Assessment process</u> [OLD] Answer: For FR purposes, the entity's RAP includes how mngt identifies business risks relevant to FS preparation as per applicable FRF, estimates their significance, <u>assesses the likelihood of their occurrence</u>, and decides upon <u>actions to respond to and manage</u> them and the results thereof. Risk Assessment is one of the critical <u>components of Enterprise Risk Management</u>. RAP involves considerations for <u>qualitative and quantitative factors</u>, definition of key performance and risk indicators, risk appetite, risk scores, scales and maps, use of data & metrics and benchmarking. <u>The various stages in a Risk Assessment process are as follows:</u> • Define Business Objectives and Goals; • Identify events that affect achievement of business objectives; • Assess likelihood and impact; • Respond and mitigate risks; • Assess residual risk.
Control Activities (Trick: Review karo Information & Physical asset me SOD hai n)	Control activities are <u>policies & procedures that help ensure management directives are carried out</u> 1. <u>Performance reviews:</u> Reviews and analyses of actual performance Vs. budgets, forecasts etc. 2. <u>Information processing:</u> Application controls, apply to the processing of individual applications (i.e., Edit Check of input data, manual follow up for exception report), and <u>general IT-controls</u>, which are policies & procedures that relate to many applications (i.e., Program Change controls) 3. <u>Physical controls</u> : (i) Physical security of <u>Assets & records</u>, (ii) <u>Periodic count</u> & comparision with Control A/c, (iii) Authorization for access to <u>computer program/files</u>. 4. <u>Segregation of duties</u>
Info. & Commun.	The <u>Information system relevant to financial reporting objectives</u>, which includes the financial reporting system, encompasses methods and records that:



[Transaction Hoa tha (identify) ? > Kab hoa tha ? Kitne ka hoa tha ? Properly present & Classify karo]

- Identify and record all valid transactions.
- Determine the **time period** in which transactions occurred to permit recording of transactions in the proper accounting period.
- Measure the **value of transactions** in a manner that permits recording their proper monetary value in the FS.
- Present properly** the transactions and related disclosures in the financial statements.
- Describe on a timely basis the transactions in sufficient detail to permit **proper classification** of transactions for financial reporting

Monitoring

- Management's monitoring of controls includes considering whether they are operating as intended and that they are modified as appropriate for changes in conditions
- The overall systems of internal control comprises of:
 - ✓ Administrative Control and **Accounting Controls**,
 - ✓ **Internal Checks** & [Explained Below]
 - ✓ **Internal Audit** are important constituents of Accounting Controls. [Explained Below]

Q12. Audit of various IT controls on data centre, network operation, application controls. → which I.C component its is ? → give example other 2 activities of above component of I.C [OLD]

Hint: it's General IT Control & Application control → "**Control Activities**", Now explain "**Performance Reviews**" & "**Physical Control**" (as mention in above notes of "**CONTROL ACTIVITIES**")

Q13. I.C. of Budgeted target sales compared with Actual Performance:: = It's **Control Activities (Performance review)** (i.e., review & analyses of actual performance vs budgets/forecasts → operational/financial data) → analyses of the relationships & investigative and corrective actions

➤ **Circumstances in which Risk can Arise or Change (Part of Entities RAP)**

Q14. Entity RAP include how mngt identified business risk relevant to FS → In which circumstances Risk can arise or Change ?

Trick (Hindi) : aqar **Growth** karni hai, Chaae India ho yaa **Foreign** to **New Product** banaane padenge, uske liye **New Technology** & **New bande** chahiye.

Entity's Risk Assessment Process: Risks can arise or change due to circumstances such as the following

- Rapid growth:** Significant and rapid expansion of operations can strain controls and increase the risk of a breakdown in controls
- Expanded foreign operations:** The expansion or acquisition of foreign operations carries new and often unique risks that may affect IC, for example, additional or changed risks from foreign currency transactions.
- 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
- New personnel:** New personnel may have a different focus on or understanding of internal control
- New technology:** Incorporating new technologies into production processes or information systems may change the risk associated with internal control.
- New or revamped info. systems:** Significant & rapid changes in info. systems can change the risk w.r.t IC
- Changes in operating environment:** Changes in the regulatory or operating environment can result in changes in competitive pressures and significantly different risks
- 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
- New A/cing pronouncements:** Adoption of New / Change in A/cing principles may affect risks in preparing FS

Points to Note (For MCQ's & Case scenerios)

- An auditor's judgement of → **what is SAAE** → **is affected by degree of risk of misstatement.**



- Obtain A. Evidence through TOC → to support any assessment of control risk which is less than high
- The lower the assessment of control risk, → more the evidence auditor should obtain that accounting and IC systems are suitably designed and operating effectively.
- **Deviations** from prescribed controls may be caused by such factors as changes in key personnel, significant seasonal fluctuations in volume of transactions and human errors. When deviations are detected the auditor makes specific inquiries regarding these matters, particularly, the timing of staff changes in key I.C functions. The auditor then ensures that TOC appropriately cover such a period of change or fluctuation.
- **Based on TOC Result (If Deviation)**, evaluate whether IC's are designed & operating as contemplated in the preliminary assessment of control risk. → deviations may result in the auditor concluding that → assessed level of control risk needs to be revised. → In such cases, → modify the NTE of substantive procedures.
- **Different controls used at different times during the period** → the auditor would consider each IC separately → breakdown in IC's for a specific portion of period requires separate consideration of the NTE of the audit procedures to be applied to the transactions and other events of that period
- **When to review I.C:** Deciding the point of time appropriate for undertaking the review of the I.C. is a matter for judgement (based on Size & complexity of operation), because of his continuing relationship he may just review the changes that have taken place in the intervening period → Can do comprehensive review in 3 Yrs
- **I.C Operating Good assumption:** The auditor's preliminary evaluation of I.C should be made on the assumption that the controls operate generally as described.

➤ Internal Check System [Monitoring of Control - Component of IC]

Definition:	Internal check system implies arranging of overall system of book-keeping & arrangement of Staff duties in such a way that no one person can carry through a transaction & record every aspect thereof.	
Objectives: <i>Business ki asset me fraud nahi ho, uske liye staff responsible hoga</i>	The following are the objectives of the internal check system: 1. To protect integrity of business by ensuring that A/c's are always subject to proper scrutiny 2. To prevent & avoid the misappropriation or embezzlement of cash and falsification of A/c's. 3. To detect error and frauds with ease 4. To avoid and minimize the possibility of commission of errors and fraud by any staff. 5. To increase the efficiency of the staff working within the organization. 6. To locate the responsibility area or the stages where actual fraud and error occurs	
General condition to the internal check system:	Q15. Reg. I.C of Sales dept → noticed Following, → do you think Work division is proper: (1) An officer was handling the sales ledger & cash receipts → should Not be handled by same person (2) Another official was handling dispatch of goods & issuance of Delivery challans → Delivery challans should be verified by authorised official, other than officer handling dispatch of goods (3) One more officer was there to handle customer and issue of receipts Further, you are required to briefly discuss general condition pertaining to the internal check system. Answer: → Internal Check System: general condition pertaining to the internal check system:	
(Special Trick :-)	Custody of Asset	(i) Persons having physical custody of assets must not be permitted to have access to the books of accounts
	Independent control	(ii) 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.
	Distribution of Power	(iii) 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.
	Updating	(iv) Timely Updation of Internal Controls



Job rotation	(v) Staff duties should be rotated from time to time so that members do not perform the same function for a considerable length of time.
Asset Control	(vi) There should exist an accounting control in respect of each class of assets , in addition, do periodical inspection to establish their physical condition.
Inventory count	(vii) For inventory taking, at close of the year , trading activities should, if possible be suspended, should be done by staff of several sections of organization.
Leaves encourag	(viii) Every member of staff should be encouraged to go on leave at least once a year .
Cash	(ix) Mechanical devices should be used, where ever practicable to prevent loss or misappropriation of cash
Budgetary Control	(x) Budgetary control should be exercised & wide deviations observed should be reconciled.

Q16. Hospital facing Pilferage in inventory, **Person in charge of inventory Outflow/Inflow (Stores)** is also responsible for **Purchase & Maintaining inventory**. Which System of Control Violated ?
Hint: Refer above notes "**Definition**" of **Internal check system** → it includes SOD or maker/checker has been Violated (also Above notes → "**General condition to the Internal Check system**")

Q17. General condition w.r.t Internal check violated in below situation :: (below is Answer)
a) **Procurement head can't have complete control over Purchase, receive goods, approve payment.**
b) **No staff rotation for 5 years** violates principle that staff duties should be rotated periodically
c) principle violated → Mr A have **physical custody of Inventory & Inventory records** (physical custody of assets should not have access to accounting records)

Effectiveness of Internal Check Depends on:

(Trick: CA-DS)

Q18. State the considerations on which effectiveness of an efficient system of internal check depends. [Old]

Considerations for the effectiveness of a System of Internal Check: The effectiveness of an efficient system of internal checks depends on the following considerations:

- Clarity of responsibility** - The **responsibility of different persons** engaged in various operations of business transactions **should be properly identified**.
- Appraisal** - **Periodic review** should be made of the chain of operations and flow. Such process may be carried out by preparing an audit flow chart.
- 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.
- Standardization** - **entire process of accounting should be standardized** by creating suitable **policies** commensurate with the nature of business, to strengthen system of internal checks

➤ Internal Audit [Monitoring of Control - Component of IC]

Q19. Purchase of raw material → takes 3-4 days to reach at plant. As per, I.C → Purchase booked in system from date of Invoice. How you would deal with above matter as internal auditor of the company

Hint: I.Audit involve → continuous & critical appraisal of entity to suggest improvement & add values to strengthen Governance (including risk mngt & I.C) → Also involve evaluating I.C to provide assurance to mngt regarding DIM of effectiveness of control.

Given Situation → give Distorted picture of Stock (as goods could be in Transit) → so **Design of I.C itself Faulty** (can have implication w.r.t GST laws also) → ask mngt to correct it.

➤ Internal control Assessment & evaluation

Standard Operating Procedures (SOPs): (Trick: Job at IT company is risky)

Q20. Auditor concerned about effectiveness of I.C. and wants to assess & evaluate the control environment.



Towards achieving his objective, he seeks your help in knowing the **Standard Operating Procedures (SOPs)** of assessment and evaluation of control

Standard Operating Procedures (SOPs): A well-defined set of SOPs helps outline role, responsibilities, process and controls. This ensures that operating controls are clearly communicated to all touch points of a process. SOPs promote consistent application of controls even during employee turnover, reducing the risk of disruptions

- (i) **Job Rotation in Sensitive Areas:** Any job carried by the same person over long period, is likely complacency & possible misuse in sensitive areas. Job rotation is regularly followed to avoid degeneration of controls. (eg. If continuously purchasing from same vendor, for long period, may due to comfort, do not ask for quotations)
- (ii) **Segregation of Job Responsibilities:** Segregation of duties is an important element of control such that **no two commercial activities should be conducted by the same person.**
- (iii) **Document the Delegation of Financial Powers:** delegation of financial & other powers to employees. A **clearly defined delegation of powers** allows controls to be clearly operated without being dependent on individuals.
- (iv) **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**. For example, at the stage of customer invoicing, application of correct rates in invoices or credit control can all be exercised directly through IT system improving control environment.
- (v) **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 are likely to be few.

Techniques of evaluation of Internal control:

Question-naire:	- Audit firms have developed their own standardised IC questionnaire on 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 & detection of its weakness. - A questionnaire usually consists of several separate sections devoted to areas such as purchases, sales, trade receivables, trade payables, wages, etc. - Questionnaire is filled by the company executives who are in charge of various areas. - 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. (No will reflect weakness in IC). - For the 1st year of engagements, issue of questionnaire is necessary. For subsequent years: May request client to confirm whether any change in the nature and scope of business has taken place (however make practice to issue Questionnaires after specific time period even if no change, lets say 3 yrs)

Q21. In the use of **standardized Internal Control Questionnaire (ICQ)**, **certain basic assumptions** about elements of a **good I.C system** are taken into account. **List down few such assumptions.**

Answer:

Basic Assumption about Elements of Good Control in Standardized I.C Questionnaire: In the use of standardized ICQ, certain assumptions about elements of good control are taken into account.

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



(vii) Certain procedures in general used by most business concerns are essential in achieving reliable IC. This is a **time-tested assumption**. **Deposit into bank of the entire receipts of a day or daily balancing of the cash book and ledgers** or periodic reconciliation with the control accounts are examples of widely used practices which are considered good I.C practices.

Check List

- Series of **instructions** /questions **on IC which auditor and his staff must follow/** answer
- The auditor initials the **space opposite the instruction**
- Question-Answer generally **'Yes', 'No' or 'Not Applicable'** is entered opposite question

Basic distinction between internal control questionnaire and check list are as under:

	Questionnaire	Check list
No of Questions	The ICQ incorporates a large number of detailed questions	Check list generally contains <u>questions relating to the main control</u> objective with the area under review.
Weakness	Weaknesses are highlighted by the 'No'	In Check list, it is indicated by 'Yes' .
In Case of "No"	The significance of 'No' in an ICQ does indicate a weakness but the significance of that weakness is not revealed automatically. (No Detail require in case of weakness)	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.
Who prepare	In ICQ, questions are usually answered by company executives	required to be answered by auditor/auditor staff .

Flow Chart:

Q22. Explain briefly the Flow Chart technique for evaluation of the Internal Control system.

- The flow-charting technique can also be resorted to for evaluation of the internal control.
- It is a **graphic presentation** of IC 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, especially 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. 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.

Properly drawn up flow chart can provide a neat visual picture of the whole activities of section or department involving flow of documents & activities. More specifically it can show :

- At what point** a document is **raised** internally or received from external sources;
- The **number of copies** in which a document is raised or received;
- Distribution** of the documents to various sections, department or operations;
- Filing** of the documents; and
- Final **disposal** by sending out or destruction
- Checking authorisation and matching at relevant stages;

Drawing of a flow chart - A flow chart is **normally a horizontal one** in which documents and activities are shown to flow horizontally from section to section and the concerned sections are shown as the vertical column heads; **in appropriate cases an individual also may be shown as the vertical column head**. Care should be taken to see that the first column head is devoted to the section or the



	individual wherefrom a transaction originates and the placements of other column heads should be in the order of the actual flow of the transaction.
Letter of Weakness:	Refer SA 265

➤ International Internal Control Frameworks:

1. Internal Control - Integrated Framework issued by Committee of Sponsoring Organizations of Treadway Commission (**COSO Framework**).
2. Guidance on Assessing Control published by Canadian Institute of CA (**CoCo**)
3. Control Objectives for Information & Related Technology (**COBIT**)
4. Internal Control- Guidance for Directors on Combined Code, published by Institute of CA in England & Wales (**known as Turnbull Report**).
5. **Sarbanes-Oxley Act** Sec-404

COSO:

Q23. Explain Integrated framework issued by Committee of the Sponsoring Organisations of the Treadway Commission (**COSO Framework**), it's **5 components** & **3 objectives** [OLD]

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 **20 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.

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: (CRO)**

(Special Trick :-)

- **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 A.S.
- **Reporting Objectives** - related to **internal & 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.
- **Operations Objectives** - related to the **effectiveness and efficiency of the entity's operations**, including operational and financial performance goals, and safeguarding assets against loss.

Guidance Note on Audit of Internal Financial Controls Over Financial Reporting (IC-FR)

ICAI has issued a Guidance Note on Audit of IC-FR which covers aspects such as Scope of reporting on internal financial controls (IFC) under **Co.Act 2013**.. The Guidance Note states as below:

"To state whether a set of FS presents a true and fair view, it is essential to benchmark and check the FS for compliance with the FRF"

➤ Residual Topics Question

Q24. **five entertainment centers** (Cash Collections). Specify adequate system towards money collection (SM)



Answer:

Control System over Selling and Collection of Tickets:-

- (i) **Printing of tickets:** Serially numbered pre-printed tickets should be used and designed in such a way that any type of ticket used cannot be duplicated by others in order to avoid forgery. The separate series of the serial should be used for such denomination.
- (ii) **Ticket sales:** The sale of tickets should take place from the Central ticket office at each of the 5 centres, preferably through machines. There should be proper control over the keys of the machines.
- (iii) **Daily cash reconciliation:** Cash collection at each office & machine should be reconciled with the no. of tickets sold. Serial number of tickets for each entertainment activity will facilitate the reconciliation
- (iv) **Daily banking:** Each day's collection should be deposited in the bank on next working day of the bank. Till that time, the cash should be in the custody of properly authorized person preferably in joint custody for which the daily cash in hand report should be signed by the authorized persons
- (v) **Entrance ticket:** Entrance tickets should be cancelled at the entrance gate when public enters the centre
- (vi) **Advance booking:** the system should ensure that all advance booked tickets are paid for
- (vii) **Discounts and free pass:** The discount policy, such that the concessional rates, say, for group booking should be properly authorized and signed forms for such authorization should be preserved
- (viii) **Surprise checks:** Internal audit system should carry out periodic surprise checks for cash counts, daily banking, reconciliation and stock of unsold tickets etc.

Q25. Prepare Checklist for Question to test I.C over Cash/bank (ICFR report), whether ICFR involve testing transaction required only at Balance sheet date (Old)

Hint: Test transaction During the FY (not only at B/S date), However extent of testing near B/S date is higher.

Have you checked that the Cashier → (i) Not authorise any **ledger** (ii) not responsible for opening **Incoming mail** (iii) Not authorise any **expenditure/receipt** (iv) not sign **cheques** (v) take annual leave **regularly**

Q26. Many purchase were without Purchase Orders (PO), and Few PO's were validated after actual purchase, and No reco. Of goods received vs ordered. explain A.procedures to address validity of A/c balance level (SM)

Answer → Audit Procedures: The following procedures may address the validity of the account balance:

- (i) **Review Vendor listing** along with the ageing details. Follow up the material amounts paid before the normal credit period and analyse the reasons for exceptions.
- (ii) Make a **selection of the purchases**, review correspondence with the vendors, purchase requisitions (internal document) and reconciliations of their accounts.
- (iii) **Meet** with the company's **Purchase officer** and obtain responses to our inquiries regarding the purchases made without purchase orders
- (iv) **Discuss** the **summary** of such issues **with the client**

SA 265 – Communication Deficiency In Internal Control To TCWG And Mnqt.

Auditor's Responsibilities	- It is not the responsibility of the auditor to identify each and every Deficiency in Internal Control and express an opinion on it. - His responsibility is "To communicate any significant deficiency in Internal Control identified during audit to management/TCWG. - Auditor identify Deficiency in IC when doing risk assessments, in order to design audit procedures, but not for the purpose of expressing an opinion on effectiveness of I.C
Requirement	- If the auditor has identified one or more deficiencies in IC, the auditor shall determine, on the basis of the audit work performed, whether, individually or in combination, they constitute significant deficiencies. - Communicate in writing significant deficiencies in internal control identified during the



	audit to TCWG on a timely basis - Auditor may Communicate orally before communicating in writing. If deficiency already communicated earlier not resolved → In Current Yr communication → Again repeat that description Or Just give reference of previous communication	
Meaning of:	Deficiency in IC:	(i) A control is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct , misstatements in the F.S on a timely basis or, (ii) A control necessary to prevent, or detect and correct , misstatements in the FS on a timely basis is missing
	Significant deficiency in IC:	A deficiency or combination of deficiencies in internal control that, in the auditor's professional judgment , is of sufficient importance to merit the attention of TCWG . It includes both: - Misstatement Actually Occurred Not Actually occurred, But likelihood that a misstatement could occur & potential magnitude of the misstatement
Written communication of significant deficiencies in IC include:	The auditor shall include in the written communication of significant deficiencies in IC: - A Description of the deficiencies and an explanation of their potential effects; and Sufficient information to enable TCWG & mngt to understand the context of the communication. In particular, the auditor shall explain that: - The purpose of the audit was for the auditor to express an opinion on the FS; - The audit included consideration of I.C. relevant to the preparation of FS in order to design audit procedures that are appropriate in the circumstances, but not for purpose of expressing an opinion on effectiveness of I.C; and - Matters being reported are limited to those deficiencies that auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to TCWG	
When to Communicate	Listed Entities: Before date of approval of FS Other entities: Before assembly of audit file (60 days from the date of A.Report)	

➤ Drafting Letter of Weakness:

Material weaknesses are defined as **absence of adequate controls on flow of transactions that increases the possibility of errors and frauds** in the financial statements of the entity.

The auditor should **communicate such material weaknesses to the mngt or audit committee, → timely basis**. This communication should be, **preferably, in writing**

It will relief auditor from his Liability, when he informed mngt/TWCG of suspected fraud

Q27. Auditor noticed material weaknesses in the IC system & he wishes to communicate it to mngt. elucidate the **important points**, auditor should **keep in the mind while drafting the letter of weaknesses in I.C** system.

Answer: As per SA 265, the auditor shall include in the written communication of significant deficiencies in IC:

- Description of the deficiencies** and an explanation of their potential effects; and
- Sufficient information to enable TCWG and mngt to understand the context of the communication.**

auditor should communicate material weaknesses to mngt or audit committee, if any, on a timely basis. should be, preferably, in writing through a **letter of weakness or mngt letter**. **Important points w.r.t such letter are follows:**

- The **letter lists down the area of weaknesses** in the system and **offers suggestions for improvement**.
- It should clearly indicate that it **discusses only weaknesses which have come to the attention** of the auditor as a result of his audit & that his examination has not been designed to determine the adequacy of



internal control for management.

- (3) This letter serves as a **valuable reference** document for management for the purpose of revising the system and insisting on its strict implementation.
- (4) 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.

Q28. Auditor reviewed I.C. → IC may not be able to capture Insurance premium due → how auditor to deal this.

Hint: Deficiency in IC exist when (1) Control **Unable** to prevent/detect Misstatement (2) Control is **Missing**.

Given case, Possibility of IC may not be able to capture Insurance premium which Due → **Significant Deficiency** (as assets may remain uninsured). → **SA 260:** deficiencies in I.C depends not only on whether a misstatement has **actually occurred, but also** on the **likelihood** → So, Auditor should communicate to TCWG significant Deficiency:

(a) **Description** of deficiency & effect (b) **Sufficient info** to enable TCWG and mgmt to understand

➤ Significant Deficiencies:

Q29. Elucidate various indicators of significant deficiencies to assess the efficiency of I.C system [Old]

Answer: As per SA 265, → indicators of significant deficiencies in I.C include, for example: **[CM-RIPP]**

1. Evidence of **ineffective** aspects of the **Control environment**, such as:
 - a. Indications that significant transactions in which management is financially interested are not being appropriately scrutinised by TCWG.
 - b. Identification of mgmt fraud, whether or not material, that was not prevented by the entity's IC.
 - c. Mngt's failure to implement appropriate remedial action on significant deficiencies previously communicated.
2. Evidence of an **ineffective entity RAP**, such as **Management's failure to identify a ROMM** that the auditor would expect the entity's risk assessment process to have identified.
3. **Absence** of **RAP** within entity where such a process would ordinarily be expected to have been established.
4. Evidence of an **Ineffective response** to **identified significant risks** (e.g. absence of controls over such risk).
5. Disclosure of a MMS due to error or fraud as **Prior period** items in the current year's Statement of P&L.
6. Evidence of **management's inability to oversee the Preparation of the financial statements**.
7. Misstatements detected by auditor's procedures that were not prevented, detected & corrected, by I.C.

Q30. examples of matters to be considered while determining significant deficiency' in I.C. [Old]

Answer: [Koi Bhi Deficiency mili to, uss deficiency ko following chize check karke dekho, ki wo deficiency significant hai ya nahi ?]

[Trick: "**Estimate**" karo ki kitna "**Loss**" ho sakta hai, "**FS Level**" ya "**Account balance level**" pe > and wo Deficiency Ki "**Wajah (cause)**" kya hai, and Future me wapas hone ka kya "**Likelihood**" hai]

As per SA 265, **examples of matters that the auditor may consider in determining whether a deficiency or combination of deficiencies in IC constitutes a significant deficiency** include:

1. The **subjectivity and complexity** of determining **estimated** amount, such as fair value accounting estimates.
2. The **susceptibility to loss** or fraud of the related asset or liability.
3. The **financial statement amounts exposed to the deficiencies**.
4. The **volume of activity** that has occurred or could occur in the **account balance or class of transactions exposed to the deficiency** or deficiencies.
5. The **cause and frequency** of the exceptions detected as a result of the deficiencies in the controls.
6. The **likelihood** of the **deficiencies** leading to **material misstatements** in the FS in the future.
7. The **interaction of the deficiency with other deficiencies** in internal control.
8. **The importance of the controls to the financial reporting process;** for example:
 - a. **General monitoring controls** (such as oversight of management).
 - b. Controls over the **prevention and detection of fraud**.
 - c. Controls over the selection and **application of significant accounting policies**.
 - d. Controls over significant **transactions with related parties**.



- e. Controls over significant transactions outside the entity's normal course of business.
- f. Controls over the period-end financial reporting process (such as controls over non-recurring JV).

➤ Other Integrated Qns:

Q31. Certain weakness in I.C notices by stat Auditor → brought the same to the knowledge of Director (MD) → Next yr huge defalcation happened → mngt want to sue the Auditor for Negligence [Old RTP]
Hint: SA 265 → if deficiency in IC identified, determine whether it's Significant Def. → communicate to TCWG / Mngt on timely basis (writing). (Explain the Given case) → (1) Whether the statutory auditor properly & adequately extended the audit programme w.r.t weakness (if auditor believe Suspected fraud/error can have material effect on Financial Info → Perform Additional procedure → thus, as long as auditor took due care, he can't held liable) (2) matter already brought to MD's attention → it's defense for auditor, now it's mngt responsibility to protect asset

SA 315 - IDENTIFYING AND ASSESSING RISK OF MATERIAL MISSTATEMENT BY UNDERSTANDING ENTITY AND ITS ENVIRONMENT:

Auditor's Objective:	- Identify and assess the ROMM, whether due to fraud or error, a) at the <u>FS</u> and b) <u>Assertion levels</u>. - Through understanding the entity and its environment, including the entity's internal control, - providing a basis for designing and implementing responses to the assessed ROMM. - This will help the auditor to reduce the ROMM to an acceptably low level.	
Business Risk:	A risk resulting from significant conditions, events, circumstances, actions or inactions that could adversely affect an entity's ability to achieve its objectives	
Significant Risk:	An identified and assessed ROMM that requires special audit consideration	
Define: Risk Assessment Procedures	The audit procedures performed to obtain an understanding of the entity and its environment, including the entity's internal control, to identify and assess the ROMM, whether due to fraud or error, at the <u>FS</u> & <u>assertion levels</u> .	
ICAI Examples	At FS Level, If Top accountant Not competent:	it is quite possible that errors could occur in the <u>FS</u> . However, the nature of such errors will not often be confined to a single A/c balance, transaction, Not likely be confined to a single assertion.
	Specific assertions	Assessment of risk should be made for each individual assertion (Completeness, valuation, accuracy etc.) - For <u>Valuation assertion</u>: assess the risk of error in payables as low; however, for inventory obsolescence it's high - For <u>MMS due to completeness</u> (missing item): inventory balance are low, But high i.r.t sales balance

➤ RAP - Identifying & Assessing ROMM

Auditor Shall Assess ROMM at:	a) The financial statement level b) The assertion level for classes of transactions, account balances, and disclosures to provide a basis for designing and performing further audit procedures (SA 330)
To Identify & Assess ROMM, Auditor Shall:	a) Identify risks throughout the process of obtaining an understanding of the entity and its environment and by considering the C/A/DS in the FS; b) Assess the identified risks, whether they relate more pervasively to FS as a whole and potentially affect many assertions;



[Activities/ Process of RAP]	c) Relate the identified risks to what can go wrong at the assertion level d) Consider the likelihood of misstatement , and whether the potential misstatement is of a magnitude that could result in a material misstatement .
RAP is not SAAE	Information obtained by RAP can be used as Audit evidence, Auditor may also perform TOC or substantive procedure along with RAP to inc. efficiency, However RAP evidence are themselves not SAAE to form an opinion

Q32. While commencing Stat audit, what should be consideration to assess ROMM & Response to Such Risk ?
Hint: SA 315 → refer above notes "process of RAP" and SA 330, Auditor response to assessed ROMM as below:

- 1) Consider the **reasons** for the assessment given to the ROMM at assertion level (C/A/DS), including:
 - a) The **likelihood** of MMS due to the particular characteristics of the relevant C/A/DS; and
 - b) Whether the risk assessment takes into account the relevant **controls**, thereby requiring the auditor to obtain audit evidence to determine whether the controls are operating effectively; and
- 2) Obtain more persuasive audit **evidence** the higher the auditor's assessment of risk.

➤ **Misstatement & Material Misstatement (Significant Risk)**

Sources of Misstatement:	1. Omission of F.S. element/ A/c's or Item 2. Omission of Information required to be disclosed 3. Disclosure not as per FRF 4. Difference between management and auditors' judgement 5. Inaccuracy in Data processing 6. Incorrect estimation
Significant Risk / Material Misstatements: (Special Audit consideration) (Example of MMS)	Q33. points that may direct Auditor to judge that the risks identified may be significant. As part of the risk assessment the auditor shall determine whether any of the risks identified are, in the auditor's judgment, a significant risk., In exercising judgment as to which risks are significant risks, the auditor shall consider at least the following: 1. Whether the risk is a risk of fraud; 2. Whether the risk is related to recent significant economic, a/c'ing, or other developments like changes in regulatory environment, etc., and, therefore, requires specific attention; 3. The complexity of transactions; 4. Whether the risk involves significant transactions with related parties; 5. Whether the risk involves significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual. 6. The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; When the auditor has determined that a significant risk exists, the auditor shall obtain an understanding of the entity's controls, including control activities, relevant to that risk.

➤ **Understanding the Entity**

Point to consider while taking Knowledge of Business:	Q34. What points to be considered while evaluating "Knowledge of Business" during audit? [Old] The broad matters to be considered while obtaining knowledge of business for a new audit assignment are set out in SA 315. These are: [IRE + FANO] (i) Relevant industry, regulatory, economic (IRE) & other external factors like applicable FRF. (ii) The measurement and review of the entity's Financial performance. (iii) The entity's selection and application of Accounting policies. (iv) The Nature of the entity, including: a. its operations;

	b. its <u>ownership</u> and governance structures; c. the <u>types of investments</u> that the entity is making and plans to make, including investments in special-purpose entities; and d. the <u>way that the entity is structured and how it is financed</u>; to enable the auditor to understand the C/A/DS to be expected in the financial statements. (v) entity's Objectives & strategies, and those related business risks that may result in ROMM. In addition to the importance of knowledge of the client's business in establishing the overall audit plan, such knowledge helps the auditor to identify areas of special audit consideration, to evaluate the reasonableness both of A/cing estimates and Mngt W.R, & to make judgement regarding the appropriateness of A/cing policies and disclosures.
Sources of obtaining info: (Special Trick :-)	Q35. What are the major sources of obtaining information about the client's business? [Old] Information about the client's business: The auditor can obtain information about client's business from the following sources: Trick: "Newspaper" wagera me Client ke baare me padha, Ki "Economy" usse kse kse Affect kar sakti h: (i) Relevant publications of the ICAI and other professional bodies, industry publication, trade Journals, magazines, newspapers or books (ii) Consideration of the state of the economy and its effects on the client's business; "Fir Client k office jao" & Usse "Discuss" karo Client se & saare "Documents" mango usse: (iii) Visits to the client's premises and plant facilities to the management. (iv) Discussions with the client; (v) The client's annual Reports to shareholders; (vi) Minutes of meetings of shareholders, board of directors and important committees; (vii) Internal financial management report for current & previous periods, including budgets "apne jaan pahchaan wale logo se pucho ki wo client ko jaante h kya" & apne "Old working paper" hai wo dekho: (viii) Firm personnel responsible for non-audit services to the client who may be able to provide information on matters that may affect the audit. (ix) The previous year's audit working papers, and other relevant files;

➤ Internal Control & IT Environment:

Use of IT:	Entity's mix of manual and automated elements in internal control
IT Possess Specific risk in IC:	Q36. IT system poses specific risks to an entity's internal control. Explain Trick: IT Personnel, Data ko, system me daalke, Process karenge 1. Possibility of Information Technology personnel gaining access beyond those necessary to perform their assigned duties thereby breaking down segregation of duties. 2. Unauthorized access to data resulting in destruction of data or improper changes to data. 3. Potential loss of data or inability to access data as required. 4. Failure to make necessary changes to systems/ programs. 5. Unauthorized change to system/ program. 6. Reliance on systems/programs inaccurately processing data or processing inaccurate data. 7. Unauthorized changes to data in Master files 8. Unauthorized or non-existent transactions/ inaccurate recording of transactions 9. Inappropriate manual intervention.
Causes of ROMM in CIS environment:	Q37. A/cing computerized → What areas to look forward for deficiencies & risk identification? Or, Areas Examined for deficiencies & Risk Identification in CIS Environment (Causes of ROMM at CIS Environment) [Old]



	The auditor in accordance with SA 315 should make an assessment of inherent and control risk for material FS assertions. In a CIS environment the risk of a MMS in FS ascertain being erroneously stated could arise from the deficiencies in the following case as: 1. <u>Program</u> developed & maintenance has some defect since inception. 2. <u>System software</u> support is improper. 3. <u>Operations including</u> processing of data are not regulated and ungoverned. 4. Physical <u>CIS security</u> may be lacking. 5. Control over access to specialized <u>utility program</u> is improper. These deficiencies would tend to have a negative impact on all application systems that are processed through the computer
Suitable:	<u>Manual elements</u> in IC may be more suitable <u>where judgment</u> and discretion are required
Reliability:	<u>Manual elements less reliable than automated</u> elements because they can be more easily bypassed, ignored, Error

SA 330 "Responses to Assessed Risks"

Types: Audit Procedure	1. Risk Assessment Procedure (RAP):	To Assess the Risk (SA 315)	
	2. Further Audit Procedure (FAP):	To Respond the Risk (SA 330):	
	<i>i.e.Type of response</i>	a) Compliance Procedure	- Test of Control (TOC)
		b) Substantive Procedure	- Test of Detail (TOD) - Analytical procedure (SAP) [SA-520]
Responses to RMM	At Financial Statement level:	1. Emphasizing to maintain Professional Skepticism. 2. Assigning more experienced staff 3. Providing more supervision. 4. Incorporating additional elements of unpredictability in the selection of Further audit procedures. 5. Making changes to NTE of audit procedures.	
	At Assertion level: [FAP includes: 1) TOC 2) Substantive procedure]	Auditor shall design and perform FAP whose NTE are based on and are responsive to the assessed RMM at the assertion level. In designing FAP to be performed, the auditor shall: (a) Consider the reasons for the assessment given to the ROMM at the assertion level for each C/A/D/S, including: 1. The likelihood of material misstatement due to the particular characteristics of the relevant C/A/DS; and 2. Whether the risk assessment takes into account the relevant controls , thereby requiring the auditor to obtain audit evidence to determine whether controls are operating effectively; & (b) Obtain more persuasive audit evidence the higher the auditor's assessment of risk.	

Test of Control (Compliance Procedure)

Meaning:	TOC are performed to obtain audit evidence about the operating effectiveness of the: a) Design of accounting & internal control System i.e., Whether they are suitably designed to



	prevent or detect & correct MMS b) Operation of IC throughout the period
3 Yrs	Auditor can test IC on a selective basis, but plan testing in such manner that all the important areas are covered in Period of 3 Yrs .
TOC may include:	a) Inspection of documents supporting transactions to gain audit evidence that IC have operated properly, for example, verifying that a transaction has been authorised b) Inquiries and observation of, IC which leave no audit trail, for example, determining who actually performs each function and not merely who is supposed to perform it. c) Re-performance involves the auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal control, for example, reconciliation of bank accounts, to ensure they were correctly performed by the entity. d) Testing of internal control operating on specific computerized applications or over the overall information technology function, for example, access or program change controls
Perform TOC When:	1. Auditor's assessment includes expectation that controls are operating effectively. 2. Substantive procedures alone cannot provide SAAE
Nature & Extent of TOC	<u>In designing and performing test of controls, the auditor shall:</u> 1) Perform Audit procedure in Combination with Inquiry to Obtain audit evidences w.r.t.: - Effectiveness of controls - Consistency of application - By whom & by what means they applied 2) Whether control dependent on Indirect control, these also need to be tested [Inquiry alone is not sufficient to test the operating effectiveness of controls: Inquiry combined with inspection or reperformance may provide more assurance than inquiry & observation]
Timing of TOC	Perform TOC for a <u>particular time</u> Or <u>throughout</u> period (For which auditor's need to rely)
PY TOC Evidence:	<u>Using Audit Evidence obtained during previous audits { i.e Yr 2018 (PY) Evidence regarding TOC using in Yr 2019 (CY) }</u> - If there is any change in control in CY then auditor shall again perform TOC in CY - If there is no such change, auditor shall do TOC in such way that all controls are tested atleast once in a 3 yr
Interim Period TOC Evidence:	<u>Using Audit Evidence obtained in Interim Period:</u> - Obtain audit Evidence for significant changes subsequent to Interim Period. - Determine the additional Evidence to be obtain for remaining period.
Concurrent Audit Re-Test of Controls:	Q38. Whether it's appropriate for auditor to use audit evidence about operating effectiveness of I.C obtained in previous audit Or, factors that may warrant a re-test of controls As per SA 330 → changes may affect the relevance of the audit evidence obtained in previous audits such that there may no longer be a basis for continued reliance. The auditor's decision on whether to rely on audit evidence obtained in previous audits for control is a matter of professional judgment. In addition, the length of time between retesting such controls is also a matter of professional judgment. Factors that may warrant a re-test of controls instead of relying on TOC of previous Yr: [Trick: P-MC-MC] Personnel changes that significantly affect the application of the control. - A significant Manual element to the relevant controls. - A deficient Control environment. Deficient Monitoring of controls. Changing circumstances that indicate the need for changes in the control.
(Special Trick :-)	



	(vi) Deficient general IT-controls.					
Substantive Procedure (TOD & SAP):						
Means:	Substantive procedure is an audit procedure designed to detect MMS at the assertion level. They comprise tests of details and substantive analytical procedures					
Mandatory:	Irrespective of the assessed ROMM , the auditor shall design and perform substantive procedures for each material C,A,DS (At Assertion Level). <u>This requirement reflects the facts that (Why Substantive is mandatory ?):</u> a) auditor's assessment of risk / Risk Assessment is judgmental, may not identify all ROMM; & b) there are inherent limitations to internal control, including management override.					
What to perform:	Depending on the circumstances, the auditor may determine that: a) Performing only SAP will be sufficient to reduce audit risk to an acceptably low level. Eg. where the auditor's assessment of risk is supported by audit evidence from TOC b) Only TOD are appropriate c) A combination of SAP and TOD are most responsive to assessed risks. [Most Effective]					
2 Types: (TOD & SAP)	Q39. what are the substantive procedures to be performed to assess the ROMM (OLD) As per SA 330, → substantive procedure is an audit procedure designed to detect MMS at the assertion level. They comprise TOD and SAP, Substantive procedure comprise of: <table><tr><td>Test of Details: (TOD)</td><td>The <u>nature of the risk and assertion is relevant</u> to the design of TOD: For example, tests of details related to the: <u>Existence or occurrence</u> assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence. <u>Completeness assertion</u> may involve selecting from items that are expected to be included in the relevant FS amount and investigating whether they are included. - In designing tests of details, the extent of testing is ordinarily thought of in terms of the <u>sample size</u>, However, other matters are also relevant </td></tr><tr><td>Substantive Analytical Procedure: (SAP)</td><td> - Substantive analytical procedures generally more applicable to large volumes of transactions that tend to be predictable over time. SA 520,"Analytical Procedures" establishes requirements and provides guidance on the application of analytical procedures during an audit - The application of planned analytical procedures is based on the expectation that relationships among data exist and continue in the absence of known conditions to the contrary. - However, the suitability of a particular analytical procedure will depend upon the auditor's assessment of how effective it will be in detecting a misstatement that, individually or when aggregated with other misstatements, may cause the FS to be materially misstated. - In Some cases, even an unsophisticated predictive model may be effective as an analytical procedure [Eg. When entity have known no. of employees at Fixed Pay → Auditor can estimate payroll by SAP → it reduce need to perform TOD) </td></tr></table>		Test of Details: (TOD)	The <u>nature of the risk and assertion is relevant</u> to the design of TOD: For example, tests of details related to the: <u>Existence or occurrence</u> assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence. <u>Completeness assertion</u> may involve selecting from items that are expected to be included in the relevant FS amount and investigating whether they are included. - In designing tests of details, the extent of testing is ordinarily thought of in terms of the <u>sample size</u>, However, other matters are also relevant	Substantive Analytical Procedure: (SAP)	- Substantive analytical procedures generally more applicable to large volumes of transactions that tend to be predictable over time. SA 520,"Analytical Procedures" establishes requirements and provides guidance on the application of analytical procedures during an audit - The application of planned analytical procedures is based on the expectation that relationships among data exist and continue in the absence of known conditions to the contrary. - However, the suitability of a particular analytical procedure will depend upon the auditor's assessment of how effective it will be in detecting a misstatement that, individually or when aggregated with other misstatements, may cause the FS to be materially misstated. - In Some cases, even an unsophisticated predictive model may be effective as an analytical procedure [Eg. When entity have known no. of employees at Fixed Pay → Auditor can estimate payroll by SAP → it reduce need to perform TOD)
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TOC & Substantive:	Because the assessment of the ROMM takes account of IC, the extent of substantive procedures may need to be increased when the results from TOC are unsatisfactory					
External confirmation as SAP:	Whether E.C. procedures	Q40. factors assist in knowing whether E.C procedures to be performed as SAP. <u>Factors that assist the auditor in determining whether E.C. procedures are to be performed as SAP include:</u>				



	are to be performed as SAP: (saamne wale ko aata bhi hai .. iccha bhi hai .. accha bhi h)	(i) The confirming party's knowledge of the subject matter - responses may be more reliable if provided by a person at the confirming party who has the requisite knowledge about the information being confirmed. (ii) The ability or willingness of the intended confirming party to respond - for example, the confirming party: • May <u>not accept responsibility</u> for responding to a confirmation request; • May consider responding <u>too costly or time consuming</u>; • May <u>concerns about the potential legal liability</u> resulting from responding; • May account for <u>transactions in different currencies</u>; or • May operate in an environment where responding to confirmation requests is not a significant aspect of day-to-day operations • In such situations, confirming parties may not respond, may respond in a <u>casual manner</u> (iii) The objectivity of the intended confirming party - if the confirming party is a related party of entity, responses to confirmation requests may be less reliable.
	Cases where E.C used:	This part of SA 330 is discussed in SA 550 (i.e., Bank confirmation, Trade receivable confirmation etc.)

Q41. Auditor **assessed ROMM as Low**, and **satisfactory I.C.** → despite this he **Chose to send External Conf.** (SM)
Hint: SA 330 states → **irrespective of the assessed ROMM** → **design & perform substantive procedures.**
SA 330 further states that auditor shall **consider whether E.C procedure are to be follows as Substantive P.**
Despite auditor assessed ROMM as low, perform substantive procedures, Due to Following Reason:
(1) assessment of Risk is **judgmental**, so **may not identify all ROMM** **(2)** There are **Inherent Limitation of I.C.**
→ it's also in accordance with spirit of **Professional Skepticism** (So above approach is correct)

Q42. While **responding ROMM of Identified Related Party**, auditor decide to **rely on I.C.**, → (a) Guide auditor reg. **necessity of TOC** to obtain SAAE (b) can he use **Evidence of Interim period reg. effectiveness of I.C** (Old)
Hint: **SA 550** → Auditor should **Desing & perform FAP** to obtain SAAE about ROMM of RPR
SA 330 → Refer Above Notes: "**Test of Control**" → in that topic, Mention → **(a) Perform TOC when (b) Timing of TOC (c) Interim Period TOC Evidence**

➤ **Other Integrated Qns:**

Q43. Auditor undertook **risk assessment** and found **detection risk can-not be reduced to acceptance level** (Old)
Hint: **SA 315 & 330** → Obtain understanding of IC, Audit risk & it's component (Inherent Risk, Detection risk)
• Use professional **judgement** to assess audit risk and **design A.procedure to reduce to acceptably low level.**
• **(Define "Detection Risk")** & Both **Inherent & control risk assessed as High**, so **considered whether Substantive procedure can provide SAAE to reduce detection risk to acceptably low level**
• If it can-not reduced to acceptable level → Express **Qualified or Disclaimer opinion**

SA 320- Materiality in Planning & Performing an Audit

About Audit Materiality	If Materiality is specified in FRF or Law, then auditor shall consider that, otherwise consider below 3 points: Material items are relatively important items i.e., the knowledge of which would influence the decisions of the users of financial statements 1. Misstatement whether individually or aggregate could reasonably / Item is material if it influences economic decision of users in FS 2. Determination of materiality is a matter of professional judgments. (Judgement about



	materiality are affected by Size or nature of misstatement) 3. Judgments about matters that are material are based on a consideration of the common financial information needs of users as a group
Other Points Reg. Materiality:	1. Auditor considers materiality at overall FS level and assertion level. 2. Materiality could be either quantitative or qualitative. 3. Sometimes statutory provisions also contain element of materiality (i.e., S-III). Materiality is not always a matter of relative size. For example, a small amount lost by fraudulent practices of certain employees can indicate a serious flaw in ICS
Determine materiality For:	- FS as a Whole - For particular C/A/DS (When auditor consider that Particular CADS misstatement can influence economic decision for amt lower than materiality)
Materiality Applied at all stages:	The concept of materiality is applied by the auditor: planning and performing the audit - evaluating the effect of misstatements on the audit - forming the opinion in the auditor's report
Performance Materiality	The amount set by auditor at less than materiality for F.S as a whole - To reduce to an appropriately low level - The probability that the aggregate of the uncorrected & undetected misstatement - Exceeds materiality for F. S. as a whole
Revision of materiality as the audit progresses (ICU)	- On becoming aware of new Information, or - Significant changes in Circumstances, or - Changes in Understanding of entity If auditor concludes that Lower materiality than initially determined → Conclude whether → need to: Revise Performance Materiality - Whether NTE of FAP remain appropriate

➤ Benchmark for deciding Materiality:

Q44. Factors that may affect the identification of an appropriate benchmark and for below Companies engaged in:
(i) **Manufacturer of A.C, regular profits** (ii) **infrastructure projects & incurred in last 2 FY, due to pandemic**

SA 320 → prescribes the use of Benchmarks in Determining Materiality for the FS as a Whole.

A percentage is often applied to a chosen benchmark as a starting point in determining materiality for FS as a whole. Factors that may affect the identification of an appropriate benchmark include following: **[A-LOVE]**

- [Modi ji]** Whether there are items on which the **Attention of the users** of the particular entity's financial statements tends to be focused
(eg., for purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets)
- [Adwani]** **nature of the entity**, where entity is at in its **Life cycle**, & the industry and **economic environment** in which the entity operates;
(Eg., If an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings)
- [Amit Shah]** The **entity's Ownership structure** and the way it is financed (for example, if an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings); and
- [Smriti Rani]** The **relative Volatility** of the benchmark.
- [Arul Jaitley]** The **Elements** of the **financial statements** (Eg. assets, liabilities, equity, revenue, expenses);



Examples of Benchmark : i.e., 20% of PBT, 20% of Total revenue, 20% of GP Etc.

Determining a % to be applied to chosen benchmark involves **professional judgment**. There is a relationship between the % and chosen benchmark, i.e., % applied to PBT will normally be higher than a % applied to revenue.

- If SRT manufacture & sale of AC, having regular profits → consider profit before tax /Earnings.
- If SRT construct large infrastructure project & incurred losses → Revenue or Gross Profit as benchmarking
- Entities doing public utility program → Total cost or net cost (expenses less revenues or expenditure less receipts) may be appropriate benchmarks. Where entity has custody of assets, assets may be an benchmark.

4. On becoming aware of new information, or
5. Significant changes in circumstances, or
6. Changes in understanding of entity

If auditor concludes that Lower materiality than initially determined → Conclude whether → need to:

- Revise Performance Materiality

Whether NTE of FAP remain appropriate

Q45. On basis of additional information, wants to re-evaluate Materiality concept, please guide:

Hint: SA 320 → auditor shall determine materiality for FS as a Whole. If there any C/A/DS for which lower misstatement amount then materiality influences Economic decision → determine materiality for particular CADs. In event of becoming aware of Information → revise materiality. , If auditor conclude Lower materiality → then → whether it's necessary to revise Performance materiality & Whether NTE of FAP remain appropriate

CHAPTER 5- AUDIT EVIDENCE

SA 500, 501, 505, 510, 530, 550

SA 500 – AUDIT EVIDENCE:

Definition:	➤ Information used by auditor in arriving at conclusions on which auditor's opinion is based. ➤ Audit evidence includes both: • Information contained in accounting records underlying the FS and • Other information Auditor need SAAE to express. 1. Sufficient = Measure of quantity 2. Appropriate = Measure of quality (Relevance & reliability)
Reliability of AE [GOD-WI]	1. Generated Internally/Externally 2. Original documents-more reliable than mere photocopies 3. Directly obtained- more reliable than obtained indirectly 4. Written documents- more reliable than Oral. 5. Independent Sources- Obtained from outside the entity
Doubt on Reliability of A.E.	• If AE obtained from One Source is Inconsistent from Another, Or • Doubt over reliability of Information to be used as A. evidence Then → Auditor shall Modify or Perform Additional Audit Procedure to resolve the matter.

➤ Management Expert:

Define:	An individual or organization possessing expertise in a field <u>other than a/cing or auditing</u> , whose work in that field is <u>used by the entity to assist the entity in preparing the FS</u> .								
Auditor Shall Evaluate: When information to be used as audit evidence has been prepared using the work of a management's expert, Auditor shall evaluate: [CCO - U - A]									
1) CCO	<u>Evaluate Competence, Capability and Objectivity [CCO] of Expert, by:</u> ✓ Personal Experience with previous work. ✓ Discussion with that expert. ✓ Discussion with others. ✓ Knowledge of expert's qualification, memberships, other forms of recognitions. ✓ Published books or papers. ✓ Auditor's expert.								
2) Understanding	<u>Obtain an Understanding of expert work:</u> ✓ Whether any professional and other standards apply. ✓ Whether expert's has Area of specialty that are relevant to audit. ✓ What Assumption & Method are used by Mgt. expert & whether they are generally accepted in that expert's field & appropriate for Financial Reporting purposes. ✓ Nature of Internal & External source data he uses.								
3) Appropriateness	<u>Evaluate the Appropriateness of Expert work:</u> <table><tr><td>Finding & Conclusion: [ICA-ORR]</td><td>Assumptions & Methods</td><td>Source Data</td></tr><tr><td>Relevance, Reasonableness & Consistency with other A.E.</td><td>Relevance and Reasonableness</td><td>Relevance (reliable) , Completeness and accuracy</td></tr></table>			Finding & Conclusion: [ICA-ORR]	Assumptions & Methods	Source Data	Relevance, Reasonableness & Consistency with other A.E.	Relevance and Reasonableness	Relevance (reliable) , Completeness and accuracy
Finding & Conclusion: [ICA-ORR]	Assumptions & Methods	Source Data							
Relevance, Reasonableness & Consistency with other A.E.	Relevance and Reasonableness	Relevance (reliable) , Completeness and accuracy							



	1. Do Inquiry with mngt expert 2. Take External Confirmation (3rd party) 3. Perform Analytical procedure 4. Observe Procedure applied by expert 5. Re-perform some calculation 6. Reviewing expert working paper 7. Discuss with other expert. etc.	1. Check whether they generally accepted within expert's field 2. Consistent with FRF 3. Whether Dependent on use of specialised models	1. Check Origin of Data (IC Over Data preparation) 2. Reviewing data completeness and internal consistency
NTE of Audit Procedure when Mngt Expert appointed: <i>[Trick: mngt ne usse "kis Kaam" ke liye "employ" hai ... maana ki wo bahot "Expertise", "Experience", hai and "Professional stnd bhi lagte hai .." > " par mngt usse fees deri hai to influence kar hi degi</i>	Q1. Company hired expert → How auditor can use info prepared by Mngt Expert as A.E ? and State matter which may affect NTE of audit procedure (Old) <u>Evaluating the Work of Management's Expert:</u> SA 500 → when info. to be used as audit evidence has been prepared using the work of a mngt expert, the auditor shall: (a) Evaluate the competence, capabilities and objectivity of that expert; (b) Obtain an understanding of the work of that expert; and (c) Evaluate the appropriateness of expert's work as audit evidence for the relevant assertion. <u>NTE of Audit Procedures:</u> SA 500 → NTE of audit procedures to be adopted by an auditor in case of management's expert, may be affected by such matters as: (i) The nature and complexity of the matter to which the management's expert relates. (ii) The nature, scope and objectives of the management's expert's work. (iii) The risks of material misstatement in the matter. (iv) Whether the mngt's expert is employed by the entity, or is a party engaged by it to provide relevant services. (v) The auditor's knowledge and experience of the management's expert's field of expertise. (vi) The auditor's previous experience of the work of that expert (vii) Whether the mngt expert is subject to technical performance standards or other professional or industry requirements. (viii) The extent to which mngt can exercise control or influence over the work of Mngt expert. (ix) The nature and extent of any controls within the entity over the mngt expert's work (x) The availability of alternative sources of audit evidence.		
Evaluate Objectivity of Mngt Expert:	Q2. Sheetal is independent expert → so whether to Evaluate Objectivity of Expert?(SM & MTP) SA 500 → While using audit evidence prepared by mngt expert → Evaluate the competence, capability & Objectivity of expert. • Some Examples of circumstances that may threaten objectivity of expert → self-interest threats, advocacy threats, familiarity threats, self-review threats and intimidation threats. • Safeguards may reduce such threats & may created by external structure (i.e., mngt expert Profession / Regulation) Or, by mngt expert work environment (eg Quality control policies) • But Safeguards can-not eliminate all threat. (Like Intimidation threat is less significance in case expert engaged by company, rather than employed) • Discuss with mngt and that expert any interests & relationships that may create threats to expert's objectivity, Interests and relationships creating threats may include: (i) Financial Interest (ii) Business & personal relationship (iii) Provision of Other Services Audit team shall evaluate objectivity of expert → An expert appointed by the entity cannot ordinarily be regarded as being more likely to be objective than other employees of entity. So, audit partner is correct (Evaluate Objectivity of Expert)		



Q3. Auditor accepted Gratuity liability valuation of Actuary, but Retirement age adopted 65 Yr, against 60 Yr.
Or, How to evaluate work of Actuary? "Or" Whether to accept findings of mngt expert in Inventory valuation ?

Hint: SA 500 → Evaluating mngt's Expert work:

(1) Evaluate CCO (2) Obtain Understanding (3) Evaluate appropriateness

Now explain the complete topic of "CCO" & "Understanding" as referred in Notes. , for appropriateness Below:

a) for expert's findings or conclusions → relevance & reasonableness & consistency

b) assumptions & Method → Relevance & Reasonableness c) source data → relevance, completeness, and accuracy

In instant case, Expert assumed 65 yrs instead of 60 yrs → can Qualify report.

➤ **Audit Procedure to Obtain Audit Evidence:**

SA 330	(a) RAP - Risk assessment procedure (b) FAP - Further Audit procedure : • Tests of Control (ToC), • Substantive 1. Tests of Details (ToD) 2. Substantive Analytical Procedures (SAP)

Q4. various audit procedures to obtain audit evidence? Or. Method of obtaining Audit evidence? Or. Obtaining A. Evidence in performing compliance & substantive procedure. Or. How to Gather More Evidences ?

It Includes Following: (ICAI ORR)

Inspection	• Examining record or docs, whether internal or external, paper electronic, or other media, or • Physical examination of an asset. Inspection of records and documents provides audit evidence of <u>varying degrees of reliability, depending on their nature and source</u> and, → in the case of internal records and documents, on the <u>effectiveness of the controls</u> over their production. An example of inspection used as a test of controls is inspection of records for evidence of authorisation. <u>Some documents represent direct audit evidence of the EXISTENCE of an asset</u>, for example, a document constituting a financial instrument such as a stock or bond. Inspection of such documents may not necessarily provide audit evidence about ownership or value.. <u>Inspection of tangible assets may provide reliable audit evidence w.r.t their existence</u>, but <u>not necessarily about the entity's rights and obligations or the valuation</u> of the assets. Inspection of individual inventory items may accompany the observation of inventory counting.
External Confirmation (EC)	• An E.C represents audit evidence obtained by auditor as a <u>direct written response</u> to the auditor <u>from a 3rd party</u>, in paper form, or by electronic or other medium. • E.C. procedures frequently are relevant when addressing assertions associated with certain A/c balances & their elements. However, E.C. need not be restricted to A/c balances only. • For Eg., the auditor may request confirmation of the terms of agreements or transactions an entity has with 3rd parties; the confirmation request may be designed to ask if any modifications have been made to the agreement and, if so, what the relevant details are. E.C. procedures also are used to obtain audit evidence <u>about the absence of certain conditions</u>, for example, the <u>absence of a "side agreement"</u> that may influence revenue recognition..
Analytical Procedures	Evaluations of financial info. made by a study of plausible relationships among both financial and non- financial data. & investigation of identified fluctuations and relationships that are inconsistent with other relevant information or deviate significantly from predicted amounts.
Inquiry	• Seeking information of knowledgeable persons: ✓ Both financial and non-financial, ✓ within the entity or outside the entity. • Inquiry is used extensively → in addition to other audit procedures • Evaluating responses to enquiries is an integral part of the inquiry process.

	• Responses to inquiries may provide the auditor with ✓ Information not previously possessed or ✓ With corroborative audit evidence ✓ Provide auditor with info. Differ significantly from other Info → Modify / perform additional procedure • Inquiries about management intent → Corroborative evidence is require in addition to inquiry to support mngt intent → understanding management's past history of carrying out its stated intentions → reasons & Ability for choosing a particular course of action • It can be Formal Written Inquiry or Informal Oral Inquiry: However in case of Oral inquiry, Auditor shall also obtain Written Representation from Mngt to confirm such inquiry • inquiry may provide important audit evidence, but, inquiry alone does not provide SAAE
Observation	Looking at a process or procedure being performed by others (Eg. inventory counting by the entity's personnel) Observation provides audit evidence about the performance of a process or procedure, but is limited to the point in time at which the observation takes place
Recalculation	Checking the mathematical accuracy of documents or records. (Manually or electronically)
Reperformance	Auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal control (Eg. Re-performing the reconciliation of bank statement or ageing of receivables)

➤ Other Integrated Qns:

Q5. Auditor verifying Export revenue (export on payment of IGST, Refund automatically credited), → Recognize export revenue on basis of "Bills of Lading" (does not appear proper). Further, 3 invoices of March'23 not recognized as export revenue because Bills of lading issued in April'23.

Hint: Can obtain evidence by: **GST return on GST portal** & correlate with **E-way Bill**.

Eway bill provide evidence that Goods moved out of Company (**Export** should be **booked when Goods Moved out**)
"Bill of Lading" is only a document issued by the carrier to the shipper.
violations of relevant accounting standards (Export revenue is understated)

SA 501- Audit Evidence: Special Considerations for Selected Items

Objective: to obtain SAAE Regarding:

- **Existence & Condition** regarding **Inventory**
- **Completeness** of **litigation and claims**
- **Presentation and disclosure** of **segment info**. As per applicable financial reporting framework

➤ **Inventory: Existence & Conditions**

Attending Physical Count (Unless Impracticable) <i>(Special Trick :-)</i>	SA 501 → When inventory is material to FS, obtain SAAE regarding existence & condition by: <u>Attendance at physical inventory counting, unless impracticable, to</u> Evaluate management's instructions and procedures for recording and count rolling the results of the entity's physical inventory counting. Observe the performance of management's count procedures. Inspect the inventory; and. - Perform test counts; - Cross matching the final inventory records with the actual inventory count results Performing audit procedures over the entity's final inventory records to determine whether they accurately reflect actual inventory count results



Other than Date of FS: <i>[Trick: Perpetual & Reliable hai to difference kyu ?]</i>	For practical reasons, If physical counting is conducted at a date other than date of the FS, the auditor shall, <u>In addition to above procedure</u>, auditor shall also perform audit procedures to obtain audit evidence about Whether changes in inventory between: - the count date & - date of the FS are properly recorded. Relevant matters to Consider, when designing audit procedures to obtain audit evidence about whether above changes in inventory are properly recorded include: - Whether the perpetual inventory Records are <u>properly adjusted</u>. Reliability of the entity's perpetual inventory records. Reasons for significant differences between the information obtained during the physical count and the perpetual inventory records				
Unable to Attend:	If auditor is unable to be present at physical inventory count on the date planned, due to unforeseen circumstances: - Auditor shall make or observe some physical counts on an alternative date, and - Perform audit Alternative procedures on intervening transactions. (to assess whether changes in inventory between date of physical count & period end date are correctly recorded) - Auditor will verify the treatment given for discrepancy noticed during inventory Count. - Obtain W.R from mngt for: completeness of information provided regarding the inventory & - assurance w.r.t Adherence to laid down procedure for physical inventory count				
Impracticable to attend count	Perform alternative audit procedures → to obtain SAAE → regarding the existence and condition → If not possible → Modify opinion as per SA 705 (Scope Limitation) <table border="1" data-bbox="321 982 1523 1444"> <tr> <td data-bbox="321 982 537 1276"> Why It's Impracticable? </td><td data-bbox="537 982 1523 1276"> - Factors such as the nature and location of the inventory, - Eg, inventory held at location that may pose threats to safety of auditor General inconvenience to auditor, however, is not sufficient to support a decision by the auditor that attendance is impracticable. SA 200, matter of difficulty, time, or cost involved is not in itself a valid basis for auditor to omit a audit procedure for which there is no alternative or to be satisfied with audit evidence that is less than persuasive. </td></tr> <tr> <td data-bbox="321 1276 537 1444"> Example of Alternate Audit Procedure </td><td data-bbox="537 1276 1523 1444"> <u>Inspection of documentation of:</u> ✓ Subsequent sale of specific inventory items acquired or ✓ Purchased prior to the physical inventory counting, May provide SAAE about the existence and condition of inventory. </td></tr> </table>	Why It's Impracticable?	- Factors such as the nature and location of the inventory, - Eg, inventory held at location that may pose threats to safety of auditor General inconvenience to auditor, however, is not sufficient to support a decision by the auditor that attendance is impracticable. SA 200, matter of difficulty, time, or cost involved is not in itself a valid basis for auditor to omit a audit procedure for which there is no alternative or to be satisfied with audit evidence that is less than persuasive.	Example of Alternate Audit Procedure	<u>Inspection of documentation of:</u> ✓ Subsequent sale of specific inventory items acquired or ✓ Purchased prior to the physical inventory counting, May provide SAAE about the existence and condition of inventory.
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Example of Alternate Audit Procedure	<u>Inspection of documentation of:</u> ✓ Subsequent sale of specific inventory items acquired or ✓ Purchased prior to the physical inventory counting, May provide SAAE about the existence and condition of inventory.				
Inventory with 3rd Party	<u>When inventory under the custody & control of a 3rd party is material to FS, auditor shall obtain SAAE regarding existence & condition of inventory by performing one or both of following:</u> Request confirmation from 3rd party w.r.t Qty & condition of Invntry held on behalf of entity. - Perform inspection or other audit procedures appropriate in the circumstances, <u>For Eg. where information is obtained that raises doubt about the integrity & objectivity of 3rd party, → perform other audit procedures instead of, or in addition to, confirmation, Like:</u> Attending, or arranging another auditor to attend, 3rd party's physical counting of inventory. Obtaining another auditor's report, or a service auditor's report, on the adequacy of the 3rd party's I.C. for ensuring that inventory is properly counted and adequately safeguarded. Inspecting documentation regarding inventory held by 3rd parties, for Eg, warehouse receipts. - Requesting confirmation from other parties when inventory has been pledged as collateral				

Q6. Mngt is taking inventory count, auditor decided not to do any inventory count, as it's duplication of work. (old)



Hint: Refer Above Notes "Attending Physical Count (Unless Impracticable)"

Q7. Auditor Unable to attend inventory due to count due to Warehouse at Border (i) How SAAE for existence & Condition of inventory to Obtain (ii) How auditor deal when attendance at physical inv counting impracticable

Hint: Refer above Notes: (i) Attending Physical Count (Unless Impracticable) (ii) Impracticable to attend count

Q8. A Due to of certain disturbances in the region, physical inventory counting could Not be carried out at the year end. The stock taking done by MANAGEMENT at some other date i.e., after a month

Hint: Refer above Notes: (i) Normal procedure of (evaluate, inspect, observe) (ii) "Other than Date of FS"

Q9. A Due to unavoidable circumstances, you could not be present at the time of annual physical verification

Hint: Refer Above notes : "Unable to Attend"

Q10. Substantial inventories of company remain with Super Ltd for job work, and Premised of Super Ltd were raided by GST officials for fake billing scam. How auditor should proceed in above matter.

Hint: Refer Above Notes : "Inventory with 3rd Party" (and in given case, integrity of the 3rd party appears to be doubtful .. as fake billing scam), → he may attend a 3rd party's physical counting or ask some other auditor to do so, inspect the record of goods sent and received back from such party (like Challans, away bill etc)

Q11. Auditor planned Physical count of inv in remote area → on 29th Mar → but due to civil protestors → plant site was blocked → and blocked lifted after 1 month, whether its "impracticability of attendance" as per SA 501.

Hint: It's not Impracticability (it's unable to attend physical count) → block lifted after 1 month. → make or observe some physical counts on an alternative date and perform audit procedures on intervening transactions

➤ Litigation & Claims: Completeness

Audit Procedure:	Design and perform audit procedures to identify litigation and claims involving the entity which may give rise to a ROMM, including:
(Trick: me kabhi legal case ni padunga .. as I Love Myself)	(a) <u>Inquiry of mngt</u> &, where applicable, others within entity, including in-house legal counsel; (b) <u>Reviewing Minutes</u> of meetings of TCWG & correspondence between entity & its external legal counsel; and (c) Reviewing <u>Legal expense accounts</u>

Communicate Entity External Legal counsel:

- If the auditor assesses a ROMM regarding litigation or claims exist, or when audit procedures performed indicate that other material litigation or claims exist, auditor shall:
 - Seek direct communication with → entity's external legal counsel.
- Above can be done by Letter of "General Inquiry" Or "Specific Enquiry":
 - Prepared by Mngt & Sent by Auditor
 - Requesting the entity external legal counsel to communicate directly with auditor
- If Law or Legal council's professional body deny / Prohibit to communicate directly with auditor → Alternate Procedure require.
- If Mngt Or Legal Counsel refuse to communicate with external legal counsel + Auditor not able to obtain SAAE using Alternate A.Procedure → SA 705 Modify Opinion

Letter of General Enquiry: "Blank Letter"	In some cases, auditor may seek <u>direct communication with entity's external legal counsel</u> through a LETTER OF GENERAL INQUIRY: • any <u>litigation and claims</u> that the <u>counsel is aware</u> of, and • an <u>assessment of the outcome</u> of the litigation and claims, and • an <u>estimate</u> of the financial implications, including costs involved
Letter Of Specific Inquiry: "Filled Letter with	If it is considered <u>unlikely that the entity's external legal counsel will respond</u> appropriately to a letter of "general" inquiry, Eg. <u>if his professional body prohibits</u> response to such letter & Have Significant Risk.



<u>Specified List of Litigation"</u> [Q. Asked] [Trick: litigation ki list deke pucho ki mngt to bolra h ki jeet jaenge case .. tra kya assessment h ? chalo meeting hi kar lete h]	Auditor may seek direct communication through a LETTER OF SPECIFIC INQUIRY. For this purpose, a letter of specific inquiry includes: • A list of litigation and claims • Where available, MGT's assessment of the outcome of each of the identified litigation and claims and its estimate of the financial implications, including costs • A request that entity's external legal counsel confirm the reasonableness of MGT's assessments and provide the auditor with further information if the list is considered by the entity's external legal counsel to be incorrect. • The auditor may seek meeting with the external legal counsel if the matter is: a) The auditor determines that the matter is a significant risk b) The matter is complex. c) There is disagreement between Mngt & external legal counsel. Ordinarily, such meetings require mngt's permission & are held with representative of mngt in attendance. [Also Obtain W.R. from mngt/TCWG for all the known actual or possible litigation → disclosed in FS & to auditor as per applicable FRF]

Meet Entity external Legal counsel:	(Trick: Meeting krke kya krenge ? → Koi acchi Dimaag wali .. Complex Movie dekhenge → nhii nhii .. meko nii dkhni .. Disagree hu ... Muje aaj Significant kaam h kuch) ➤ In certain circumstances, the auditor also may judge it necessary to meet with the entity's external legal counsel to discuss the likely outcome of the litigation or claims. <u>This may be the case, for example, where:</u> a) The auditor determines that the matter is a significant risk b) The matter is complex. c) There is disagreement between Mngt & external legal counsel. Ordinarily, such meetings require mngt's permission & are held with a representative of mngt in attendance.

Q12. Legal fees of 10 lacs paid to Lawyer, No details provided → Now auditor want to directly connect with Lawyer, she obtain Address of Lawyer from invoice, & sent Inquiry letter on auditor letterhead. Is her approach proper ? what she trying to achieve by corresponding with Lawyer of company ?

Hint: SA 501 → letter **Prepared by Mngt & Sent by Auditor** → **requesting to communicate directly to Auditor**. So, approach is wrong, she should make mngt aware of her intention & it should be prepared by Mngt. Her Purpose is to → **identify litigation & claims** involving which may give rise to a ROMM. As it may have a material effect on the FS and thus may be required to be disclosed or accounted for in the FS.

Segment Information: Presentation & Disclosure	
Audit Procedure: [UA]	Obtain SAAE w.r.t presentation and disclosure of segment information as per FRF: (a) Obtaining an understanding of methods used by mngt in determining segment info. Further, (i) Evaluating whether such methods are likely to result in disclosure in accordance with the applicable FRF (ii) Where appropriate, testing application of such methods (b) Performing analytical procedures or other audit procedures appropriate in circumstances
Understanding Method used by Mngt: (Special Trick :-)	Q13. Auditor is concerned with presentation & disclosure of segment info included in Company's Annual Report. Auditor want to ensure that methods adopted by mngt for determining segment info. have resulted in disclosure in accordance with applicable FRF. Guide GHK with 'Examples of Matters' that may be relevant when obtaining an understanding of the methods used by the mngt with reference to relevant SA's. As per SA 501: Example of matters that may be relevant when obtaining an understanding of the



P&L, B/S
Pichle saal ka ..
agle saal ka

methods used by management in determining segment information and whether such methods are likely to result in disclosure in accordance with the applicable FRF include:

- Sales, transfers** and charges between segments, & elimination of intersegment amounts
- The allocation of **assets** and costs among segments
- Comparisons of **budgets** & other expected results, for Eg, operating profits as a % of sales
- Consistency with prior periods**, and the adequacy of the disclosures wrt inconsistencies

SA 505 : External Confirmation

Means:	External confirmation (EC) may be defined as audit evidence obtained as a direct written response → to the auditor → from a 3rd party (the confirming party) → in paper form, or by electronic or other medium. (It's more reliable → As coming from External Source i.e., independent Party)	
Situation when E.C required: (SA 330)	Q14. Write a short note on Situations where external confirmations can be used. [old] Bank balance from bankers Account receivable balances Inventories held by third parties Property title deeds held by third parties Investments purchased but delivery not taken Loan from lenders Account payable balances - Long outstanding share application money	
External Confirmation Procedures:	Auditor shall maintain control over external confirmation requests, including: - Determining the information to be confirmed or requested; - Selecting the appropriate confirming party; (Party must be knowledgeable) Designing the confirmation requests, including determining that requests are properly addressed and contain information for responses to be sent directly to the auditor; Sending the requests, including follow-up requests, to confirming party.	
Factors- Designing Confirmation Requests: <u>[Qn Given]</u>	Factors to consider when designing confirmation requests include: - The ability of the intended confirming party to confirm or provide the requested information (for example, individual invoice amount versus total balance). <u>[Saamne wala kon hai?]</u> - The assertions being addressed. <u>[Usse kya puchna hai ?]</u> - Specific identified risks of material misstatement, including fraud risks. <u>[Usse kya puchna hai ?]</u> Prior experience on the audit or similar engagements. <u>[baaki apan khoodka experience use leke ?]</u> - The layout and presentation of the confirmation request. <u>[Presentation & communication dekh lenge]</u> - The method of communication (Eg., in paper form, or by electronic or other medium). Mngt's authorization or encouragement to the confirming parties to respond to the auditor. Confirming parties may only be willing to respond to a confirmation request containing management's authorization.	
Types of EC Request:	Positive Confirmation (+ve)	Negative Confirmation (-ve)
	A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the	A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.



	requested information.	
Positive External Confirmation effect (+ve):	Effect of using Positive external confirmation request: • Reply to the auditor in all cases, either by indicating the confirming party's agreement with the given information, or by asking the confirming party to provide information. • Response to +ve confirmation request ordinarily is expected to provide reliable audit evidence • There is a risk, however, that a confirming party may reply to the confirmation request without verifying that the information is correct. • Auditor may reduce this risk by using +ve confirmation requests that do not state amount (or other information) on the confirmation request, and ask the confirming party to fill in the amount or furnish other information. • But, use of this type of "blank" confirmation request may result in lower response rates because additional effort is required of the confirming parties.	
Factors to be Considered while Sending Negative Confirmation: (Trick: H-RED flag hai neg. confirmation)	Auditor shall not use negative confirmation requests as the sole substantive audit procedure to address an assessed ROMM at the assertion level unless all of the following are present: 1) The auditor has assessed the Risk of material misstatement as low and has obtained SAAE regarding the operating effectiveness of controls relevant to the assertion; 2) A very low Exception rate is expected; and 3) The population of items subject to negative confirmation procedures comprises a large number of small, Homogenous, account balances, transactions or conditions; 4) The auditor is not aware of circumstances or conditions that would cause recipients of negative confirmation requests to Disregard such requests. The failure to receive a response to a negative confirmation request does not explicitly indicate receipt by the intended confirming party of the confirmation request or verification of the accuracy of the information contained in the request. So, a failure of a confirming party to respond to a -ve confirmation request provides significantly less persuasive audit evidence than does a response to a positive confirmation request.	

Q15. Direct Question on → "factors to be considered by auditor when designing a confirmation request" & "effects of using POSITIVE EXTERNAL CONFIRMATION". [old]

Q16. Auditor want to use want to use confirmation procedures & also intends to use NEGATIVE confirmation. What are the factors to be considered for the same (Old) → Refer Above notes "Factor to consider while designing Confirmation request" & "Factor to consider while Sending Negative Confirmation request"

Q17. Auditor used Negative Confirmation for Trade payable → for 1 Old outstanding of Rs. 25 Lacs credit, No confirmation was received :: → SA 505, Negative confirmation → respond only if Confirming party disagrees. It's **less persuasive Evidence**. → **failure to receive** response in -ve confirmation **Not explicitly indicate** intended party confirmation on accuracy of information. → In Given case , **examine subsequent cash disbursements** or **correspondence from 3rd parties**.

Non response for -ve confirmation not means that there is some misstatement → But, if auditor identifies factors of doubts about the reliability → obtain further audit evidence to resolve those doubts

Q18. (Hint RTP May'25) → for a **Positive Confirmation** → a **response received was of different amt**, ::: For a Negative confirmation → no response was received ... What should be auditor action ?
Hint: For +ve confirmation → It's **Exception** (difference between info confirmed by party vs entity record), It **needs to be assessed** to entire population after analyzing difference reason. → **evaluate whether SAAE obtained or FAP as per 330 is necessary for exception**.
Company should be asked to investigate & reconcile the discrepancy indicated by the confirming party.
For -ve confirmation → Non- response implies that creditor agrees. auditor is not required any action.

➤ Management Refused to Send Confirmation Request:

Management Refused to Send Confirmation Request:

- Inquire the mngt **reason** of refusal → Seek evidence to their validity and reasonableness
- Evaluate **Implication** of mngt refusal on auditor's assessment of relevant ROMM & NTE of other procedure
- Perform **alternative audit procedure** → to obtain relevant & reliable A.evidence

If refusal is unreasonable + Unable to obtain evidence from alternate procedure → Communicate to TCWG & determine Implication on Audit report (SA 705 modify opinion)

Q19. AGM Ltd. has requested you, Not to send balance confirmations to a particular group of receivables [old]
Hint: Refer Above Notes "Mngt refused to send confirmation request"

❖ Result of External confirmation Procedure:

1	Factors raising Doubt over reliability of response →	Obtain further A.Evidence to resolve doubts
2	Response is not Reliable → (May not rec. directly or from other than intended party)	- Consider affect on NTE of other procedure Assessment of ROMM
3	Confirming party do not respond →	Perform Alternate audit procedure
4	No confirmation rec. & alternate procedure not possible	Affect auditor's opinion as per SA 705

❖ Example of Alternate audit procedure (i.e., When Confirmation not received):

- In case of Debtor → Vouch Sales Bills, Subsequent receipts shipping documents
- In case of Creditors → Vouch subsequent payments/disbursements, purchase bill etc., GRN note.

Q20. Auditor have sent **positive confirmation requests** to 30 creditors. Received the confirmation within 1 week.
 Later on, out of 30 creditors → 25 GST registration cancelled. (Hint: Mngt may have created Bogus party)
Hint: SA 505 → if response of E.C is Not Reliable → evaluate implication on assessment of ROMM (incl Fraud) & Related to NTE of other A.procedure. = In Given case, Registration cancellation indicated **Businesses were Closed** → it raised questions about reliability of response.

Factors that may indicate doubts about the reliability of a response include:

- (i) Was received by the auditor **indirectly** (ii) Appeared **not to come from the originally intended confirming party**.
 In given case, indicate **It not came originally from Intended Party** → may indicate **Fraud Risk Factor**.

SA 510-Initial Audit Engagements - Opening Balances

Auditor's Objective:	<u>Obtain SAAE in respect of opening balances (OB) about whether:</u> OB contain misstatements that materially affect the current period's FS; and Appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's FS, or changes thereto are properly Accounted for and adequately Presented and Disclosed (APD) as per applicable FRF
Predecessor Auditor:	The auditor from a different audit firm , who audited the financial statements of an entity in the prior period and who has been replaced by the current auditor.

Q21. Q 1 (Lock) (a) What are 'Initial Audit Engagements'?

- (b) to satisfy about 'Opening Balances' are free from misstatements, which may materially affect current FS. Lay down audit procedure, → (i) when last yr FS audited by another auditor; & (ii) when FS audited for 1st time.
 (c) If, after performing procedure, → you are not satisfied about 'Opening Balances'; what approach you will adopt in drafting your audit report in two situations mentioned in (b) above? [old]

Answer:

a)	Initial Audit Engagement	As per SA 510 initial audit engagement is an engagement in which either: i. The FS for the prior period were not audited ; or ii. The FS for the prior period were audited by a predecessor auditor .
b)	FS Audited by Another Auditor	<u>If the prior period's financial statements were audited by a predecessor auditor:</u> - The auditor may be able to obtain SAAE regarding the opening balances by perusing the copies of the audited FS including the other relevant documents relating to the prior period FS such as supporting schedules to the audited FS. - Ordinarily, the current auditor can place reliance on the closing balances contained in the FS for the preceding period, except when during the performance of audit procedures for the current period the possibility of misstatements in opening balances is indicated.
b)	FS Audited First Time	When the audit of financial statements is being conducted for the first time, - The auditor has to perform auditing procedures to obtain SAAE. Since opening balances represent effect of transaction & events of the preceding period and accounting policies applied in the preceding period, the auditor need to obtain evidence having regard to nature of opening bal, materiality of the opening balances & A/cing policies. - Since it will not be possible for auditor to perform certain procedures, e.g., observing physical verification of inventories, etc. the auditor may obtain confirmation, etc. and perform suitable procedures in respect of fixed assets, investments, etc. The auditor can also obtain management representation with regards to the opening balances.
C)	Drafting Audit Report	If the auditor is unable to obtain SAAE regarding the opening bal, the auditor shall express a qualified opinion or a disclaimer of opinion , as appropriate. Further, If the auditor concludes that the opening balances contain a misstatement that materially affects the current period's FS, and the effect of the misstatement is not properly accounted for or not adequately presented or disclosed, auditor shall express qualified/adverse opinion .

(Above Answer Ends)

➤ Master Answer for Opening balance:

Audit Procedures to be followed in case of initial audit engagement: As per SA 510, auditor **shall obtain SAAE** about whether the opening balances contain misstatements that materially **affect the current period's FS** by:

- (i) Determining whether the prior period's **closing balances** have been **correctly brought forward** to the current period or, when appropriate, any adjustments is disclosed as prior period items in current P&L;
- (ii) **No Misstatement** exists in **opening balance**
- (iii) Determining whether the **opening balances reflect the application of appropriate accounting policies** in CY (Consistently applied, or changes thereto are properly accounted & adequately presented & disclosed as per FRF)
- (iv) Performing one or more of the following:
 - a. **Where the prior year FS were audited**, → perusing the **copies of the audited FS** including the other relevant documents relating to the prior period financial statements;
[Ordinarily, the current auditor **can place reliance on the closing balances** contained in the financial statements for the preceding period, **except when during the performance** of audit procedures for the current period the **possibility of misstatements** in opening balances is **indicated**.]
 - b. Evaluating **whether "audit procedures performed in the current period" provide evidence relevant to the opening balances; or "Specific Procedure Require"** to obtain evidence for SAAE
- (v) Performing "specific audit procedures" to obtain evidence regarding the opening balances:
 - ✓ **For current assets & liabilities** → Some audit evidence can ordinarily be obtained as part of audit procedures during the current period. Eg., **collection/payment of opening Bal** of receivables & payables will provide evidence of existence, rights & obligations, completeness & valuation at beginning of period.
 - ✓ **In respect of other assets & liabilities such as fixed assets, investments long term debt** → auditor will



examine the records relating to opening balances. The auditor may also be able to get confirmation from 3rd parties (e.g., balances of long-term loan obtained from bank) & Mngt confirmation

- **If Misstatement exist in Op. Balance** → If the auditor obtains audit evidence that the opening bal contain misstatements that could materially affect the current period's FS, auditor shall **perform such additional audit procedures** as are appropriate in the circumstances to determine the effect on the current period's FS. If the auditor concludes that such misstatements exist in the current period's FS, the auditor shall **communicate the misstatements with the appropriate level of management** and TCWG as per SA 450

(Above Master Answer Ends)

"Specific Audit Procedures" to obtain evidence regarding the opening balances regarding **INVENTORY**:

For Inventory: Obtain SAAE about opening inventory by:

- **Observing a current physical inventory** count & **reconciling** it to **opening** inventory Qty.
- Performing audit procedures on the **valuation of the opening** inventory items
- Performing audit procedures on **gross profit and cut-off**

Q22. Auditor wants to get satisfied about Opening Balance are free from misstent (Initial Audit Engmnt) & if after performing procedure, he is not satisfied with Correctness of Op. Balance, draft audit report. (old)

Hint: Refer above "Master answer for opening Balance" and "Refer Qn 1st" for "Drafting Audit Report"

Q23. Last year Company was audited by some another CA, steps you take to ensure Closing Bal. correctly B/F. (old)

Hint: Refer Above "Master Answer for Opening Balance"

Q24. for Debtor of Rs. 150 Lacs (continued from last Yr), CA Jack has not obtain any A.Evidence, on the affirmation of mngt that there is no receipts → & last year it was already audited by predecessor auditor.

Hint: Refer Above "Master Answer for Opening Balance" + SA 580 → Auditor should have requested W.R + he should not exclude the Audit procedure of Closing balance → Hence Guilty of Misconduct (Gross Negligence)

Q25. 2021-22 Unaudited, and for FY 2022-23 → appointed auditor on 31/07/22 → Auditor is having doubt about opening inventory (material). Does there exist any responsibility on his part in such situation.

Hint: SA 510 → evaluate whether audit procedures performed in current period provide evidence w.r.t Op Bal or specific A.procedures are required to be performed. → In above situation, Current period procedure provide little evidence about Op. inventory → Refer Above Notes → "Specific Audit Procedures" for Op bal of **INVENTORY**"

SA 530 – Audit Sampling

Sampling	Application of audit procedures to less than 100% of items within a population relevant under audit, such that all sampling units (i.e all items in population) have a equal chance of selection . This is to ensure that items selected represent the entire population which enables the auditor to draw conclusions and express his opinion based on a pre-determined objective (Audit sampling should provide a reasonable basis for conclusion about the population)		
Tolerable misstatement	Monetary amount set by the auditor to obtain appropriate level of assurance that Monetary amount set by the auditor is not exceeded by actual misstatement in population (TOD)		
Tolerable rate of deviation	Rate of deviation set by the auditor to obtain appropriate level of assurance that the Rate of deviation set by auditor is not exceeded by Actual rate of deviation in the population (TOC)		
Factors influencing sample size		TOC	TOD
	An increase in auditors' assessment in RMM	Increase	Inc.
	An increase in tolerable rate of deviation on tolerable misstatement	Dec	Dec



	An increase in expected rate of deviation on amount of misstatement	Inc	Inc
	Increase in population	Negligible	Negligible

➤ 2 Approaches of Sampling: (Statistical & Non-Statistical)

Q26. Write short notes on Statistical and Non-Statistical Sampling. [old]

Answer SA 530 "Audit Sampling" (Define Audit Sampling)

Select sample items in such a way that the sample can be expected to be representative of the population.

There are 2 major methods in which the size of the sample & selection of sample are determined.

Statistical sampling	Non-statistical sampling
[Random Selection of Sample + Use of Probability theory while evaluating sample result & Sampling risk]	[Other than Statistical sampling]
- Method of audit testing which is more scientific than testing based entirely on the auditor's own judgment because - it involves use of mathematical laws of probability in determining the appropriate sample size in varying circumstances. - It has wide application where a population consists of a large number of similar items and more in the case of transactions involving compliance testing, trade receivables' confirmation, payroll checking, vouching of invoices and petty cash vouchers.	Experience: Under this method, the sample size and its composition are determined on the basis of the personal experience and knowledge of the auditor. Simple: This method is in common because of its simplicity. Example: purchases or sales ledger to be checked. For example, March, June & September may be selected in year one and different months would be selected in the next Yr. Surprise: An attempt would be made to avoid establishing a pattern of selection year after year to maintain an element of surprise as to what the auditor is going to check. Yr. End: It is a common practice to check large number of items towards the close of the year so that the adequacy of cut-off procedures can also be determined

Note → The decision **whether to use a SS or NSS approach is a matter for the auditor's judgement**. However, **sample size is not a valid criterion** to distinguish between SS & NSS Approach

➤ Methods of Sample Selection:

[Trick: **RSS-HMB** me har kisi ko nahi lete, alag-alag method se sampling karte hai fir lete h]

Q27. Describe the principal methods of selection of samples.

Random Sampling:	This method is applied through random number generators , for example, random number tables. 2 types of Random Sampling:	
	Simple Random Sampling:	Each unit of the whole population has an equal chance of being selected (No Auditor Bias) → Random Number table (Can be using Computer or Picking any number Randomly, Suitable for homogeneous population having a similar range [Eg. Homogenous: Debtor from Rs. 55K to 225K, But not From Rs. 500 to Rs.11 lacs])
	Stratified Sampling:	Dividing the whole population to be tested in a few separate groups called strata and taking a sample from each of them. Each stratum is treated as if it was a separate population (divided on basis of auditor's judgement) → highly diversified/heterogeneous population → Converted into → Homogeneous
Systematic Sampling (Interval)	- No. of sampling units in population is divided by the sample size to give a sampling interval, - Eg., 50, and having determined a starting point within the first 50, each 50th sampling unit thereafter is selected.	



Sampling)	• Starting point may be determined haphazardly (Can use computer Random Number generator) • [5000 population, need 100 samples → $1000/100 = 50^{\text{th}}$]
Haphazard sampling:	• Auditor selects the sample without following a structured technique. • Auditor would nonetheless avoid any conscious bias or predictability (Eg. Always choosing or avoiding the first or last entries on a page) • Haphazard selection is not appropriate when using statistical sampling. • Neither involve judgement, Not Random Number Table
Monetary Unit Sample	It is a type of value-weighted selection in which sample size, selection and evaluation results in a conclusion in monetary amounts .
Block Sampling:	• This method involves selection of a block(s) of contiguous items from within the population. • Block selection cannot ordinarily be used in audit sampling because most populations are structured such that items in a sequence can be expected to have similar characteristics • Although in some circumstances it may be an appropriate audit procedure to examine a block of items, it would rarely be an appropriate sample selection technique when the auditor intends to draw valid inferences about the entire population based on the sample.

➤ SAMPLING RISK & NON-SAMPLING RISK:

Q28. Write a short note on **Sampling Risk**. Or, While applying sampling technique, Which risk factors to consider

I] Sampling Risk

Meaning:	• Risk that the auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. This risk will always Exist. • If Acceptable sampling risk is Low → Larger Sample Size Needed

2 types of erroneous conclusions (Type of Sampling Risk):

<u>Over-Reliance:</u> ➤ For TOC: Controls are more effective than they actually ➤ For TOD: MMS not exist, when in fact it does The auditor is primarily concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion . This is because of over reliance on the internal controls.	<u>Under-Reliance:</u> ➤ For TOC: Controls are Not effective than they actually ➤ For TOD: MMS exist, when in fact it does not This type of erroneous conclusion affects audit efficiency as it would usually lead to additional work to establish that initial conclusions were incorrect. This is because of under reliance on the TOC and detailed substantive procedures performed by the auditor. Here risk of giving wrong opinion is minimum but it will lead to more detailed checking which is time consuming.

(Above Answer Ends)

II] Non-Sampling Risk

The risk that the auditor reaches an **erroneous conclusion** for any **reason not related to sampling risk**. It can **never** be **mathematically Measured** (i.e., Human Error, Misinterpretation of Results etc.)

Q29. Drawn some samples for TOC & TOD, He reached **erroneous conclusion** that controls are **less effective**.

Outlining the above risk involved, discuss how it is going to affect his audit of the company

Hint: Refer Above Notes: "Define Sampling Risk" & "Under Reliance"

➤ SAMPLING PROCEDURE & SSD:

SSD



Sample Size:	Sufficient to reduce sampling risk to an acceptably low level				
Select samples:	In such way → each sampling unit in population has a chance of selection (Representative of population)				
Sample Design:	Auditor shall consider purpose of audit procedures and characteristics of population <table border="1"> <tr> <td>Stratification: (can refer Qn also Given in Additional PDF)</td><td> Dividing a population into discrete sub population which have identifying characteristics is called as Stratification Each stratum is treated as if it was a separate population Each Sub population is called as Stratum and units under those sub population are referred to as Strata Eg: Like based on monetary value, Expense checking can be bifurcated as: a) Vouchers < Rs. 1 lacs (b) Voucher between 1 lac to 5 lacs (c) Vouchers > 5L Now auditor can decide that, he will check 10% in strata "a", 25% in Strata "b", 50% in strata "c" </td></tr> <tr> <td>Value Weighted Selection:</td><td> - When performing TOD → it may be efficient to identify the sampling unit as the individual monetary units that make up the population. Having selected specific monetary units from within the population, - Eg. the accounts receivable balance, the auditor may then examine the particular items, i.e., individual balances, that contain those monetary units. - benefit of this approach → audit effort is directed to the larger value items because they have a greater chance of selection, and can result in smaller sample sizes (Eg, Total Debtor of 50 Lacs: So, take List of All Debtors: Debtor A, B, C, D, E of 30 Lacs, 10 Lacs, 5 Lacs, 3 Lacs, 2 Lacs → Now in whole list, test the Top items mainly, i.e., 30L & 10L... for rest can do few items checking) </td></tr> </table>	Stratification: (can refer Qn also Given in Additional PDF)	Dividing a population into discrete sub population which have identifying characteristics is called as Stratification Each stratum is treated as if it was a separate population Each Sub population is called as Stratum and units under those sub population are referred to as Strata Eg: Like based on monetary value, Expense checking can be bifurcated as: a) Vouchers < Rs. 1 lacs (b) Voucher between 1 lac to 5 lacs (c) Vouchers > 5L Now auditor can decide that, he will check 10% in strata "a", 25% in Strata "b", 50% in strata "c"	Value Weighted Selection:	- When performing TOD → it may be efficient to identify the sampling unit as the individual monetary units that make up the population. Having selected specific monetary units from within the population, - Eg. the accounts receivable balance, the auditor may then examine the particular items, i.e., individual balances, that contain those monetary units. - benefit of this approach → audit effort is directed to the larger value items because they have a greater chance of selection, and can result in smaller sample sizes (Eg, Total Debtor of 50 Lacs: So, take List of All Debtors: Debtor A, B, C, D, E of 30 Lacs, 10 Lacs, 5 Lacs, 3 Lacs, 2 Lacs → Now in whole list, test the Top items mainly, i.e., 30L & 10L... for rest can do few items checking)
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Audit procedure:	- Auditor shall perform audit procedures on each item selected, - If auditor is unable to perform procedure on selected item → perform it on replacement item (Eg. To Cheque Payment Authorization, Auditor Found one Cancelled Cheque, He Must Ensure that Cheque is cancelled properly, then he can replace item) → - If auditor is unable to apply designed audit procedure (Sales book lost) Or, Unable to apply suitable alternative procedure to selected item, - Auditor shall treat that item as: <u>Misstatement</u> in case of TOD <u>Deviation</u> in case of TOC				
Nature & Cause of Deviation / Misstatement	- Evaluate nature & cause of deviation identified, it's effect on audit procedure - A Evaluate the sample result: Consider both Qualitative & Quantitative factors while evaluating samples Anomaly: In extremely rare condition when auditor consider deviation as Anomaly → obtain high degree of assurance that such sample is not representation of population → Perform Additional procedure & obtain SAAE				
Projecting:	Projecting Misstatement (Not in SM → Refer Additional Booket)				
Evaluate result of sampling	<u>Auditor shall evaluate:</u> - The results of the sample; and Whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested. <u>if audit sampling has not provided a reasonable basis for conclusions about the population:</u> Request mngt to investigate misstatement & do necessary adjustment				

- b) **NTE of FAP** to achieve require assurance (Eg. In case of TOC → auditor might extend the sample size, test an alternative control or do substantive procedure)

Q30. Guide auditor his role, if **Audit sampling** has not provided a reasonable basis for conclusion about population.
Hint: SA 530, Refer above notes → "Evaluate result of sampling"

➤ **OTHER QUESTIONS:**

Q31. When audit sample selected on a random basis, no statistical process for selection of samples needs to be followed". Comment (**Old**) → **Correct:** **Hint:** SA 530 → refer "Audit Sampling" definition.

- **Statistical sampling** have 2 characteristics (**Random Selection of Sample** + Use of **Probability to evaluate result**)
(Easy Language → statistical sampling ka kaam hi hai Random way se sample select karna, agar aap already random sample selection kar chuke ho .. then, Again statistical process is not require to select sample)

Q32. An Auditor while **analysing the errors / evaluating the misstatement** in a sample need to **consider qualitative aspects** also, as well as: → (a) **Nature & Cause** of Misstatement, (b) Whether it's an **Anomaly**, (c) **common features** in all misstatements, (d) whether an **Intentional** misstatement, (e) consider **Qualitative also**

SA 550 - RELATED PARTIES

SA's Requirement:	This SA assist auditor in: • Identifying and assessing the ROMM associated with RPR and RPT, & • in designing audit procedures to respond to the assessed risks
Auditor's Responsibility	Where FRF establishes requirements → Disclosure → w.r.t. RPR, / RPT and balances Even if FRF have no requirement → auditor needs to ensure that disclosure given → for True & Fair presentation + not misleading
Definition of Related Party:	(i) A related party as defined in the applicable FRF, Or, (ii) Where the applicable FRF establishes minimal or no related party requirements: - A person or entity having control or significant influence, over reporting • Directly/ Indirectly • Through one or more intermediaries over reporting entity - Entity over which reporting entity has control /significant influence directly or indirectly through one or more intermediaries; or Entity under common control with reporting entity, through: • Common controlling ownership • Owners who are close family members • Common key management However, entities that are under common control by a state (i.e., a Central/ national, regional or local government) are not considered related unless they engage in significant transactions or share resources to a significant extent with one another.

➤ **Matters to Be Included in Engagement Team discussion wrt to MMS due to Related Party**

Q33. Audit engt team **discussed SA 315 & 240**, consideration of **Susceptibility of FS to MMS due to fraud or error** could be due **related party**. Highlight the matters that are to be addressed in the discussion (**Old**)

"As per SA 550 "Related Parties", the **engagement team discussion** that **SA 315 and SA 240 require** shall include **specific consideration of the susceptibility of the FS to MMS due to fraud or error that could result from the entity's related party relationships and transactions.**

Accordingly matters that are to be addressed in the **discussion by CA Z among the engagement team include:**

[Trick: Professional Skepticism maintain karna ki koi bhi Condition or documents mile Non-Disclosed RPT k > Why mngt not identified & accounted it > It must be Fraud]

1. The **nature and extent of the entity's relationships and transactions with related parties** (using, for example,



- the auditor's record of identified related parties updated after each audit).
2. An emphasis on the importance of **maintaining professional skepticism** throughout the audit regarding the potential for material misstatement associated with related party relationships and transactions.
 3. The **circumstances or conditions** of the entity that may **indicate the existence of related party** relationships or transactions that management has **not identified or disclosed** to the auditor (e.g., a complex organisational structure, use of special purpose entities for off-balance sheet transactions, or an inadequate info. system).
 4. The records or **documents** that may **indicate the existence of related party relationships** or transactions.
 5. The **importance that mngt & TCWG attach to the identification, appropriate a/cing for, and disclosure of RPR & RPT** (if the applicable FRF establishes RP requirements), and the related risk of management override of relevant controls.
 6. In addition, the discussion in the context of fraud may include specific consideration of **how related parties may be involved in fraud**. For example:
 - (a) How special-purpose entities controlled by management might be used to facilitate earnings mngt.
 - (b) How transactions between the entity and a known business partner of a key member of management could be arranged to facilitate misappropriation of the entity's assets"

➤ **Matters to Be Included in Engagement Team discussion wrt to MMS due to FRAUD (SA 240)**

[Trick: Discuss karo jo bhi 1 dusre k pass idea h wo exchange karne k liye ... ki kese Audit procedure lagaae Fraud ko respond karne k liye >> Fraud bhi 2 jane kar sakte h >> Employees.. (Lifestyle acchi karni ho) or mngt > kuki mngt pe pressure ho sakta h > isliye earning manage krne k liye FR fraud kara ho]

Discussing the susceptibility of the entity's FS to MMS due to fraud with ET (SA 240):

[Provides an opportunity for more experienced engagement team members to share their insights about how and where the FS may be susceptible to material misstatement due to fraud → **Enables the auditor to consider an appropriate response**]

The discussion may include such matters as:

- An **exchange of ideas among E.T. members** about how and where they believe the entity's FS may be susceptible to MMS due to fraud, how mngt could perpetrate and conceal fraudulent FR, and how assets of the entity could be misappropriated.
- A consideration of **how an element of unpredictability will be incorporated** into the NTE of the audit procedures to be performed.
- A consideration of the **audit procedures that might be selected to respond** to the susceptibility of entity's FS to MMS due to fraud and whether certain types of audit procedures are more effective than others.
- An emphasis on the importance of **maintaining a proper state of mind** throughout the audit regarding the potential for MMS due to fraud.
- Consideration of types of circumstances that, if encountered, might indicate the **possibility of fraud**
- A consideration of any **allegations of fraud** that have come to the auditor's attention.
- A consideration of management's involvement in **overseeing employees with access to cash or other assets** susceptible to misappropriation.
- A consideration of any **unusual or unexplained changes in behavior or lifestyle** of management or employees which have come to the attention of the E.T.
- A consideration of known **external & internal factors affecting the entity that may create an incentive or pressure for management or others to commit fraud**, provide the opportunity for fraud to be perpetrated, and indicate a culture or environment that enables management or others to rationalize committing fraud.
- Consideration of circumstances that might be indicative of earnings mngt & practices that might be followed by **mngt to manage earnings that could lead to fraudulent FR**.
- A consideration of the **risk of management override of controls**.



➤ FULL PROCEDURE FOR RP & RPT

Q34. auditor wants to be sure adequacy of R.P disclosures? guide him in identifying possible source of R.P info. [old]

Answer

As per SA 550 → Auditor should review Info provided by the mngt identifying the names of all known R.P. However, it's mngt, which is primarily responsible for identification of RP. The duties of an auditor with regard to reporting of RPT as required by AS 18 "Related Party Disclosures" is given in SA 550.

- (i) SA 550 requires that to **identify names of all known related parties**,
- (ii) Some arrangements that may indicate the **existence of previously unidentified or undisclosed RPR /RPT**
- (iii) Obtaining further information on **significant transactions outside the entity's normal course of business** enables the auditor to evaluate whether fraud risk factors,
- (iv) Finally, **obtain a W.R** from the mngt concerning the completeness of info provided w.r.t identification of R.P.

➤ How to Identify Related Parties:

Q35. how to verify existence of R.P, OR reviewing the records & Docs of company reg RPT, Describe the steps.

As per SA 550 "Related Parties", during the audit, the auditor **shall remain alert**, when inspecting records or documents, for arrangements or other information that may indicate the existence of related party relationships or transactions that management has not previously identified or disclosed to the auditor. Example-

- (i) Entity **Income Tax Returns**.
- (ii) **Information supplied by the entity to regulatory** authorities.
- (iii) **Documents associated with the entity's filings** with a securities regulator (e.g., prospectuses).
- (iv) **Shareholder registers** to identify the entity's principal shareholders.
- (v) **Contracts and agreements with key management** or those charged with governance
- (vi) Records of the **entity's investments** and those of its pension plans.
- (vii) Statements of conflicts of interest from management and those charged with governance.
- (viii) Significant contracts and agreements not in the entity's ordinary course of business.
- (ix) Specific invoices and correspondence from the entity's professional advisors.
- (x) **Life insurance policies** acquired by the entity.
- (xi) Significant contracts re-negotiated by the entity during the period.
- (xii) **Internal auditors' reports**.
- (xiii) Arrangements that may indicate the existence of previously unidentified or undisclosed related party relationships or transactions.

In particular, the auditor shall inspect the following for indications of the existence of related party relationships or transactions that management has not previously identified or disclosed to the auditor:

- (i) **Bank, legal and third-party confirmations** obtained as part of the auditor's procedures;
- (ii) **Minutes of meetings of shareholders** and of those charged with governance; and
- (iii) Such other records or documents as the auditor considers necessary in the circumstances of the entity.

➤ Existence of previously unidentified or undisclosed RP & RPT :

Auditor procedure: Undisclosed Related Party [Qn]	Q36. aspects that statutory auditors shall consider on identification of previously undisclosed related party transactions by the management. (Nov'24) <u>If Auditor identify any unidentified / undisclosed RP or RP transaction:</u> Communicate relevant info. to other members of Engagement team, to assist them, whether RAP including ROMM needs to be reassessed. - Where applicable Financial Reporting Framework establishes related party requirements:



- a. Request mgt. to identify all transactions with newly identified RP
- b. Inquire as to why entity's controls over RPR/ RPT failed to enable identification or disclosure of that Related Party
3. Perform appropriate substantive audit procedures relating to such newly identified Related parties or significant RPT
4. Reconsider risk that other R.P & Significant RPT may exist → that mngt has not identified & perform additional audit procedures as necessary
5. If non-disclosure by mngt is intentional (i.e. indicative of ROMM due to fraud), evaluate the implications for the audit → re-evaluate the reliability of management's responses to the auditor's inquiries and management's representations to the auditor

➤ Transaction Outside Normal Course of Business:

Audit procedure when Outside Normal course of Business (Biased RPT) (BTD)	<u>If Auditor Identified significant RP Transactions outside Entity's Normal course of Business:</u> • Inspect underlying contracts to evaluate whether: ✓ Business rationale (or Lack of), Suggest fraudulent F.R. or misappropriation of assets ✓ Examine the Terms of transactions are consistent with mngt explanations ✓ Collect evidences for appropriate accounting & Disclosure in compliance of FRF. • Obtain evidences w.r.t. approval and authorisation of transaction. (Evaluate whether Fraud risk factor is present + Obtain W.R that all RPR disclosed / accounted
Examples: (Special Trick :-)	Q37. examples of significant transactions outside the entity's normal course of business. [old] Examples of transactions outside the entity's normal course of business may include: (Trick: Equity kharidi outside India se, paisa nahi diya ya discount jayada liya.....) • Complex equity transactions, such as corporate restructurings or acquisitions. • Transactions with offshore entities in jurisdictions with weak corporate laws. • The leasing of premises or the rendering of management services by the entity to another party if no consideration is exchanged. • Sales transactions with unusually large discounts or returns. • Transactions with circular arrangements, for Eg, sales with a commitment to repurchase. • Transactions under contracts whose terms are changed before expiry. Understand nature of Above Transaction → involves obtaining an understanding of the business rationale of the transactions, and terms & conditions under which these have been entered into.

Q38. During audit you come across a RPT which prima facie appears to be biased. How would you deal

Hint: Refer Above notes: Auditor procedure: Outside Normal Course of Business

Q39. LW Ltd is Manufacturing company → But it's Labour intensive (not require Machines), Another Company MLW Ltd (in which his director has interest), Sold 1 Crore machine to LW Ltd at Market Rate.

[Hint: RP sold one machine to Us, which have no use for our company] → Significant RPT outside normal course → Evaluate Business rationale or lack (Fraudulent FR or Missap. Of assets), to understand economic reality of such transaction. = Given Case, No primary rationale, machine has not use → it represent Fraud risk Factor

➤ Disclosure of Related Party Transaction (AS 18 / Ind As 24):

❖ Disclosure required as per AS 18

Name of RP	Description of RP relationship	Description of transaction
Volume of transaction	Any other important elements in transaction	Amount O/s & Doubtful debt provision w.r.t that RP at yr end
Amount Written off / written Back i.r.t Debt due from /to R.P		



❖ **Disclosure → When 2 Entities are Related, Because they Both are Under Control of Same Govt:**

As per Ind AS 24, a reporting entity is **exempt from disclosure requirements i.r.t RPT & O/S balances**, with:

- (i) a **government** that has **control** or joint control of, or significant influence over, the reporting entity; +
- (ii) **another entity** that is a **related party because** the **same Govt** has **control** or joint control of, or significant influence over, **both the reporting entity and the other entity**.

If a reporting entity applies the above exemption, it shall disclose the following:

- (1) the **name of the government** and the **nature of its relationship** with the reporting entity
- (2) Following information in sufficient detail to enable users of the entity's FS to understand effect of RPT:
 - i. the **nature and amount** of each **individually significant transaction**; and
 - ii. for **other transactions** that are **collectively**, but not individually, **significant**

Q40. A firm of a father and a son is receiving Rs. 2 lakhs towards job work done for XYZ Ltd. Father is Managing Director of XYZ Ltd. having substantial holding. He is saying there is no need to disclose. **[old]**

Hint: Refer Above disclosure require as per AS 18, → if Not disclosed → Modify opinion

Q41. A govt company has purchase goods from Another Govt company under same govt Control. (R.P) → Management informed that no disclosure is necessary **[old]**

Hint: Refer above: **When 2 Entities are Related, Because they are Under Control of Same Govt (Need Disclosure)**

➤ **OTHER QUESTIONS**

Q42. Audit team has identified few matters: **[old]**

ensure compliance of Ind AS 24 / AS 18 RP Disclosures & Below required to report to TCWG as per SA 260.

- (i) The **long-term borrowings from the parent company has no written terms** → **Need Separate Disclosure**
- (ii) **computers received from the parent company free of cost**, → **Need Separate Disclosure**
- (iii) **Rs.3.25 Lakhs paid to R.P for marketing services, (arm's length pricing is Rs. 3L)** → **Need RPT Disclosure**
- (iv) Auditor **asked certain info relating to one RPT of Rs. 47 lac but CFO refused**. → **limitation of scope SA 705**

Further assess reporting requirement under Caro Clause xiii

➤ **INTEGRATED CASE STUDY QUESTIONS & MCQ's:**

Q43. CS → Honest Speciality Chemicals Private Ltd → various products for **fertilizer units, (SM)**

- Company has **received customs notices** → **filed an appeal** → **penalty, could be more than 10% of sales.**
- Different Inventories → **liquid chemicals (in tanks & Pipelines), powdered (in drums), coal (in open area)**
- The company has **prepared its inventory details by involving a mngt expert.**

Q.1. audit procedures for verifying existence & condition of company's inventories w.r.t its nature of operations?

Hint: → Attendance at physical inventory counting to:

- (i) **Evaluate mngt's instructions & procedures** for entity's physical inventory counting like:
 - The **existence of appropriate control activities**: collection of used physical inventory count records, accounting for unused physical inventory count records, count and recount procedures.
 - The **accurate identification of stage of completion of WIP, slow moving, obsolete**, and of inventory in tanks, in pipes and in open areas.
 - The **procedures used to estimate physical quantities**, for liquid chemicals lying in process, tanks, pipelines, in open areas like coal pile, etc.
 - **Control over the movement of inventory** between areas and the shipping and receipt of inventory before and after the cut off date.

[Now mentioned normal procedure of Attending Inventory Count (SA 501): Hint: "Evaluate, inspect, Observe"]

Q.2 company has prepared inventory details by involving a mngt's expert. discuss responsibilities of auditor.

Hint: The company deals with speciality chemicals which are in liquid condition, powdered condition, lying in the huge tanks or in plants etc. The **unit of measurement** for each of the above categories may be different and could involve **technical and mathematical principles** involving technical and scientific expertise.

The auditor shall evaluate : **CCO-U-A** of Expert (i.e., Competency, capability, understanding, appropriateness)

Q.3 additional procedures, auditor need to carry out in respect of stocks lying with consignees?

Hint: Refer SA 501: "**Inventory Held with 3rd Party**"

Q.4. What procedures should the auditor need to undertake for litigation matters?

Hint: Refer SA 501: "**Auditor Procedure**" & "**Letter of Specific Enquiry**" as mentioned in "Litigation & Claims"

Below Points Are Summary of MCQ's of Above Case Study:

- 1) The objectivity of the management's expert is likely to be lesser if → expert is employed by the entity
- 2) "Whether 100% of inventory is covered in the count" → it's irrelevant in planning physical inventory counts ?
- 3) External confirmations for receivables are not reliable in which → The confirmation is signed by plant manager
(Wrong Option: response directly received by the auditor, confirmation came from the address of party)
- 4) The new auditor planned certain procedures w.r.t. opening balances. Which of following procedures is not in accordance with SA 510? → Ascertaining whether predecessor auditor had attended physical inventory count

Q44. → **C.S:** "Trustworthy Real Estate Pvt Ltd" with Mr. Bharose Lal as MD & his wife, Maya, owned company. The company had floated one SPV "Real Trust Developers Pvt Ltd" in which a foreign entity became a JV partner with a 50% stake. (JV has head office in Mumbai → to invest in SRA Slum Rehabilitation & develop commercial units for sale.)

Mr. Bharose Lal was in financial difficulty & huge O/s exposure to banks/suppliers. Mrs. Maya was from a very wealthy family but had an expensive lifestyle and was always short of funds to maintain life style.

Mr. Bharose Lal sensed a golden opportunity in the new venture because the foreign partner had no knowledge of Indian regulations & how SRA projects solely dependent on the local partner to get all the permissions etc

Mr. Bharose Lal has a dominant personality and a powerful influence on functioning, and everybody looks to him for guidance, The governance structure was very poor in the organization

The dealings in the SRA project are not very transparent and above board but are very opaque. Given the above situation, CA Sceptic (Auditor) wants to discuss with the audit team areas and situations where ROMM is possible and there are chances of having an undisclosed related party relationship to misappropriate funds.

Q.1. Please guide the engagement team on the further course of action as per SA 550. (SM)

Hint: [Refer SA 550: "**Engagement Team Discussion for MMS due to RP & RPT**" & "**Engagement Team (E.T) - Discussion for Fraud**"]

Q.2: What are fraud risk factors in given case?

Hint: In the given case scenario following **fraud risk factors** can be segregated in the **2 conditions**.

1) An incentive or pressure to commit fraud:

- **Financial difficulty** with huge outstanding dues towards vendors and Financial Institutions.
- **Expensive lifestyle.**
- **Requirement to fund Rs. 5 crore as equity** contribution in the SPV.

2) A perceived opportunity to commit fraud:

- **Dependency of the foreign partner** and no knowledge of the foreign partner of local laws

- The risk is due to the way real estate industry functions and particularly risk due to SRA business model
- Dominant personality of MD, which can lead to management override of controls for undisclosed business relationships with M/s. Useless and Sons (P) Ltd.

Q.3: In given case, each partner in JV has to bring a contribution of 5 crores & Mr Bharose Lal had appointed one agency "Useless Pvt Ltd", to get consent from the slum dwellers, for which agency was paid 20 crores Fees as Kitty to get the job done.

CA Sceptic inclines that there is some connection between the 20 crores paid and, simultaneously, within a short span, the infusion of INR 5 crores as equity by Mr. Bharose Lal. Please guide CA Sceptic in establishing this link based on the guidance available in SA 550 and SA 240.

Hint:

If auditor identifies arrangements or information that suggests existence of RPR/RPT that mngt has not previously identified or disclosed to the auditors, the auditor shall determine whether the underlying circumstances confirm the existence of those relationships or transactions.

[Refer & Mention SA 550: Existence of previously unidentified or undisclosed RP & RPT :]

- The Auditor needs to carry out verification & inspection of the ownership structure and the review of the FS of the M/s. Useless and Sons (P) Ltd through the MCA website and establish the nexus between the two.
- The Auditor needs to carry out an inspection of the data filed by Mr. Bharose Lal for his group companies to establish any past transactions/relationships between the two entities
- The Auditor needs to ask for all the documents for the utilization of INR 20 crore and can investigate by visiting the parties involved and asking for confirmation directly.

Q.4: If, based on additional audit procedures → CA Sceptic, established that there is a likelihood of misappropriation of funds & FS as whole may be MMS, how CA Sceptic needs to plan the future action?

Hint: reassess the reliability of evidence previously obtained (as doubts about completeness & truthfulness of representations made and about the genuineness of accounting records and documentation)

[Refer SA 240: "If auditor is unable to continue performing" i.e., Determine the professional and legal responsibilities → Whether it is appropriate to withdraw → If the auditor withdraws → Discuss mngt/TCWG etc]

Below Points Are Summary of MCQ's of Above Case Study:

1. Method that Mr. Bharose Lal can indulge to commit fraud? → Using undisclosed business partners to misappropriate funds in the garb of making a business transaction and thus siphoning off the funds.
2. Given case, main factor giving rise to ROMM is: → vulnerability & dependence of foreign partner on local partner.
3. Given case, which is the most important red flag for auditor: → Undisclosed RPR to siphon off the funds.
4. Which of the following is not a fraud risk factor? → Floating of a new SPV itself.

CHAPTER 6- COMPLETION & REVIEW

SA 560, 570, 580

SA 560: Subsequent Events (S.E) - (Link AS 4 & Ind As 10)

➤ Subsequent Events:

Meaning (Link AS 4 & Ind As 10)	Events occurring between: - Date of the financial statements and - Date of the auditor's report, Facts that become known to the auditor: After the date of the auditor's report.		
2 Types		Type 1: Existed on Date of FS	Type 2: After date of FS
	That provide evidence of conditions	Existed at date of financial statements	Arose after date of financial statements
	Adjusted:	Adjustments require in FS	Not Adjustments require in FS, Only Disclosure
	Example:	- Debtor existed on BS date, but became insolvent after - Legal dispute existed on BS date, settled after BS	- Loss of P&M by Fire after BS - Sale of Share & Debenture

➤ Audit Procedures:

Case I) Regarding Events Occurring between: - Date of the Financial Statements and - Date of the Auditor's Report	
SAAE:	- Auditor shall perform A.procedures designed to obtain SAAE that all events occurring between the date of FS & auditor's report that require adjustment or disclosure in FS are identified - However, Auditor is not expected to perform additional audit procedures on matters to which previously applied audit procedures have satisfactory conclusions
Audit Procedure:	Auditor shall perform the procedures required above, cover the period from the date of the FS to the date of the auditor's report. Auditor shall consider following for risk assessment: Obtaining understanding of any procedures management has established to ensure that subsequent events are identified. Inquiring of Mngt & TCWG as to whether any S.E have occurred which might affect FS Reading minutes, if any, of meetings, of the entity's owners, mngt and TCWG, that have been held after the date of the FS and inquiring about matters discussed at any such meetings for which minutes are not yet available - Reading the entity's latest subsequent interim FS, if any. When, as a result Above Procedure, auditor identifies any events that require adjustment of, or disclosure in FS → determine whether each such event is appropriately reflected in FS.
W.R:	Auditor shall request Mngt and, where appropriate, TCWG, to provide a W.R as per SA 580, That all events occurring subsequent to the date of FS & for which the applicable FRF requires adjustment or disclosure have been adjusted or disclosed.



Specific Inquiry to evaluate S.Events:

[in Audit Procedure: Point no. 2]

(Special Trick :-)

Q1. Guide auditor with matters where specific enquiry may be conducted to evaluate S.E.[old]

SA 560 → in inquiring mngt &, where appropriate, TCWG, as to whether any subsequent events have occurred that might affect the FS, may make specific inquiries about the following matters:

Trick: Asset Related

- (i) Whether any assets have been **appropriated by Govt or destroyed**, example, by fire or flood.
- (ii) Whether **sales or acquisitions of assets** have occurred or are planned.
- (iii) Whether any events have occurred that are relevant to the **recoverability of assets**.

Liability Related:

- (iv) Whether **new commitments, borrowings** or guarantees have been entered into.
- (v) Whether any events have occurred that are relevant to the measurement of estimates or **provisions** made in the financial statements.
- (vi) Whether there have been any developments regarding **contingencies**.

Share Capital Related:

- (vii) Whether there have been **increases in capital or issuance** of debt instruments, such as issue new shares or debentures, or agreement to merge or liquidate has been made or is planned.

Remaining is Unusual:

- (viii) Whether any **unusual accounting adjustments** have been made or are contemplated.
- (ix) Whether any events have occurred or are likely to occur that will bring into question the appropriateness of accounting policies used in FS, as would be the case, for example, if such events call into question the validity of the going concern assumption.

Q2. auditor's responsibility regarding subsequent events. OR, F.S of Mar'20, Covid hit on Apr'20 → audit procedures would you perform to ensure that all subsequent events are considered [Old]

Hint: Refer Above Notes: → (1) "Meaning of S.Events" (2) "2 types of S.Event" (3) "Audit Procedure" for Subsequent Events [Don't Mention "Specific Enquiries" in Audit procedure]

Q3. Audit FY 2023-24 → Audit is near to Completion → in July 24 One of Buyer Suit company for Goods supplied in Aug'23 (Substandard Goods) → Mngt agreed for Settling it for Rs. 4 Crore , FS is Silent [SM]

Hint: Mngt agreed for Settlement of Rs 4 Crore (Out of Court) → it's a Subsequent Event → Existed on B/S date, required Adjustment → Further SA 560, request mngt/TCWG, To provide W.R that all subsequent events for which applicable FRF requires adjustment or disclosure have been adjusted or disclosed.

In Given Case, if absence of the same, he should consider the impact of the said event and report accordingly

➤ **Auditor's Obligation for Event Occurring "AFTER DATE OF AUDITOR's REPORT":**

Auditor's Obligation for Event Occurring "AFTER DATE OF AUDITOR's REPORT" :

Case II- But Before Date of FS are issued	Case III- But After Date of FS have issued
➤ Auditor has no obligation to perform any audit procedures regarding the FS after the date of the auditor's report ➤ However, when, after the date of auditor's report but before the date FS are issued, a fact becomes known to the auditor: May have caused the auditor to Amend the auditor's report, the auditor shall: • Discuss the matter with mngt. & TCWG • Determine whether FS need amendment • Inquire how mngt intend to address matter in FS	➤ After FS have been issued, Auditor has no obligation to perform any audit procedures regarding such FS. ➤ However, when, after FS have been issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of auditor's report, May have caused the auditor to amend the auditor's report, the auditor shall: • Discuss the matter with mngt. & TCWG • Determine whether FS need amendment • Inquire how mngt intend to address matter in FS



If Mngt. amend the F.S. auditor shall:

OPTION 1 → When Amendment is not restricted only to the subsequent event causing amendment

- Carry out audit procedure on amended FS
- **Extend these procedures** to date of new A.R &
- Provide **new A.Report** on amended FS

New A.Report shall **not be dated earlier** than date of approval of amended F.S

OPTION 2 → When L&R / FRF Allows the mngt to amend FS but Amendment is restricted only for Subsequent event identified (So, **Audit procedures are also RESTRICTED** to that identified Event only)

- Amend the audit report to include an **additional date. (DUAL DATING)** Or
- Issue new /Amended Audit report** & include the **EOM/OM** para
(In both "a" & "b" Mention that Audit Procedure on S.E are restricted solely to the amendment made in FS as mentioned in the relevant note to the FS)

- Carry out procedures on amended FS.
- Review the **steps taken by mngt** to ensure that anyone who received previously issued FS together with A.report thereon is informed of situation

(Now Same as Case II, Just consider 1 new point as Below)

In new / amended A.Report, Shall also include **EOM/OM**: "referring to Note of FS, discuss the **reason for amendment** in FS

Note: New auditor's report shall not be dated earlier than the date of approval of the amended FS

If mngt refuses to amend the F.S.

• Modify the report if not yet provided to entity. • If report already issued, notify to mngt & TCWG not to issue F.S. to 3rd party. • If mngt still issues F.S., take appropriate action to prevent reliance A. report (obtain Legal Advice)	• Inform Management & TCWG that the auditor will seek to prevent reliance on Audit report • If Mngt is silent, take necessary steps to prevent reliance on Audit report (obtain Legal Advice)

Author's Note: If Qn is silent regarding "Whether Amendment is restricted or Not" → always Assume that Amendment is "NOT RESTRICTIVE" i.e., **OPTION 1**

Q4. Year ended 31/03/21 → A.report signed on 04/05/2021. → On 06/05/21 received govt communication reg. Rs 5800 Crore incentive pending, Approved now & would paid before May'21. → Director wish to amend FS by include it in FS of 31/03/21. On 08/05/21 Board Amended FS → requested auditor to issue fresh report.

Hint: → [Refer Above Notes: Case II - After Date of Audit Report, But Before Date of FS are issued] (Don't mention Option 2 i.e., Dual dating) → (Explain the Given Case, exact same as Question)

Auditor can issue **new A.report** but **date** of A.report should **not be earlier** than **date of amended FS approval.**

➤ **Other Integrated Qns:**

Q5. for 31/03/23 → Rain in Sep'22, stock damaged & insurance claim lodged → So **Insurance Receivable** of 1 Cr on 31/03/23 → However, on 15/05/23 → **only 45 lacs** provided by insurance Co. You have finished Substantive procedure in May'23. [Hint → Insurnc Claim exist at Yr end, received after Yr end, Before A.R]

Hint: Condition existed at FS date (Claim Receivable). → But S.E → **Claim settled for 45L** (A. Report not yet issued) , So, FS of 31/03/23 should be **Adjusted** & mngt should be asked appropriate action to adjust FS properly reflected in FS as per Applicable FRF

Q6. for 31/03/23 → BOD Proposed a dividend of Rs. 1Cr on 17/04/23 (not yet approved in AGM). A.report **WILL BE** finalized by 31/07/23. (Hint: Dividend proposed **AFTER Yr** → Non-Adjustment, Only Disclosure Require)

Hint: It's a Condition arose After Reporting Period. → **no obligation/Liability** at the **reporting date** as per **Ind AS 1**. **Not require recognition** of above **Proposed Dividend** in FS (Not require Adjustment → Just Disclosed in FS Notes)



- Q7.** Labour salary negotiation → case existed on B/S date, But amt was not provided in FS → Company lost case after B/S date, before A.report (OLD) = → Hint: It's Adjusting Event
Hint: AS 4 (event occurring after BS date), AS 29 (Need Provision) → Perform procedure to Obtain SAAE from FS date to A.R date., Further Require Provision & Adjustment as per AS 4 & AS 29 . (If mngt not agree → Qualify)
- Q8.** Fire broke on 15/05/21 → inventory lying since 01/03/21 → was totally destroyed (FS not yet approved in AGM & No provision for this loss in FS) = [Hint: Non-Adjustment Event] = AS 4 → No condition exist on B/S date. → However ensure Going Concern (loss not materially affect Enterprises). = → Company is Correct, Provision is not needed, But Proper Disclosure is required.
- Q9.** (MTP'24) → Audit report date 25/07/21, Case filed against company on 04/08/21 (For incident caused in factory on 17/01/21 → may result heavy penalty). → FS amended, But Mngt disclosed it as "Contingent Liability for court case" (no additional disclosure like Amt, details etc.) → mngt told auditor if any further description needed, Put in EOM para of A.Report. (i.e., After A.R but Before FS issued)
- (a) Whether Auditor properly adhere SA 560 responsibility (b) Whether Mngt view is correct w.r.t Disclosure
Hint: (a) (i) Discuss matter with Mngt (ii) determine if FS need amended (iii) how mngt intend to address this in FS If mngt not take necessary steps to ensure that anyone in receipt of previous FS → Notify mngt → seek prevent ...
 (b) SA 706: EOM para is not substitute for: (i) Modified opinion (ii) FS Disclosure (iii) Going Concern event
 → The said contention of mngt is not valid as 'EOM' cannot be used as a substitute for disclosures of FS

SA 570 – GOING CONCERN: [Link with Clause 19 of CARO 2020]

GC basis of accounting:	- Under the going concern basis of accounting, the FS are prepared on the assumption that entity is a going concern and will continue its operations for the foreseeable future. - General purpose FS prepared using the GC basis of accounting, unless management either - Intends to liquidate the entity or to cease operations, or - has no realistic alternative but to do so. - Special purpose FS can be prepared without GC assumption also. - When use of GC basis of accounting is appropriate → It Means → assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business.
SA 701 KAM	When SA 701 applies → - Matters relating to going concern may be determined to be key audit matters, and - Explains that a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a GC is, by its nature, a KAM
Mngt. Responsibilities:	- It is Mngt responsibility to assess entity's ability to continue as a going concern - Even if FRF not include an explicit requirement to do so. (AUDITOR SHALL REQUEST Mngt TO EXTEND GC ANALYSIS to ATLEAST 12 month)
Auditor's Responsibility:	- to obtain SAAE regarding appropriateness of Mngt use of the GC basis of accounting in the preparation of the FS, and - to conclude, based on audit evidence obtained, whether a material uncertainty exists about the entity's ability to continue as a going concern. Not Guarantee: As per SA 200, Due to Inherent limitation → Absence of any reference to a material uncertainty about the entity's ability to continue as a GC in an auditor's report cannot be viewed as a guarantee as to the entity's ability to continue as a going concern.
Auditor's Objective:	Conclude on the basis of Evidence obtained that whether a M.U. exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a GC;



	- Obtain SAAE about appropriateness of Mngt use of GC ass. in FS prepare & presentation - Determine implications on auditor's report.				
Remain Alert for Event & C:	Auditor shall remain alert throughout the audit for audit evidence of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern				
Risk assessment procedure [Qn]	Risk Assessment Procedures and Related Activities: - When performing RAP as required by SA 315, Auditor shall consider whether events or conditions exist that may cast significant doubt on entity's ability to continue as GC. - In so doing, Auditor shall determine whether mngt has already performed a preliminary assessment of the entity's ability to continue as a going concern, and: <table border="1"> <tr> <td>If such assessment performed</td><td> - Auditor shall Discuss assessment with Mngt and - Determine whether Mngt has identified events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern and, if so, management's plans to address them </td></tr> <tr> <td>If not yet performed</td><td> - Auditor shall discuss with Mngt the basis for intended use of GC basis of accounting, and - Inquire of management whether events or conditions exist that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern. </td></tr> </table> The auditor shall remain alert throughout the audit for AE of events or conditions that may cast significant doubt on the entity's ability to continue as a GC.	If such assessment performed	- Auditor shall Discuss assessment with Mngt and - Determine whether Mngt has identified events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern and, if so, management's plans to address them	If not yet performed	- Auditor shall discuss with Mngt the basis for intended use of GC basis of accounting, and - Inquire of management whether events or conditions exist that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.
If such assessment performed	- Auditor shall Discuss assessment with Mngt and - Determine whether Mngt has identified events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern and, if so, management's plans to address them				
If not yet performed	- Auditor shall discuss with Mngt the basis for intended use of GC basis of accounting, and - Inquire of management whether events or conditions exist that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.				

➤ **Events or Conditions That May Cast Significant Doubt on the Entity's Ability to Continue as a GC:**

Q10. For examining going concern assumption, what **important indications** should be evaluated & examined? [old]

SA 570 → requires that while planning a performing audit procedure & in evaluating the results thereof, auditor should consider the appropriateness of the **GC** assumption underlying the preparation of the FS. In assessing such a risk, the auditor should examine the following indications:

Following are the examples:

I] Financial	II] Operating
1) Net liability or net current liability position. 2) Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment; or excessive reliance on short-term borrowings to finance long-term assets. 3) Indications of withdrawal of financial support by creditors . 4) Negative operating cash flows indicated by historical or prospective financial statements. 5) Adverse key financial ratios . 6) Substantial operating losses or significant deterioration in the value of assets	1) Loss of key management without replacement 2) Loss of a major market, key customer(s) , franchise, license, or principal supplier(s). 3) Labor difficulties 4) Shortages of important supplies 5) Emergence of a highly successful competitor 6) Management intentions to liquidate the entity or to cease operations
	III] Other
	1) Non-compliance with capital or other statutory or regulatory requirements , such as solvency or liquidity requirements for financial institutions.



7) Inability to pay creditors on due dates.	2) Pending legal or regulatory proceedings against the entity that may, if successful, result in claims that the entity is unlikely to be able to satisfy.
8) Inability to comply with the terms of loan agreements .	3) Changes in law or regulation or government policy expected to adversely affect the entity.
9) Change from credit to cash -on-delivery transactions with suppliers.	4) Uninsured or underinsured catastrophes when they occur.
10) Inability to obtain financing for essential new product development or other essential investments	

➤ Additional Audit Procedures: When Events or Conditions are Identified:

Additional Procedures (Mitigating Factors) [Qn] (Special Trick :-)	In such case, perform additional audit procedures (including mitigating factors), to Obtain SAAE that whether or not due to those events, M.U exists of entity ability to continue as G.C: <i>[Trick: Bhai.. Baaki saari baatein Baad me karenge > tune to abhi tak GC assessment bhi nahi kara > pahle wo Kar > ab bata > Ki isko mitigate karne k liya kya PLAN hai ? Additional Cash kaha se aaega ... yaar teri baatein bilkul reliable nahi lag rhi > tu sab likh ke de (WR)]</i> - Where management has not yet performed an assessment of the entity's ability to continue as a going concern, requesting management to make its assessment Evaluating mngt's plans for future actions i.r.t. its G.C assessment, whether the outcome of these plans is likely to improve situation and whether mngt plans are feasible in circumstances. - Considering whether any additional facts or information have become available since the date on which management made its assessment. (Subsequent) - Where the entity has prepared a cash flow forecast, & analysis of the forecast is a significant factor in considering the future outcome of events or conditions in the evaluation of management's plans for future actions: - Evaluating the reliability of the underlying data generated to prepare the forecast; and - Determining whether there is adequate support for assumptions underlying the forecast. - Requesting W.R from Mngt regarding their future action plans and feasibility of plans.
Above Audit procedure may include: [Qn] (Special Trick :-)	Audit procedures that are relevant to the requirement as stated above may include the following: <i>Trick: "Meeting" karo "Legal Council" ke saath > bhai "Customer ke orders" hai > par poora karne k liye "Finance" hi nahi h ... kya kare wo to case kar denge ... Aree koi baat nahi.. tum kaam to suru karo > "subsequently" "Cash" to kahi se bhi aa jaaega > "FS" me jo "asset" hai wo bech denge > "loan" le Inge</i> Reading minutes of the meetings of shareholders, those charged with governance and relevant committees for reference to financing difficulties - Inquiring of the entity's legal counsel regarding the existence of litigation and claims and the reasonableness of management's assessments of their outcome - Evaluating the entity's plans to deal with unfilled customer orders. - Confirming the existence, legality and enforceability of arrangements to provide or maintain financial support with related and third parties and assessing the financial ability of such parties to provide additional funds - Performing audit procedures regarding subsequent events to identify those that either mitigate or otherwise affect the entity's ability to continue as a going concern. - Analyzing and discussing cash flow, profit and other relevant forecasts with Mngt - Analyzing and discussing the entity's latest available interim financial statements.



- h) Determining the adequacy of support for any **planned disposals of assets**.
- i) Reading the **terms of debentures & loan agreements** to determining any **breached** in that.
- j) Confirming the existence, terms and adequacy of **borrowing facilities**.
- k) Obtaining and reviewing **reports of regulatory actions**.

➤ **Answer Starting Language when Event or Condition identified ... and auditor to apply procedures:**

As per SA 570 Going Concern, if **events or conditions have been identified** that may cast significant doubt on the entity's ability to continue as a going concern, the auditor **shall obtain SAAE** to determine whether or not a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern (hereinafter referred to as "material uncertainty") **through performing additional audit procedures, including consideration of mitigating factors. These procedures shall include:**

Q11. MNO Ltd, doubt over G.C, Company led into Insolvency Proceedings on 31/08/20, however Resolution plan was approved on 02/03/21 by Committee of Creditors (CoC). & NCLT approval obtained on 04/05/21. (Old)

Hint: refer Above Notes → "**Answer Starting Language**" & "**Additional Procedure (mitigation Factors)**", → In the instant case, the approval of the resolution plan is a significant mitigating factor → events and conditions are mitigated effectively and there is no material uncertainty

Q12. Company customer base is reducing, creditors payment delayed etc. what audit procedure as per SA 570 ? and how auditor deal if G.C assumption is appropriate but M.U exist & Adequate disclosure is there. (SM & MTP)

Hint: Above Notes → "**Answer Starting Language**" & "**Additional Procedure (mitigation Factors)**", + Also Mention → include separate Section in Report → "**Draw user attention in FS**" & "**state that these events indicate M.U**"

Q13. (SM) → Company engaged in Poultry Birds & Eggs → Due to several Bird flu pandemic → sales decreased 80%, Livestock wiped off. → Now Mngt want New Bird batches (No fresh credit, Further existing W.C. Loan to repay by Next year) → Company plans longer credit from Animal feed supplier. → further, company taking additional safety measure for birds (Vaccination) → Mngt Prepared **Cash Flow forecast**. (Discuss auditor approach to examine G.C assumption)

Hint: Refer Above Notes: "**Answer Starting Language**" → Reg. Cash Flow Forecast, evaluate Below:

(a) Evaluate **reliability** of Underlying data (b) **Assumption** → Can Evaluate these By:

(i) Verify new bird assumption (as no fresh credit) (ii) verify cash flow include repayment of Loan (iii) how supplier extend longer credit (iv) company accounted inc. in expense due to vaccination (v) pollution reduction expenses

Q14. Company, inc. in competitor, Inc. in Raw material price, Unable to repay Borrowing → Auditor to evaluate mngt assessment of G.C by Studying **Projected Profit Statement**, Comment on that Audit Procedure. (Old)

Hint: Refer Above Notes: "**Answer Starting Language**" → Obtain SAAE, perform Additional audit procedure → focus on **CASH FLOW forecast (not profit projection)** → then evaluate → 1) Reliability of underlying data (2) support of assumptions

➤ **Implication on Auditor's Report / Reporting :**

When mngt prepared FS on assumption of G.C:

GC appropriate:	Unmodified Opinion			
Use of GC is Inappropriate:	Adverse opinion: <table><tr><td>Liquidation Basis:</td><td>When GC not appropriate, Mngt may elect to prepare FS as per another basis (Liquidation) → UNMODIFIED OPINION → mention in EOM para (SA 706)</td></tr></table>		Liquidation Basis:	When GC not appropriate, Mngt may elect to prepare FS as per another basis (Liquidation) → UNMODIFIED OPINION → mention in EOM para (SA 706)
Liquidation Basis:	When GC not appropriate, Mngt may elect to prepare FS as per another basis (Liquidation) → UNMODIFIED OPINION → mention in EOM para (SA 706)			
GC Appropriate but Material Uncertainty Exist:	Use of the GC Basis of Accounting is Appropriate but a Material Uncertainty Exists: ➤ Use separate section with a heading that includes reference to the fact that a material uncertainty related to going concern exists alerts users to this circumstance. <table><tr><td>Determine whether Adequate disclosure regarding this is given in F.S.?</td></tr></table>		Determine whether Adequate disclosure regarding this is given in F.S.?	
Determine whether Adequate disclosure regarding this is given in F.S.?				



	Yes	• Unmodified opinion, And • separate section: "Material Uncertainty Related to Going Concern"
	No	• Qualified opinion or Adverse opinion: As SA 705 • In Basis for Qualified (Adverse) Opinion: State that → material uncertainty exists → may cast significant doubt on entity's ability to continue as a GC and FS do not adequately disclose this matter
No assessment	If mngt unwilling to make or extend its assessment → consider the implications for A.report.	

➤ **Other Points:**

Significant delay in Approval of FS	Ask Reason from Mngt & TCWG → If auditor believes that its due to event relating to GC → Perform additional procedure as given above, when such even identified → and consider impact on reporting also, as given below
Adequate disclosure of Events in FS:	• Principal events/conditions may cast significant doubt on entity ability to continue as GC • management's plans to deal with them • Disclose that it has material uncertainty related to GC, in significant doubt on GC, may unable to realize its assets and discharge liabilities
For Litigation :	In answer mention: SA 250 + SA 570 + Co. Act 143(3)(j) of Rule 11

General Master Answer → When, auditor concludes that → **management's use of the G.C is appropriate** in the circumstances **but a material uncertainty exists**:

Part 1 → Auditor shall determine whether the FS:

- 1) **Adequately disclose the principal events** or conditions (E&C) that may cast significant doubt on the entity's ability to continue as a G.C **and management's plans to deal with these events** or conditions; and
- 2) **Disclose clearly that there is a material uncertainty** related to E&C that may cast significant doubt on the entity's ability to continue as a G.C and, so, **may be unable to realize its assets & discharge its liabilities.**

Part 2 → if There is Adequate Disclosure in FS →

- (a) Express **Unmodified Opinion** &
- (b) Include **Separate Section** under Heading, "**M.U relating to G.C**" to:
 - (i) Draw attention of the note of FS, that disclose the matter related to G.C
 - (ii) **State that these events or conditions indicate that a M.U exists** that may cast significant doubt on the entity's ability to continue as a G.C & that the auditor's **opinion is not modified in respect of the matter.**

also required to report as per **clause (xix) of CARO 2020** (explain Caro Clause)

(Also Explain the Given Question → Events & Conditions explained in Qns)

➤ **Going Concern Reporting Qns:**

Q15. Involve Uncertainty about G.C, & Suitably Disclosed in Notes to Accounts. State reporting requirement

Hint: Refer Above "General Master Answer"

Q16. Govt ban export to Korea, (in which company has Major customer) → G.C assumption is appropriate but M.U exist → this fact duly reflected in FS.

Hint: Refer Above "General Master Answer"

Q17. Power generating company uses Coal as raw material, but due to some scam in coal block allotment, it's Ban. KMP's also left company, not have W.C. finance. Etc. → All these **not reflected in FS**. → Auditor's Action ?

Hint: When the use of **G.C. Accounting Is Inappropriate** but FS prepared using G.C → express :

- (a) **Qualified / Adverse** Opinion (b) in **basis of Opinion** mention that M.U exist for G.C, but not reflected in FS
- Explain All G.C issues in Given Case → "**Adverse Opinion**" required + **CARO Clause xix**

Q18. Chemical Manufacturer → **received a Show cause** notice form Tribunal for Violating Environmental Laws



(Penalty of Rs. 500 Crore), Unaudited Profit show Rs.35 Crore → (Disclosed this matter in FS Footnote as: company has received a show cause notice from Tribunal. judgment would be in favour of company, no provision created) → How auditor to report this matter (MTP'24 & SM)

Hint: SA 250 → Law not have direct effect on FS (i) Inquire mgnt (ii) Inspecting correspondence.

- Sec 143(3)(j) r.w. Rule 11(a) → report whether Company disclosed impact of pending litigation in FS.
- SA 570 → determine in FS (i) Adequate disclosure of events & Condi. (2) Disclose clearly that there is M.U.
- If Adequate disclosure not made: (a) Qualify/Adverse (b) in basis of Modified/Adverse Opinion
- In given case, Penalty is more than Profit → issue **adverse opinion**

Q19. Company has 1 illegal project, Litigation pending on Court → It loose, May lead to Bankruptcy. Auditor Action ?

Hint: SA 250 → Non-Compliance has material effect & not reflected in FS → Qualify/Adverse (SA 705)

SA 570 → Event/condition significant doubt on G.C → No disclosure in FS → material & pervasive → **Adverse Opin.**

Q20. Company Accepted that use of G.C assumption is inappropriate and itself disclosed the same in F.S notes.

Hint: → auditor shall express adverse opinion. whether or not F.S include disclosure of the inappropriateness of G.C

➤ Other Integrated Qns:

Q21. Company has Definite plan to close business in Short time. FS prepare on the same basis as Last Yr. → Just additional Note that Business shall cease in near Future. Auditor indicated this in KAM only by a reference to a possible Cessation. Comment on Auditor reporting. (Old)

Hint: Mngt intent to liquidate is a Event of significant doubt on G.C. → SA 570 → If event & Cond (E&C). identified that cast sig. doubt on GC but no M.U : Evaluate **whether FS give Adequate Discl.**

SA 701 → when matter relating to G.C determined as KAM → explain that a M.U related to E&C that may cast significant doubt on entity ability to continue as G.C is by KAM →, also Auditor's responsibility to communicate KAM Therefore, auditor is required to Communicate the KAM as per SA 570 in above stated manner. Simple reference as to a possible cessation of business is not sufficient

Q22. Company disclosed the Suit in Notes (that it exist), no provision, because mgnt saying it's without merit (Old)

Hint: AS 29 / Ind AS 37 → contingent liability is possible obligation → arises from past events & existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events

- SA 570 → Pending legal or regulatory proceedings can be events → may cast significant doubt about GC.
- When GC is appropriate → but MU exists, → determine whether FS adequately describe events & mgnt plans
- given case → evaluate the source data that suit is without merit. If the auditor finds uncertainty → request mgnt to make 5 crore provision → If not → qualify.

Q23. Trade Payable Ageing (In Crores):

Particular	Less than 1 yr	1-2 yr	2-3 yr	More than 3 yr	Total
Others	2	4	3	1	10

& current ratio, NP ratio drastically decreased, (-ve) drawing power. There is no information in FS & notes

Hint: Company not able to pay to O/S 1 year or more (80% of total dues), Financial ratios are adverse, etc. etc. so MU exists may cast doubt on GC → no express disclosure of this fact in FS → issue qualified or adverse

Q24. C.S.Qn. Infinity Hospitality Ltd → business of running hotels in tourist destinations. long-term leases ranging from 10 to 12 years lock in, not cover the force majeure clause (i.e., Will not be able to cancel contract in case of extra-ordinary events).

capital structure of the company was debt oriented and over-leveraged. Primary working capital was blocked There were landslides and roads were blocked. The entire tourist season was washed away. The impact on travel, tourism and hospitality business was very severe.

Based on the case scenario, you are required to provide your answers to the following: - (SM)

Q.1 What additional audit procedures must the auditor undertake as per SA 570 based on facts given in case?

Hint: [Refer: Additional Audit Procedures: When Events or Conditions are Identified - Full Table]



Q.2: what RAP should auditor consider for arriving at a conclusion based on the mngt assertion of entity being GC?

Hint: [Refer the "RISK ASSESSMENT PROCEDURE"] ..Hint as below:

RAP required by SA 315, whether events or conditions exist that may cast doubt ability to continue GC →

Consider whether mngt has already performed preliminary assessment of entity's ability to continue as G.C:

- Discuss the assessment with mngt and determine whether mngt has identified events and conditions that, individually or collectively, cast doubt on ability to continue as G.C. & if so, mngt's plan to address them.
- The auditor shall **specifically draw attention of Management on following events** or condition and get the response on how they plan to address them:
 - ✓ The company is debt heavy and over leveraged. The leased properties are having considerable lock-in period with absence of force majeure clause. There are no contingency reserves available with company. All these factors shall be taken into account while performing RAP.

Q.3. What should be approach of the auditor if the Mngt agrees that the material uncertainly exists, but the entity is a Going Concern? Also discuss reporting requirements

Hint: [Refer "Reporting Requirement" → Summarized as below]

Uncertainty exist, but GC is appropriate → Determine whether the financial statements:

- Adequately disclose principal events or conditions that make a significant doubt & mngt's plan to deal
- Disclose clearly → material uncertainty related to events or conditions may cast significant doubt on entity ability to continue as G.C & therefore, that it may be unable to realize its assets, and discharge liabilities
- The disclosures may include:
 - Mngt's evaluation of significance of events or conditions
 - Significant judgements made by mngt as a part of its assessment of entity ability to continue as GC
 - Disclosures about magnitude of potential impact of principal events or conditions, & likelihood & timing of the occurrence
 - Auditor express unmodified opinion & separate section heading "Material Uncertainty Related to G.C" :
 - Draw attention to the note in the FS that discloses the events or conditions and
 - State that events are conditions indicate that a material uncertainty exists

Q.4 What if the auditor believes, on the basis of his additional audit procedures → entity is not a G.C., but the mngt is not accepting the same? What course of action the auditor needs to undertake ?
auditor is required to express an adverse opinion.

Q.5: What kind of written representation does auditor need to obtain in case of scenario covered in Q3 above? needs to obtain W.R. from mngt / TCWG, regarding their plans for future action & feasibility of these plans.

MCQ Summary of Above Case Study Qn:

- Which is Not a financial event as per SA 570 G.C → Opening of a new chain of hotels by renowned competitor
- mitigating measure as the management is unable to pay lease rentals → Restructure the lease agreement and negotiate for deferment and relief [Do not terminate the employees]
- Which is not a responsibility of the auditor relating to communicating events may cast significant doubt on the entity's G.C. assertion? → Perform additional audit procedures to identify events/ conditions beyond 12 months from the date of F.S (Because it's mngt's responsibility)
- Written Representation need to be mandatorily obtained from: → CFO

SA 580: Written Representation:

Define:	• It is a <u>written statement by Mngt</u> provided to the auditor to <u>confirm certain matters</u> or to support other audit evidence. • It does <u>not include financial statements</u>, assertions therein, or supporting books and records.		
Matters covered in WR:	Mngt resp.:	Request Mngt to provide a W.R that it has <u>fulfilled its responsibility for the preparation of the FS</u> in accordance with the applicable FRF	
	Other SA:	Other SAs require the auditor to request written representations	



	Auditor determine:	If, in addition to such required representations, the auditor determines that it is necessary to obtain one or more W.R to support other audit evidence relevant to the FS or one or more specific assertions in the FS, the auditor shall request such other written representations.
Date of WR:	Shall be as near as practicable to the date of A.report, but not after, the date of the auditor's report on the FS	
Period Covered:	- The WR shall be for all financial statements and period(s) referred to in the auditor's report. - as mngt needs to reaffirm that the W.R it previously made w.r.t prior periods remain appropriate - The auditor's report cannot be dated, before the date of the written representations	
CFO	W.R. is for some matters is mandatory to be acquire from CFO	

Q25. State basic elements/Features of Management Representation Letter. [old] → Hint: Refer Above Full Table

Q26. Mngt argued that W.R. can be Verbal also (not written) → further what should date & period of W.R, OR

Q27. W.R dated 1st April 2024, Mngt is saying that can't provide W.R of Earlier period F.S, as they were not there
Hint: SA 580 → W.R are necessary A.evidence, → & A.report cannot be dated, before date of W.R.

Refer Above table : "Date of W.R.", "Period Covered"

Situations may arise where current Mngt were not present during all periods referred to in A.report. → they may say that they are not in position to provide W.R. because they were not in place during the period. This does not diminish such persons' responsibilities for the FS as a whole. → W.R that cover whole relevant period(s) still applies.
If mngt does not provide W.R → reevaluate Integrity of mngt, take appropriate action & Impact on A.report (SA 705)

➤ FORM OF W.R

- It shall be in form of "representation letter" addressed to the auditor.
- If L&R requires mngt to make written public statements about its responsibilities, → that Matter again Not Needed to be included in the representation letter.

Q28. (Hint RTP May'25) → Case study → (a) can WR be Verbal (b) What should be form of W.R ?

➤ W.R as Audit Evidence (it's Corroborative A.E, Not SAAE)

[Trick: A.evidence kya hota hai ? Kya ye A. evidence hai ? Ha hai par SAAE nii hai ... baaki evidence bhi chahiye]

- Audit Evidence:** info. used by auditor in arriving at conclusions on which audit opinion is based.
- Similar to inquiry it's A.Evidence:** W.R are necessary information that auditor requires in audit. Accordingly, similar to responses to inquiries, written representations are audit evidence
- Requested From:** those responsible for preparation & presentation of FS.
- Not SAAE:** Although WR provide necessary audit evidence, they do not provide SAAE on their own about any of the matters with which they deal.
- Not affect other Evidence:** Furthermore, fact that mngt has provided reliable W.R. does NOT affect the nature or extent of other audit evidence that the auditor obtains about the fulfillment of management's responsibilities, or about specific assertions.

Q29. Auditor not able to get confirmation about Value of Machine → so he accepted Mngt certificate to prove it.

Hint: physical verification of assets is primary responsibility of Mngt. But, auditor is required to examine the verification programme adopted by mngt & must satisfy himself about existence, ownership & valuation of assets. → SA 580 → auditor should seek corroborative evidence from Other sources also, → & should evaluate whether such W.R are reasonable & consistent with other evidences, But → W.R cannot be a substitute for other audit evidence
→ Given case is a limitation on the scope of his examination → so, Auditor is not right.

➤ Reliance / Reliability of W.R.



Doubt Over Reliability of W.R.:

If auditor has concerns about the competence, integrity, ethical values or diligence of Mngt, or about its commitment →	Auditor shall determine the effect that such concerns on ✓ Reliability of representations (oral or written) & ✓ Audit evidence in general
if WR inconsistent with other audit evidence →	Perform audit procedures to resolve the matter (consider whether RAP remain appropriate, if Not, revise risk assessment & NTE of FAP)
If matter remains unresolved →	Reconsider the assessment of competence, integrity, ethical values or diligence of mngt , or of its commitment to or enforcement of these, & shall determine the effect of this on • Reliability of representations (oral or written) and • Audit evidence in general.
If auditor concludes that the WR are not reliable →	Take appropriate actions , including effect on the opinion in the auditor's report in accordance with SA 705 .

MCQ: If auditor identified significant issue relating to mngt integrity/competence etc. → but auditor still concluded that W.R are reliable → in such case → this Significant matter will be documented as per SA 230

Q30. what is meant by "W.R" and indicate to what extent an auditor can place reliance on such representations.
Hint: Explain above topics → "Define" W.R., "W.R. as Audit Evidence" (i.e., Although W.R provide necessary audit evidence, they do not provide SAAE on their own), "Matters covered in WR", "Reliance / Reliability of W.R"

➤ Mngt Refuse to Provide W.R.

Q31. In the course of audit of ABC Ltd. its **Mngt refuses to provide WR**. As an auditor what is your duty?

As per SA 580 "WR" → if mngt does not provide one or more of the requested W.R. the auditor shall:

- (i) **Discuss the matter** with management,
- (ii) **Re-evaluate the Integrity of the management** and evaluate the effect that this may have on the reliability of representations (oral or written) and audit evidence in general, and
- (iii) **Take appropriate actions**, including determining the possible effect on the opinion in the auditor's report.

The auditor should **disclaim** an opinion on the FS if mngt does not provide W.R in accordance with SA 705 "Modifications to the Opinion in the Independent Auditor's Report".

➤ Obtain W.R as per SA 540 (i.e., Assumptions & Estimates are Reasonable):

Q32. Substantial amount is recognized for **Obsolescence of inventory & warranty Provision** → Auditor wants to obtain W.R to determine whether the assumption & estimates used are reasonable. (old)

As per SA 540 → obtain W.R from mngt &, where appropriate, TCWG → whether they believe significant assumptions used in making A/cing estimates are reasonable. **SA 580** → discusses the use of W.R .
WR about accounting estimates recognised or disclosed in the FS may include representations:

[Trick: jo bhi a/cing estimate h, wo bilkul "Appropriate" hai or humne uska "Dhindhora" peet diya hai hai nd "Hum aisa hi karenge" > baaki agar "subsequently" aage kuch change ho to to kuch kah nahi sakte]

- (i) About the **appropriateness** of measurement processes, including related assumptions & models, used by mngt in determining a/cing estimates in the context of applicable FRF, & consistency in application of processes.
- (ii) That **disclosure** related to accounting estimates are complete & appropriate under the applicable FRF.
- (iii) That the assumptions appropriately reflect management's **intent & ability to carry out specific** courses of action on behalf of the entity, where relevant to the accounting estimates and disclosures.
- (iv) That **no subsequent event** requires adjustment to the accounting estimates and disclosures included in FS.

Q33. Mngt denied to provide W.R. in respect of **obsolescence of inventory and warranty obligations** in FS, auditor



has issued a clean report. Please comment. [old]

Hint: Exactly same Answer a above Question & SA 580 → if mngt does not provide requested WR shall

(a) Discuss with mngt; (b) Re-evaluate integrity of (c) Take appropriate actions, including SA 705.

➤ **Other Integrated Qns:**

Q34. audit was completed and report dated 31.7.23 was issued.

Point out, if there is any, **anomaly in written representation** reproduced below:

15th April, 2023 → To CTK & Associates Chartered Accountants

Hint: → Date of W.R. shall be as near as practicable to, but not after, the date of the auditor's report.

In the given situation, W.R. is dated 15th April 2023. The audit report is dated 31st July 2023.

It could signify that all subsequent events after date of F.S requiring adjustments or disclosure may not have been adjusted or disclosed in F.S by management

CHAPTER 7.1- REPORTING

SA 700, 701, 705, 706, 710, 720

SA 700- FORMING AN OPINION AND REPORTING ON FS

Applicable:	• On General Purpose set of FS	
Auditor's Objective:	- To form an opinion on FS based on evaluation of conclusions drawn from A.evidence obtained; - To express clearly that opinion through a written report.	
Definition: (Special trick :-)	General purpose financial statements	Special purpose financial statements
	FS prepared in accordance with general purpose framework	FS prepared in accordance with Special Purpose Framework
	General purpose framework	Special purpose framework
	FRF designed to meet Common financial info. needs of wide range of users , it may be: 1) Fair presentation framework 2) Compliance framework	FRF designed to meet financial information needs of specific users , it may be: 1) Fair presentation framework 2) Compliance framework
	Fair Presentation Framework	FRF that requires compliance with the requirements of framework , & : - Acknowledges explicitly or implicitly that, to achieve fair presentation of the FS, it may be necessary for mngt. to provide disclosures beyond those specifically required by the framework, Or - Acknowledges explicitly that it may be necessary for mngt. to depart from a requirement of the framework to achieve fair presentation of the FS. Such departures are expected to be necessary only in extremely rare circumstances
	Compliance Framework	FRF that requires compliance with the requirements of framework But: Does not include acknowledgements as given in Fair presentation framework.
Auditor shall also evaluate as to <u>whether the FS achieve fair presentation</u> by considering: - The overall presentation, structure and content of the FS; and - Whether the FS, including the related notes, represent transactions and events in a manner that achieves fair presentation.		
Unmodified Opinion (SA 700)	The auditor shall express an unmodified opinion when, - Auditor concludes that the FS are prepared, in all material respects, - in accordance with applicable FRF	
Modified Opinion (SA 705)	Auditor shall modify opinion as per SA 705, If the auditor: - Concludes that based on A.evidence obtained → FS as whole are NOT free from MM, Or, Unable to obtain SAAE to conclude that → FS as whole is free from MM	
Language of Unmodified opinion:	<u>When FS prepared with Fair Presentation Framework:</u> - In our opinion, the accompanying financial statements present fairly, in all material respects, [...] in accordance with [the applicable financial reporting framework]; or - In our opinion, the accompanying financial statements give a true and fair view of [...] in accordance with [the applicable financial reporting framework] <u>When FS prepared with Compliance Framework:</u> The auditor's opinion shall be that the accompanying FS are <u>prepared, in all material respects, in accordance with [the applicable financial reporting framework]</u>.	



[Not appropriate to use phrases → "with the foregoing explanation" or "subject to" i.r.t Unmodified opinion]

➤ To Form an Opinion Evaluation by auditor:

Conclusion shall take into A/c [Not in SM]	Obtain reasonable assurance → FS prepared in all material aspect as per FRF & Obtain reasonable assurance that FS as whole are free from MMS: <u>That conclusion shall take into account:</u> a) Whether SAAE has been obtained; b) Whether uncorrected misstatements are material , individually or in aggregate; c) The evaluations .
Evaluation by Auditor to check whether FS are prepared in accordance with requirements of applicable FRF:	
Specific Evaluation by auditor (Evaluate whether) [Not in SM]	<i>Trick: Dr. STEP or,</i> <i>Trick: "FS Relevant & reliable" hi tab kahlaaega jab "Accounting policy" & "Estimate" sahi ho bilkul, & "Disclosure" me "terminology" bhi bata dna</i> 1) The info. presented in the FS is relevant, Reliable , comparable, and understandable 2) The A/cing Policies selected & applied are consistent with the applicable FRF & appropriate; 3) The FS adequately disclose Significant accounting policies selected and applied; 4) The accounting Estimates made by mngt are reasonable 5) The FS provide adequate Disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the FS; and 6) The Terminology used in the FS, including the title of each FS, is appropriate

Q1. disclosed "Contingent liability" (without quantifying the effect & proper explanation) → how this disclosure affects them while forming an opinion on. **(Old)**

Hint: Ind As 37 → brief description of the nature of the contingent liability needed

(a) estimate of its financial effect; (b) indication the uncertainties reg. amount or timing of any outflow; and (c) the possibility of any reimbursement.

SA 700 → evaluate in view of applicable FRF requirement → [Refer Above: "Specific Evaluation by auditor"]

Given case, modify opinion → considering the financial effect of liability not disclosed properly.

➤ Elements of AUDITOR's REPORT (shall be in Writing)

Q2. Enumerate the 'Basic Elements of Audit Report' as enshrined in SA 700. [old]

As per SA 700, → the auditor's report includes the following basic elements: [TAO-B-GK-M-AAO-SPD]

	Heading	Content
1	Title	clearly indicates that it is the report of an independent auditor
2	Addressee	To whom the auditor's report is to be addressed, Generally Shareholders or TCWG (Partner's in case of Firm)
3	Auditor's Opinion	Heading " Opinion " 1) Identify the entity whose financial statements have been audited 2) State that the financial statements have been audited ; 3) Identify the title of each statement comprising the financial statements 4) Refer to the notes , including the summary of significant accounting policies ; and 5) Specify the date of, or period covered by, each FS comprising the FS
4	Basis for Opinion	Heading " Basis for Opinion ": 1) States that the audit was conducted in accordance with Standards on Auditing ; 2) Refer section of auditor's report that describes auditor's responsibilities under SAs; 3) 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 4) States whether auditor believes → obtained sufficient & appropriate Audit evidence to provide a basis for the auditor's opinion.
5	Going Concern	Where applicable, the auditor shall report in accordance with SA 570 (Revised).
6	Key Audit Matters [KAM]	For audits of complete sets of general-purpose FS of listed entities , the auditor shall communicate key audit matters in the auditor's report in accordance with SA 701. [L&R may require communication of KAM for audits of entities other than listed entities.]
7	Mngt Responsibility for FS	a) Preparing the FS as per applicable FRF, & for such IC as mngt determines is necessary to enable the preparation of FS that are free from MMS, whether due to fraud or error b) Assessing the entity's ability to continue as a going concern and whether use of GC basis of A/cing is appropriate as well as disclosing, if applicable, matters relating to GC The auditor's report shall use the term that is appropriate in the context of the legal framework applicable to the entity and need not refer specifically to "management" . In some entities, the appropriate reference may be to TCWG or other (<u>When oversight are different from those who fulfill the responsibilities</u>)
8	Auditor's Responsibilities for Audit of FS :	
	Location of A. responsibility for FS audit	• Within the body of report • Within an appendix to the auditor's report, then, auditor's report shall include a reference to the location of the appendix, Or, • On website of an appropriate authority: By a specific reference within the auditor's report to the location of such a, where L&R or national auditing standards expressly permit the auditor to do so. (If not inconsistent with, requirements of this SA)
9	Other Reporting Responsibilities	• If the auditor addresses other reporting responsibilities in the auditor's report on the FS that are in addition to the auditor's responsibilities under the SA's, Titled: Report on "Other Legal and Regulatory Requirements" i.e., CARO • If other responsibility presented in same section → clearly differentiate the other reporting responsibilities from the reporting that is required by the SAs • If separate section → 2 heading as → "Report on the Audit of the FS" → now next to that → "Report on Other Legal and Regulatory Requirements"
10	Signature:	by engagement partner & Name of Audit firm + Membership no. + Firm Reg. no. + UDIN [In case of Individual CA → Signed in individual name or firm name of sole proprietor] [In case of Partner Firm → sign in the firm name → only the partner in firm who is CA]
11	Place	Ordinarily CITY where the audit report is signed
12	Date	Date of Auditor's Report: Not earlier than the date on which auditor has obtained SAAE

Q3. Draft relevant portion of Audit report for → Auditor issued **Unmodified opinion**, But **Material Uncertainty exist** for **G.C** due to Pending Litigation (Appropriate disclosure in FS)

Answer: **Material Uncertainty Related to Going Concern**

We draw attention to Note 10 in the FS, which indicates that the outcome of a litigation on account of labour laws is pending during the year 31/03/23. As stated in Note 11, this event or condition, indicate that a **M.U exists** that may cast significant doubt on Company's ability to continue as a G.C. Our opinion is not modified i.r.o this matter.

➤ **Auditor's Responsibilities for the Audit of the Financial Statements:**

Trick for above > OMR Sheet bharte waqt > Skepticism rkha h .. y meri hi responsibility hai > ye chiz examiner ne phle hi communicate kar di thi

I) This section of the auditor's report shall state:



a) Objectives of the auditor to:	(i) Obtain reasonable assurance → FS as a whole → free from MM whether due to fraud or error (ii) Issue an auditor's report that includes the auditor's opinion .
b) Reasonable:	It's reasonable assurance, not guarantee that it will always detect MMS
c) Misstatements can arise from fraud or error:	(i) They are considered material if → expected to influence the economic decisions of users (ii) Provide a definition or description of materiality as per applicable FRF

II) The Auditor's Responsibilities for the Audit of the FS section of the auditor's report shall further:

a) Professional skepticism	State that auditor exercises professional judgement & maintains professional skepticism throughout the audit.
b) State Auditor's responsibilities [RIA ki GF meri responsibility hai]	i) To identify and assess the ROMM → whether due to fraud or error → Design and perform A.procedures responsive to those risks → Obtain SAAE for auditor's opinion ii) Obtain an understanding of Internal control → relevant to the audit iii) Evaluate appropriateness of A/cing policies & Reasonableness of estimates iv) conclude appropriateness of management's use of Going concern basis of accounting v) When FS are prepared in accordance with a Fair presentation framework → whether FS represent the underlying transactions & events in to achieves fair presentation.

III) The Auditor's Responsibilities for the Audit of the FS section of the auditor's report also shall:

a) Communication as per SA 260:	State that the auditor communicates with TCWG → planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control
b) Listed Co.	For audit of Listed company → state that auditor provides TCWG statement that → it complied with relevant ethical requirements regarding independence
c) SA 701	For Listed co. → KAM are communicated in accordance with SA 701.

Q4. Auditors have affirmed in **A.report communication of significant audit findings including significant deficiencies in I.C. to TCWG. Where such matters included in A. report & importance of such communication.**

Hint: Such matters are stated in "**The Auditor's Responsibilities for the Audit of the FS**" section.

Communication of significant audit findings & deficiencies → Such communication **assists TCWG in fulfilling their responsibility to oversee the financial reporting process** and in fulfilling their oversight responsibilities.

➤ 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:

Q5. auditor's report referred the International SA's *in addition to* SA's of ICAI. advise auditor reg A.report

As per SA 700, → an auditor may be required to conduct an audit as per, in addition to the SA's issued by ICAI, the International SA's or auditing standards of any other jurisdiction. **If this is the case, auditor's report may refer to SA's in addition to the International SA's, but the auditor shall do so only if:**

- 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:**
 - To form a **different opinion, or**
 - Not to include** an **EOM or OM** paragraph that, in the particular circumstances, is required by SAs; and
- 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 SA's. However, reference to "**law or regulation**" in above paragraph shall be read as reference to the SA's. The auditor's report shall thereby identify such SA's



When auditor's report refers to both the ISAs or auditing standards of a specific jurisdiction & SA's issued by ICAI, the auditor's report shall clearly identify the same including the jurisdiction of origin of the other SA's

➤ Supplementary Information Presented with the Financial Statements:

Q6. Company in addition to FS → Prepare 1 additional P&L that disclose specific expenses & is in appendix of FS (not covered in applicable FRF) → How to Deal in A.report ? Or

Q. Notes of FS include an Explanation or Reconciliation, to comply with another FRF (Old)

If supplementary information that is not required by the applicable FRF is presented with the audited FS:

- 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.

That an additional P&L that discloses specific items of Expenses → auditor may consider this to be supplementary information that can be clearly differentiated from the FS.

Additional P&L A/c is NOT considered an integral part of audited FS & auditor shall evaluate that supplementary information is presented in a way that sufficiently & clearly differentiates it from audited FS.

SA 701 : Communicating Key Audit Matters in The Independent Auditor's Report:

Applicability:	Applicable in audit of Listed companies only, However, SA 705 (Revised) prohibits the auditor from communicating key audit matters when the auditor disclaims an opinion on the FS, unless required by law or regulation
Define KAM:	- KAM are those matters that, in auditor's professional judgement were of most significance in the audit of the FS of the current period. - Key audit matters are selected from matters communicated with TCWG
Purpose of KAM:	Q7. Explain clearly the purpose of communicating key audit matters. [old] - To enhance the communicative value of auditor's report by providing greater transparency about the audit that was performed. In Auditor's Judgement → Communicating KAM provides additional information to intended users of FS to assist them in understanding those matters that, in the auditor's professional judgement, were of most significance in the audit of FS of current period. In Management Judgment → Communicating KAM may also assist intended users in understanding the entity and areas of significant management judgement in audited FS.

Matters Determine KAM: [RJS]	Q8. what are the matters that auditor should keep in mind while determining KAM. [old] The auditor shall determine, <u>from the matters communicated with TCWG</u>, those <u>matters that required significant auditor attention</u> in performing the audit. In making this determination, the auditor shall take into account the following: [RJS] (i) Areas of higher assessed ROMM or significant risks identified in accordance with SA 315 Identifying & Assessing the ROMM through Understanding the Entity & Its Environment. (ii) Significant auditor judgments relating to areas in FS that involved significant mngt Judgment, including a/cing estimates that have been identified as <u>having high estimation uncertainty</u>. (iii) The effect on the audit of Significant events or transactions that occurred during period
Examples of KAM	1. Assessment of Impairment 2. Provision for losses and contingencies 3. Valuation of financial instruments, 4. Matters relating to Revenue recognition, 5. Taxation matters

Q9. Direct Question → "define KAM" & "discuss factors determining KAM". [old]

Q10. Company has Complicated revenue contract, involve significant effort in revenue by audit team member → this is also communicated to TCWG → Mngt is saying revenue can't be a KAM in A.report. (Old)

Hint: SA-701, Refer Above "Matters Determine KAM" (Now explain given case → it's KAM)

Q11. Implementation of ERP during year → Due to this Significant effect on Auditor's strategy → Can it be KAM ?
As this matter not linked with matter disclosed in FS, so can it be KAM ? (Old + MTP'23)

Hint: refer above: "Matters determine KAM" → Matters communicate with TCWG are generally linked with FS, However, these matters are Not Always KAM → rather which are most significant to Audit, are considered as KAM.
→ Further, there can be matter which are Significant for auditor attention (KAM), but not disclosed as in FS, Like, Implementation of New IT System (if such a change had a significant effect on the auditor's overall audit strategy), Mainly when changes in system affect revenue recognition, Hence, It's **KAM**

➤ **KAM is Not Substitute or Not to Report when:**

KAM is Not Substitute:	SA 705 Modification	Key audit matter is not a substitute for the matter that giving rise to modified opinion under SA 705
	SA 570 Event doubt on GC	KAM is not a substitute for reporting required under SA 570 w.r.t. Material event & condition → existence of M.U as to events that cast significant doubt on an entity ability to continue as Going Concern. (Auditor shall report modification / Going concern in accordance with applicable SA, and include a reference to basis for Qualified [Adverse] opinion or the material ascertaining related to going concern section in the KAM Section)
	Disclosure in FS	Its not a substitute for disclosures in the FS that the applicable financial reporting framework requires
		Separate opinion on Individual Matter
In case of Disclaimer of Opinion (SA 705) → Non to Include KAM		
Circumstance in which KAM Not to Communicate:	Q12. KAM & Circumstances in Which a Matter Determined to Be a KAM Is Not communicated, <u>Circumstances in Which a Matter Determined to Be a KAM Is Not Communicated in Report:</u> (i) Law or regulation precludes public disclosure about the matter; or (ii) In extremely rare circumstances, the <u>auditor determines that the matter should not be communicated in the auditor's report because the adverse consequences</u> of doing so would reasonably be expected to outweigh the public interest benefits of such communication. This shall not apply if the entity has publicly disclosed info. about matter.	



- Q13.** MTP 2024 → → Mngt has **waive off some Creditor/Liability UNILATERLY** → as Raw material was Defective, → even **refused Creditor** to obtain External confirmation (as it may be used by creditor as proof of liability)
- ⇒ **As, Liability** is a present obligation of the entity to transfer an economic resource (Settle, Transfer, Replace)
- ⇒ **SA 505** refusing E.C not appear valid & Reasonable → **Maintain Professional Skepticism** for Possibility of misstatement, → perform alternative A.procedure & consider implication of same for her audit.
- ⇒ **SA 705** → Modify opinion when (a) Obtain SAAE that FS not free from MMS (b) Unable to Obtain SAAE
- ⇒ in this case, **KAM is not Proper, Modify the opinion** as per SA 705 (**Inability to obtain SAAE**)

➤ Language for Communicating KAM

Q14. advice on "Communicating Key Audit Matters" in the Auditor's Report. Guide him. [old]

The auditor shall describe each KAM, using an **appropriate subheading, in a separate section** of auditor's report under the heading "Key Audit Matters".

The introductory language in this section of the auditor's report shall state that:

- KAM are those matters that, in the auditor's professional judgment, were of **most significance** in the audit of the FS [of the current period]; and
- These matters were addressed in the context of the audit of the FS as a whole, and in forming the auditor's opinion thereon, and the auditor does **not provide a separate opinion** on these matters.

The description of each KAM in the KAM section of the auditor's report shall include a reference to the related disclosure(s), if any, in the FS and shall address:

- Why the matter was considered to be one of most significance** in audit and therefore determined KAM
- How the matter was addressed** in the audit.

The auditor shall describe each key audit matter in the auditor's report unless:

- Law or regulation precludes public disclosure about the matter; or
 - In extremely rare circumstances, auditor determines that the matter should not be communicated in auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication. This not-apply if entity has publicly disclosed this matter.
- Shall not communicate a matter as KAM → when auditor required to modify (SA 705) → as result of that matter.

Eg. presentation in auditor's report if auditor has determined there are **no KAM Identified i.e. communicate KAM** → [Except for the matter described in the Basis for Qualified (Adverse) Opinion section or M.U Related to G.C section,] We have determined that there are no [other] KAM to communicate in our report.]

Q15. Issued **adverse opinion**, Further, there is **No KAM other than that.**, whether need to report KAM (old)

Hint: SA 700 & 701 → Communicating **KAM is not a substitute for disclosures in the FS.**

- When qualified or adverse opinion (SA 705), presenting the description of a matter in Basis for Q/A Opinion
- When expresses a qualified or adverse opinion, **communicating other KAM would still be relevant** for enhancing user understanding of audit.
- the auditor **MAY determine that no other matters are KAM**, in the given case, Adverse Opinion & KAM as: → **KAM: Except for the matter described in the Basis for Adverse Opinion section, we have determined that there are no other key audit matters to communicate in our report.**

➤ Other Integrated Qns:

Q16. Listed Company → **Audit report extract**, communicated with CFO → "Company **recognize revenue** when goods control is transferred, contract is **Complex (require Judgement)**, However Revenue policy is **in compliance with Ind AS 115** → **We tested few samples** for revenue checking " → What auditor trying to report (SM)

Hint: → Above is in nature of **KAM & under heading "Key audit matters"** → **[Refer Above Notes → "Define KAM"]**

- KAM determine from matters **communicated with TCWG**, which require **auditor significant attention** in audit.



- Above matter → revenue is complex, require judgement, also describe how matter addressed by auditor.

SA-705 MODIFICATION TO THE OPINION IN THE INDEPENDENT AUDITOR'S REPORT

SA 700	SA 705: 3 Types of Modified Opinion		
Unmodified Opinion	Modified Opinion (3 types)		
	Qualified Opinion	Adverse Opinion	Disclaimer of Opinion

➤ Which type of opinion is appropriate?

Decision regarding which type of modified opinion is appropriate depends upon:

Material	The nature of the matter giving rise to the modification, that is, • Whether the financial statements are materially misstated or, • in case of an inability to obtain SAAE, may be materially misstated; and
pervasiveness	The auditor's judgement about the pervasiveness of the effects or possible effects of the matter on the FS. (<u>not localised to any one or two elements</u> of a FS, but the impact is <u>across various elements</u> of the FS) Meaning of Pervasive: (i) Are not confined to specific elements, accounts or items of the FS; (ii) represent a substantial proportion of FS; or (iii) In relation to disclosures, are fundamental to users' understanding of the FS.

Objective:	Modified opinion on the financial statements that is necessary when: (a) auditor concludes, based on A.evidence obtained, FS as a whole is not free from MMS; or (b) auditor is unable to obtain SAAE to conclude that FS as a whole are free from MMS.		
Circumstances when modification require:	1) Auditor concludes, based on audit evidence obtained → FS as whole are not free from MM , or 2) The auditor is unable to obtain SAAE to conclude that the FS as a whole are free from MM.		
Types of modifications		Pervasive	Not Pervasive
	Material Misstatement	ADVERSE	QUALIFIED
	SAAE not obtained	DISCLAIMER	QUALIFIED

➤ 3 Types of Modified opinion:

Qualified Opinion	Adverse Opinion	Disclaimer of Opinion
The auditor shall express a qualified opinion when auditor: a) Having obtained SAAE, concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the FS; or b) Unable to obtain SAAE on which to base the opinion, but auditor concludes that the possible effects on the FS of undetected misstatements, if any, could be material but not pervasive.	The auditor shall express an adverse opinion when auditor: Having obtained SAAE → Concludes that Misstatement → Individually or in the aggregate are both material & Pervasive	The auditor shall disclaim an opinion when: He is unable to obtain SAAE & He concludes that the possible effects on the FS of undetected misstatements could be both material & pervasive <u>(Refer Below**)</u>

** Disclaim Opinion:

- The auditor shall disclaim an opinion when, in **extremely rare circumstances** involving **multiple uncertainties**, the auditor concludes that, notwithstanding having obtained SAAE regarding each of the individual uncertainties, it is not possible to form an opinion on the FS due to the potential interaction of the uncertainties and their possible cumulative effect on the FS.
- If, after accepting the engagement, → **Mngt Imposed Limitation on audit scope** → that the auditor considers likely to result in the need to express a **qualified opinion or to disclaim** an opinion on the FS, the auditor shall **request that management remove the limitation** → If **refuses to remove** the limitation, the auditor shall **communicate the matter to TCWG**, unless all of TCWG are involved in managing the entity, and determine whether it is possible to perform **alternative procedures to obtain SAAE**.

Q17. In what **circumstances** does A.report require **Modifications** ? and **Types of Modifications** ? (SM)

Hint: Refer above "**Circumstances when modification require**" & Above Given table of "**3 Types of Modified Opinion**")

Q18. Auditor found significant observation → could lead to **MMS**. Mngt has different view on that. **Reporting** ? (SM)

Hint: (**Explain Above Given table of "3 Types of Modified Opinion"**)

Q19. Misstatement of non-write off of a huge trade receivable (2 crore) → mngt refused to correct → PBT Profit of Rs. 1 crore in company. **Materiality** is 5% of PBT. What type of Opinion ? (SM)

Hint: Refer above "**Circumstances when modification require**" & "**Definition of "Adverse Opinion"**"

Uncorrected misstatement is 200% of PBT → Hence **Material**. Further, **Substantial write off** can **Significantly impact financial position** → so **Material & pervasive** → **Adverse Opinion**

➤ **Form and Content of the Auditor's Report When the Opinion is Modified**

Q20. "When the auditor modifies the audit opinion, **brief the special considerations required for expressing:**

(a) **Qualified Opinion**; (b) **Adverse Opinion** and (c) **Disclaimer of Opinion**.

Answer:

Auditor's Opinion Section: Use Following "Heading" : i.e., "Qualified Opinion" / "Adverse" "Disclaimer"		
Qualified Opinion	Adverse Opinion	Disclaimer of Opinion
Qualified opinion due to a MM in the FS, state that: In the auditor's opinion, <u>except for the effects of the matter(s) described in the Basis for Qualified Opinion</u> section: When reporting in accordance with: a) Fair presentation framework: accompanying financial statements <u>present fairly, in all material respects (or give a true and fair view of) [...]</u> in accordance with [the applicable FRF]; or b) Compliance framework: accompanying FS have been <u>prepared, in all material respects, in accordance with [the applicable FRF]</u>. Unable to obtain SAAE:	Adverse opinion, the auditor shall state that, in the auditor's opinion, <u>because of the significance of the matter(s) described in the Basis for Adverse Opinion</u> section, When reporting in accordance with: a) Fair presentation framework: accompanying financial statements <u>do not present fairly (or give a true and fair view of) [...]</u> in accordance with [the applicable FRF]; or b) Compliance framework: accompanying financial statements have <u>not been prepared, in all material</u>	Auditor Disclaims an opinion, a) State that the auditor does not express an opinion on the accompanying FS; b) State that, <u>because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion</u> section, the auditor has not been able to obtain SAAE to provide a basis for an audit opinion on FS; and c) Amend the statement required by SA 700 (Revised), which indicates that the FS have been audited, to state that the "auditor was engaged to audit the FS."



the auditor shall use the corresponding phrase "except for the possible effects of the matter(s) ..." for the modified opinion

respects, in accordance with [the applicable FRF].

[Instead of FS have been Audited]

Q21. certain audit evidence were not consistent with the affirmation made in the FS. Affect auditor's report ? Or, audit evidence of incorrect disclosure of related party transactions and structured finance deals
Hint: SA 705 → The decision regarding which type of modified opinion is appropriate depends upon:

- nature of matter giving rise to modification, whether FS are MMS or, inability to obtain SAAE, may be MMS; &
- The auditor's judgment about the pervasiveness of the effects or possible effects of the matter on FS.

In present case, → modify his report as per SA 705, Should issue qualified or adverse opinion:

- express a qualified opinion when, misstatements, → **material, but not pervasive**, to the FS
- express an adverse opinion when misstatements, → **material and pervasive** to the FS.

➤ In Case of Disclaimer of Opinion

Description of Auditor's Responsibilities <i>[SA's me likha hai wo sab follow kara hai > Independence follow karne ka > wo kari > fir bhi SAAE nii mila]</i>	When Auditor disclaims an opinion due to inability to obtain SAAE, description of the auditor's responsibilities required by SA 700 include only following: - A statement that the auditor's responsibility is to conduct audit in accordance with SA's and to issue an auditor's report - A statement that, however, <u>because of the matter(s) described in the Basis for Disclaimer of Opinion section</u>, the auditor was not able to obtain SAAE to provide a basis for an audit opinion on the FS; and - statement about auditor independence & other ethical responsibilities required by SA 700 (Revised). [Auditor's report shall not include the reference to section of auditor's report that describes the <u>auditor's responsibilities</u> and statement & <u>auditor's believing that sufficient appropriate audit evidence obtained</u>
KAM (SA 701)	Unless required by law or regulation → Not include a Key Audit Matters as per SA 701
SA 720:	Not include Other information (SA-720)
Communicate TCWG:	When auditor expects to modify opinion → shall communicate with TCWG the circumstances that led to the expected modification and the wording of the modification. Auditor is required to discuss & deliberate with TCWG the audit findings & type of misstatements
Special Point:	In case of Adverse or Disclaimer opinion → Audit report shall not contain unmodified opinion i.r.t any element in FS

Q22. description of auditor's responsibilities → when auditor disclaims an opinion ? [old]

Hint: Refer Above "Description of Auditor's Responsibilities"

➤ Inability to Obtain SAAE:

It can be Due to:

Circumstances beyond the control of the entity:	<u>Examples of circumstances beyond the control of the entity include when:</u> - The entity's accounting records have been destroyed. - The accounting records of a significant component have been seized indefinitely by governmental authorities.
Circumstances relating to the nature or	<u>Examples of circumstances include when:</u> The entity is required to use the equity method of accounting for an associated entity,



timing of the auditor's work:	and the auditor is unable to obtain SAAE about the latter's financial information to evaluate whether the equity method has been appropriately applied. - The timing of the auditor's appointment is such that the auditor is unable to observe the counting of the physical inventories. - The auditor determines that performing substantive procedures alone is not sufficient, but the entity's controls are not effective.
Limitations imposed by management:	Examples of an inability to obtain SAAE when: - Management prevents the auditor from observing the counting of the physical inventory. - Management prevents the auditor from requesting external confirmation of specific account balances.

Q23. auditor's inability to obtain SAAE (Scope limitation) may arise from: (i) Circumstances **beyond the control of entity**; (ii) Circumstances w.r.t **auditor's work**; or (iii) **Limitations imposed by mngt.** → Explain with **examples**. **[old]**
Hint: Refer above Notes (Explain Full table):

➤ **Due to a Mngt Imposed Limitation after the Auditor Has Accepted the Engagement**

Mngt has **imposed limitation on scope** of audit that the auditor considers is **likely to result in the need to** express a **qualified opinion** or to **disclaim an opinion** on the FS → Request that Mngt remove the limitation:

If management remove the limitation:	If management refuses to remove the limitation:	
Proceed with audit procedures	- Auditor shall communicate the matter to TCWG, unless all TCWG involved in Mngt & - Perform alternative procedures to obtain SAAE	
	Still unable to obtain SAAE & Possible effects of misstatement:	
	Material & not pervasive	Material & Pervasive
	Qualify the opinion	Withdraw from the audit, where practicable & Possible under L&R - If not possible to withdraw: Disclaim an opinion
As Discussed above → If Auditor Withdraw → before withdrawing, the auditor shall communicate to TWCG any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion		

Q24. After accepting Audit → mngt imposed certain limitations on scope → result inability to obtain SAAE → indicate your response ? **Hint:** (refer Above Table → "**mngt imposed limitation**")

Q25. What are **obligation of auditor**, who **withdraw due to Non-cooperation** of mngt (Old)
Hint: SA 705 → Inability to obtain SAAE due to limitation → **Practicability of withdraw depend on Completion stage**.

- If withdrawal necessary → Communicate matter to regulators & entity owners
- In case of Resignation → Sec 140(2) of Co.Act apply → within 30 days file it to registrar.

➤ **If Auditor's Decide to WithDraw:**

TWCW:	Before withdrawing → communicate to TCWG any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion.	
Withdrawal not possible: [LISTED Co.]	For Listed Companies: As per SEBI LODR, not permit withdrawing from engagement without issuing audit / review report:	
	Case: If the auditor resigns within 45 days from the end of a quarter of FY →	Then Auditor Shall Before such resignation, Issue limited review/ audit report for such quarter



	If the auditor resigns after 45 days from the end of a quarter of a FY →	Issue the limited review/audit report for such quarter <u>as well as</u> the next quarter
	if the auditor has signed the limited review/ audit report for the first 3 quarters of a FY →	Issue the limited review/ audit report for the last quarter of such FY <u>as well as</u> the audit report for such FY
Unlisted Co.:	ICAI announcement: That auditor of an unlisted company shall not mention "professional pre-occupation" as a reason for the resignation. → The auditor shall <u>mention the reasons clearly</u> for the resignation in the resignation letter issued to the Company.	

➤ Basis for Opinion

Basis for Opinion: Amend the "heading" of "Basis of Opinion" as follows:		
Basis for Qualified Opinion	Basis for Adverse Opinion	Basis for Disclaimer of Opinion
	Include in the Basis for Opinion Section:	
If MMS of FS relates to specific amount in FS →	Description and quantification of the financial effects of the misstatement, unless impracticable	
If it is not practicable to quantify →	Auditor shall so state in this section	
If MMS of FS relates to narrative disclosure →	Explanation of how the disclosures are misstated	
If MMS of FS relates to non-Disclosure of info →	a) Discuss the non-disclosure with TCWG b) Nature of the omitted information c) Unless prohibited by law or regulation, include the omitted disclosures	
Inability to obtain SAAE →	Reasons for that inability	

Q26. auditor of ABC Ltd → draft **qualified opinion & basis for qualified opinion** for departure from applicable FRF:
 • Further, Between the FS date & auditor's report date, there was a fire in the entity's production facilities, which was disclosed as a subsequent event → In auditor's judgment, matter is importance for fundamental to users' understanding of the FS. But not require significant auditor attention in the audit of the FS in current period [old]

Answer:

Qualified Opinion

We have audited the standalone FS of ABC Limited ("the Company"), which comprise the balance sheet as at March 31, 20X1, and the statement of P&L, (statement of changes in equity) and the statement of cash flows for the year ended, & notes to the FS, including a summary of significant accounting policies and other explanatory information (in which are included the Returns for the year ended on that date audited by the branch auditors of the Company's branches located at (location of branches)) → 2. In our opinion and to the best of our information and according to the explanations given to us, except for the effects of the matter described in the Basis for Qualified Opinion section of our report, the aforesaid FS present fairly, in all material respects, or give a true & fair view in conformity with the accounting principles generally accepted in India of the state of affairs of the Company as at March 31st, 2XXX and profit/loss, (changes in equity) and its cash flows for the year ended on that date.

Basis for Qualified Opinion

As explained in Note XX of Financial statement, The Company's short-term marketable securities are carried in the statement of financial position at xxx. Management has not marked these securities to market but has instead stated them at cost, which constitutes a departure from the Accounting Standards prescribed in section 133 of the Companies Act, 2013. The Company's records indicate that had management marked the marketable securities to market, the Company would have recognized an unrealized loss of Rs.xxx in the statement of comprehensive income for the year. The carrying amount of the securities in the statement of



financial position would have been reduced by the same amount at March 31, 20X1, and income tax, net income and shareholders' equity would have been reduced by Rs.xxx, Rs.xxx and Rs.xxx, respectively. We conducted our audit in accordance with Standards on Auditing (SAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the FS section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the FS under the provisions of the Companies Act, 2013, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the ICAI's Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion. The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with SA 701.

- Those responsible for oversight of the FS differ from those responsible for the preparation of the FS.
- In addition to the audit of the FS, the auditor has other reporting responsibilities required under Co Act 13

Q27. auditor of XYZ Ltd, → draft Adverse Opinion & basis for adverse opinion due to MMS of Consolidated FS.

- The CFS are **materially misstated due to non-consolidation of a subsidiary.** → MMS is **pervasive** & The effects of the misstatement on the CFS have not been determined because it was not practicable to do so. [old]

Answer:

Adverse Opinion : We have audited the accompanying consolidated FS of XYZ Ltd (hereinafter referred to as the "Holding Company") and its subsidiaries (the Holding Company and its subsidiaries together referred to as "the Group"), its associates & jointly controlled entities, which comprise the consolidated balance sheet as at March 31, 2XXX, the consolidated statement of P&L, (consolidated statement of changes in equity){where applicable} & consolidated statement of cash flows for the year then ended, and notes to the consolidated FS, including a summary of significant accounting policies (hereinafter referred to as the "consolidated FS").

In our opinion and to the best of our information and according to the explanations given to us, because of the significance of the matter discussed in the Basis for Adverse Opinion section of our report, the accompanying consolidated FS DO NOT give a true and fair view in conformity with the accounting principles generally accepted in India, of their consolidated state of affairs of the Group, its associates and jointly controlled entities, as at March 31, 20XX, of its consolidated profit/loss, (consolidated position of changes in equity) {where applicable} and the consolidated cash flows for the year then ended.

Basis for Adverse Opinion : As explained in Note X, the Group has not consolidated subsidiary PQR Company that the Group acquired during 20XX because it has not yet been able to determine the fair values of certain of the subsidiary's material assets and liabilities at the acquisition date. This investment is therefore accounted for on a cost basis. Under the accounting principles generally accepted in India, the Group should have consolidated this subsidiary and accounted for the acquisition based on provisional amounts. Had PQR Company been consolidated, many elements in the accompanying consolidated financial statements would have been materially affected. The effects on the consolidated financial statements of the failure to consolidate have not been determined. We conducted our audit in accordance with Standards on Auditing (SAs) specified under section 143(10) of the Companies Act, 2013. Our responsibilities under those Standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group, its associates and jointly controlled entities, in accordance with the Code of Ethics and provisions of the Companies Act, 2013 that are relevant to our audit of the consolidated financial statements in India under the Companies Act, 2013, and we have fulfilled our other ethical responsibilities in accordance with the Code of Ethics and the requirements under the Companies act, 2013. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our adverse opinion.

Q28. auditor of ABC Ltd, → draft Disclaimer Opinion & basis for Disclaimer opinion due to Inability to obtain SAAE, for multiple elements of F.S → was also unable to obtain audit evidence about entity's inventories & receivable. material & pervasive to the FS. [old]

Answer

Disclaimer of Opinion: We were engaged to audit the FS of ABC & Associates ("the entity"), which comprise the balance sheet as at March 31, 20XX, the statement of P&L, (the statement of changes in equity) (where



applicable) and statement of cash flows for the year then ended, and notes to the FS, including a summary of significant accounting policies.

We do not express an opinion on the accompanying FS of the entity. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for Disclaimer of Opinion:

We were not appointed as auditors of the Company until after March 31, 20X1 and thus did not observe the counting of physical inventories at the beginning and end of the year. We were unable to satisfy ourselves by alternative means concerning the inventory quantities held at March 31, 20X0 and 20X1, which are stated in the Balance Sheets at Rs. xxx and Rs. xxx, respectively. In addition, the introduction of a new computerized A/c's receivable system in September 20X1 resulted in numerous errors in accounts receivable. As of the date of our report, management was still in the process of rectifying the system deficiencies and correcting the errors. We were unable to confirm or verify by alternative means accounts receivable included in the Balance Sheet at a total amount of Rs. xxx as at March 31, 20X1. As a result of these matters, we were unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded inventories and accounts receivable, and the elements making up the statement of P&L (and statement of cash flows).

Q29. Acquired 55% shares → not prepared Conso. FS, because on date of Acquisition the Fair value Not been ascertained → frame Opinion para. → HINT: MMS is Pervasive → so Draft "Adverse Opinion" & "Basis of..."

Q30. Company financing arrangements are & company is unable to re- negotiate or obtain the replacement financing. Company may be unable to realize its assets and discharge its liabilities. Notes to accounts → FS discuss magnitude of financing arrangements; expiration do not include discussion on the impact. Thus, notes do not fully disclose this fact. What opinion ? [old] → HINT: Inadequate Disclosure → Qualified

Q31. (Exactly same Qn as above i.e., → unable to re- negotiate or obtain replacement financing, etc.) But this time → financial statements (and notes thereto) do not disclose this fact. → HINT: Adverse Opinion

Q32. During audit, unable to obtain SAAE about a single element of the consolidated FS. Auditor was also unable to obtain audit evidence about the financial info of a JV investment that represents over 90% of the entity's net assets. What kind of opinion needed ? → Hint → Material & Pervasive → "Disclaimer"

Q33. loans and advances of ₹ 55,00,000/- given to Sarvagya Pvt Ltd, Company has not furnished any agreement to Auditor, So he unable to verify term, interest and other. → Hint: Material + Non-Pervasive → Qualified

Q34. faced an extraordinary event (earthquake), destroyed a lot of business, it indicate M.U on ability to continue as GC. notes to the FS of the company do Not disclose this. → material & pervasive. → "Adverse Opinion"

Q35. → debtors of ₹ 150 crores, no balance confirmation was received. → provision for Bad debt is inadequate. → Further for Inventories (which constitutes 40% of the total assets), mngt not done physical verification & not maintained adequate inventory records. Auditor unable to undertake physical inventory. → Hint: → "Disclaim"

➤ OTHER INTEGRATED QUESTIONS

Q36. The Mngt had introduced the new computerized accounts receivable system, still mngt is rectifying new system deficiencies → the earlier system of accounting of receivables had been discarded. The auditor was unable to obtain SAAE about entity's accounts receivable and inventories. (Material & Pervasive)

(a) Write opinion paragraph. (b) auditor's responsibility to report a KAM for which no disclosures in FS

(c) Where should the **placement of the KAM** section be in the auditor's report? [old]

Hint: (a) Disclaimer Opinion (Now Write Para for "Disclaimer of Opinion" & "Basis of Disclaimer")

(b) When communicating KAM → the fact that there are no disclosures in FS related to a matter which is KAM does not relieve auditor from requirement to communicate it. (communicate it as KAM unless L&R precludes public)

(c) Place of KAM Section:

- Generally placed **after Basis for Opinion paragraph** & **before Management's Responsibility Para**
- In case, 'Material uncertainty relating to G.C para exist (SA 570) → then **KAM section is placed after that**.
- SA 706 → When a **KAM section is presented** → **EOM para may be presented either directly before or after KAM**

SA 706 Emphasis of Matter Paragraph and other matter paragraph

Objective:	To draw users' attention , when in the auditor's judgement it is necessary to do so, by way of clear additional communication in the auditor's report, to: - A matter, although appropriately presented or disclosed in the FS, that is of such importance that it is fundamental to users understanding of the FS; or - As appropriate, any other matter that is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.	
	Emphasis of Matter Paragraph (EOM)	Other Matter Paragraphs (OM)
Definition:	EOM para included in auditor's report: that refers to a matter appropriately presented or disclosed in the FS → that, in auditor's judgement, is of such importance that it is fundamental to users' understanding of FS.	OM para included in auditor's report: that refers to a matter other than those presented or disclosed in the FS → that, in the auditor's judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.
Condition to include:	• If the auditor considers it necessary to draw users' attention • to matter presented or disclosed in FS • that, in auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements	• If the auditor considers it necessary to communicate/Draw user Attention • matter other than those that are presented or disclosed in the FS • that, in auditor's judgement, is relevant to users' understanding of audit, auditor's responsibilities or the auditor's report
Para shall be included, Provided:	SA 705: Auditor would not be required to modify the opinion as a result of matter & If SA 701 applies, Matter has not been determined to be a key audit matter	- This is not prohibited by L&R ; & - If SA 701 applies, the matter has not been determined to be a key audit matter
Separate section:	When the auditor includes an EOM Para: - Include para in separate section of auditor's report with appropriate heading that includes term "Emphasis of Matter"; - Include in para 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 Not modified: Indicate that auditor's opinion is not modified i.r.o the matter emphasized.	When the auditor includes an OM para: in the auditor's report, the auditor shall include the paragraph within a separate section with the heading "Other Matter," or other appropriate heading.
Examples:	1) Early application (where permitted) of a new accounting standard that has a material effect on the FS.	1) Branch is audited by another auditor



["Pahle" "earthquake" aaya tha, "Baad" me "Subsequent" kya hoga wo bhi pata nhi]	2) A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position 3) An uncertainty relating to future outcome of exceptional litigation or regulatory action. 4) A significant subsequent event that occurs between the date of the FS and the date of the auditor's report. 5) Etc.	2) Another set of FS prepared in accordance with another general-purpose framework and that the auditor has issued a report on those financial statements 3) Auditor's report is intended solely for the intended users, and should not be distributed to or used by other parties. 4) Etc.

Specific requirements for the auditor to include **Emphasis of Matter paragraphs** in the auditor's report in certain circumstances. These circumstances include:

- When a **FRF** prescribed by L&R would be **unacceptable** but for the fact that it is prescribed by L&R.
- To alert users that the FS are prepared in accordance with a **special purpose framework** (SA 800).
- When facts **become known to the auditor after the date of the auditor's report** and the auditor provides a new or amended auditor's report (i.e., **subsequent events**).

Inclusion of EOM para will Not Affect Auditor's Opinion,

An Emphasis of Matter paragraph is **not a substitute for**:

SA 705:	A modified opinion in accordance with SA 705, when required by the circumstances
SA 570:	Reporting in accordance with SA 570, when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a GC
FRF Disclosure:	Disclosures in FS that the applicable FRF requires management to make, or that are otherwise necessary to achieve fair presentation

Communicate with TCWG:

If the auditor expects to include an EOM or OM para, in the auditor's report, the auditor shall communicate with TCWG regarding this **expectation and the wording** of this paragraph.

Place in AR	Before or After KAM (Key audit report), based on auditor's judgement.

Q37. Write short note on EOM para Or, Enumerate certain important matters included in EOM para.

Hint: A report can be **Modified for matters that do not affect the Auditor's opinion**. (has obtained SAAE that the matter is Not MMS in the FS) → refer above notes → "condition to include", "Examples of EOM & "specific circumstance EOM needed"

[However widespread use of EOM para may diminish effectiveness of Auditor's communication about such Matter]

Q38. Examples of **EOM** which may have **adverse effect on functioning** of company & **not affect functioning** (Old).

Answer

Examples of EOM which may have an **Adverse Effect on the Functioning** of the Company: Examples of circumstances where the auditor may consider it necessary to include an EOM para are:

(pahle Earthquake aaya.. baad me subsequently ...)

- Early application** (where permitted) of a new accounting standard that has material effect on FS.
- A **major catastrophe** that has had, or continues to have, a significant effect on entity's financial position.
- An **uncertainty relating to the future outcome** of exceptional litigation or regulatory action.
- A **significant subsequent event** that occurs between the date of FS and the date of the auditor's report.
- The **going concern assumption is appropriate but** there are several factors leading to a material uncertainty that may cast a significant doubt about the Company's ability to continue as a going concern; or
- a **material uncertainty regarding the outcome of a litigation** wherein an unfavourable decision could result in a significant outflow of resources for the company, etc.



Examples of Emphasis of Matters which may not affect the Functioning of the Company are:

- (i) When a **FRF prescribed by L&R** would be **unacceptable** but for the fact that it is prescribed by L&R.
- (ii) To alert users that the FS are prepared in accordance with a **special purpose framework**.
- (iii) When **facts become known to the auditor after** the date of the auditor's report and the **auditor provides a new or amended auditor's report** (i.e., subsequent events).
- (iv) on **managerial remuneration** which is **subject to the approval of the Central Government**.
- (v) relating to accrual of a contractually receivable claim based on management estimate where the ultimate realisation could be different from the amount accrued;
- (vi) on frauds that have been dealt with in the FS of the company and would not have any a/cing effect on FS.

Q39. EOM is mandated. → when A. Report is on FS prepared in accordance with **Special Purpose Framework [old]**

Hint: **EOM para is mandatory** when FS is as per SPF. → **SA 706 & 800**, A.report on Special purpose FS shall include an **EOM para alerting users** of A.report that FS are prepared in SPF & **not suitable for another purpose**.

Include Para under an appropriate heading:

- **Restriction on Distribution or Use:** In addition to alert required above, auditor may consider it appropriate to indicate that the auditor's report is intended solely for specific users. restricting distribution of report. So, above EOM para maybe expanded to include these **other matters**, and heading may be modified accordingly

➤ Language of EOM & OM Para

Q40. auditor wants to draw the user's attention for some matter, though his opinion is not modified → Draft para:

- 1) company has a **plan to resume its construction activities** of it's thermal power project, which was suspended in FY 2018-19. power project **comprises of the PPE amounting to ₹ 5.95 crore** and CWIP of ₹ 147.50 crore.
- 2) The FS of **5 branches are included in the Standalone FS** (total assets of ₹ 90 crores & total revenue from operations of ₹ 40 crores). The FS of these branches have been **audited by the branch auditors**. (SM)

Answer:

Emphasis of Matter

We draw attention to the following **note of the standalone financial statements**:

Note 27 regarding the plans of the Company to resume construction/developmental activities of a thermal power project. carrying amounts of project at 31/03/21 comprise of PPE of ₹ 5.95 crore & CWIP of ₹ 147.50 crore.

Our opinion is not modified in respect of this matter.

Other Matter

We did not audit the financial statements of 5 branches included in the Standalone FS of the company whose financial statements reflect total assets of ₹ 90 crores as at 31.03.2021 and total revenue from operations of ₹ 40 crores for the year ended on that date. The FS of these branches have been audited by the branch auditors whose reports have been furnished to us, and our opinion in so far as it relates to the amounts and disclosures included in respect of these branches, is based solely on the report of the branch auditors.

Our opinion is not modified in respect of this matter.

Q41. Fancy Ltd transferring it's Delhi branch Business to Nancy Ltd (along with all Assets/Liability), → that branch FS is not prepared as per Going concern, & correctly disclosed this matter in Note XX of FS. → Draft Suitable Opinion Para & basis of Opinion, along with disclosure of Note XX with suitable place in audit report

Hint → Draft "Unmodified Opinion" & "basis", Further, Draft "EOM para"

➤ Other Integrated Qns:

Q42. Observation 1: one of warehouse affected by Major flood (major loss), But not material → Disclosed in FS.

Observation 2: Due to flood, few records completely destroyed (not duplicate record), not pervasive, but material.



Hint: Observation 1 → EOM & Observation 2 → Qualified Opinion

Q43. Govt introduce Law to reduce production. Mngt assessed the impact over financial position & appropriately disclosed the same in FS. → & it's fundamental to users understanding → auditor want to use OM Para.

Hint: SA 706, → disclosed in FS, → shall include an EOM in the auditor's report provided:

(i) not be required to modify the opinion for this matter (ii) Matter is Not KAM

Other Matter Paragraph is not in order, it should be disclosed in Emphasis of Matter Paragraph.

Q44. Business of Executing construction contract → having non-current receivables of Rs.500 Crore. (these are due to cost overruns due to change in work scope by client, it's in arbitration → company considered above amount as Fully recoverable, as stated in Notes). Auditor relied on W.R. by mngt & included in EOM.

Hint: SA 706 → refer above → "Define EOM para" & "Objectives of SA 706" →

Include EOM only when Auditor not be required to modify Opinion as per SA 705.

(given case, Auditor not performed any other A.procedure like Verifying customer contracts, Status of arbitration etc.) → W.R. is not SAAE → so Modify opinion (Can't include EOM)

➤ Difference between KAM & EOM:

Q45. EOM & KAM Difference (RTP - Nov'23)

KAM (SA 701)	EOM (SA 706)
Matters that, in auditor's professional judgment, → <u>most significance in audit</u> of FS of current period. <u>selected from matters communicated with TCWG</u>	Matter appropriately <u>presented or disclosed in the FS</u> that, in the auditor's judgment, is of such importance that it is <u>fundamental to users' understanding</u> of the FS
draw further attention to its relative importance → provides additional information to intended users, auditor's professional judgment, were of most significance in the audit	may be a matter that is not determined to be a KAM as per SA 701 (i.e., <u>because not require significant auditor attention</u>), but in auditor's judgment, is fundamental to users' understanding (i.e., Subsequent event)
provide intended users a basis to further engage with management and TCWG	The auditor may do so by presenting the matter more prominently than other matters in the KAM section (<u>e.g., as the first matter</u>)

SA 710 -Comparative Info & Figures & Comparative FS

Auditor's Objective:	- To <u>obtain SAAE</u> about whether the <u>comparative information included</u> in the FS has been presented, <u>in all material respects, in accordance</u> with the requirements for comparative information in the <u>applicable FRF</u>; and - To report in accordance with the auditor's reporting responsibilities
Comparative Info.	The <u>amounts and disclosures</u> included in the FS in respect of <u>one or more prior periods</u> in accordance with the <u>applicable FRF</u>, it includes: 1) Corresponding Figures 2) Comparative FS
Corresponding Figures:	Q46. Write a short note on <u>Corresponding figures</u>. Comparative information where <u>amounts & other disclosures</u> for prior period are <u>included as an integral part</u> of the current period FS and are <u>intended to be read only in relation to</u> the amounts and other disclosures relating to the current period. The level of detail presented in the corresponding amounts and disclosures is dictated primarily by its relevance to the current period figures



Comparative F.S:	Comparative info where amounts & other disclosures for the prior period are included for comparisons with the FS of the current period but, if audited, are referred to in the auditor's opinion. The level of information included in those comparative FS is comparable with that of the FS of the current period.

➤ Audit Reporting: Corresponding Figures

Auditor's opinion on the financial statements **refers to the current period only**

So, Generally Audit opinion NOT refer to corresponding figures, **Except** in below cases:

Auditor's report in **prior period FS was modified** and the subject matter is **still unresolved** →

(Special :-)

Modify opinion in current audit report (FS) also.

In Basis the Basis for Modification para:

- When Effect on current period figures are material:** Refer to both → current period's figures & corresponding figures in the description of the matter giving rise to the modification (i.e., Basis of modification) when the effects or possible effects of the matter on the current period's figures are material; or
- In other cases (Not Materially affect Current period),** explain that the audit opinion has been **modified because of the effects or possible effects of the unresolved matter** on the comparability of the current period's figures and the corresponding figures.

Auditor's report on **prior period FS was Unmodified**, But in CY auditor obtains audit evidence w.r.t. **existence of material misstatement in prior period F.S.** →

Express qualified/ adverse opinion on current F.S. w.r.t. Corresponding figures if misstatement has not been dealt as required by applicable FRF

(Hence, Prior period FS audit report include modification → **But It's resolved & Properly disclosed + accounted** → auditor's opinion of the **current period need not refer to modifications**)

Prior Period FS Not Audited →

State in an **"Other Matter paragraph"** → that corresponding figures are unaudited. However, it will **not relieve the auditor of the requirement to obtain SAAE** that the opening balances do not contain misstatements that materially affect the current period's FS

Prior Period FS audited by Predecessor Auditor →

If the FS of prior period were audited by a predecessor auditor, + If permitted by L&R to refer Predecessor Auditor's report on Corresponding Figures + Auditor decides to do so → the auditor shall state in an **"Other Matter Para"**:

- That FS of prior period were **audited by predecessor** auditor
- Type of opinion** expressed by him & if modified, then reason
- Date of that report** → unless predecessor auditor's report on the prior period's FS is revised with the FS

Q47. Auditor's opinion shall **not refer to corresponding figures except** in some circumstances. Explain (Old).

Hint: opinion on FS **refers to current period only** → Generally A.opinion NOT refer corresponding figures, **Except:**

Refer above Note → "Auditor's report in **prior period FS was modified** and the subject matter is **still unresolved**" & "Auditor's report on **prior period FS was Unmodified**, But in CY auditor obtains audit evidence w.r.t. **existence of material misstatement in prior period F.S.**"

(Above Answer Ends)

➤ Audit Reporting: Comparative FS

Refer Each Period:	Audit opinion to refer to each period for which F.S. are presented and on which opinion is expressed.		
Opinion of Prior FS is differ now:	If opinion on prior period FS expressed in current period differs from Opinion expressed in the relevant prior period , give substantive reason for difference in Other Matter Para (706)		
Prior Period FS Not Audited (same as above)	Auditor to State in " OM Para " in auditor's report that Comparative figures are Unaudited (However Such statement does not relieve auditor of requirement to Obtain SAAE that opening balances not contain misstatements that materially affect Current period's FS)		
Prior period FS audited by Predecessor Auditor:	If the FS of prior period were audited by a predecessor auditor, in addition to expressing an opinion on the current period's FS, the auditor shall state in an "Other Matter Para": - That FS of prior period were audited by predecessor auditor - Type of opinion expressed by him & if modified, then reason - Date of that report → unless predecessor auditor's report on the prior period's FS is revised with the FS <table border="1" data-bbox="342 621 1516 842"> <tr> <td> MMS exist in Prior-period FS → on Which Predecessor auditor issue report without modification: </td><td> - Auditor shall communicate misstatement with appropriate level of mngt and TCWG and request that the predecessor auditor be informed. - If the prior period FS are amended, and predecessor auditor agrees to issue a new auditor's report on the amended FS of the prior period, the auditor shall report only on the current period </td></tr> </table>	MMS exist in Prior-period FS → on Which Predecessor auditor issue report without modification:	- Auditor shall communicate misstatement with appropriate level of mngt and TCWG and request that the predecessor auditor be informed. - If the prior period FS are amended, and predecessor auditor agrees to issue a new auditor's report on the amended FS of the prior period, the auditor shall report only on the current period
MMS exist in Prior-period FS → on Which Predecessor auditor issue report without modification:	- Auditor shall communicate misstatement with appropriate level of mngt and TCWG and request that the predecessor auditor be informed. - If the prior period FS are amended, and predecessor auditor agrees to issue a new auditor's report on the amended FS of the prior period, the auditor shall report only on the current period		

➤ Auditor's responsibilities regarding comparatives

Q48. short note on Auditor's responsibilities regarding comparatives, Or, corresponding figures? [old]

SA 710, establishes standards on the auditor's responsibilities regarding comparatives.

- The auditor shall **determine whether the FS include the comparative information** required by the applicable FRF & whether such info is appropriately classified. For this purpose, the auditor shall Perform Specific Procedure evaluate whether:
 - The **comparative information agrees** with the amounts and other disclosures presented in the prior period;
 - The **A/cing policies** reflected in comparative info are **consistent** with those applied in current period or,
 - if there have been **changes** in accounting policies, whether those changes have been properly accounted for and adequately presented and **disclosed**.
- **If the auditor becomes aware of a possible MMS** in comparative info, the auditor shall
 - **Perform such additional audit procedures** as are necessary in the circumstances to obtain SAAE to determine whether a MMS exists.
 - **If auditor had audited the prior period's FS**, the auditor shall also **follow relevant requirements of SA 560**
- As required by **SA 580**, **the auditor shall request written representations** for all periods referred to in the auditor's opinion. The auditor shall also obtain a specific written representation regarding any prior period item that is separately disclosed in the current year's statement of profit and loss.

➤ Basis of Modification:

Q49. A. Report of P Ltd → 2019-20 contained Qualification reg. Non-Provision of Doubtful debt Or Decline in Investment Market value. How would you repor in Yr 2020-21, in Below 2 cases

(i) Company does **not make provision** for Doubtful debt in 2020-21 (ii) Maked **adequate provision** in 2020-21 [SM]

Hint: Auditor's responsibilities in cases where audit report for an earlier year is qualified is given in SA 710,

- When the auditor's report on the prior period, included a qualified, disclaimer or an adverse opinion and matter



is resolved and properly accounted for or disclosed in FS as per applicable FRF → the auditor's opinion on the current period need **not refer to the previous modification**.

- if above **modification is unresolved**, → auditor shall **modify the auditor's opinion on current period's FS**.

In the "**Basis for Modification**" paragraph in the auditor's report, the auditor shall either:

(i)	When Effect on current period figures are material	Refer to both → current period's figures & corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or
(ii)	In other cases	Explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.

In the instant Case,

- If P Ltd. does **not make provision** → auditor will have to **modify report for both** current and PY's figures.
- If however, the **provision is made**, the auditor need **not refer to the earlier year's modification**.

Q50. Last year audit report was modified that depreciation is charged to P&L, instead of putting it in CWIP, → whether such modification in P.Y audit report have audit implication on C.Y. ?

Hint: Exact same answer as Above Qn

SA 720- Auditor's Responsibility in relation to Other Information

Objective	To consider whether there is a material inconsistency between the other information & ✓ the financial statements ; <u>or</u> ✓ the auditor's knowledge obtained in the audit respond appropriately when the auditor identifies that such material inconsistencies (Auditor is not required to issue opinion on Other Info , he just need to READ it)
Other Info	Financial or non-financial information (other than financial statements and the auditor's report thereon) included in an entity's annual report.
Not Applicable:	This SA is NOT applicable on <u>preliminary announcements of financial information</u> ; or <u>securities offering documents</u> , including <u>prospectuses</u> .

Example of "Amounts" & "Other Items" in Other Information

Q51. Examples of "Amount" & "Other Items" included in "Other Information" as per SA 720 (Old - Nov'19)

Examples of Amounts or Other Items that May Be Included in the Other Infor: (This list is not exhaustive)

Amounts:

- Items in a **summary of key financial results**, such as **net income**, **earnings per share**, **dividends**, sales and other operating revenues, and purchases and operating expenses.
- Selected **operating data**, such as **income from continuing operations** by major operating area, or sales by geographical segment or product line.
- Special items**, such as **asset dispositions**, **litigation provisions**, **asset impairments**, **tax adjustments**, **environmental remediation provisions**, and **restructuring and reorganization expenses**.
- Liquidity and capital resource information**, such as **cash**, **cash equivalents** and **marketable securities**; **dividends**; and **debt**, **capital lease** and **minority interest obligations**.
- Capital expenditures** by segment or division.
- Financial measures or ratios**, such as **gross margin**, **return on average capital employed**, **return on average shareholders' equity**, **current ratio**, **interest coverage ratio** and **debt ratio**. Some of these may be directly reconcilable to the financial statements.
- Amounts involved in**, and related financial effects of, **off-balance sheet arrangements**.
- Amt's involved in** **guarantees**, **contractual obligations**, **legal or environmental claims**, & other contingencies.



Other Items:

- (i) Explanations of critical **accounting estimates and related assumptions**.
- (ii) Identification of related parties and descriptions of transactions with them.
- (iii) Articulation of the entity's policies or approach to manage commodity, foreign exchange or interest rate risks, such as through the use of forward contracts, interest rate swaps, or other financial instruments.
- (iv) **Descriptions of the nature of off-balance sheet arrangements**.
- (v) **Descriptions of guarantees, indemnifications, contractual obligations**, litigation or environmental liability cases, and other contingencies, including mngt qualitative assessments of the entity's related exposures.
- (vi) **Descriptions of changes in legal or regulatory requirements**, such as new tax or environmental regulations, that have materially impacted the entity's operations or fiscal position, or will have a material impact on the entity's future financial prospects.
- (vii) Management's qualitative assessments of the impacts of new financial reporting standards that have come into effect during the period, or will come into effect in the following period, on the entity's financial results, financial position and cash flows.
- (viii) General descriptions of the business environment and outlook.
- (ix) Overview of **strategy**.
- (x) Descriptions of **trends in market prices** of key commodities or raw materials.
- (xi) Contrasts of supply, demand and regulatory circumstances between geographic regions.
- (xii) Explanations of specific factors influencing the entity's profitability in specific segments

Special Points:

- Try to obtain document containing Annual report → **Prior to date of audit report**
- If not possible to obtain before date of AR → Read such info. **As soon as practicable**

➤ Auditor's Procedure to Check Whether Inconsistency Exist in FS & Other Info

Q52. Explain **Auditor's Procedure** to evaluate whether any Inconsistency exist between FS & Other Info (Old)

Obtaining the Other Information	The auditor shall: (a) Determine, through discussion with Mngt, which documents comprises the annual report, and the entity's planned manner and timing of the issuance of such documents; (b) Make appropriate arrangements with Mngt to obtain in a timely manner and, if possible, prior to the date of auditor's report, the final version of documents comprising the annual report; (c) When some or all of the documents determined above will not be available until after the date of the auditor's report → request mngt to provide a WR that the final version of the documents 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 & Considering the Other information	The auditor shall READ the other information & consider (a) Whether there is a material inconsistency between the other information & the F.S., (b) Whether there is a material inconsistency between the other information and auditor's knowledge obtained in the audit, in the context of audit evidence obtained and conclusions reached in the audit. While reading the other information, the auditor shall remain alert for indications that the other information not related to the F.S. or the auditor's knowledge obtained in the audit appears to be materially misstated

➤ When Material Inconsistency Identified between FS & Other Info

Material inconsistency identified in other information, perform other procedures to conclude whether:

MMS in Other Information	MMS in F.S.	auditor understanding of entity & its environment need to update



Request mgnt to correct the Other Info / FS:

- 1) **If Mngt Agrees:** determine that correction has been made
- 2) **If Mngt refuse:** refer Below

Other info obtained PRIOR to Date of Audit report	Revision of FS necessary but mgnt. refuse →	Modify the opinion
	Revision of Other info . Necessary, but mgnt. refuse →	➤ Communicate to TCWG that correction needed. <u>If TCWG also refused to Correct:</u> ✓ Consider the implications on auditor's report & "Other Info Section" describing inconsistency ✓ Withdraw from Engmnt (where possible)
Other info obtained AFTER date of audit report	Revision of FS Necessary →	Follow procedure given in SA 560
	Revision of Other info Necessary, but mgnt refuse →	✓ Notify concern to TCWG ✓ Take appropriate action to bring them to attention to user

Q53. MMS in other information exists. Guide Auditor to how to respond to that MMS of other info obtained prior to the date of auditor's report. Or if, Auditor conclude the same after date of auditor's report? [old]

Hint:

If the auditor concludes that a MMS of other info exists, request mgnt to correct the other info. If mgnt:

- (i) **Agrees** to make the correction → Auditor shall **determine that the correction has been made**; or
- (ii) **Refuses** to make the correction → Auditor shall **communicate** the matter with **TCWG** and **request to correct**

If the auditor concludes that a MMS exists in other info obtained prior to the date of the auditor's report, & other info is not corrected after communicating with TCWG, auditor shall take appropriate action, including:

- (i) **Considering the implications for A.report** & communicating with TCWG about how auditor plans to address the MMS in the auditor's report;
- (ii) **Withdrawing from the engagement**, where withdrawal is possible under applicable law or regulation.

If auditor concludes that MMS exists in other Info obtained after the date of auditor's report, auditor shall:

- (i) If the other information is **corrected** → **perform the procedures necessary** in the circumstances; or
- (ii) If the other information is **not corrected after communicating with TCWG** → **take appropriate action** considering the auditor's legal rights and obligations, to **seek** to have the uncorrected MMS **appropriately brought to the attention of users** for whom the auditor's report is prepared

Q54. Annual report indicating downward trend in Market price, However Actual profit in FS gone in Reverse Direction. Mngt is saying audit scope does not cover the disclosure made by mgnt in annual report (IMP)

Hint: Auditor's response when MMS exist in Other Info. (SA-720).

→ Request mgnt to provide support for the basis of management's statements in the other Info. → Based on mgnt's further explanations, → the auditor may be satisfied that the other info is not materially misstated. (For example, management explanations may indicate reasonable and sufficient grounds for valid differences):

if auditor concludes that MMS in other Info exists, → request mgnt to correct the other Info, If mgnt:

- (i) Agrees to make the correction, the auditor shall determine that the correction has been made; or
- (ii) Refuses to make the correction, → communicate the matter with TCWG & request that the correction needed *Mngt statement is incorrect.*

➤ **REPORTING** (read only)

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) **In case of Audit of Listed Entity FS** → the auditor has **obtained**, or **expects to obtain**, other information; Or,



b) In case of Audit of Un-Listed Entity FS → the auditor has obtained some or all of the other information.

Section Shall Include:	
a) Statement that Mngt is responsible for other information:	
b) Identification of: (Exam)	(i) Listed & Unlisted → Other information, if any, obtained by auditor PRIOR to date of auditor's report; & (ii) Listed → For an audit of FS of a listed entity, other information, if any, expected to be obtained AFTER the date of the auditor's report.
c) Statement that auditor's opinion does NOT cover the other information and, accordingly, that 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) Obtained PRIOR to the date of the auditor's report:	When other info. has been obtained prior to the date of the auditor's report, either: (i) A statement that auditor has nothing to report; or, (ii) If auditor has concluded that there is an uncorrected MMS of other information, a statement that describes the uncorrected MMS of the other information

➤ Reporting Prescribed by Law or Regulation (read only)

If auditor is required by a relevant L&R to refer to other information in auditor's report using a specific layout or wording, the auditor's report shall refer to SA's only if auditor's report includes, at a minimum:

- Identification of the other information obtained by auditor prior to the date of auditor's report;
- A description of the auditor's responsibilities with respect to the other information; and
- An explicit statement addressing the outcome of the auditor's work for this purpose.

Some Other Matters (Not covered in SA's):

➤ Notes to A/c's & Qualification:

Qualifications in Audit report	Notes to A/c's in F.S
Auditor records his disagreement on the matters by way of qualifications in the auditor's report, ➤ While Qualifying the report, use phrase: "except for" ➤ Don't use: "With the foregoing explanation" "Subject to" (these are not sufficiently clear or forceful) Should be clear and unambiguous manner Where the Auditor answers any of the statutory affirmations in the negative or with a qualification, his report shall state the reasons for such answer.	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, where Auditor's disagree by qualification

➤ Some Differences:

Q55. Write a short note on Certificate for Special Purpose vs. Audit Report

Certificate	Audit report



A certificate is a written confirmation of the "accuracy of the facts" stated therein and does not involve any estimate or opinion	Term 'report' is used where an expression of opinion is involved. → It usually made after enquiry, examination or review of specified matters and includes auditor's opinion
An auditor may thus, certify the circulation figures of a newspaper or the value of imports or exports of a company.	Auditor gives a report, he is responsible for ensuring that the report is based on factual data, that his opinion is as per facts, & is arrived at by the application of due care & skill.
An auditor's certificate represents that he has verified certain figures and is in a position to vouch safe their accuracy as per his examination of documents and books of account.	opinion may differ from one professional to another., There is no question of exactitude in case of a report since the information contained therein is based on estimates and involves judgement element
Under Co.Act, 2013, a number of situations are there where an auditor is required to issue a certificate, like under Sec 66 of Co. 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.

Q56. Direct Questions on Below Differences:

(i) Reporting to Shareholders vs. Reporting to those Charged with Governance

Reporting to Shareholders	Reporting to those Charged with Governance
Section 143 of Co.Act, 2013 deals with reporting to Shareholders. (Statutory A. Report addressed to members)	SA 260 deals with the provisions relating to reporting to TCWG
Statutory Audit Report is on true and fair view and as per prescribed Format.	It is a reporting on matters TCWG like audit scope, A.procedures, audit modifications, etc.
Statutory Audit Reports are in public domain	It's an internal document i.e., private report.

(ii) Audit Qualification vs. Emphasis of Matter:

Audit Qualification	Emphasis of Matter
SA 705 deals with provisions of Audit Qualification	SA 706 deals with the provisions relating to EOM.
Audit Qualifications are also known as "subject to report" or "except that report". Modifications that there is a MMS in the FS due to which the modification to the opinion of the auditor is necessary.	EOM is included in A.report to draw users' attention to important matters which are already disclosed in FS & are fundamental to users for understanding. EOM presupposes that there is SAAE and the matter has been correctly disclosed.
Audit Qualifications are given when auditor has concluded that the F.S. are materially misstated or do not confirm to the FRF. Depending upon the nature of MMS being pervasive or otherwise the appropriate type of modified opinion is issued.	EOM Para is issued when the auditor feels that it is necessary to invite attention to a particular mater which has been appropriately disclosed in the F.S. which in the opinion of the auditor is necessary for better understanding of the financial statement.



CHAPTER 7.2 : CARO, 2020 & Co. Act

Powers conferred by **section 143(11)** of the Co. Act, 2013, CG issued **Companies (Auditor's Report) Order, 2020**

➤ Applicability:

Applicable to:	• Every company including a foreign company (as defined in Sec. 2(42) of the Co.Act, 2013) : Even to Dormant & Electricity companies also • Applicable in case of branches also																							
Not applicable to:	Insurance company Banking company Company U/s 8 of Co.Act2013 OPC & Small Company under Co.Act Private Company (Not being a subsidiary or holding company of a public company) Below all condition need to be fulfil: Small Company: 2(85) Of Co.Act 2013, other than a public co: (1) Paid Up S/c ≤ Rs. 4 Crores, AND (2) Turnover ≤ Rs. 40 Crores (Imm. preceding FY) (Further it should not be, Sec 8 Co, Holding or Subsidiary of any, Governed by any special act company) <table><tr><td>Paid-up capital & Reserves & Surplus</td><td>As on balance sheet date</td><td>≤ ₹ 1 crore</td></tr><tr><td>Total borrowings from any bank or financial institution</td><td>at any point of time during the FY</td><td>≤ ₹ 1 crore</td></tr><tr><td>Total revenue as disclosed in Schedule III (including revenue from discontinuing operations)</td><td>as per the financial statements</td><td>≤ ₹ 10 crore</td></tr></table> • If Company is small company, then CARO is not applicable even if it falls in Pvt. Co. Limits • CARO shall not apply to the auditor's report on consolidated financial statements except Para 3(xxi).			Paid-up capital & Reserves & Surplus	As on balance sheet date	≤ ₹ 1 crore	Total borrowings from any bank or financial institution	at any point of time during the FY	≤ ₹ 1 crore	Total revenue as disclosed in Schedule III (including revenue from discontinuing operations)	as per the financial statements	≤ ₹ 10 crore												
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Inclusions & Exclusions	• Inclusions: i.e., For CARO applicability, following items are included to calculate limit: <table><tr><td>Paid Up Capital & Reserve</td><td>Borrowing</td><td>Revenue</td></tr><tr><td>Equity share capital</td><td>Loan from Bank, FI, NBFC</td><td rowspan="2">Disclosed in Schedule III comprises of: • Revenue from operations • Other Income. </td></tr><tr><td>Preference share capital</td><td>Loans may be in any form: • Term loan, Demand loans, • Cash credit overdraft, • Export credit, Bill purchased/discounted • Short term, long term • Secured, Unsecured • Credit card O/s </td></tr><tr><td>Amount originally paid up on forfeited shares</td><td rowspan="3">Other than finance company: - Sale of products - Sale of services - Other operating revenues </td></tr><tr><td>Calls in arrear (Deduct)</td></tr><tr><td>Capital reserves</td></tr><tr><td>Revenue reserves</td><td rowspan="6">Other income shall consist: - Interest Income - Dividend Income - Net gain/loss on sale of investments/Fixed Asset - Other non-operating income (net of expenses directly attributable to such income) </td></tr><tr><td>Security premium</td></tr><tr><td>Revaluation Reserves.</td></tr><tr><td>P&L Credit Balance (to be add)</td><td>Non-fund-based credit facilities converted into fund based credit facilities</td></tr><tr><td>P&L Debit Balance (Reduce)</td><td rowspan="2">Interest accrued as well as due</td></tr><tr><td>ESOP Reserves</td></tr></table> • Exclusions: i.e., For CARO applicability, following items are excluded to calculate limit:			Paid Up Capital & Reserve	Borrowing	Revenue	Equity share capital	Loan from Bank, FI, NBFC	Disclosed in Schedule III comprises of: • Revenue from operations • Other Income.	Preference share capital	Loans may be in any form: • Term loan, Demand loans, • Cash credit overdraft, • Export credit, Bill purchased/discounted • Short term, long term • Secured, Unsecured • Credit card O/s	Amount originally paid up on forfeited shares	Other than finance company: - Sale of products - Sale of services - Other operating revenues	Calls in arrear (Deduct)	Capital reserves	Revenue reserves	Other income shall consist: - Interest Income - Dividend Income - Net gain/loss on sale of investments/Fixed Asset - Other non-operating income (net of expenses directly attributable to such income)	Security premium	Revaluation Reserves.	P&L Credit Balance (to be add)	Non-fund-based credit facilities converted into fund based credit facilities	P&L Debit Balance (Reduce)	Interest accrued as well as due	ESOP Reserves
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ESOP Reserves																								



	Paid Up Capital & Reserve	Borrowing	Revenue
	Share application	Loan from individual	Advance received
	Call in advance	Interest accrued but not due	Excise Duty/GST

Q1. types of companies covered under Companies (Auditor's Report) Order, 2020 ? Or, Whether CARO applicable on:
(a) Educating child Ltd company U/s 8 of Co. Act, 2013 **(b)** ASHU PVT. LTD. ,company had borrowed ₹70 Lakhs each from a bank and financial institution independently. Turnover for the year was Rs. 900 lakhs. [OLD]

Hint: → Explain CARO "Applicable to" & "Not-Applicable to" as explained in above notes

(a) Not applicable → u/s section 8 **(b)** Ashu Pvt. Ltd. CARO 2020 is applicable as borrowing in aggregate exceeds ₹1 cr

Q2. Astha Pvt. Ltd. has fully paid capital of ₹ 140 lakh. During the year, company had borrowed ₹ 15 lakh each from a bank and a financial institution independently. It has turnover (Net of excise ₹ 50 lakh which is credited to a separate account) of ₹ 475 lakh. Will CARO, 2020 be applicable to Astha Pvt. Ltd.? [OLD]

Answer

Applicability of CARO, 2020: The CARO, 2020 specifically exempts a private Lts company, not being a subsidiary or holding company of a public company, having a paid up capital and reserves and surplus not more than ₹ one crore as on the balance sheet date and which does not have total borrowings exceeding ₹ 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 ₹ ten crore during the financial year as per the financial statements.

In the case of Astha Pvt. Ltd., it has outstanding loan of ₹30 lakh (₹15 lakh + ₹15 lakh) collectively from bank and financial institution which is less than ₹1 crore ₹ and turnover is ₹4.75 crore i.e. also less than ₹ 10 crore and not exceeding the limit. However, it has paid capital of ₹140 lakh i.e. more than ₹ 1 crore.

Thus, in view of ₹ 140 lakh paid up capital which is exceeding the prescribed limit for exemption, **CARO, 2020 will be applicable to Astha Pvt. Ltd.**

Q3. Pvt. Ltd.'s paid up Capital & Reserves are less than Rs. 50 lakhs & it has no outstanding loan. Its sales are ₹ 6 Cr before deducting Trade discount Rs 10 lakhs & Sales returns Rs. 95 lakhs. services rendered by company Rs. 10L

Hint: theory same as explained in above question → turnover: ₹5.05 crores (6 - 0.10 - 0.95 + 0.10 crore). → not applicable.

Q4. E-Tech Pvt. Ltd., has an aggregate O/S loan of ₹20 lakhs from Banks & ₹30 lakhs from Financial Institutions,

Hint: In the instant case the total borrowings do not exceed ₹100 lakhs during year, CARO reporting is not required

Q5. A Private limited company reports the following position as on 31st March, 2021: → is CARO applicable ? [OLD]

Paid up capital → 60 Lacs	Revaluation reserves → 20 Lacs	Capital reserves → 22 Lacs	P & L A/c (Dr.) → 4 lacs

Hint: → Explain CARO "Applicable to" & "Not-Applicable to" as explained in above notes

- In the present case, paid-up capital and reserves ₹98 Lacs (60 + 20 + 22 - 4), So **CARO is not applicable**

Illustration: H Pvt Ltd. (not a small company) had taken overdrafts from 2 banks with a limit of ₹40 lacs each against the security of fixed deposit and an unsecured overdraft from a financial institution of ₹36 lacs. The said loans were outstanding as at 31st March, **CARO is Applicable**, as Total borrowing amounts to Rs. (40*2 + 36 = 116 lacs)

➤ Matters to be included in Auditor's Report

Para 3(i)]	Property, Plant and Equipment (Link AS 10/Ind As 16)
Adequacy of Records	- Whether the company is maintaining proper records showing full particulars, including quantitative details and situation of <u>Property, Plant and Equipment</u> - Whether the company is maintaining proper records showing full particulars of <u>intangible assets</u>;
Physical verification	- Whether these Property, Plant and Equipment have been physically verified by the management at <u>reasonable intervals</u>; - whether any <u>material discrepancies</u> were noticed on such verification and if so, whether the same have been properly <u>dealt in the books</u> of account; [Note: Reasonable interval depends upon the circumstances of each case i.e. Value of asset,



	Geographical location etc., While an <u>annual verification</u> may be reasonable, it may be impracticable to carry out the same in some cases. Even in such cases, the verification programme should be such that <i>all assets are verified at least once in every 3 years.</i>]					
Title Deed	- Whether the title deeds of all the immovable properties (other than properties where the <u>company is the lessee</u> 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					
Revaluation 10%	- 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 <u>each class</u> of Property, Plant and Equipment or intangible assets;					
Benami	- 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 FS					

Q6. X Ltd. closed its manufacturing operations & sold all its manufacturing assets during March, 2021. However, it intends continue its trading Operation. i.e. fixed assets, company carried out a **physical verification** at 31/03/21 & found a material **discrepancy of ₹1 lac**, which was W/o. Kindly incorporate in your audit report. [OLD]

Hint → Explain Para 3(i) of CARO → Whether mngt verify PPE at reasonable interval, material discrepancies dealt

- SA 570 → perform appropriate procedures to **ensure appropriateness of G.C assumption**, as sold all its mfd FA's
- Auditor should incorporate the below mentioned para in his report:

"As per AS-1, "Disclosure of Accounting Policies", "the enterprise is normally viewed as G.C, that is as continuing its operation for the foreseeable future. It is assumed that the enterprise has neither the intention nor the necessity of liquidation or of curtailing materially the scale of its operations." Although the company has disposed off its manufacturing F.A during the FY ending on 31-3-2021, it is still a going concern in the form of a trading company. "The property, plant and equipment have been physically verified by the mngt at reasonable intervals; material discrepancies were noticed on such verification and the same have been properly dealt with in the books of account;"

Q7. Under CARO, 2020, how would you report: **factory building**, in its FS in the **name of one of its director**, Or, Q. ABC Ltd. owns a piece of **Land**. → The **title deeds is deposited with Bank** for obtaining Loan, CARO, 2020? ,Or, Q. **property is pending to be registered in the name of Company**, due to certain procedural issues associated with the Registration though the Company is having a valid possession. **The Company has disclosed this amount under Fixed Assets though no disclosure of non-registration** is made in the notes [OLD]

Hint: → Para 3(i)(c) of CARO, 2020, whether the title deeds is in name of company

What is Title deeds:

- Registered sale deed / transfer deed / conveyance deed, etc. of land, land & building together, etc. purchased, allotted, transferred by any person including any government, government authority / body / agency/ corporation, etc. to the company.
 - In case of leasehold land and land & buildings together, covered under the head property, plant and equipment (fixed assets), the lease agreement duly registered with the appropriate authority
- If title deeds are not held in name of the company, details thereof to be provided in the below mentioned format:

Description	Gross	Held in	Whether	Period held - indicate	*Reason for not being



of property	carrying value	name of	promoter, director or their relative or employee	range, where appropriate	held in name of company

Q8. Crux → Even if PPE is removed from Active use, and kept in Disposal → So, it's not inspected by mngt from last 10 Year → it's not in compliance with CARO 2020, Clause 1 (a) & (b) → even though it's retired, but inspection is needed (Old)

Para 3(ii)]	Inventories (Link AS 2/Ind As 2)
Physical verification	- 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;
Working capital limit (Excess of Rs. 5 crore)	Whether during any point of time of the year, the company has been sanctioned working capital limits in excess of 5 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;

Q9. For CARO, 2020, Auditor made the following observations, that may be relevant for reporting: [OLD]

Sr	Observations
a	One of the PPE taken on a lease ('right of use') by Sinwar Ltd. was revalued based on the valuation by a registered valuer & net carrying value of PPE in aggregate was changed from ₹4 crore to ₹4.45 crore.
b	During year, cash credit limit of ₹5.5 crore was sanctioned by DMC Bank based on security of current assets which was reduced to ₹4.5 crore after 6 months. In this connection, quarterly returns have been filed by company with the DMC bank which are in agreement with Books

Hint

(a) Explain Clause (i) (d) of Para 3 of CARO 2020, → (i.e., PPE revaluation concept)

Changed from ₹4 crore to ₹4.45 crore i.e. change was 10% or more. → report amount of change of ₹45 lakh

(b) Explain Clause (ii) (b) of Para 3 → (i.e., Working capital loan in excess of 5 crore)

sanctioned a cash credit limit of ₹5.5 crore → report the same in accordance with Clause (ii) (b)

Q10. Physical verification of only 40% of inventory has been conducted by company. Balance 60% will be conducted in next year due to lack of time. As a statutory auditor, how would you report under CARO 2020 [OLD]

Hint: Explain Clause (ii) of Para 3 of CARO, 2020 i.e., conducted at reasonable intervals by mngt → responsibility of the mngt which should normally verify all material items at least once in a year and more often

Requirement of CARO, 2020 has not been fulfilled → consider the impact thereof on FS and his report.

[Note: "Reasonable intervals" depends on circumstances of each case. → nature of inventories, their location and the feasibility of conducting a physical verification, Normally, wherever practicable, all the items of inventories should be verified by the management of the company at least once in a year]

Q11. Jam Pvt Ltd → CA Roy is Auditor. During the year Company obtained working capital facilities from Bank for ₹ 10 crore (goods as primary security). Mngt furnished periodically quarterly statement to bank as follows:

Period of Qtr	Stock Value as per Books (Crore)	Stock Value submitted to Bank (₹ in crore)
Q1-2021-22	11.5	14
Q2-2021-22	14.75	17
Q3-2021-22	11.5	14
Q4-2021-22	15.25	15.25

The management of did not disclose the above variations in notes as there is no variations as on the Balance sheet date how CA Roy should deal and disclosure/reporting requirements if any, as per the Co. Act, 2013 & CARO, 2020. [OLD]



Hint: → Schedule III of Co. Act, →, "where the company has borrowings from banks or financial institutions on the basis of security of current assets, it shall disclose the following :

- (a) **whether quarterly returns** or statements of current assets filed by the company with banks or financial institutions are in **agreement** with the **books** of accounts.
- (b) **if not**, summary of **reconciliation** and reasons of material discrepancies, if any to be adequately disclosed."
- **Further, Explain** → Para(ii) of **CARO 2020** → Working capital excess of 5 Crore
- There are variation in Q-1, Q-2 & Q3 : Reporting required in Co. Act & CARO :

Qtr	Books Value of Stock	Statement to Bank	Variation
Q1-2021-22	11.5	14	Excess reporting of stock to Bank by 2.50 crore
Q2-2021-22	14.75	17	Excess reporting of stock to Bank by 2.25 Crore
Q3-2021-22	11.5	14	Excess reporting of stock to bank by 2.50 crore

Q12. Hint → Always check **Sanctioned Limit** (Not Utilised Limit) for checking W.C exceeding 5 CRORE **[Nov'24]**

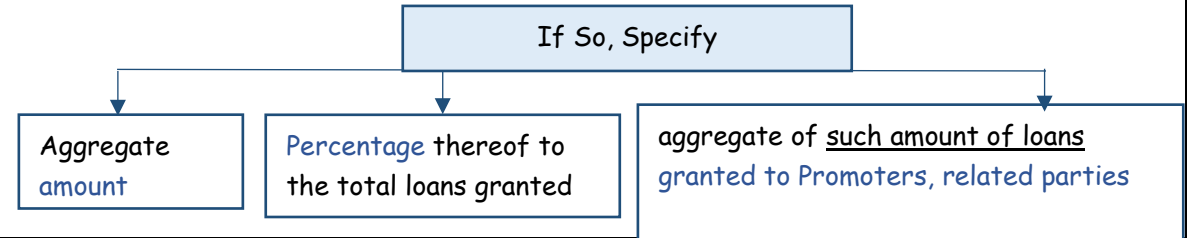
Q13. Hint → Qn given **Different inventories** (FG, RM, Stores, WIP) → So **check % of Difference** between **Physical verification Vs Books** → if change is > 10%, **[(Physical Value (-) Book Value) / Physical Value]** Then report discrepancy **[RTP'25]**

Para 3(iii)	Investments, Guarantee/Security, Loans or Advances Given (Link S-III, SA550)
Whether during the year the company has <u>made investments in</u> , <u>provided any guarantee or security</u> or <u>granted any loans or advances</u> in the nature of loans, secured or unsecured, to companies, firms, Limited Liability Partnerships or any other parties, if so,	
Loan, Advance, Guarantee & Security - To Group - Non- Group	Whether during the year the <u>company has provided loans or provided advances</u> in the nature of loans, or stood <u>guarantee</u> , or provided security to any other entity [<i>not applicable to companies whose principal business is to give loans</i>], if so, indicate- (A) The aggregate " amount during the year ", and " balance outstanding " <u>at the balance sheet date</u> with respect to such loans or advances and guarantees or security to subsidiaries, joint ventures and associates ; (B) 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 ;
Terms prejudicial	whether the <u>investments made</u> , <u>guarantees</u> provided, security given and the terms and conditions of the grant of all <u>loans and advances</u> in the nature of loans and guarantees provided are not prejudicial to the company's interest ;
Loan given Schedule	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
Overdue >90 days	if the amount is overdue, state the total amount overdue for more than 90 days , and whether reasonable steps have been taken by the company for recovery of the principal and interest
New Loan to repay old loan (Special :-)	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 overdues of existing loans given to the same parties, If So. Aggregate amount of such dues renewed or extended or settled by fresh loans 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]

Loan repayable on demand

- 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,



- Above Loan & advances cover the Financial support given to anyone (But not include normal advance given to purchase the goods)

Q14. M Ltd has given certain loans to related parties and also has accepted certain deposits. As an auditor, how you include the above items in paragraph 3 of CARO, 2020? (Nov 19) [OLD]

Hint: → Explain Above Para 3 clause (iii) & Para 3 clause (v)

Q15. company has advanced a loan to a firm in which a director was interested at a rate lower than the prevailing market rate as well as there was no agreement on terms of repayment. How auditor will report in CARO [OLD]

Hint:

- Para 3 (iii)(a) of CARO, 2020 : whether during year → provided loans or advances in loans
- Para 3(iii)(b) of CARO, 2020, requires the auditor to report whether the terms and conditions.....
- Present case, company has granted a loan to a firm in which a director is interested, the terms and conditions of which are prejudicial to the company interest, hence auditor may report as under:
 "According to the information and explanations given to us and based on the audit procedures conducted by us, we are of the opinion that the terms and conditions of loans granted by the company to a firm in which a director of the company is interested, (total loan amount granted ₹ -- -- and balance outstanding as at balance sheet date ₹-----) are prejudicial to the company's interest on account of the fact that the loans have been granted at an interest rate of ____% per annum which is significantly lower than the cost of funds to the company and also lower than the prevailing yield of government security close to the tenor of the loan"
- Para 3(iii)(f) of CARO, 2020 whether the loans either repayable on demand or without specifying any terms

Q16. Loan Has given to subsidiary, but squared up during the year, How do you frame CARO 2020 report . [OLD]

Hint: Explain Para 3(iii)(a) & 3(iii)(b), Guidance Note on CARO, 2020 as by ICAI states, while examining the loans, the auditor should also Consider the loans/advances that have been squared-up during the year & report such transactions.

Report will be as follows:

"The Company has granted loan of ₹2 Crore @ 15% p.a. to 2 of its subsidiaries during the Financial Year 2020-21. The maximum amount involved during the year was ₹2.00 crore and the year-end balance of such loans was Nil".

Para 3(iv)

Compliance of provisions of Secs. 185 & 186 (Link S-III, SA 550)

In respect of loans given, investments made, guarantees, and security whether provisions of Sections 185 and 186 of the Companies Act, 2013 have been complied with. If not, provide details thereof.

Para 3(v)

Public Deposits Accepted



Comply RBI, Sec 73 & 74	i.r.o. deposits accepted by the company or amounts which are deemed to be deposits, whether the <u>directives issued by the RBI</u> and the <u>provisions of sections 73 to 76</u> or any other relevant provisions of the Companies Act and the rules framed thereunder, where applicable, have been <u>complied</u> with. <i>If not, the nature of such contraventions be stated;</i>
Order by Court	If an order has been passed by <u>Company Law Board</u> or <u>NCLT</u> or <u>RBI</u> or <u>any Court</u> or any other <u>Tribunal</u> , whether the same has been <u>complied with or not?</u>

Para 3(vi)	Cost Records
Whether maintenance of cost records has been specified by the CG u/s 148(1) of the Companies Act, 2013 and whether such accounts and records have been so made and maintained.	

Q17. CARO, 2020 requires the auditor to report whether maintenance of cost records has been specified by the Central Government & whether maintained. briefly explain the audit procedure [OLD]

Hint: clause (vi).

1. Order requires auditor to **report whether cost records** have been made & **maintained when required** in 148(1)
2. The auditor should obtain a **written representation** from the management.
3. Should do a **general review** of cost records to ensure that the records as prescribed are made and maintained
4. **report on this clause also** where → maintenance of cost records is required **but cost audit is not mandatory**

ICAI Illustration: Should the auditor examine the cost record in detail while reporting under CARO?

CARO does **NOT** require a detailed examination of Cost Records. The Auditor should, therefore, **conduct a GENERAL review of Cost Records** to ensure that the records as prescribed are made and maintained. The word "made" applies in respect of Cost Accounts, and the word "maintained" applies in respect of Cost Records relating to Materials, Labour, Overheads, etc.

Para 3(vii)	Statutory Dues (Link SA-250, Ind As 37, AS 29, Sec 143(3)(j))
Undisputed statutory dues	Whether the company is regular in depositing undisputed statutory dues including <u>GST, PF, ESI, income-tax, sales-tax, service tax, duty of customs, duty of excise, VAT, cess and any other statutory dues</u> to the appropriate authorities and If not, the extent of the arrears of outstanding statutory dues as at the last day of the FY concerned for a period of more than 6 months <u>from the date they became payable</u> , shall be indicated
Disputed	Where statutory dues referred above 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).

Note:

- Non-payment of **advance income tax** would constitute default in payment of **statutory dues**
- **"Disputed"**: where there is a **positive evidence or action on the part of the company** to show that it has not **accepted the demand** for payment of tax or duty, e.g., where it has gone into appeal.
- **Materiality need to be consider by Auditor** → Eg, Company is Paying **Lumpsum ESI everytime** on Due date, and **after exact complex calculation, if any difference left**, that difference company **adjust in next month** (immaterial amount) → it will be considered as Regularly depositing (**no need to report**)

Q18. During audit → it is noticed that out of ₹12 Lacs of provident fund in the books, only ₹2 Lacs has been remitted to the authorities. due to financial problems they have not remitted but will remit soon [OLD]

Hint: Explain Para 3(vii)(a) of CARO, 2020

- **SA- 250** → also requires the auditor to obtain SAAE regarding compliance with the provisions of those L&R generally recognised to have a direct effect on the determination of material amounts and disclosures in the FS"
- Company is not regular in depositing PF Fund needs to be disclosed by auditor in audit report (vii)(a) of CARO, 2020



Q19. show cause notice from GST department of demand of ₹25 lakhs in December 2020. The company replied to the above notice in Jan 2021 contending that it is not liable for the levy. No further action was initiated by the GST department As the auditor of the company, what is your role in this? [OLD]

Hint: → Explain Para 3(vii) & Explain SA-250 requirement as explained in above question

- A mere representation to the Department shall **not constitute the dispute**, So **no reporting** is required.
- **But if** auditor is of opinion that exist a **dispute**, then as per **AS 29/Ind As 37**, Then **provision** required to be made & should also report amount of dues not deposited & forum where dispute is pending.

Similar Qn → **RTP'25** → Just this time **Amount is pending from July'23** (FY 2023-24) → So, Reporting is required in **Clause 7(a)** .. not in (b)

Q20. XYZ Pvt. Ltd. → Audit for year ended 31-3-2021. The audit assistant observes following dues:

- **Income Tax** relating to Assessment Year 2017-18 ₹125 lacs – **Appeal is pending** before Hon'ble ITAT since 2016
- **Customs duty ₹85 lakhs** – **Demand notice received** on 15-9-2020 but **no action has been taken** to pay or appeal.

As an auditor, how would you bring this fact to the members? [OLD]

Hint:

- **For Income tax**, (Its Disputed) Reporting required in **Para 3(vii)(b)** of CARO 2020 as follows:

S.No	Name of Statute	Nature of Dues	Amount in lacs	Period to which amount relates	Forum where dispute pending
1	Income-tax Act, 1961	Income Tax	125.00	AY 2015-16	ITAT

- **For Custom Duty**, Company has not taken any action and is outstanding for more than 6 months (Its undisputed), reporting under **Para 3(vii)(a)**

Para 3(viii)

Unrecorded Income: (Link SA 240)

- 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,
- **If so**, whether the previously unrecorded income has been **properly recorded in the books** of account during the year;

Q21. You are appointed as Auditor of XMP Pvt. Ltd. for FY 2021-22 after the resignation of RS & Co.

During audit you noticed that a **survey has been conducted** on December 2021 by Income Tax Department for **unrecorded sales of Rs. 5 lakhs**. **Company surrendered & disclosed these transactions** to assessing officer and paid taxes thereon. **However, company has not recorded those transactions in Books**. Report above in **CARO** [SM]

Hint: → Explain : **Clause (xviii)** - The auditor would be **required to report resignation** of auditor

- **Explain : Clause (viii)** - Though Company surrendered and disclosed these transactions before the Assessing Officer and paid taxes thereon. The auditor would be **required to report** in CARO as per **Clause (viii)**
- Since it is a statutory obligation on the part of the auditor to report in terms of CARO, mngt should record.

Para 3(ix)

Repayment of Dues (Link SA 570, Clause 3/4)

Defaulted

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 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

NOTE: Submission of application for re-schedulement/restructuring does not mean that no default has occurred

Wilful

b) Whether the company is a **declared wilful defaulter** by any bank or financial institution or

defaulter	other lender
Fund Diverted	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
Short to long term	d) Whether funds raised on short term basis have been utilised for long term purposes , if yes, the nature and amount to be indicated;
Fund for Sub/JV	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;
Pledge Securities of Sub/JV	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

Q22. A term loan was obtained from a bank for ₹80 lakhs for acquiring R&D equipment, out of which ₹ 15 lakh was used to buy a car for use director who was looking at R&D activities. how would you report under CARO [OLD]

Hint: Refer Above clause (ix)(c) of CARO, 2020, → whether term loans were applied for the purposes

- Auditor should **examine the terms & conditions of the term loan with the actual utilisation**. If finds that the fund has **not been utilized** for the purpose → the report should **state the fact**.
- **Explain Given Case** → Therefore, **car though used for R&D Director cannot be considered as R&D equipment**
- **Report in clause (ix)** that → term loan taken for R&D equipment, ₹15 lakhs was not utilised for the intended purpose

Q23. LM Ltd. had obtained a term loan of ₹300 lakhs from a bank for the construction of a factory. Since there was a delay in the construction activities, the said funds were temporarily invested in short term deposits. [OLD]

Hint: → refer above clause (ix)(c) of CARO, 2020, → whether term loans were applied for the purposes

- Here, auditor should report the fact in his report that pending utilization of the term loan for construction of a factory, the funds were temporarily used for the purpose other than the purpose

Q24. K Ltd. took a term loan from a bank in 2015 for ₹200 lakhs repayable in 5 equal instalments of ₹40 lakhs from 31st March, 2016 onwards. It repaid the loans due in 2016 & 2017, but defaulted in 2018, 2019 & 2020. As auditor of K Ltd, what's your responsibility assuming that company has sought reschedulement of loan? [OLD]

Hint: → Explain above Clause (ix)(a) → i.e., Whether company has defaulted → report in format (make table)

- K Ltd. defaulted in repayment of dues for 3 Yrs. **Application for rescheduling will not change the default position**
- Hence, report in CARO report that → the **Company has defaulted in its repayment** of dues to the bank to the **extent of ₹120 lakhs** and evaluate its consequential impact on the audit report.

Q25. R Ltd. as at 31st March, 2021 defaulted in the repayment of interest and principal due to a Bank. Due date was 28/02/21. However, defaulted amount was paid on 05/04/21. The company is of the opinion that since the default is set right before audit completion, so not to be reported in CARO. Comment and draft report [OLD]

Hint: Same Answer as above question [Clause (ix)(a)], Just add below Points also:

- As per **Schedule III of Co. Act, 2013**, → **terms of repayment** of loans is **required to be disclosed** in notes. & also disclose of **period & amount of continuing default** as on B/S date in repayment of loans and interest, separately.
- In the given case, remain outstanding as at March 31, 2021, So **reporting is required**
- **Conclusion:** State in Report → **"Company has defaulted in repayment of principal & interest to financial institution amounted to ₹, that become due on 28th Feb, 2021. However, the it was settled by company on 5th April, 2021.**

Q26. Gautam Ltd had borrowed ₹1000 crore from XYZ Bank. Principal → repayable after 5 years, and interest → payable at the end of each year. Gautam Limited defaulted the 5th instalment of interest payment & principal which was due on **June 30, 2021**. On March 31, 2021, Gautam Ltd approached bank to **restructure the existing liability**. As a result, the existing principal and outstanding and overdue interest was restructured into a **new loan amounting to ₹1,100 crore**. The **mngt did not provide any disclosure for the default on the loan**. Above said restructuring agreement was approved and signed on April 8, 2022. As a result, on March 31, 2022, the restructuring was still not approved. Guide statutory auditors in the reporting of this transaction. [OLD]

Hint: Explain above Clause (ix)(a) → i.e., Whether company has defaulted → report in format (make table).....

- given case → default continued till the end of the year & on 08/04/22, a restructuring agreement was signed, No disclosure was provided by the company
- Also, auditor needs to consider the impact of such non-disclosure and non-compliance with the financial reporting framework and accordingly auditor needs to either issue qualified or an adverse opinion as per SA 705.

Q27. Discuss the matters to be included in the auditor's report regarding statutory dues and repayment of loans or borrowing to a financial institution, bank, Government or dues to debenture holders as per CARO, 2020 [OLD]

Hint: → Refer Clause (vii) (a) for statutory dues & Clause (ix) (a)) for default in repayment of loan

Para 3(x)	Money raised by public issue and preferential Allotment (Link Clause 3/4/9)
Application of Money raised by public issue	a) Whether moneys raised by way of <i>initial public offer or further public offer (including debt instruments)</i> 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
Preferential allotment	b) Whether the company has made any <i>preferential allotment or private placement</i> 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

Para 3(xi)	Fraud by or on Company: (Link SA240)
	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 u/s 143(12) 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;
NOTES: • Inquiry under this clause is restricted to frauds 'noticed or reported' during the year. • auditor is also required to comply with the requirements of SA 240 also along with this clause • Only noticed frauds shall be included here and not the suspected frauds • While reporting, auditor may also consider the principles of materiality outlined in Standards on Auditing	

Q28. What are reporting requirements in audit report under the Co. Act, 2013 / CARO, 2020 for the following:

- A fraud has been committed against the company by a vendor of the company.
- The company has committed a major fraud on its customer and the case is pending in the court.
- A fraud has been committed against the company by an officer of the company
- A fraud has been reported in the cost audit report but not noticed by statutory auditors in his audit. [OLD]

Hint: → Explain Clause (xi) of CARO 2020 (As given in above notes);

- Explain 143(12) of Co. Act, 2013, i.e., → fraud is being or has been committed against the company by officers or employees of the company → report to CG (if fraud ≥ Rs. 1 Crore) or Audit Committee/ Board in other cases
- Fraud committed against the company **by a vendor** of the Company:
 - In case **employees or Mngt** are involved in fraud committed by vendor → report in **CARO 2020 and 143 (12)**
 - **Suspected fraud by vendors, customers** and other 3rd parties should be **dealt with in accordance with SA 240**. So, reporting has to be done in accordance with SA 240,.
 - Company committed major fraud on its customer, case is pending in court: → **reported Clause (xi)**
 - Reporting required to C.G. [u/s 143(12)] if amount of fraud exceeds ₹1 Cr & Also Para 3(xi) of CARO 2020
 - Effect of such fraud on FS need to be reported & Para 3(xi) requires reporting of fraud

Q29. how you report following in CARO: ABC Pvt. Ltd. is a manufacturer of jewellery. A employee of Company informed you that **Company does not properly disclose the purity of gold used on the jewellery**. [OLD]

Hint: Explain Para 3 clause (xi) of CARO, 2020 (as explained in above notes)

- **Explain Given case** → its' defrauding the customer. Mngt is deceiving customers to obtain illegal advantage.



- As per SA 240 → the auditor is concerned with fraudulent acts that cause a MMS in FS. Hence as long as books of account are not falsified arising out of difference in the purity of gold → it has no implication for the auditor.
- Conclusion: for CARO 2020 → is no implication for misstatement in the FS. Hence, no reporting is necessary.

Q30. Scope of auditor's inquiry under clause (xi) of para 3 of Companies (Auditor's Report) Order, 2020 is restricted to frauds 'noticed or reported' during the year. It does not require auditor to discover such frauds [OLD]

Hint: → Explain Para 3 clause (xi) of CARO, 2020 (as explained in above notes)

- Scope of auditor's inquiry under clause (xi) is restricted to frauds "noticed or reported" during year. It may be noted → It does not relieve the auditor from his responsibility to consider fraud & error in an audit of FS.
- In other words, irrespective of the auditor's comments under this clause, → required to comply SA 240.

Q31. Internal Auditor of the Company has identified a fraud in employees recruitment by the HR manager.. The amount of such fraud is expected to be ₹12 Lakhs. How stat auditor report in CARO 2020?

Hint: → Auditor is required to report the matter as per Para 3(xi) of CARO, 2020

Para 3(xii)	Nidhi Companies:
1:20	Whether the Nidhi Company has complied with the Net Owned Fund to Deposits in the ratio of 1: 20 to meet out the liability;
10%	Whether the Nidhi Company is maintaining 10% unencumbered term deposits as specified in the Nidhi Rules, 2014 to meet out the liability
Any Default	whether there has been any default in payment of interest on deposits or repayment thereof for any period and if so, the details thereof;

Q32. CARO, 2020 : Clause(xii) Nidhi Company has complied provisions of Nidhi Rules → What audit procedures [OLD]

Hint → Explain Para 3(xii) of CARO 2020 as explained above

- As per Rule 3(d) **Net Owned Funds** are defined as → **paid-up equity share capital + free reserves (-) accumulated losses (-) intangible assets** appearing in the last audited B/S. (Preference shares, shall not be included)
- A Nidhi company can accept fixed deposits, recurring deposits and savings deposits from its members in accordance with directions notified by CG. The **aggregate of such deposits is referred to as "deposit liability"**.
- Auditor should ask mngt to provide the computation of the deposit liability and net owned funds as per above..

Para 3(xiii)	Transactions with related Parties: (Link SA550, AS 18, Ind As 24)
Sec 177 & 188	Whether all transactions with the related parties are in compliance with Secs. 177 and 188 of Companies Act, 2013 where applicable
Disclosure	the details have been disclosed in the F.S etc. as required by the <u>applicable accounting standards</u> .

Note: Auditor can refer SA 550, "Related Parties" which has prescribed auditor's responsibilities regarding related party relationships and transactions when performing an audit of financial statements, including guidance on the procedures to be performed by auditors

Q33. Long-term borrowings from parent has no agreed terms, neither interest nor principal has been repaid. CARO

Hint: → Auditor is required to report the matter as per Para 3(xiii) of CARO, 2020

Q34. Amount of Rs. 4 lacs paid as marketing expenses a Partnership firm in which Company managing director is partner with Profit sharing ratio at 30%. However, **Arm's length of that service is Rs. 1.5 Lakhs**, no separate disclosure in FS for this. Comment and report as per CARO. (Nov'20)

Hint: → Auditor is required to report the matter as per Para 3(xiii) of CARO, 2020, Auditor shall report:

1. Nature of the RPR and underlying transaction → MG Associates is a partnership firm in which Director of MM Ltd is partner, with a PSR of 30 %. Payment of ₹ 4 Lakhs to MG Associates is a RPT.
2. Amount involved is Consideration for the Marketing services rendered by MG Associates (₹ 4 Lakhs p.m.) is higher than the arm's length pricing by ₹ 1.50 Lakh p.m. (₹ 18 Lakhs p.a.)



Para 3(xiv)**Internal Audit System:**

- Whether company has an internal audit system commensurate with the size and nature of its business
- Whether reports of the Internal Auditors for the period under audit were considered by statutory auditor.

Para 3(xv)**Non-cash transactions with directors**

- Whether the company has entered into any non-cash transactions with directors or persons connected with directors and
- if so, whether provisions of Section 192 of Companies Act, 2013 have been complied with

Q35. Q. RNT Ltd. has entered into non-cash transactions with Mr. Ram, son of one of the directors, OR, Q. Candy Ltd., decided to acquire a land →, which had been owned by Mr. Sidhant, who is a director of the Company. he gave that land to the company in exchange of a site owned by the company located at the next street.

Hint: CARO REPORTING: Explain para 3 (xv) – Non-Cash Transaction

- **Clause – (Xiii) – Related Party Transaction:** "explain this clause" → reporting require here also

Above answer is as per New ICAI SM, however in Exam, ICAI has given Some more points as Below:

For above reporting → **Obtain W.R.** : whether company undertake any non-cash transaction with Director [192(1)] **Sec 192 of Co. Act.13** → restrict non-cash transactions involving directors or persons connected with them, section prohibits the company from entering into following types of arrangements unless it meets the conditions:

- An arrangement by which a director of company or its holding, subsidiary or associate company or a person connected with such director acquires or is to acquire assets for consideration other than cash, from company.
- An arrangement by which the company acquires or is to acquire assets for consideration other than cash, from such director or person so connected

Auditor should check compliance of sec 192(2) & **verify notice of general meeting** that it includes Arrangement.

Transaction is approved by Board → auditor should state that whether **approval in General Meeting has obtained**

Documents to be verified, to identify existence of Non-cash transactions:

- (1) **Register of Loans**, Guarantee, Security, contract etc. in which director is interested
- (2) Movement of **Fixed assets register** (3) minutes of **general meeting** (4) report on **AGM**

Para 3(xvi)**Registration with RBI:**

- Whether the company is required to be registered u/s 45-IA of the Reserve Bank of India Act, 1934 and if so, whether the registration has been obtained.
- 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 India Act, 1934;
- 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;
- 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;

Para 3(xvii)**Cash Losses:**

- Whether the company has incurred cash losses in the financial year and in the immediately preceding F.Y.,
- if so, state the **amount** of cash losses;

Notes:

ICAI has clarified → that even in case where **Cash Losses incurred in Current** Financial year, but there was **profit in Last year** → then **also reporting is require** (if there is loss in Last Yr, then mention last year loss also)

Q36. The company had incurred a cash loss of ₹ 39 lakh during financial year compared to a cash profit of ₹ 15 lakh in the previous FY. Whether CARO reporting needed? (Old) **Hint:** Yes, Reporting require in (xvii)

Para 3(xviii)**Resignation of statutory auditor [Link ADT-3 Sec 140(2)]**

- **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

Q37. During the year, Auditor had offered to resign. However, they later decided to postpone their resignation to the following year. → It will **NOT** Attract reporting under (xviii) clause.

Para 3(xix)	Material uncertainty - company ability to meet its liabilities (Link SA 570)
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.	

Para 3(xx)	Transfer of unspent CSR amount:
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 6 months of the expiry of the financial year in compliance with 2nd proviso to <u>Sec. 135(5)</u> of the said Act; b) Whether any amount remaining unspent u/s 135(5) of the Companies Act, pursuant to any ongoing project, has been transferred to special account in compliance with the provision of <u>Sec. 135(6)</u> of the said Act. <u>Illustration for easy explanation of above clause:</u> 2% of Avg profit comes out to ₹100 lacs, out of which amount already spent is Rs. 20 lacs, So out of remaining UnSpent amount of Rs.80 lacs ✓ <u>For Ongoing project (i.e. Multi Year), Assume its Rs.60 lacs:</u> • Transfer within 30 days from end of FY to special a/c "Unspent CSR A/c" • To be spend within 3 years • If not transfer within 30 days from end of 3 yrs to Fund in S-VII ✓ <u>Other than Ongoing project Assume its Rs.20 lacs:</u> Transfer within 6 months from end of FY to fund in S-VII	

Para 3(xxi)	Qualifications or adverse remarks in CARO Reports of group companies:
a) Whether there have been any qualifications or adverse remarks by the respective auditors in the CARO reports of the companies included in the consolidated financial statements (CFS), b) If yes, indicate the details of the companies and the paragraph	

Q38. CA. F has been appointed as **Auditor of XYZ Ltd (CFS)**. XYZ Ltd has **one subsidiary, namely AT Pvt Ltd**, auditor is **CA. B**. CA. B issued a **qualification in CARO 2020 for AT Pvt Ltd, stating that short-term funds raised were utilised for long-term purposes**. Whether CARO reporting is required in CFS?

Hint → **Para 2 of CARO 2020:** → CARO do not apply to auditor's report on CFS **except for clause (xxi)**.

Clause (xxi) of Paragraph 3 of CARO 2020: *Explain the clause.*

CA F responsibility:

- Report under Clause (xxi) of Paragraph 3 of CARO 2020:** Include comment in CFS
 - Incorporate Qualification by CA B:** i.e., short-term funds raised and utilized for long-term purposes
 - Mention Paragraph Number:** provide para. number of CA B's CARO report where the **qualification** is stated
- Containing the qualifications or adverse remarks only. Reporting under this is only required for those entities included in the consolidated financial statements to whom CARO 2020 is applicable

➤ **Reasons to be stated for unfavourable or qualified answers:**

Where, in the auditor's report, the answer to any of the questions referred to in paragraph 3 is:



a) Unfavourable or Qualified	The auditor's report shall also state the basis for such unfavourable or qualified answer, as the case may be
b) Unable to express any opinion	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.

➤ Companies Act (Sec 143) - Duties of Auditor

Duty of Auditor to Inquire on Propriety matters: 143(1) (Special Trick :-)	Note: The auditor is NOT required to report on below matters, unless he has any special comments (Adverse) to make on any of the items referred to therein.		
	a)	Loans & Advance	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)	Books Entries	Whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company
	c)	Cost>Sales	Where the company not being an investment company or a banking company , 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)	Deposit	Whether loans & advances made by company have been shown as deposits
	e)	Expense	Whether personal expenses have been charged to revenue a/c
	f)	Shares for Cash	• 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, & • if no cash has actually been so received, whether the position as stated in the BOA and the balance sheet is correct, regular and not misleading.
145: Duty to Sign Audit Report:	Person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company as per provisions of <u>Sec 141 (2) & qualifications</u> , <u>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</u> and shall be <u>open to inspection by any member</u> of the company.		
143(3) Reporting (Special Trick :-)	NOTE: 143(3) reporting is required even if there is no adverse remark on below matters		
	a)	Obtained all Information	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
	b)	Books of account	• Whether, in his opinion, proper BOA as required by law have been kept by the company • Examination of those books & proper returns adequate for the purposes of his audit have been received from branches not visited by him
	c)	Branch Report	Whether the Branch office audit report of the company sent to him & manner he dealt with that report while preparing own report
	d)	B/S P&L agrees BOA	Whether the company's balance sheet and P&L account dealt with in the report are in agreement with the books of account and returns
	e)	A.S	Whether, in his opinion, FS comply with the accounting standards ;
	f)	Comment on Financial transactions	the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company
	g)	Director	Whether any director is disqualified from being appointed as a director



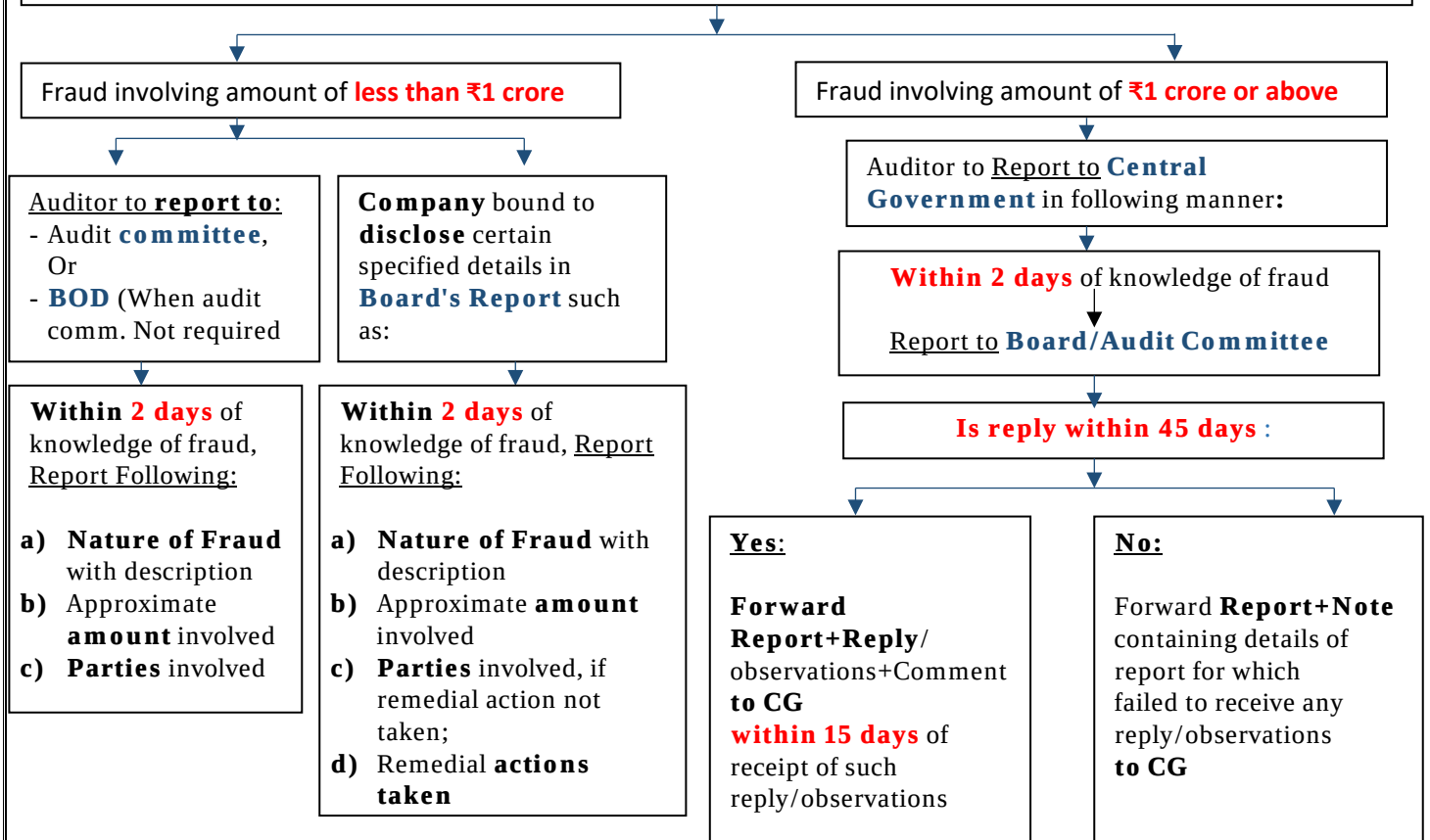
	disqualified	under u/s 164(2).
h)	Qualification	Any qualification , reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith
i)	Internal financial controls	Whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such controls; This clause in NOT APPLICABLE to: Private company which is (i) OPC or Small company ,Or, (ii) Which has turnover less than Rs. 50 crores as per latest audited financial statement AND has aggregate borrowings from banks or FI or any body corporate at any point of time in the FY less than ₹ 25 crore.
j) Any Other Matter (Rule 11) (Also applicable for Banking company auditor's report) Link Point 1 with: SA 250 & CARO C-7		
Any such other matters as may be prescribed. Rule 11: The auditor's report shall also include their views and comments on the following matters, namely:- - Whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement - whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses (Including Derivative contract) - whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company - Whether the Mnt 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), Not even through 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; - Whether the Mngt 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; - 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 MMS - Whether dividend declared or paid during the year by company is in compliance with Sec 123 of the Companies Act, 2013.		

	- Whether the company (i.r.o. FY 2022-23 & onwards) has used such accounting software for maintaining its BOA which has a feature of recording audit trail (edit log) facility & - 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 <u>Audit Trail means</u>, 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 ➤ <u>Section 197(16) of the Companies Act, 2013:</u> [Reporting requirement for auditors of public companies needs to be covered in auditor's report under the Section "<u>Report on Other Legal and Regulatory Requirements</u>"] <u>Whether excess remuneration paid to director?</u> "The auditor of the company shall, in his <u>report under section 143</u>, 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
143(4) : Reason for qualification	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
143(8):	<u>LATER ON SEPRATELY DISCUSSED : "Branch Audit"</u>
143(9)/(10) : Auditing Standards	143(9): Every auditor shall comply with the auditing standards 143(10): CG may prescribe the standards of auditing, as recommended by the ICAI, in consultation with and after examination of the recommendations made by the NFRA
143(10): CARO	CG may direct that auditor's report shall include a statement on such matters as specified in order issued by it. (CARO, 2020)
143(12)	<u>LATER ON SEPRATELY DISCUSSED : "Fraud Reporting"</u>



Duty of Fraud Reporting [Section 143(12) of Companies Act, 2013 & Rule 13 of CAAR, 2014]

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**:



While Reporting to C.G:

- Report shall be **sent to Secretary of MCA**, in a **sealed cover** by Registered Post with Acknowledgement Due or by Speed Post followed by an e-mail in confirmation of the same
- 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
- Report shall be in **ADT-4** format

Some Other Points

- Provisions of fraud reporting shall **also apply**, mutatis mutandis, to a **cost auditor** & a **secretarial auditor**
- If any auditor, cost accountant or company secretary in practice does **not comply with the above provisions**, **Penalty** will levy on them:
 - ✓ **Rs.5 lacs** : In case of **Listed company**
 - ✓ **Rs.1 lacs** : In case of **Other company**

The auditor is also required to **report under clause (x) of CARO, 2020** → whether any fraud **by 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.

Requirement of **SA 240** also needs to be fulfill by auditor

Q39. Auditor has reason to believe that **fraud involving Rs.75 lakhs** has been committed in company **BY its employee**. Any under statutory obligation to report to **C.G** by filing prescribed **form on MCA**? (**MTP & SM**)



Hint: Sec 143(12) of Co. Act 2013, Rule 13. → If fraud is INR 1 crore or above → report the matter to CG.
In given case, 75 lacs, → so, **no statutory obligation to report matter to CG** by filing ADT-4 on MCA portal.
report the matter to the **audit committee** constituted under **sec 177** or to **Board**. Also clause (xi) **CARO, 2020**.

➤ **Below are Old Course Qns Hint → Full Question is Covered in Additional PDF Book**

Q40. BOD Can-not refuse the auditor to refer the Minutes Book (Sec 143 grant power of right of access)

Q41. → Below is the Crux:

- Auditor observed that **Advances were made without proper security** → Clause (a) of Sec 143(1)
- **Trade payables & trade receivables** are adjusted in books → Clause (b) of Sec 143(1) ... mere book entries
- Personal expenses were charged to revenue → Clause (e) of section 143(1)
(For above points, Auditor should extend audit procedure, and can consider to modify the reports)

Q42. Director business Foreign trip, advances was expended without proper supporting → SA 500, obtain SAAE, and Sec 143(1)(e) (personal expenses shall not charge to P&L)

Q43. Company has **Not Maintained proper Books** → Sec 143(3)(b).

Q44. Enquiry of Propriety Matters:

- "**Deed of Hypothecation**" & "**Statement of stock**", these documents to be checked by auditor when company has taken loan in lieu of hypothecation of goods
- When "**Cost of debenture**" is not ascertainable → consider "**BOOK VALUE**" as cost
- When "**Cost of Bonus share**" is not ascertainable → consider "**Average cost**" (as average cost per share)
- Company has **allotted shares to NBFC (As it was not able to repay Loan)** → this will also be considered as "**Shared allotted for Cash**"

CHAPTER 8- SPECIALIZED AREA

SA 800, 805, 810

SA 800:	special considerations applicable i.r.t <u>audit of F.S.</u> prepared as per special purpose framework (SPF)
SA 805:	special considerations applicable to an <u>audit of a single FS</u> <u>or</u> of a <u>specific element, account</u> or item of a FS.
SA 810:	responsibilities of an auditor when undertaking an <u>engagement to report on summary F.S.</u> <u>derived from financial statements audited in accordance with SAs</u> <u>by that same auditor.</u>

SA 800- Special consideration - Audits of FS prepared in accordance with Special purpose framework

Scope: <i>i.e IFRS, US-GAAP</i>	- SAs in the 100-700 series apply to an audit of FS - This SA deals with special considerations → in following those SA's (SA 100-700) → to an audit of FS prepared in accordance with a special purpose framework (SPF) This SA does NOT override requirements of other SA's, nor does it purport to deal with all special considerations that may be relevant in circumstances of engagement SA 800 → Deals with complete set of FS in accordance with SPF SA 805 → Deals with special considerations relevant to an audit of a single FS or of a specific element, account or item of a FS.

Q1. SA 800 Explain, by giving **examples**, meaning of **special purpose framework**.

SPF:	- Special purpose framework: A FRF designed to meet the FI needs of specific users. - The FRF may be a fair presentation framework or a compliance framework
Example of SPF:	- Cash basis a/cing (Receipt & payment) → For Cash flow information → On creditor's request - FRF established by regulator → to meet requirement of that regulator - Financial reporting prepared as per some Contract i.e., provisions of a contract → i.e., Loan agreement / Provision grant

Objective:	When applying SAs in an audit of FS prepared in accordance with a SPF, is to address appropriately the special considerations relevant to: - The acceptance of the engagement; <i>[Below Notes]</i> - The planning and performance of that engagement; and <i>[Qn Given]</i> - Forming an opinion and reporting on the FS but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control <i>[Below Notes]</i>

Considerations When Accepting the Engagement: (Whether FRF is acceptable?) <i>(ICAI in Paragraph - Just read for MCQ's)</i>	User's Need:	For SPF → Key factor of acceptance of FRF is financial info needs of users
	FRF by Authorised Organisation	If an Authorised organisation (For certain type of entity) establishes F.R. standards for SPFS through a transparent and deliberative process, these are presumed acceptable . (Eq. RBI in case Banks)
	FRF Prescribed by L&R:	L&R (e.g., by a regulator) may prescribe a framework for SPFS for specific entities, presumed acceptable unless evidence suggests otherwise.
	Conflict in FR vs L&R:	Any conflict between financial reporting standard & legislative requirement → Take action as per SA 210 .
	FRF by Provisions of	When FR is prescribed by reporting provisions of a contract or sources other than above described → acceptability of the FRF need to be determined by



	contract or other source:	considering whether the framework exhibits attributes normally exhibited by acceptable FRF as per requirements of SA 210.
	Judgement:	In the case of a SPF → acceptable FRF is a matter of professional judgment.
	➤ SA 210 requires the auditor to determine the acceptability of the FRF applied in the preparation of the FS. In an audit of special purpose financial statements (SPF's), the auditor shall obtain an understanding of: [PIA] • The Purpose for which the FS are prepared; • The Intended users; and • The mgt steps to determine that the Applicable FRF is acceptable in circumstances.	
Forming an Opinion and Reporting Considerations <u>(Description of Applicable FRF in FS)</u> <i>Trick: Purpose, Mngt Choice 701, 706, 720</i>	➤ Apply the requirement of SA 700 Description of Applicable → FRF Whether FS adequately Describe Applicable FRF? : Whether the FS adequately describe the applicable FRF (In case of FS prepared as per Provision of Contract, evaluate whether FS adequately describe significant interpretation of Contract) → SA 700 will be applicable for → form & content of the Audit report (AR). In case of an AR on SPF shall state: • AR shall also describe the purpose for which the FS prepared, and if necessary → Intended users (Or refer note in Special Purpose FS, that contain that Info.) • If mgt has a choice of FRF in preparation of FS → Explain mgt's responsibility for such FS for determining that the applicable FRF is acceptable • SA 701 Applicable → When KAM Communicated, SA 701 applies entirely • SA 720 is also applicable when → Mngt plans to issue report accompanying the Special FS, for purpose of providing information of matters presented in FS to owner/similar stakeholder. (So, that report will be considered as annual report for purpose of SA 720) • SA 706 → Auditor May (if consider appropriate) → Use "OM Para" in A.R. of S.P. FS → to refer to the A.R. of General Purpose FS i.e., → in that "OM para", he may write to user → to refer "A.R. of General Purpose FS" or Refer Matters reported in General Purpose FS as per SA 706, Like M.U. exist for G.C" etc.	
Alert users:	Alert user in "EOM para" → that the FS are prepared in accordance with a SPF → not be suitable for another purpose (To avoid misunderstandings)	
Restriction on Distribution or Use	Special purpose FS may be used for any other purpose also (other than intended users), so in addition to alert (as discussed above), Auditor shall indicate users that: (Other Matter Para) • Auditor's report is intended solely for specific users • Depending on L&R → Restrict distribution or use of Auditor report (Ambiguous → in 2 different-Different MCQ's → ICAI Gave Different-Different Answer → One time ICAI mentioned this in EOM & one time in OM Para)	
Author's Note:	• Whatever the normal work we need to do as per SA 200-700 we will perform here also • Just do some more additional work & consideration • Like SA 320 is for materiality → We have to consider materiality as per our judgement → even if mngt have decided some threshold with user in contract that they will ignore errors upto this amount	

➤ **Auditor's Consideration for planning & performing an Audit in case of SPF**

Q2. what considerations undertaken while would be planning & performing an Audit in case of SPF? [OLD]

Answer: While planning & performing Audit of such, the Auditor should consider below mentioned factors:

[Trick: Saari "Accounting Policy" & "SA's" follow karo > par "kuch SA's me Special" dhyaan rakhna, Jab as per padega, jab as



per "Contract" FS bana ho > kyuki unki "Materiality" jyada hoti h > Fir "Financial statement" banao ab acche se]
"Or" → SA 200, SA 320 (ke 2 points) , SA 315, SA 260, 700

- As per SA 200, Comply all SAs relevant to Audit (Comply with each requirement of SA, Unless entire SA is not relevant), In Exceptional Circumstances, 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 SAs in an Audit of special purpose FS → may require special consideration by the Auditor.
 - ✓ For example, in SA 320, judgments about matters that are material to users of the FS are based on a consideration of the common financial information needs of users as a group.
 - ✓ But, In the case of an Audit of special purpose FS, however, those judgments are based on a consideration of the financial information needs of the intended users.
- SA 315 requires auditor to obtain an understanding of entity's selection & application of A/cing policies. In the case of FS prepared in accordance with the provisions of a contract, the auditor shall obtain an understanding of any significant interpretations of the contract that mngt made in the preparation of those FS.
- In the case of special purpose F.S., such as those prepared in accordance with the requirements of a contract, Mngt 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 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 F.S.
- SA 260, Communication with TCWG → it required auditor to determine the appropriate person's within the entity structure → when both i.e., General purpose FS & Special purpose FS are prepared → person responsible for the oversight of special purpose FS may not be the same as TCWG responsible for the oversight of the preparation of those general purpose FS
- SA 700 Applicable → When forming an opinion and reporting on special purpose FS, the auditor shall apply the requirements in Revised SA 700.

Q3. CA Lalita is auditor. She is also offered professional work of audit of F.S prepared specifically for meeting requirements of a loan agreement. She accepted that & want to disclose this fact in "Emphasis of matter Paragraph" in audit report to be issued by her for this specific engagement. Is her approach proper?

Hint: → CA Lalita is proper. She can accept such engagement even though she is auditor. need, EOM para.

Q4. CA Lakshmi has prepared a draft audit report for F.S. of X Ltd. prepared in accordance with financial reporting provisions of a contract with Y Ltd. She has drafted an unmodified opinion to be given in audit report. Besides, she has also drawn attention in draft audit report to Note "A" to the FS which describes the basis of accounting. How she should ensure that report would not be misused? Draft a suitable para.

Hint:→ She may consider it appropriate to indicate that the auditor's report is intended solely for specific users. restricting the distribution or use → the paragraph alerting the readers may be expanded to include these other matters and the heading modified accordingly. The draft para should read as under: -

EOM Para → "Basis of Accounting and Restriction on Distribution and Use"

Without modifying our opinion, we draw attention to Note A to the financial statements, which describes the basis of accounting. The financial statements are prepared to assist the company to comply with the financial reporting provisions of the contract referred to above. As a result, the financial statements may not be suitable for another purpose. Our report is intended solely for X Ltd. and Y Ltd. and should not be distributed to or used by parties other than X Ltd. and Y Ltd.

SA 805: Special consideration – Audits of Single FS & Specific Elements, Accounts or Item of FS

A Single F.S or Element of FS:	• "Element of a financial statement" means an "element, account or item of a FS"; • Single FS: ✓ Example: Cash flow statement, or ✓ a specific element of a FS (for example, cash/bank balance) includes related notes. ✓ The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information relevant to the FS or to the element	
Example of Elements:	• Accounts receivable, Allowance for doubtful accounts receivable, Inventory etc. • Schedule of externally managed assets & income of private pension plan • Schedule of net tangible assets including notes • Schedule of disbursement in relation to a lease property inc. explanatory notes • Schedule of profit participation or employee bonuses.	
Scope:	• SA 805 deals with special consideration in application of SA 100 to 700 w.r.t. audit of Single FS or element of FS • Not applicable to: ✓ Report of component auditor (issued on request of Principal auditor for purpose of Audit of CFS) ✓ Override other SA's	
Not Apply:	SA 805 Not applicable on → report of a component auditor issued as a result of work performed on the financial info. of a component at the request of a group engagement team for purposes of an audit of group F.S	
Objective:	Special considerations relevant to: • The acceptance of the engagement; • The planning and performance of that engagement; and • Forming an opinion and reporting on the single FS or on specific element, account or FS item.	
Considerations When Accepting the Engagement: [SOF] <i>(ICAI in Para – Read Only)</i> <i>(Special Trick :-)</i>	Application of SA's	SA 200 requires the auditor to comply with all SAs relevant to audit, Unless entire SA is not relevant: • This applies to audit of Single F.S. even if auditor also audits complete F.S. • If auditor not also engaged to audit complete FS, consider practicability of audit of Single F.S./Specific Element in accordance with SA's. • Compliance of relevant SA's not practicable in Single FS/element → when auditor is not also engaged to audit of complete FS → as not have understanding of entity, I.C, accounting records etc. → need further evidence to corroborate audit evidence acquired from the accounting records. • Certain SAs require audit work may be disproportionate (i.e., Extensive work) to element being audited → It may not be practicable because of the audit effort required. auditor concludes that an audit of a single FS / element as per SAs may not be practicable, the auditor may discuss with mngt whether another type of engagement might be more practicable.
	Applicability of FRF •SA 210 •Adequate Dis •FRF is based on Complete	• SA 210 Determine acceptability of FRF applied in preparation of Single F.S. • Determine whether application of FRF will result in presentation that provides adequate disclosures to enable users to understand information conveyed in Single FS or element • If Single FS/Element prepared as per "Applicable FRF", which is Based (extracted) from a FRF established by an authorised or recognised standards setting organisation for preparation of Complete FS (IFRS/Ind As) → in that



	FS FRF Form an Opinion	case → to determine acceptability → check whether that "Applicable FRF" includes all the requirement of Broader FRF relevant to presentation of Single FS to provide adequate disclosures. - Expected form of opinion depends upon applicable FRF & L&R. - SA 210 requires that agreed terms of engagement include the expected form of report to be issued. - Consider whether expected form of opinion is appropriate in circumstances. - Auditor's decision as to the expected form of opinion is a matter of professional judgment.
Consideration when Planning & Performing an Audit: <u>[4 point SA's ke,</u> Saare SA's follow karo → Adapt them & carefully consider them <u>3 Point Full FS vs Single FS ke]</u> Audit evidence (SA 500) → Interrelated → SA 320 materiality		- Auditor shall Adapt all SA's relevant to the Audit as necessary in circumstances of engmnt. - Careful consideration of relevance of each SA is necessary. SAs such as SA 240, SA 550 and SA 570 are, in principle, relevant. This is because the element could be misstated as a result of fraud, the effect of related party transactions, or the incorrect application of the going concern assumption under the applicable FRF. - SA 260 (it requires auditor to determine appropriate person with whom communicate) → people overseeing the preparation of a single FS/specific element might be different from those People who overseeing the full set of FS. So, the application of communication requirements is modified - SA's For audit of Full F.S → Need to be adapted as necessary in the circumstances when applied to the audit of a single F.S. For example, WR from mngt. about the complete set of F.S. would be replaced by WR about single element in accordance with the applicable FRF. - When auditing Single F.S. along with Full F.S., audit evidence obtained as part of audit of full F.S. may be useful but auditor needs to plan & perform audit of Single F.S. to obtain SAAE. - Some items of Complete FS may be interrelated with element of F.S., auditor need to perform procedures on interrelated items also. (as can-not consider single FS/Element in isolation) - Materiality for a Single F.S. may be lower that materiality for full F.S., this will affects NTE of audit procedures and the evaluation of uncorrected misstatements.
➤ Forming an Opinion & Reporting:		
General Points: <u>(read Only)</u>		- Apply requirement of SA 700, as well as When applicable → SA 800, as well as apply the reporting requirements in other SAs (Adapted as necessary in circumstances of engmnt) - SA 700 require to evaluate whether FS provide adequate disclosure, so for audit of Single FS Element, ensure as per FRF requirement, provides adequate disclosures to enable the intended users to understand the information conveyed in the FS or the element. - Going Concern → Depending on applicable FRF used in Preparation of Single FS /Element & Depending upon How SA 570 Applies to that engagement → In Audit report the description of Mngt's responsibilities relating to G.C may need to be adapted, as necessary. - KAM → SA 700 requires to Communicate KAM as per SA 701 for audit of Complete set of General-Purpose FS (So SA 701 not applicable, Unless auditor use it Voluntary) - Other Information → SA 720 Applicable When → reports containing or accompanying the single FS or specific element of FS (for Purpose of providing Info related on matters presented in Single FS, that report is consider as Annual Report) - Signature of Auditor → Signed by Engagement Partner in Personal Name + Also Name of Firm (if it's Firm) + Mention Membership Number + Firm Registration number - If also engaged to report on full FS → issue separate reports (Separate opinion) - If audited SFS published with audited full FS → presentation of SFS should be differentiated from full FS → Otherwise do not issue report on SFS, until satisfied with the

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Chp 8: SA 800, 805, 810



	differentiation.						
Consider Implication of Full FS on Single FS: (Trick: uska Nature ?, kya wo Sabko Effect kar rha h, dono me kitna difference hai (FRF, FS Time, A.R. Time), ?	Auditor should consider the implication on A.R. of Single FS / Element, if any, of certain matters included in the A.R. on the complete set of FS, (It's a matter of Professional Judgement, to consider whether matter included in A.R. of Full FS is relevant for A.R. of Single FS/Element). <u>Factors that may be relevant in considering those implications include:</u> 1) The nature of matter described in the A.R. of complete set of FS & the extent to which it relates to what is included in the single FS or a specific element. 2) The pervasiveness of matter described in the A.R. on the complete set of FS 3) The nature and extent of the differences between the applicable FRF's 4) The extent of the difference between the period covered by the complete set of FS compared to the period of single FS/element 5) The time elapsed since the date of the auditor's report on the complete set of the FS Example: • If Qualification in Full FS Relates to Debtors, & Specific element is Debtor only → so there will be implication • However, if Specific element is Long term debt, then Less likely to impact						
In case Full FS matter not have any Implication:	Even when certain matters included in the auditor's report on the complete set of FS, do not have implications for the audit of Single FS/ Element: Auditor may consider appropriate to refer that in "OM Para" of A.R. on Single FS/Element (Eg. M.U. relating to G.C is mention in A.R. of Full FS., Auditor of Single FS may refer it)						
In case Full FS Modified / EOM / OM etc :	<table border="1"> <tr> <th colspan="2">In case Full FS Contains →</th></tr> <tr> <td>a) Modified opinion as per SA 705</td><td>b) EOM/OM Para as per SA 706</td></tr> <tr> <td>c) M.U related to G.C : SA 570</td><td>d) uncorrected MMS of other information SA 720</td></tr> </table> the auditor shall consider the implications, if any, that these matters, may have for the audit of the single FS or of the specific element of a FS & for the auditor's report thereon..	In case Full FS Contains →		a) Modified opinion as per SA 705	b) EOM/OM Para as per SA 706	c) M.U related to G.C : SA 570	d) uncorrected MMS of other information SA 720
In case Full FS Contains →							
a) Modified opinion as per SA 705	b) EOM/OM Para as per SA 706						
c) M.U related to G.C : SA 570	d) uncorrected MMS of other information SA 720						
In case Full FS is Adverse or Disclaimer:	➤ Determine effect on Single F.S. ➤ If necessary to issue "adverse" / "disclaimer" opinion on full FS → unmodified opinion on SFS cannot be expressed However, for separate audit of specific element, an unmodified opinion can be expressed if: a) Not prohibited by L&R; b) Audit report on element is not published together with AR on full FS; & c) Element does not constitute a major portion of full F.S. <table border="1"> <tr> <td>"Adverse" or "Disclaimed" on Full FS</td><td>Shall not issue → Unmodified opinion on a single FS/Element → <u>even if single FS is not published together</u> → <u>because Single FS is deemed to constitute a major portion of those FS</u></td></tr> <tr> <td>"Modified" / EOM/OM on Full FS</td><td>~~Even If those modification/EOM/OM not relates to that element~~ → then also May refer that modification in "OM Para" of Single/element FS report (Relevant to the users' understanding of the audited FS)</td></tr> <tr> <td>Disclaimer on Full FS w.r.t. Results of Operations and cash flows</td><td>where relevant, and an "unmodified opinion" regarding 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.</td></tr> </table>	"Adverse" or "Disclaimed" on Full FS	Shall not issue → Unmodified opinion on a single FS/Element → <u>even if single FS is not published together</u> → <u>because Single FS is deemed to constitute a major portion of those FS</u>	"Modified" / EOM/OM on Full FS	~~Even If those modification/EOM/OM not relates to that element~~ → then also May refer that modification in " OM Para " of Single/element FS report (Relevant to the users' understanding of the audited FS)	Disclaimer on Full FS w.r.t. Results of Operations and cash flows	where relevant, and an " unmodified opinion " regarding 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.
"Adverse" or "Disclaimed" on Full FS	Shall not issue → Unmodified opinion on a single FS/Element → <u>even if single FS is not published together</u> → <u>because Single FS is deemed to constitute a major portion of those FS</u>						
"Modified" / EOM/OM on Full FS	~~Even If those modification/EOM/OM not relates to that element~~ → then also May refer that modification in " OM Para " of Single/element FS report (Relevant to the users' understanding of the audited FS)						
Disclaimer on Full FS w.r.t. Results of Operations and cash flows	where relevant, and an " unmodified opinion " regarding 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.						

Q5. CA P is auditor for **auditing complete set of FS.** express **adverse** opinion. He is also **auditing Debtors** of company in a separate engagement. **Can he express unmodified opinion i.r.o Debtor ?**

Hint: Refer Above "**Forming an Opinion & Reporting**" - "**Refer In Case Full FS is Adverse or Disclaimer**"

Generally "NO", but can express If : not prohibited by L&R, Not published together with Full FS A.R., etc.

Q6. CA Surya is auditor for F.S of an entity prepared in accordance with financial reporting provisions of a contract. He is also offered audit of Debtor. Can he accept such engmnt? Discuss brief his audit approach.
Hint: → SA 800 also applies, In the given case, → It is a special purpose framework (SPF). The auditor of FS prepared in accordance with SPF is also offered audit of Debtor. Hence, his audit approach should include considering requirements of both SA 800 and SA 805.

Q7. CA G is offered appointment for audit of Creditor of F.S of a company. However, FS prepared under Co. Act, 2013 are audited by CA Jignesh. Discuss why it would be practically difficult for CA G.
Hint: → Compliance with the requirements of SAs relevant to the audit of a single FS or of a specific element of a FS may not be practicable when the auditor is NOT also engaged to audit entity's complete set of FS. 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 FS. Accordingly, the auditor may need further evidence to corroborate audit evidence acquired from the accounting records. In case of an audit of a specific element of FS, certain SAs require audit work that may be disproportionate to the element being audited. → If the auditor concludes that Single FS audit or of a specific element may not be practicable, auditor may discuss with mngt whether another type of engmnt might be more practicable.

SA 810: Engagements to Report on Summary Financial Statements

Summary F.S	• Historical FI that is derived from FS (Audited FS) • but that contains less detail than the FS, • while still providing a structured representation consistent with • that provided by the FS. (different L&R may use different terminology to describe such HFI)
SCOPE:	auditor's responsibilities → undertaking an engagement to report on summary FS → derived from FS audited in accordance with SAs by that same auditor.
Objectives of Auditor:	• Determine whether it is appropriate to accept the engagement • Form an opinion on the SFS based on an evaluation of the conclusions drawn from the evidence obtained; and • Express clearly that opinion through a written report that also describes the basis for that opinion.
Applicability of Criteria: <i>[Mera to ladka / ladki ka criteria aisa h ki > Nature accha hona chahiye bas > uske baare me Information nikali ki Mislead to ni kar rha n.. to hi purpose poori hoga]</i>	Q8. List out few factors affecting auditor's determination of the acceptability of the applied criteria before accepting audit of summary FS. (May'24 & SM) ➤ Applied criteria refer to the criteria applied by mngt in preparation of summary FS. ➤ Mngt is responsible for the determination of info that needs to be reflected in the summary FS so that they are consistent, in all material respects, with or represent a fair summary of the audited FS. As it includes limited information and limited disclosure, there is an increased risk that they may not contain the information necessary so as not to be misleading in the circumstances. This risk increases when established criteria for the preparation of summary FS do not exist. When L&R Prescribe any criteria → then as per SA 210 → it's presumed to be acceptable criteria. (Otherwise Developed by mngt) Factors affecting the auditor's determination of 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 FS and • Whether applied criteria will result in summary FS that are not misleading in circumstances

➤ Engagement Acceptance:

Q9. Management want to appoint you as an Auditor of Summary FS, prepared of Investors. Mention the factors

you would **consider before accepting such engagement to report** of summary FS. [OLD]

Answer:

As per SA 810, → the auditor shall perform the following procedures, and any other procedures that the auditor may consider necessary, as the basis for the auditor's opinion on the summary FS:

Trick: Agar "aap full FS ke auditor" ho to hi summary FS ki audit karna > jo "Mngt ne FS" banaya hai > Uspne "Opinion" dena ki > ye Mngt ne banaya hai acche "Criteria" se > agar aapko cross check karna ho to "Full FS" bhi le lo

- **Accept** an engagement to report on SFS, **only when the auditor has been engaged** to conduct an **audit** in accordance with **SAs of the FS** from which the SFS are derived.
- Before accepting an engagement to report on SFS, the auditor shall
 - 1) Determine whether the **applied criteria are acceptable**;
 - 2) **Obtain the agreement of mgt that it acknowledges and understands its responsibility**:
 - a) For the **preparation of the SFS** in accordance with the applied criteria.
 - b) To make the **audited FS available to the intended users of the SFS without undue difficulty** (**or, if L&R provides** that the audited FS need **not be made available** to the intended users of the SFS and establishes the criteria for the preparation of the SFS, to **describe that L&R** in the SFS); &
 - c) To **include the AR on the SFS** in any document that contains the SFS and that indicates that the auditor has reported on them.
 - 3) Agree with mgt the **form of opinion** to be expressed on the SFS.
- If the auditor concludes that the applied **criteria are unacceptable** or is unable to obtain the agreement of mgt mentioned above, the auditor shall **not accept the engagement**, unless required by L&R to do so.
- **Non-Compliance of SA's** : i.e., **Criteria was Unacceptable**, But **L&R required auditor to accept the engmnt & Follow L&R** :
 - 1) Audit report on SFS shall **NOT indicate that engmnt was conducted in accordance with SA's**
 - 2) Include appropriate reference of this fact in terms of engagement
 - 3) Determine effect on engagement of audit of Audited FS

[Adequate disclosure of the **summarised nature of the summary FS and identity of the audited FS**, may, for example, be provided by a title such as **"Summary FS prepared from the audited FS for the year ended March 31, 20XX"]**

➤ **Nature of Procedures:**

Q10. procedures to perform & consider necessary as basis for forming an opinion on summary FS? [OLD]

Answer:

As per SA 810 → the auditor shall perform the following procedures, and any other procedures that the auditor may consider necessary, as the basis for the auditor's opinion on the summary FS:

Trick: Auditor bolega > ye "Summary" FS hai bhai > jisko Alag "criteria" se banaya hai > haalanki isme saari "Necessary information" hai > par fir bhi agar kisiko "Full FS" chahiye to lelo > nd iss summary FS ko usse "Compare" kar lo

- 1) Evaluate whether the summary FS **adequately disclose their summarized nature** and **identify the audited FS**.
- 2) Evaluate whether the summary FS **adequately disclose the applied criteria**
- 3) Evaluate whether the summary FS with the **applied criteria**.
- 4) Evaluate, in view of **purpose** of the summary FS, whether the summary FS **contain information necessary**, and are at an appropriate level of aggregation, so as **not to be misleading in the circumstances**.
- 5) **When summary FS are not accompanied by the audited FS**, evaluate whether they describe clearly:
 - a) From whom or **where the audited FS are available**; **or**
 - b) The **L&R specifies that the audited FS need not be made available** to the intended users of the summary FS and establishes the criteria for the preparation of the summary FS.
- 6) Evaluate whether the **audited FS are available to the intended users of the summary FS without undue difficulty**, unless law or regulation provides that they need not be made available and establishes the criteria



for the preparation of the summary financial statements.

- 7) **Compare the summary FS with** the related information in the **audited FS** to determine whether the summary FS agree with or can be re-calculated from the related information in the audited FS.

Form an Opinion:

If Unmodified opinion on Summary FS (SFS)	<u>Need be expressed on Summary F.S, Use any of following phrase:</u> • SFS are consistent, in all material respects, with audited FS as per applied criteria, Or, • The SFS are a fair summary of the audited FS as per applied criteria <u>If L&R prescribes different wording of opinion on SFS then above, the auditor shall:</u> • Apply "Nature of procedure" given above & Further AP to enable the auditor to express the prescribed opinion • Evaluate whether user of SFS might Misunderstand opinion → Whether additional explanation in AR can mitigate misunderstanding → If No → Don't accept engagement (<u>unless</u> required by L&R to do so, So it will not refer that engmntg was conducted as per SA's)						
Modified Opinion on SFS	Q11. if Summary FS is not fair summary of audited FS, Implication on Audit Report ? SA 810 Express adverse opinion → if SFS are not consistent in all material respects with or are not a fair summary of audited FS in accordance with applied criteria. (& Mngt not agree to make necessary changes)						
Qualified Opinion / EOM/ OM Para in Report on Audited FS	Q12. Consider that the audit report on FS issued by CA Madhur contains qualified opinion. Can he issue an unmodified opinion on summary FS derived from audited FS ? Discuss. When the Auditor's report on Audited F.S includes: <table border="1" data-bbox="349 993 1474 1108"> <tr> <td>a) Qualified opinion as per SA 705</td><td>b) EOM/OM as per SA 706</td></tr> <tr> <td>c) MU w.r.t G.C as per SA 570</td><td>d) Communicating KAM as per SA 701</td></tr> <tr> <td colspan="2">e) A statement that describes an uncorrected MMS of the other Info (SA 720)</td></tr> </table> Yes, he can issue an unmodified opinion, When Auditor is satisfied that the summary FS are consistent, in all material respects & fair summary of audited FS in accordance with applied criteria, <u>Audited report on Summary FS will contain:</u> a) State that audit report on FS contains qualified opinion/EOM/ OM para/MU w.r.t G.C / KAM/ statement describing MMS in other Info AND b) Describe: • Basis for qualified opinion on audited FS, & the effect thereof (if any) on summary FS; & • Matters referred in EOM/OM or MU w.r.t G.C in the Audited FS, & the effect thereof (if any) on summary FS; & • The uncorrected MMS of the other Info → and the effect(s) thereof, if any, on the info included in a document containing the summary FS & the auditor's report thereon.	a) Qualified opinion as per SA 705	b) EOM/OM as per SA 706	c) MU w.r.t G.C as per SA 570	d) Communicating KAM as per SA 701	e) A statement that describes an uncorrected MMS of the other Info (SA 720)	
a) Qualified opinion as per SA 705	b) EOM/OM as per SA 706						
c) MU w.r.t G.C as per SA 570	d) Communicating KAM as per SA 701						
e) A statement that describes an uncorrected MMS of the other Info (SA 720)							
Adverse Opinion/ Disclaimer of Opinion on Audited FS	Q13. auditor of company, has expressed adverse opinion on audited FS. What additional points he has to keep in mind while expressing opinion on summary FS? Report on SFS is required to include the following: 1. Statement that audit report contain adverse/disclaimer opinion; 2. Description of basis of such opinion; and 3. Statement that as a result of adverse/disclaimer of opinion it is inappropriate to express an opinion on Summary FS						
Timing of Work & Event	When the auditor reports on the summary FS after the completion of the audit of the FS, the auditor is not required to obtain additional audit evidence on the audited FS for subsequent events to audited FS						



Subsequent to Auditor's report on Full Audited FS	➤ <u>SFS audited report may be dated later than the date of AR on the audited FS.</u> • In such cases, the AR on the SFS shall <u>state that the SFS and audited FS do not reflect the effects of events that occurred subsequent to the date of the AR on the audited FS that may require adjustment of, or disclosure</u> ➤ <u>The auditor may become aware of facts that existed at the date of the AR on the audited FS, but of which the auditor previously was unaware.</u> • In such cases, the auditor shall <u>not issue the AR on the SFS until the auditor's i.r.t the audited FS in accordance with SA 560 has been completed.</u>							
Summary FS AR Date	➤ Summary FS Audited Report shall NOT be dated before: • Date of <u>obtaining SAAE</u> • <u>Date of report of Audited FS (Full)</u>							
Restriction on Distribution or Use or Alerting Readers to Basis of Accounting:	When distribution/use of the AR on the audited FS is restricted , or the said report alerts readers that the audited FS are prepared in accordance with a special purpose framework , the auditor shall include a similar restriction or alert in the AR on the SFS.							
Comparatives:	• If audited FS contain comparatives, but → SFS do not → auditor shall determine <u>whether such omission is reasonable.</u> • If omission is unreasonable → auditor shall <u>determine the effect on AR of SFS.</u> • If the SFS contain comparatives reported on by another auditor, the AR on the SFS shall also contain the matters required by SA 710 in the AR on the audited FS.							
Unaudited Supplementary Info. Presented With SFS	• Evaluate whether any <u>unaudited supplementary information presented with the SFS is clearly differentiated from the SFS.</u> • If not, the auditor shall ask <u>mgt to change its presentation.</u> If mgt refuses, auditor shall explain in AR on the SFS that <u>such information is not covered by that report.</u>							
Other Info.in Documents Containing SFS:	• read the information → Consider <u>whether there is a material inconsistency between the information and the SFS</u> • If material inconsistency identified → whether SFS/ information <u>needs revision</u> → <u>Discuss with Mngt</u> • If Information needs Revision → <u>But mngt refused</u> → <u>Auditor shall take appropriate action in the circumstances (Including implication on Auditor's report on Summary FS)</u>							
Auditor Association	• On Document containing SFS → Entity is mentioning that this SFS is audited → But that document does not contain Audit report → request mngt. to include A.report • If mngt. refuse → Carry out other <u>appropriate procedure</u> → <u>to prevent mgt from inappropriately associating the auditor with the SFS in that document.</u> Auditor may engage himself in AUDITED FS, But NOT in SUMMARY FS, If Auditor aware that <u>entity plans to make a statement that refers to the auditor and the fact that summary FS are derived from FS audited</u>, the <u>auditor shall be satisfied that:</u> a) The <u>reference to auditor is made</u> in the context of auditor's report on audited FS; & b) The statement does <u>not give impression that auditor has reported on summary FS.</u> If not the case of (a) & (b) → request mngt to change statement / Appoint auditor for SFS also → If mngt refuse → <u>carry out other appropriate actions designed to prevent management from inappropriately referring to the auditor.</u>							
Elements on Audit report of Summary FS	<table><tr><td>Title:</td><td>a) clearly indicating it as the report of an <u>independent auditor</u></td></tr><tr><td>addressee.</td><td>b) If addressee of summary FS A.Report are different than Audited FS → Evaluate appropriateness (Terms of engmnt, purpose of engmnt)</td></tr><tr><td>Identifies SFS</td><td>c) Identification of SFS, including the <u>title of each statement</u> [When Summary FS will be included in document that contains info. Other</td></tr></table>	Title:	a) clearly indicating it as the report of an <u>independent auditor</u>	addressee.	b) If addressee of summary FS A.Report are different than Audited FS → Evaluate appropriateness (Terms of engmnt, purpose of engmnt)	Identifies SFS	c) Identification of SFS, including the <u>title of each statement</u> [When Summary FS will be included in document that contains info. Other	
Title:	a) clearly indicating it as the report of an <u>independent auditor</u>							
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Identifies SFS	c) Identification of SFS, including the <u>title of each statement</u> [When Summary FS will be included in document that contains info. Other							
[TAI - O DSR								

8.10 | Page

Chp 8: SA 800, 805, 810



MA SPD]*(Special Trick :-)*

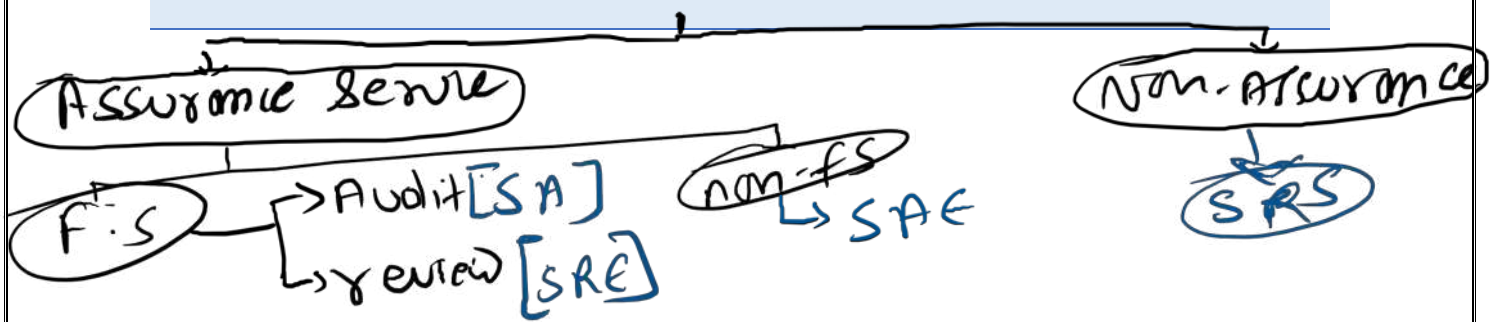
	than Summary FS, Then → Identify the page number on which summary FS presented (if form presentation allows the same)]
Identify audited FS	d) Identification of audited FS
Opinion	e) A Clear expression of Opinion
Not contain all disclosure	f) Statement that → SFS do not contain all disclosure of FRF of Audited FS → Hence SFS is not substitute of Full Audited FS
Subsequent events not reflected	g) If required → If AR on SFS date is later than AR of Audited FS → State that SFS & Audited FS → do not contain effect of subsequent events after audited FS date
Reference of Audited FS	h) Reference to the A.R on Audited FS → it's date → fact that unmodified opinion is expressed on it.
mgt's responsibility	i) Explaining that mgt is responsible for the preparation of the SFS as per applied criteria.
Auditor's responsibility	j) statement that the auditor is responsible for expressing an opinion , based on the Audit procedures conducted as per this SA. (whether the Summary FS are consider in all Material respect / fair summary → of the Audited F.S)
Sign	k) The auditor's signature + FRN + ICAI membership no. + UDIN
Date	l) Not earlier than: 1) The date on which the auditor has obtained SAAE on which to base the opinion, including evidence that the summary FS have been prepared and those with the recognised authority have asserted that they have taken responsibility for them; and 2) The date of the auditor's report on the audited FS
Place	m) the place of Signature

Q14. CA Madhur is auditor has issued audit report dated 15th June. The audit report on **summary FS** derived from such audited FS is dated 15th July of that particular year. Discuss **whether there exists any additional reporting responsibility** for auditor in such a situation for audit report on summary FS.

Hint: "the **auditor's report on summary FS** should **state** that the summary financial statements and the audited FS do **not reflect the effects of events that occurred subsequent to the date of the auditor's report on the audited financial statement**"

CHAPTER 9- AUDIT RELATED SERVICES

SRS 4400 & 4410



[SQCs are to be applied for all services covered by "Engagement Standards"]

Q1. How do "related services" differ from assurance engagements?

Assurance Engagement:	Practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users, evaluation or measurement of a subject matter against criteria
Non-Assurance Services: (Related Services)	Not involve opinion on truth & fairness of FS: Standards on Related Services (SRE) , Eg.: - Preparation of tax returns where no conclusion conveying assurance is expressed. Consulting (or advisory) engagements such as management and tax consulting. - Engagements covered by SRS, such as: Agreed-upon procedures engmt & compilations of financial or other information
Agreed Upon Procedure (AUP):	Auditor engaged by client to issue a report of factual findings , based on specified procedure performed on specified subject matter of specified element , A/c or item of F.S. say, A/c payable, A/c receivable , purchases from related parties & sales and profits of a segment of an entity , or a F.S, say, a B/S or even a complete set of F.S. [He MAY NOT be Auditor of Company F.S.]
SRS 4400:	Engagements to Perform Agreed-upon Procedures Regarding Financial Information
SRS 4410:	Compilation Engagements

SRS 4400 - Engagements to Perform Agreed-upon Procedures Regarding Financial Information:

Scope & Objective:	- Provide guidance on the auditor's professional responsibilities when an engagement to perform agreed-upon procedures (AUP) regarding financial information (FI) is undertaken and on the form and content of the report that the auditor issues. (This SRS Auditor is not necessary required to be a main auditor of FS) - Auditor is engaged by the client to issue a report of factual findings, based on specified procedures performed on specified subject matter of specified elements, accounts or items of a FS (Eg. Accounts payable, accounts receivable, purchases etc.) - Auditor simply provides a report of the factual findings of AUP, no assurance is expressed by him in his report. Instead, users of report assess for themselves the procedures & findings reported by auditor & draw their own conclusions from the work done by the auditor Report is restricted to those parties that have agreed to the procedures to be performed
Audit Vs. Agreed Procedure:	- An audit expresses an opinion and provides assurance to users agreed-procedures engagement, only a report of the factual findings of agreed-upon procedures is provided (users draw their own conclusions based on factual findings of report)



Example of A/c Payable:	<u>Example, an AUP engagement to evaluate validity of accounts payable may state the following:</u> 1) Comparing of names of major suppliers and the amounts outstanding as on a date to the related names and amounts in the trial balance 2) Obtaining suppliers statements or confirmations from suppliers of O/s balance on a date 3) Comparison of such statements or confirmations to the amounts in trial balance Actual finding (i.e. Any variance of A/c from T.B shall be stated) → without providing an assurance		
General Principles: (IPC-OP)	• Auditor should comply with the Code of Ethics issued by the ICAI		
	Integrity;	Professional competence & due care	Confidentiality
	Objectivity	Professional conduct	Technical standards
	• Independence is NOT a requirement for AUP engagement → However, Terms / objective of engagement may require auditor to comply with the independence → Where the auditor is not independent, a statement to that effect should be made in report of factual findings .		
Terms of Engagement: (Nov'24) Kyu kar re h ? Kispe kr re h? Kya kr re h? Sabko ni bolo (Special Trick :-)	Q2. AUP → What matters will you include in engagement letter addressed to the mngt? (nov'24) Matters to be Agree Include Following: • 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 • Stated purpose for the engagement • Identification of the FI to which the AUP will be applied. • NTE of the specific procedures to be applied. • 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) Matters Included in Engagement: Auditor sends an engagement letter documenting the key terms of appointment • A listing of the procedures to be performed as agreed-upon between the parties • A statement that the distribution of report of factual findings would be restricted to the specified parties who have agreed to the procedures to be performed		
Procedures and Evidences {ICI-OR}	The auditor should carry out the procedures agreed-upon and use the evidence obtained as the basis for the report of factual findings: • Inquiry and analysis • Obtaining Confirmations • Inspection . • Observation • Re-computation , comparison and other clerical accuracy checks		

➤ **REPORTING** (points have to be kept in mind for being included in the report):

Q3. (SM) → Company asks you to carry out process of confirmation of its Debtors. Work only involves preparing & sending confirmation, analysis of variations → points to be kept in mind for inclusion in report ?

Elements of Report: The report of factual findings should contain:

[Trick: TAI - ne SP - SD - AP - sabka exam diya - RR - DPS]

- 1) **Title;**
- 2) **Addressee** (ordinarily, the appointing authority);
- 3) **Identification of specific financial** or non-financial information to which the AUP have been applied;
- 4) A statement that the **procedures performed were agreed-upon** with the recipient;
- 5) A statement that the engagement was performed in accordance with the **SRS applicable**



- 6) Identification of the **purpose** for which the AUP were performed
- 7) A listing of the **specific procedures** performed;
- 8) A **description of the auditor's factual findings** including sufficient details of errors & exceptions found
- 9) A **statement** that the procedures performed do **not constitute either an audit or a review** (no assurance);
- 10) 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
- 11) A **statement** that the **Report is restricted** to those parties that have agreed to the procedures;
- 12) 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 to the entity's FS taken as a whole;
- 13) **Date** of the report;
- 14) **Place** of signature; and
- 15) Auditor's **signature**.

Q4. Company has huge Debtors → mngt want to evaluate Validity of Debtors (names, balance, contract) → despite not being statutory auditor. (a) Explain nature of engmnt, whether she can accept? (b) While reporting, what precautions should be taken so that reader do not misunderstand it's scope

Hint:

a) above is an engagement to perform agreed upon procedures. i.e., auditor to issue a report of factual findings based on specified procedures performed on specified subject matter.

SRS 4400. → person performing related services need necessarily be the auditor (CA. Karuna can accept)

b) Refer above point → 9,10,11,12 of reporting (i.e. Statement, Statement, Statement, Statement)

SRS 4410 - Compilation Engagements

Scope:	Assist Mngt: (FI+Hist)	Practitioner's responsibilities when engaged to assist mgt with the preparation and presentation of historical FI as per FRF without obtaining any assurance on that info, & to report on the engagement in accordance with this SRS
	Non-FI & Non-His:	It may be adapted for other than historical FI & Non-FI after doing necessary changes & applying procedures
	Not Assurance:	NOT an assurance engagement → not require the practitioner to verify accuracy or completeness of info provided by mgt for compilation (No Opinion/No review)
	Mngt Retain responsblty:	Mgt retains responsibility for the FI and the basis on which it is prepared & presented (Including Judgement, estimation, choosing appropriate A/cing policy)
	Different FRF:	Different FRF can be used to prepare & present financial information (Use of FRF will depend on the nature of the entity and the intended use)
- Reporting under this SRS, include whether: ✓ FI is required under provisions of applicable L&R ✓ If External parties other than intended users are likely to associate, info. may be misunderstood		
SQC 1:	Its applicable: Q.C w.r.t Compilation engmnt, <u>Engmnt partner shall take responsibility for:</u> - The overall quality of each compilation engagement to which that partner is assigned and - The engagement being performed in accordance with the firm's Q.C policies & procedures	
Ethical	Q5. In compilation engagement of SRS 4410. Is required to comply ethical requirements of Ethics ? Practitioner shall comply with relevant ethical requirements, In complying with the Code of Ethics, threats to the practitioner's compliance with relevant ethical requirements are required to be identified and appropriately addressed	



	(Independence not Apply: However, L&R may specify requirements or disclosure rules pertaining to independence.)
Objective:	Q6. Objectives of compilation engagement. [OLD] As per SRS 4410 → the objective of a compilation engagement is for an accountant to use a/cing expertise, as opposed to auditing expertise, to collect, classify and summarize financial info. • Apply accounting & financial reporting expertise to assist mgt in preparation & presentation of FI in accordance with an applicable FRF based on information provided by mgt; & • Report in accordance with the requirements of this SRS.
Document File:	(it's not 60 days) Final engagement file should be assembled on timely basis after engagement report has been finalized in accordance with the time limits set by the firm.

Compilation Engagement	
Definition:	Engagement in which a practitioner applies accounting and financial reporting expertise to assist mgt in the preparation and presentation of FI of an entity in accordance with an applicable FRF, and reports as required by this SRS.
Various Purpose	Q7. List out few intended purposes of a "compilation engagement." (SM & RTP'25) It may be for Various Purpose Including: 1) To comply mandatory periodic FR requirements established in law or regulation, if any or 2) Unrelated to mandatory financial reporting under relevant L&R (internal Use), Example: • For Mngt or TCWG, prepared on a basis appropriate for their particular purposes (such as preparation of financial information for internal use). • For periodic F.R undertaken for external parties under a contract or other form of agreement (such as F.I provided to a funding body to support 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)

Q8. MNC Ltd has engaged CA Lalit to help company in compilation of financial info. Discuss key issues w.r.t this engagement & the manner it differ from assurance engagements. & applicability of SQC 1 this

Hint: Refer Above "Definition" & "Various Purpose" given above of "Compilation engagement" and Below

- "Assurance engagement" → in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria. Means → practitioner gives an opinion → users able to make confident decisions knowing well that chance of information being incorrect is diminished.
- A compilation engagement is not an assurance engagement. → Not require the practitioner to verify accuracy or completeness of info provided by mngt for compilation, Not to gather evidence for audit opinion or a review.
- Yes, SQC 1 is applicable to all Engagement & Q.C Standards. Since SRS 4410 is also one them → SQC 1 applies.

➤ Engagement Acceptance/ Continuance

Q9. Hired CA to compile FS of interim period. Draft enmngt letter & specific focus on mngt Responsibility. [OLD]

Agreeing the Terms of the Engagement:

- The intended use and distribution of the FI, and any restrictions
(Mera kaam , Tera Kaam → fir Meri Responsibility, teri responsibility)
- Identification of the applicable FRF;
- The objective and scope of the CE;
- The responsibilities of the practitioner, including to comply relevant ethical requirements;
- The responsibilities of mgt for:



- ✓ The **FI**, and for the preparation and presentation thereof, in accordance with a FRF that is acceptable in view of the intended use of the FI and the intended users;
- ✓ Design, **implementation and maintenance of such IC** as mgt determines is necessary to enable the preparation of FS free from MM, whether due to fraud or error;
- ✓ The **accuracy & completeness of the records**, documents, explanations and other info provided by mgt for the CE; and
- ✓ **Judgments** needed in the preparation and presentation of the FI, including those for which the practitioner may provide assistance; and
- The **expected form and content** of the practitioner's report.

[**On recurring compilation engmnt** → evaluate whether circumstances including changes **require terms of engmnt to be revised** & whether there is need to remind mngt of the existing terms of engagement]

Q10. terms of engagement with management. → mention **responsibilities of the mngt** to be agreed **SRS 4410**.

Hint: Refer Above Qn of Drafting Engagement letter → "**Responsibilities of Management**"

➤ Performing Engagement:

[Bhai .. Muje chalaake koi bhi verification nahi karna h, par agar koi Misstatement saamne aaya → to correct karao .. wrna withdraw karo .. (baaki deemed correct maano sab)]

Q11. Define characteristics of Compilation engmnt. & approach of CA P for performing the Engagement ? [SM]

Answer: [Refer Above Notes "**Compilation Engagement**" for Definition & Below answer for Performing:

[**Trick:** "**Understanding lo business**" ki, "**Discuss karo mngt**" se "**FI compile**" karne k liye > fir usse "**read**" karo 1 baar ki koi bhi "**inaccuracy**" to nii h .. agar hai .. to mngt ko bolo "**rectify**" karne k liye ya "**withdraw**" karo]

- 1) Practitioner shall **obtain an understanding** of the following matters:
 - a) The **entity's business** and operations, including the entity's **accounting system** and **accounting records** and
 - b) The applicable **FRF**, including its application in the entity's industry.
- 2) Shall **discuss with mgt**, or TCWG as appropriate, those **significant judgments** for which the practitioner has provided assistance
- 3) Practitioner shall **compile the FI using the records**, documents, explanations and other information, including significant judgments, **provided by mgt**
- 4) **Prior to completion**, shall **read compiled FI** in light of **practitioner's understanding** of **entity's business** & applicable **FRF**
- 5) If, the practitioner **becomes aware that the records, documents, explanations** or other information, including significant judgments, provided by mgt are **incomplete, inaccurate** or otherwise unsatisfactory, the practitioner shall **bring that to the attention of mgt** and **request the additional or corrected information**
- 6) If the practitioner is **unable to complete the engagement because mgt has failed to provide records, documents**, explanations or other information, including significant judgments, as requested, the practitioner shall **withdraw** from the engagement and inform them of the reasons for withdrawing
- 7) **If the practitioner becomes aware that:**
 - ✓ The compiled FI does **not adequately refer to or describe the applicable FRF**;
 - ✓ Amendments to the compiled FI are required for the FI not to be **materially misstated**; or
 - ✓ The compiled FI is otherwise **misleading**

Practitioner shall **propose the appropriate amendments** to mgt → If **mgt declines** → **withdraw** → inform them of the **reasons**

If withdrawal Not possible → determine the professional and legal responsibilities
- 8) Practitioner shall obtain an acknowledgement from **mgt or TCWG**, as appropriate, that they have taken **responsibility for the final version of the compiled FI**.



Q12. You appointed to **compile the FS of a partnership firm**. You discovered that **inventory is grossly understated**, (AS 2 not followed) → whether it's **outside your scope**, as it's **not audit**. (MTP'24)

Hint: SRS 4410 → Mention **above Point No 6, 7 & 8** of "**Performing Engagement**" i.e., **Unable to complete, become aware that (withdraw), acknowledge from mngt.**

Q13. While **performing compilation engmnt** → Observed that theft loss in inventory of 1 Crore → **insurance co. repudiated (rejected)** → Amount is still under trial balance "Current assets"

Hint: → Given Case, Rs. 100 lacs is in "current assets" → **amendments required for the FI not to be MMS.**

If practitioner becomes aware → **amendments required** → **propose appropriate amendments to mngt.**

If mngt declines, → **withdraw** from engmnt & inform mngt & TCWG reasons of withdraw.

If withdrawal not possible, → **determine the professional & legal responsibilities applicable in circumstances.**

➤ Documentation

Q14. documentation requirements by a practitioner while performing a compilation engagement SRS 4410.

[Trick: "Final Version of FI" ko Compare karo "underlying records" se > uske baad jo bhi "significant matters" mile usse evaluate karo ...]

The practitioner shall include in the engagement documentation:

- Significant matters** arising during the compilation engagement and how those matters were addressed by the practitioner
- A **record of how** the **compiled financial info. reconciles with the underlying records**, documents, explanations and other information, provided by management and
- A **copy of the final version of the compiled financial Info** for which mngt or TCWG, as appropriate, has acknowledged their responsibility, and the practitioner's report

The practitioner may consider also including in the engmnt documentation a copy of the **entity's trial balance, summary of significant A/cing records** or **other info** that the practitioner used to perform compilation.



CHAPTER 10- Review of Interim Financial Information

SRE 2400, 2410

➤ Some Key Words to understand before Starting Review (SRE)

Limited Assurance: Negative Assurance (Review)	- Moderate Level of assurance (Opinion) i.e., Lower level of assurance than audit - Where engagement risk is reduced to a level that is acceptable in circumstances but where that risk is greater than for a reasonable assurance engagement. - Low checking (Generally Analytical procedure) i.e., Fewer Procedure & gathers SAAE on basis of which limited conclusions can be drawn up - The combination of NTE of evidence gathering procedures is at least sufficient for the practitioner to obtain a meaningful level of assurance. (To be meaning it's likely to enhance the intended users confidence about the FS) - However, "review" is related to FS prepared on historical financial info. just like an audit. <u>[i.e., Nothing has come to our attention that causes us to believe that the FS do not give a true and fair view]</u>

Q1. Contrast review assignment with Stat audit of company's FS w.r.t SCOPE & REPORT issued. (OLD Answer)

Audit	Review
Audit is a type of reasonable assurance engagement providing reasonable level of assurance.	Limited assurance engagement providing lower level of assurance than reasonable assurance engagement
It performs elaborate and extensive procedures including TOC 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

Standards on Review Engagement (Moderate Level of assurance / Negative/Limited Opinion)

SRE 2400:	Engagements to Review Historical Financial Statements
SRE 2410:	Review of Interim Financial Info. Performed by the Independent Auditor of the Entity

SRE 2400: Engagements to Review Historical Financial Statements

Scope:	• The <u>practitioner's</u> responsibilities when engaged to <u>perform a review of historical FS</u> when the practitioner is not the auditor of the entity's FS; and • The form and content of the practitioner's report on the FS. • This SRE is to be <u>applied, adapted as necessary</u>, to reviews of other <u>historical FI</u>. • FS prepared as per FRF can be : <u>Fair FRF</u> <u>or</u> <u>Special purpose FRF</u>		
Practitioner	• CA or CA Firm in public practice [Here he should not be auditor of the same entity]		
Not applicable:	• This SRE does not address a review of an <u>entity's FS or interim FI</u> performed by a practitioner <u>who is the independent auditor</u> of the entity's FS. • SRE 2410: When <u>auditor's</u> performing <u>Qtr Review Engagement. (Interim Financial Info.)</u> [However, if other practitioner performing review of IFI → SA 2400]		
Summary of Applicability:		Review of FS	Review of IFI
	Independent Auditor	SRE 2400 <i>[Doubted]</i>	SRE 2410



	Other Practitioner	SRE 2400	SRE 2400
Review Historical FS:	- The review of historical FS is a limited assurance engagement, - In a review of FS, the practitioner expresses a conclusion designed to enhance the degree of confidence of intended users regarding the preparation of an entity's FS as per applicable FRF. - Conclusion is based on the practitioner obtaining limited assurance (Report includes a description of the nature of a review engagement) - The practitioner performs primarily inquiry and Analytical Procedure to obtain SAAE as the basis for a conclusion on the FS as a whole, expressed as per the requirements of this SRE. - If the practitioner becomes aware, FS may be materially misstated, the practitioner designs and performs additional procedures, as the practitioner considers necessary in the circumstances, to be able to conclude on the FS in accordance with this SRE.		
Objective:	Obtain limited assurance, primarily by performing inquiry and Analytical Procedure, about whether the FS as a whole is free from MM → practitioner to express a conclusion on whether anything has come to the practitioner's attention that causes the practitioner to believe the FS are not prepared, in all material respects, as per applicable FRF; and - When limited assurance cannot be obtained and a qualified conclusion is insufficient → either disclaim a conclusion or, where appropriate, withdraw from engagement if withdrawal is possible under applicable L&R.		
Practitioner shall Comply With Ethical & QC : <i>[Engt level Qlty Control are Same as SRS 4410]</i>	Each SRE requirement → practitioner shall comply with each requirement of this SRE → unless a requirement is not relevant → Don't mention that compliance with this SRE unless complied with all - Relevant ethical requirements → Including Independence Professional Skepticism and Professional Judgment Engagement Level Quality Control: Engagement Partner (EP) shall have assurance skill, financial reporting skill: The EP shall take responsibility for: ✓ The engagement being performed in accordance with the firm's QC policies. ✓ The overall quality of each review engagement to which that partner is assigned ✓ The direction, supervision, planning and performance of the review engagement in compliance with professional standards and applicable regulatory requirements; ✓ The practitioner's report being appropriate in the circumstances		

Q2. As per **condition in the contract**, Roma Ltd is required to **get its FS reviewed** on a quarterly basis in accordance with the **F.R provisions of the contract**. Can they get it reviewed from accountant in practice?

Hint: FS prepared as per **SPF** → can also be reviewed by a professional accountant in practice (**SRE 2400**)

➤ Acceptance and Continuance of Client Relationships and Review Engagements

Factors affecting Accept & Continuance:	Q3. consideration of engmnt continuance & relevant ethical requirements, Wr.t. SRE 2400, , state circumstances when practitioner shall not accept review engagement. [OLD] As per SRE 2400: "Factors Affecting Acceptance & Continuance of Client Relationships" Unless required by law or regulation, the practitioner shall not accept review engagement if: Trick: Yaar muje to samaj hi nii aara "Rational" hi kya h iss engt ko karane ka "Audit" hi karani chahiye thi > "Kuch information to de ni rhe, poora "limitation of scope" to laga Rakha h > de bhi rahe h to pe "Doubt" hora h muje to uss info pe > kyuki wo log "independent" to hai nii
(Special Trick :-)	(a) The practitioner is not satisfied: - That there is a rational purpose for the engagement. (i.e., objectives specified for engagement may not be achieved by review, i.e., Need Audit or Limitation is imposed) Review engmnt is appropriate in circumstances. (Preliminary understanding indicates, review is not appropriate, other type of engmnt require, eg. Audit, if audit/assurance engmnt



	prohibited → recommend compilation engagement) (b) Practitioner's preliminary understanding of the circumstances → indicates that information needed to perform the review engagement is likely to be unavailable or unreliable; (c) mngt or TCWG impose a limitation on the scope of practitioner's work, will result in disclaimer. (d) The practitioner has cause to doubt management's integrity such that it is likely to affect proper performance of the review; (e) Practitioner has reason to believe that relevant ethical requirements, including independence, will not be satisfied;
Precondition: (Special Trick :-)	Preconditions to accept review engagement → Q4. review of historical FS (you have not audited FS). → preconditions prior to accepting [OLD] As per SRE 2400, Preconditions, Prior to accepting a review engagement, the practitioner shall: ➤ Determine whether the FRF applied in FS is acceptable including, in the case of special purpose FS, obtaining an understanding of the purpose for which the FS are prepared and of the intended users; and ➤ Obtain the agreement of mgt that it acknowledges and understands its responsibilities: a) For preparation of FS in accordance applicable FRF, where relevant, their fair presentation; b) For such internal control as mgt determines is necessary to enable the preparation of FS that are free from MM, whether due to fraud or error; and c) To provide the practitioner with: • Access to all information of which mgt is aware that is relevant to the preparation of the FS, such as records, documentation and other matters; • Additional information that the practitioner may request from mgt for the purpose of the review; • Unrestricted access to persons within the entity from whom the practitioner determines it necessary to obtain evidence. ➤ 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 mgt or TCWG. ➤ If changes cannot be made to satisfy the practitioner as to those matters, the practitioner shall not accept the proposed engagement unless required by L&R (Then not include any reference of SRE).
Precondition (After Acceptance)	If it is discovered AFTER the engagement has been accepted → Above Preconditions are NOT satisfied → Discuss the matter with mngt & TCWG to determine: • Whether the matter can be resolved • Whether it is appropriate to continue with the Engmnt and • Whether and, if so, how to communicate the matter in the practitioner's report.
Agreeing the terms of engagement:	The practitioner shall agree terms of the engagement with mgt or TCWG, as appropriate, prior to performing engagement. (Engagement letter or other suitable form of written agreement) On recurring review engagements → evaluate whether circumstances require the terms of engagement to be revised or remind
Change in Term:	No reasonable justification → do not agree the change, If reasonable justification → agree on and record the new terms in writing
➤ Performing the Engagement	
Materiality:	Determine materiality for the FS as a whole (practitioner's judgment about what is material i.r.t FS is same regardless of level of assurance) → Revise it on aware of new information
FS agree with records:	Practitioner shall obtain evidence that FS agree with, or reconcile to, the entity's underlying accounting records



Obtain Understanding:	Obtain understanding of Entity & its environment (to identify areas in FS where MMS exist) → Include same as SA 315 → IRE FANO i.e., Industry, regulatory, environment, entity operation, ownership etc.	
Designing & Performing Procedures (Inquiry & Analytical Procedures):		
In obtaining SAAE for conclusion on FS as whole, practitioner shall design & perform inquiry & analytical procedure:		
a) To address all material items in the FS, including disclosures and		
b) To focus on addressing areas in the FS where MMS are likely to arise.		
[He may perform procedures as per circumstance; however, it will not alter objective to achieve limited assurance]		
Inquiry:	- Includes seeking information from mngt and other persons within the entity. - include matters such as relating to making of accounting estimates, identification of R.P , about significant, complex / unusual transactions, actual, suspected fraud, Subsequent events, basis for mngt's assessment of entity's ability to continue as a GC, material commitments, contractual obligations or contingencies that have affected or may affect the entity's FS including disclosures and material non-monetary transactions or transactions for no consideration in the financial reporting period under consideration. - May also extend Inquiries to obtain non-financial data - Evaluating the responses provided by mngt is integral part - Perform Further Inquiries i.r.t identified inconsistencies →to considers reasonableness & consistency of mngt's responses as compare to auditor procedure result & understanding of entity - Depending on the engagement circumstances, inquiries may also include inquiries about: (i) Actions taken at meetings of owners, TCWG and committees thereof, and proceedings at other meetings, if any, that affect the info. & disclosures contained in F.S. (ii) Communications the entity has received, or expects to receive, from regulatory agencies (iii) Matters arising in course of applying other procedures	
Analytical Procedure:	Consider whether the data from the entity's A/cing system & accounting records are adequate for the purpose of performing the analytical procedures.	
Importance of Inquiry & Analytical Procedure in Review:	Inquiry assist in:	Analytical procedure assist in:
	Evidence obtained through inquiry is often the principal source of evidence about mngt intent. However, information available to support mngt intent may be limited. In that case, - Understanding mngt's past history of carrying out its stated intentions, - mngt's stated reasons for choosing a particular course of action, and - mngt's ability to pursue a specific course of action may provide relevant info. to corroborate the evidence obtained through inquiry. Application of professional skepticism in evaluating responses provided by mngt is important to enable the practitioner to evaluate whether there are any matters that would cause the practitioner to believe the FS may be MM. Performing inquiry procedures also assists	[Inquiry se → Understanding hoi → par wo Inconsistent hai → means MMS hai] - Obtaining or updating practitioner's understanding of entity & its environment, including to be able to identify areas where MMS are likely to arise in FS. - Identifying inconsistencies or variances from expected trends, values or norms in the FS such as the level of congruence of the FS with key data, including key performance indicators. - Providing corroborative evidence i.r.t other inquiries or analytical procedure already performed. - Serving as additional procedures when the practitioner becomes aware of matters that cause the practitioner

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	practitioner in obtaining practitioner's understanding of entity and its environment, to be able to identify areas where MMS are likely to arise in FS.	to believe that the FS may be materially misstated

Q5. Discuss why "inquiry" is important as an audit procedure in an engagement to review financial statements.

Hint: Refer Above "Inquiry Assist in" [But if Question is of higher marks: Explain About "Inquiry" also]

Q6. review as per SRE 2400, → certain procedures → Naming them & there importance (MTP 2024)

Hint: inquiry and analytical procedures to obtain SAAE as basis for a conclusion on the FS as a whole

Now mention above "Importance of Inquiry & Analytical Procedure", (However, Don't mention those 3 points of mngr intent, as mentioned in Importance of inquiry i.e., understand mngr past history, reason, ability)

Procedures to Address Specific Circumstances: [GROF]	
Going Concern:	Q7. A review of FS includes consideration of entity's ability to continue as a G.C. practitioner becomes aware of events or conditions that may cast significant doubt about the entity's ability to continue as a G.C. Enumerate steps to be taken by practitioner (MTP'24 & SM) Review of FS includes consideration of entity's ability to continue as a going concern 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: Inquire mngr about plans for future actions affecting the entity's ability to continue as a G.C. and about the feasibility of those plans, and also whether mngr believes that the outcome of those plans will improve the situation regarding the entity's ability to continue as a G.C. Evaluate results of above inquiries, to <u>consider whether mngr's responses provide a sufficient basis to:</u> - <u>Continue to present the FS on going concern</u> basis if the applicable FRF includes the assumption of an entity's continuance as a going concern or <u>Conclude whether the FS are MMS</u>, or are otherwise misleading regarding the entity's ability to continue as a going concern and Consider management's responses in light of all relevant information of which the practitioner is aware as a result of the review.
Related parties:	Shall remain alert for info. that may indicate the existence of RPR or RPT that the management has not previously identified , outside normal course of business.
Use of work performed by Other:	Work performed by other practitioners possessing expertise in a field other than accounting or assurance → if he uses that work → shall take appropriate steps to be satisfied that the work performed is adequate for the practitioner's purposes
Fraud & Non-Comply L&R:	If any suspected fraud / Non comply of L&R → communicate matter to mngr & TCWG → request them to assess effect on FS . Whether responsibility to report to party outside the entity.

Additional procedures when practitioner becomes aware that statements may be materially misstated:

When FS are materially misstated → shall design and perform additional procedures to enable practitioner to:

- Conclude** that the matter(s) is not likely to cause FS as a whole to be materially misstated, Or
- Determine** that the matter(s) causes the FS as a whole to be materially misstated

Professional Judgement:	Additional procedures w.r.t an item the practitioner has cause to believe may be materially misstated in the FS will vary, depending on the circumstances , and is a matter for the practitioner's professional judgment .
Additional	1) Additional inquiry or analytical procedures , for Eg., being performed in greater detail or



Procedure to obtain SAAE:	being focused on the affected items (i.e., amounts or disclosures concerning the affected accounts or transactions as reflected in the FS); or 2) Other types of procedures , for example, substantive TOD or external confirmations
Subsequent Event:	1) Between Date of FS & Date of Report: Events between these dates may require adjustment or disclosure → request management to correct those misstatements. 2) After date of practitioner's report <u>[Exactly same as SA 560]</u>

Q8. In review of F.S → gathered upon inquiry that there is a possibility of MMS → how you proceed, SRE 2400.
Hint: Refer Above whole table "Additional procedures when practitioner becomes aware that statements may be materially misstated" (other than Subsequent Event)

Q9. ICAI Example [A/c Receivable]: Example when additional procedures may be necessary in Review:

During review, analysis of accounts receivable shows a material amount of past due receivable, for which there is no allowance for doubtful debts. → may be materially misstated.

The practitioner then inquires of mngr whether there are uncollectible A/c receivable that need to be impaired.

Depending on management's response, the practitioner's evaluation of the response may:

- Enable the practitioner to **conclude** that **A/c receivable balance is NOT** likely to **materially misstated**. In that case, **no further procedures** are required
- Enable practitioner to determine that **matter causes the FS to materially misstated**. **No further procedures** are required, and practitioner would form conclusion that FS as a whole are materially misstated.
- Lead the practitioner to continue to **believe** that the **A/c receivable balance is likely to be materially misstated**, **while not providing SAAE** for the practitioner to **determine that they are in fact misstated**. In that case, the practitioner is required to **perform additional procedures**, for example, **requesting from mngr an analysis of amounts received** for those accounts **after the balance sheet date** to identify uncollectible accounts receivable.

The evaluation of the results of the additional procedures may enable the practitioner to get to (a) or (b) above.

If not, the practitioner is required to:

- Continue performing additional procedures until** the practitioner **reaches either (a) or (b) above** or
- If** practitioner is **not able to either conclude** that **matter is not likely to cause the FS** as a whole to be **materially misstated or**
To **determine** that matter does cause the **FS as a whole to be materially misstated**, **then a scope limitation exists** and the practitioner is **not able to form an unmodified conclusion** on the FS.

Obtain Written Representation:	
Obtain WR:	W.R. are important source of evidence in review engagement. If management modifies or does not provide the requested W.R, it may alert possibility that one or more significant issues exist
Content W.R	<u>"Refer Additional PDF"</u>
Evaluating evidence obtained from the procedures performed	
Obtain SAAE:	Evaluate whether SAAE obtained from procedures performed &, if not , the practitioner shall perform other procedures
If Not SAAE:	If SAAE not obtained from Inquiry & Analytical procedure & to form conclusion:
	The practitioner may: Extend work performed or Perform other procedures judged by the practitioner to be necessary in circumstances.
	If above is not Practicable or Not able to Obtain SAAE by above procedure also : Determine effect on practitioner's report



Limitations have on the scope of the review • Not able to obtain SAAE → Discuss with Mngt & TCWG • If able to obtain SAAE by performing other procedures → It will not constitute a limitation even if unable to perform a specific procedure • Limitation on Scope: May have other implications → Such as → practitioner's consideration of areas where the FS are likely to be materially misstated, and engagement continuance					
Forming the practitioner's conclusion on FS					
While Forming Conclusion, Consider:	Shall also consider the impact of: 1) Uncorrected misstatements identified during the review, and in the previous year's review of the entity's FS, on the FS as a whole 2) Qualitative aspects of the entity's A/cing practice, including indicators of possible bias in management's judgments <u>If FS prepared using fair present. framework, practitioner's consideration shall also include:</u> a) Overall presentation, structure & content of FS as per applicable FRF b) Whether FS including notes achieves fair presentation, True & Fair for FS as a whole				
Unmodified:	FS as a whole → obtained Limited Assurance → Phrase: ➤ Fair Presentation Framework: "Based on our review, nothing has come to nothing has come to our attention that causes us to believe that the FS do NOT give a true and fair view (or do not present fairly, in all material respects), in accordance with the applicable FRF" ➤ Compliance Framework: Based on our review, nothing has come to our attention that causes us to believe that the financial statements are not prepared, in all material respects, in accordance with the applicable financial reporting framework				
➤ Modified Opinion:					
When?	• FS are materially misstated, Or, • Unable to obtain SAAE FS that are material i.r.t. the FS as a whole				
Heading:	• Use the heading "Qualified Conclusion," "Adverse Conclusion" or "Disclaimer of Conclusion," as appropriate, for the conclusion paragraph in the practitioner's report. • "Basis for Qualified Conclusion," "Basis for Adverse Conclusion" or "Basis for Disclaimer of Conclusion," as appropriate (Provide a description of the matter)				
FS is Misstated:	<table border="1"> <tr> <td>Qualified Opinion:</td><td> a) "Based on our review, except for the effects of the matter(s) described in the Basis for Qualified Conclusion paragraph, nothing has come to our attention that causes us to believe that the FS do not give a true & fair view (or do not present fairly, in all material respects), OR, b) <u>For Compliance: Same as Above</u> → (But instead of T&F) FS are not prepared, in all material respects, as per applicable FRF </td></tr> <tr> <td>Adverse Opinion:</td><td> a) "Based on our review, due to the significance of the matter(s) described in the Basis for Adverse Conclusion paragraph, the FS do not give a true and fair view (or do not present fairly, in all material respects), in accordance with the applicable FRF," OR, b) <u>For Compliance: Same as Above</u> → (But instead of T&F) FS are not prepared, in all material respects, in accordance with the applicable FRF. </td></tr> </table>	Qualified Opinion:	a) "Based on our review, except for the effects of the matter(s) described in the Basis for Qualified Conclusion paragraph, nothing has come to our attention that causes us to believe that the FS do not give a true & fair view (or do not present fairly, in all material respects), OR, b) <u>For Compliance: Same as Above</u> → (But instead of T&F) FS are not prepared, in all material respects, as per applicable FRF	Adverse Opinion:	a) "Based on our review, due to the significance of the matter(s) described in the Basis for Adverse Conclusion paragraph, the FS do not give a true and fair view (or do not present fairly, in all material respects), in accordance with the applicable FRF," OR, b) <u>For Compliance: Same as Above</u> → (But instead of T&F) FS are not prepared, in all material respects, in accordance with the applicable FRF.
Qualified Opinion:	a) "Based on our review, except for the effects of the matter(s) described in the Basis for Qualified Conclusion paragraph, nothing has come to our attention that causes us to believe that the FS do not give a true & fair view (or do not present fairly, in all material respects), OR, b) <u>For Compliance: Same as Above</u> → (But instead of T&F) FS are not prepared, in all material respects, as per applicable FRF				
Adverse Opinion:	a) "Based on our review, due to the significance of the matter(s) described in the Basis for Adverse Conclusion paragraph, the FS do not give a true and fair view (or do not present fairly, in all material respects), in accordance with the applicable FRF," OR, b) <u>For Compliance: Same as Above</u> → (But instead of T&F) FS are not prepared, in all material respects, in accordance with the applicable FRF.				
Unable to Obtain SAAE:	• <u>Qualified</u> or <u>Disclaimer</u> of Opinion <table border="1"> <tr> <td>Withdraw:</td><td> Shall withdraw from Engmnt if following conditions are present: 1) Limitation of scope by mngt → not able to obtain SAAE </td></tr> </table>	Withdraw:	Shall withdraw from Engmnt if following conditions are present: 1) Limitation of scope by mngt → not able to obtain SAAE		
Withdraw:	Shall withdraw from Engmnt if following conditions are present: 1) Limitation of scope by mngt → not able to obtain SAAE				



		2) Effect of misstatement is Material & pervasive 3) Withdrawal possible under applicable law or regulation
	Qualify:	<i>Language of "Qualified opinion" is discussed above</i>
	Disclaimer:	a) Due to the significance of the matter(s) described in the Basis for Disclaimer of Conclusion paragraph, the practitioner is unable to obtain SAAE to form a conclusion on the FS; & b) Accordingly, the practitioner does not express a conclusion on FS.

Include the reason(s) for the inability to obtain SAAE

➤ The Practitioner's Report (Element's)

Q10. Discuss the elements of the practitioner's report for the Historical FS review engagement? **[OLD]**

As per SRE 2400 → The practitioner's report for the review engmnt shall be in writing, & shall contain:

Trick: "TAI M SPD C ME DSP"

- a) **Title:** which shall clearly indicate that it is the report of independent practitioner for review engagement;
- b) **The Addressee(s),** as required by the circumstances of the engagement
- c) **Introductory paragraph** that:
 - (i) Identifies the financial statements reviewed, including identification of the title of each of the statements contained in the set of FS and the date and period covered by each FS;
 - (ii) Refers to the summary of significant accounting policies and other explanatory information; and
 - (iii) States that the financial statements have been reviewed;
- d) **Mngt Responsibility:** A description of the responsibility of management for the preparation of the financial statements, including an explanation that management is responsible for:
 - (i) Their preparation in accordance with the applicable financial reporting framework including, where relevant, their fair presentation;
 - (ii) 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) **Special Purpose FS:** If the financial statements are special purpose financial statements:
 - (i) A description of the purpose for which the FS are prepared and, if necessary, the intended users, or reference to a note in the special purpose FS that contains that information; and
 - (ii) 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) **Practitioner Responsibility:** 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) **Description of a review of financial statements** and its limitations, and the following statements:
 - (i) A review engagement under this SRE is a limited assurance engagement;
 - (ii) 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
 - (iii) 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) **Conclusion:** A paragraph under the heading "Conclusion" that contains:
 - (i) The practitioner's conclusion on the FS as a whole in accordance with this SRS, as appropriate; and
 - (ii) A reference to the applicable financial reporting framework used to prepare the FS.



- i) **Modified:** 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 in accordance with this SRS, as appropriate; and
 - 2) A paragraph, under an appropriate heading, that provides a **description of the matter(s) giving rise to the modification**;
- j) **Ethical Requirements:** A reference to the practitioner's obligation under this SRE to comply with relevant ethical requirements;
- k) The **Date** of the practitioner's report, Shall **Not report date earlier than obtained SAAE** for basis of conclusion on FS, including being satisfied that: -
- 1) All the statements that comprise the FS under the applicable FRF, 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 FS
- l) The practitioner's **Signature**; and
- m) The **Place** of signature.

Q11. What is significance of "date of report" in a review report?

Hint: Refer above "**K**" **Point** in - **Elements** of Above Practitioner's report, Further explain that "Subsequent even responsibility " *[Note: Above Qn answer is Missed by ICAI in SM ...So this is As per Author]*

Q12. Practitioner's report of review engagement in form of "**conclusion**" also contains a **description of a review of FS & its limitations**. Which statements included in practitioner's report for this (SRE 2400) (MTP'24)

Hint: refer above "**Point G**" of practitioner reports element

EOM / OM Para:	<table> <tr> <td data-bbox="349 959 479 1165">EOM:</td><td data-bbox="479 959 1513 1165">Practitioner may consider it necessary to <u>draw users' attention</u> to a matter <u>presented or disclosed in the FS</u> that, in the <u>practitioner's judgment</u>, is of such <u>importance</u> that it is <u>fundamental to users' understanding</u> of the FS → can give EOM → Provided that → SAAE obtained that No MMS exist in F.S (Location: Just after practitioner's conclusion on FS)</td></tr> <tr> <td data-bbox="349 1165 479 1207">OM:</td><td data-bbox="479 1165 1513 1207">Other than those that are presented or disclosed in the FS that</td></tr> </table>	EOM:	Practitioner may consider it necessary to <u>draw users' attention</u> to a matter <u>presented or disclosed in the FS</u> that, in the <u>practitioner's judgment</u> , is of such <u>importance</u> that it is <u>fundamental to users' understanding</u> of the FS → can give EOM → Provided that → SAAE obtained that No MMS exist in F.S (Location: Just after practitioner's conclusion on FS)	OM:	Other than those that are presented or disclosed in the FS that
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OM:	Other than those that are presented or disclosed in the FS that				
Other Reporting responsibility:	Practitioner may be requested to address other reporting responsibilities → in addition to the practitioner's responsibilities under this SRE → Add in Separate Section "Report on Other Legal & Regulatory Requirements" (Just after report headed "Report on FS")				

➤ Procedure for the Review of F.S.

Q13. to review system & the info generated from the FS. Discuss **procedures** performed by you as company auditor for review of FSs. (Old)

As per SRE 2400 "Engagements to Review FS", procedures for the review of FS will ordinarily ,

In obtaining SAAE as the basis for a conclusion on the FS as a whole, the practitioner shall design and perform inquiry and Analytical procedure:

- a) To address **all material items** in the FS, including disclosures; and
- b) To focus on addressing **areas in the FS where MM are likely** to arise.

The practitioner's inquiries of mgt and others within the entity, as appropriate, shall include the following:

Trick : SA 240, 250 → 520, 540, 550, 560, 570(2) → IND AS 37 & 115 → baaki jo bacha wo Unusual

- a) The existence of any actual, suspected or alleged:
 - (i) **Fraud or illegal acts** affecting the entity; and **(SA 240)**
 - (ii) **Non-compliance with provisions of L&R** that are generally recognized to have a direct effect on the determination of material amounts and disclosures in the FS, such as tax and pension L&R; **(SA 250)**



- b) In designing **Analytical procedure**, the practitioner shall consider whether the data from the entity's accounting system and accounting records are adequate for the purpose of performing the AP. (SA 520)
- c) How mgt makes the **significant accounting estimates** required under the applicable FRF; (SA 540)
- d) The identification of **related parties and RPT**, including the purpose of those transactions; (SA 550)
- e) Whether mgt has identified and addressed **events occurring between the date of the FS and the date** of the practitioner's report that require adjustment of, or disclosure in, the FS; (SA 560)
- f) The basis for mgt's assessment of the entity's ability to continue as a **going concern**; (SA 570)
- g) Whether there are **events or conditions that appear to cast doubt** on entity's ability to continue as a Going Concern (SA 570)
- h) **Material commitments, contractual obligations** or contingencies that have affected or may affect the entity's FS, including disclosures; and (IND AS 37)
- i) **Material non-monetary transactions** or transactions for no consideration in the financial reporting period under consideration. (IND AS 115)
- j) Whether there are **significant, unusual or complex transactions**, events or matters that have affected or may affect the entity's FS, including: (UNUSUAL)

[Trick: "Contract" me enter hoe "RPT" ke saath > "Business" kara fir uski "JV" pass kari "Year end" pe]

- (i) Significant **changes to the terms of contracts** that materially affect the entity's FS, including terms of finance and debt contracts or covenants;
- (ii) Effects or possible implications for the entity of transactions or relationships with related parties;
- (iii) Significant **changes in the entity's business** activities or operations;
- (iv) Significant **journal entries** or other adjustments to the FS;
- (v) Significant **transactions occurring or recognized near the end** of the reporting period;
- (vi) The **status of any uncorrected misstatements** identified during **previous engagements**; and

SRE 2410: Review of Interim Financial Information Performed by the Independent Auditor of the Entity

Interim financial Information (IFI)	Financial information: - prepared & presented as per applicable FRF - comprising either of Complete or condensed set of FS - for period shorter than entity's FY (Eg. Qtr)
Scope:	When auditor undertakes an engmnt to review interim financial Info (IFI) of audit client (i.e., Undertaken by Main Independent auditor of FS)
Objective:	- Express a conclusion whether, on the basis of review, anything has come to auditor's attention that <u>causes auditor to believe that the IFI is NOT prepared, in all material respects</u> as per applicable FRF [In contrast to Audit, do not provide basis for expressing an opinion that FS is T&F, & not designed to obtain reasonable assurance that IFI is free from MMS] - The auditor makes inquiries & performs analytical and other review procedures in order to <u>reduce to a moderate level the risk</u> of expressing an inappropriate conclusion when the IFI is materially misstated
Agreeing the terms of engagement:	The auditor & client should agree on the terms of engagement . The agreed terms of the engagement are ordinarily recorded in an engagement letter . → Nature of engagement and, in particular, → objective and scope of the review, → mngt's responsibilities, → extent of the auditor's responsibilities, → assurance obtained, and → nature and form of the report..



Procedure for Review:

Understanding Entity & its Environment (Inc. IC):

["Docs" padho → jese "FS" → uss hisaab se "Materiality" decide karo → fir "Risky" & "MMS" are pe "Audit procedure" lagao then "Inquiry of mngt"]

(Special Trick :-)

- Auditor should have an understanding of the entity and its environment, including its internal control → relates to the preparation of both annual and interim FI, sufficient to plan and conduct the engagement so as to be able to:
 - a) **Identify types of potential MM** and consider the likelihood of their occurrence, OR
 - b) Select the **inquiries, analytical and & review** procedures
- **Even if Main auditor has obtained understanding of entity & I.C. in AUDIT, then also he should obtain understanding again**, including I.C. → as I.C. for preparation of Annual FS may differ from I.C for preparation of Interim F.I

Q14. Auditor of a listed company required quarterly review of FS for regulatory requirement. Discuss 5 procedures, to update his understanding of company for carrying Qtr review.

Procedure performed by auditor to Understand Entity, Environment & IC:

- **Read documentation**, to extent necessary, of Preceding year's audit & reviews of prior interim period (s) of current year & corresponding interim period(s) of prior year, to enable Auditor to identify matters that may affect current-period IFI
- Read **most recent annual** & comparable prior period **IFI**.
- Consider **materiality** with reference to applicable FRF as it relates to IFI to assist in determining NTE of procedures to be performed and evaluating effect of misstatements.
- Consider **significant risks**, including Risk of mgt override of controls identified in audit of prior yr's FS.
- Consider Nature of **corrected MM & identified uncorrected** immaterial misstatements in prior year's FS.
- Consider significant **financial accounting & reporting matters** of significance like material weaknesses in Internal Control
- Consider **results of Audit procedures** performed for current year's FS.
- Consider **results of Internal audit performed** & subsequent actions taken by mgt
- **Inquiring of mgt** about: -
 - ✓ Results of mgt assessment of Risk that IFI may be MMS due to fraud.
 - ✓ Effect of changes in the entity's business activities.
 - ✓ Significant changes in IC & potential effect of such changes on preparation of IFI
 - ✓ Process by which IFI prepared & reliability of A/c records to which IFI reconciled.

A Recently Independent Auditor, Who has Not yet performed the Audit of FS → Doing IFI review → should obtain an understanding of the entity and its environment, including I.C

Inquiries, Analytical and Other Review Procedures:

[Reading & understanding only]

ICAI has given answer in Para

- Review NOT require tests of a/cing record through inspection, observation or confirmation
- Inquiry From → primarily of persons responsible for financial and accounting matters & applying analytical and other review procedures
- Inquire Before or Simultaneous → auditor may perform many of the review procedures before or simultaneously with entity's preparation of IFI
- FS Auditor is same as IFI auditor → For convenience and efficiency, auditor may decide to perform certain audit procedures concurrently with the review of IFI.
- Inquiry about Litigation & Claim → Ordinarily not require to corroborating inquiries for litigation & claim (inquiry letter to lawyer etc.) → However, if a matter comes to auditor's attention cause to believe whether IFI is not prepared, in all material respects & auditor believes entity's lawyer may have pertinent information.
- Subsequent Events → Inquire whether mgt has identified all events up to the date of the review report that may require adjustment to or disclosure in the IFI.



- Subsequent Event (After Date of Review report) → It is **not necessary** for auditor to perform other procedures to identify events occurring after the date of review report
- If Matter require material adjustment in IFI → when any material adjustment require in IFI to prepared it as per FRF → auditor should **make additional inquiries** or **perform other procedures** to enable auditor to express a conclusion in the review report.
- Going Concern → Inquire **whether mgt has changed its assessment of the entity's ability** to continue as a **going concern**

As a result of inquiry → aware of events or conditions that may cast significant doubt →

Auditor should:

- ✓ **Inquire of management as to its plans for future** actions based on its going concern assessment, the **feasibility** of these plans, &
- ✓ **Consider adequacy of disclosure** about such matters in the interim financial info.

[However, it is **not ordinarily necessary for auditor** to corroborate the feasibility of management's plans and whether the outcome of these plans will improve the situation]

Auditor may obtain evidence that **IFI agrees or reconciles with the underlying accounting records by**, tracing IFI to:

- The **accounting records**, such as the general ledger, or a consolidating schedule that agrees or reconciles with the accounting records; and
- Other **supporting data in entity's records** as necessary.

Q15. issued a **review report dated 28.7.2022** for financial results of a company for **Qtr ending 30.6.2022**.

Describe his responsibility, for events occurring from 1.7.2022 till date of review report (SRE 2410).

Answer: 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. (*Answer Ends*)

Accompanying Information	Auditor should read the other information that accompanies the IFI to consider whether any such information is materially inconsistent with the IFI → Discuss matter with Mngt ➤ If IFI Needs Amendment → Mngt refuse → Considers implications for review report ➤ If Other Info needs amendment → Mngt Refuse: • Include in Review report → <u>additional paragraph describing material inconsistency</u>, Or • <u>withholding issuance review report</u>, Or, • <u>withdrawing</u> from engagement ➤ If other info which is Not presented in IFI (But have MMS i.e., incorrectly stated or present) → Amendment necessary → mngt refuse → action → Notify TCWG & obtain legal advice
Evaluation of Misstatement:	Evaluate whether individually or aggregate → uncorrected misstatement → are material to IFI Misstatement (including inadequate disclosures) → whether material adjustment is required to be made in IFI Auditor exercises professional judgment in evaluating the materiality of any misstatements that the entity has not corrected.
Communication:	• Matter comes to the auditor's attention that causes the auditor to believe that it is necessary to make a material adjustment to the IFI → communicate this matter as soon as practicable to the appropriate level of mgt. • Mngt not respond within reasonable period → Inform TCWG • either orally or in writing → affected by factors such as the nature, sensitivity and significance of the matter → But must document the Communication ➤ TCWG do NOT respond appropriately within a reasonable period of time: • Whether to modify the report; or

- possibility of **withdrawing** &
 - Possibility of **resigning** from the appointment to **audit the annual FS**.
- **If any fraud or non-compliance of L&R identified** → communicate → matter as soon as practicable to the appropriate level of mgt
 - Auditor should communicate relevant matters of governance interest arising from the review of interim financial information with those charged with governance
 - **As a result of IFI review, auditor may become aware of matters that in opinion of auditor are both important & relevant to TCWG** in overseeing the FR & disclosure process. The auditor **communicates such matters to TCWG**.

Q16. CA. Seerat is conducting **review of Qtr financial info** (she is also auditor). She believes that it is **necessary to make a material adjustment** to quarterly financial info. **She has communicated the matter to CFO and audit committee, no response was received.** What are the options available to her?

Hint: [Refer above "communication" - TCWG not respond : **Modify, withdrawing, Resign annual FS**] (answer ends)

Departure from the FRF:	Management does not correct the IFI → express a Qualified or Adverse conclusion → Modification describes the nature of departure → if practicable Effect on IFI → if No adequate disclosure → if practicable includes, necessary information in review report → Modify report by adding an Explanatory Paragraph
Going concern uncertainty exist:	Q17. Case study related to Going Concern reporting → covered in Question Bank (May'24) • If matter is adequately disclosed → EOM para (Not SA 570 Para) • If not adequately disclosed → Qualified or adverse [If Prior Audit/Review report have EOM pare w.r.t material uncertainty → and it's still exist → and Adequate Disclosure is made in Current IFI → adding a paragraph to highlight continued material uncertainty. i.e., modifies the review report on the current IFI by adding a para to highlight the continued material uncertainty]

Q18. **review of quarterly results** (of which you are auditor), → **major fire in fabric processing plant** of company during the quarter. machinery & inventories of plant **were uninsured** → leading to **substantial losses**. matter is **disclosed in interim FI appropriately**. Discuss, how you proceed to deal with the same in review report?

Hint: Its an example of **events or conditions** → may cast **significant doubt about the G.C assumption**.

SRE 2410, if, as a result of inquiries or other review procedures, a MU relating to an event or condition comes to the auditor's attention that →, & **adequate disclosure** → the auditor modifies review report by adding an EOM.

Therefore, **EOM paragraph** should be added in review report. (answer Ends)

Limitation on Scope:	Auditor is unable to complete the review → communicate, in writing , → appropriate level of mgt and to TCWG → reason why the review cannot be completed
Limitation imposed by Mngt:	• Not accept an engagement (preliminary knowledge of limitation on scope) • If, after accepting the engagement → Request mngt for removal → if mngt refuse → communicate TCWG (in writing, Why review can-not completed) [Communicate such matter also, which require IFI material adjustment] • If L&R require to continue → Disclaim the opinion (reason why the review cannot be completed)
Other Limitation:	Rare circumstances, • If Material & Not pervasive → Qualify report
Annual FS:	If there is Qualified Opinion on Annual FS → <u>because of limitation on scope of</u>

		audit → <u>considers whether that limitation on scope still exists</u> and, if so, the <u>implications for review report</u> .
Document Containing IFI	➤ Terms of agreement shall include → where any document containing IFI indicates that such information has been reviewed by the entity's auditor → Review report shall also be included in the document ➤ If report not included by mngt → seek legal advice determining appropriate course of action (possibility of resigning from appointment to audit the annual FS.) ➤ If IFI Consist of "condensed set of FS" (i.e., not necessarily include all info that included in complete set of FS):	
	In case of Listed Co.	Presumed that users of IFI will have access to the latest audited financial statements
	Other Case:	• Auditor discusses with Mngt → to include statement → that IFI is to be read in conjunction with the latest audited FS. • In Absence of such Statement → auditor may consider that whether IFI may be misleading & Implication for review report

CHAPTER 11 - Prospective Financial Info. & Other Assurance services

SAE 3400, 3402, 3420

Standards on Assurance Engagements (SAE): Relates to examination of **Prospective financial information OR, Non-Financial Matters** (i.e., Design & Operation of Control) [**Moderate Assurance**]:

SAE 3400	The Examination of Prospective Financial Information
SAE 3402	Assurance Reports on Controls at a Service Organisation
SAE 3420	Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus

SAE 3400 - The Examination of Prospective Financial Information

Scope:	• Not necessarily be performed by statutory auditor of entity's FS • Examine & report on prospective FI including examination procedures for best-estimate and hypothetical assumptions • Not Apply: Examination of prospective F.I expressed in general or narrative terms. (Eg. management's discussion and analysis in an entity's annual report) • Follow Other SA's: to the extent practicable
Prospective Financial Information (PFI)	➢ <u>Financial Information based on:</u> • Assumptions about events that may occur in the future & • Possible actions by an entity. ➢ It is highly subjective in nature and its preparation requires the exercise of considerable judgment. <u>Prospective financial information can be in the form of :</u> • a forecast, • a projection, • or a combination of both (for example a 1-year, forecast plus a 5-year, projection.)

Forecast: [5% trend of inc. in sales]	Projection: [Hypothetical situation: Eg., Assuming Govt abolish Customs]
PFI prepared on basis of: • Assumptions as to future events which mgt expects to take place as of the date on information is prepared & • actions mngt expects to take (Best-estimate assumptions i.e., Based on Past Experience, No provision for risk in case of deviation)	PFI prepared on the basis of: • Hypothetical assumptions about future events and mgt actions which are NOT necessarily expected to take place, such as when some entities are in a start-up phase <u>or</u> are considering a major change in the nature of operations; or • A mixture of best-estimate and hypothetical assumptions
Eg. In present market conditions, the CFO of X Ltd. expects sales to Inc. by 5% over the next quarter. Therefore, a 5% sales increase is his financial forecast for the period	Eg. X Ltd. may project a course of action to take when one or more hypothetical situations arise, such as creating a new product → assuming the possibility of different events, financial projections serve as an outline for evaluating the desired outcomes X Ltd. expects to see, including its financial, cash flow and operational outcomes.

Nature of Assurance:	Events & actions that have not yet occurred and might not occur, evidence to support assumption are also future oriented (Speculative in nature) → Therefore, an opinion as to whether the



	results shown in the prospective FI will be achieved → cannot be expressed
Mngt Responsibility: [SAB - P]	- including the identification and disclosure of the Sources of information, - the underlying Assumptions. - the Basis of Forecasts and - Preparation and presentation of the PFI,
Q1. SAE 3400: differentiate a forecast from projection? and example. + explain nature of assurance provided Hint: Refer above "Forecast", "Projection" & "Nature of assurance"	
Can Accountant Associate with PFI? [SAB Vouch Nahi kar sake] (Special Trick :-)	Q2. Discuss, how, a Chartered Accountant can be associated with prospective financial information without violating relevant provisions of the Chartered Accountants Act, 1949. Attest function performed by a Chartered Accountant → varied stakeholders like banks, Investors → intend to place greater reliance on reports of Projected C.F / P&L signed by CA Clause 3 of S-2 (CA Act 1949): CA in practice shall be deemed to be guilty of professional misconduct, if he permits his name or the name of his firm to be used in connection with an estimate of earnings contingent upon future transactions in a manner which may lead to belief that he vouches for the accuracy of forecast. Above clause does not preclude a CA from associating his name with prospective FS → He Can participate in preparation of financial forecasts & can review them, provided he indicates clearly in his report the - Sources of information, - Basis of forecasts and also - Major Assumptions made in arriving at the forecasts and So long as he does not vouch for the accuracy of the forecasts. The same also applies to projections made on the basis of hypothetical assumptions
Auditor's Duty:	The auditor may be asked to examine and report on the PFI to enhance its credibility, whether it is intended for use by third parties or for internal purposes Obtain SAAE: - PFI prepared on the basis of the assumptions - Mgt's best-estimate assumptions → Not unreasonable In case of hypothetical assumptions → assumptions consistent with purpose of info. - Properly presented & all material assumptions are adequately disclosed → including whether they are best-estimate assumptions or hypothetical - PFI is prepared on a consistent basis with historical FS (appropriate a/cing policies) [Principles laid down in other SAs should be applied to the extent practicable.] [Author's note: Auditor not in position to express opinion that whether result shown in PFI achieve He can only provide moderate assurance (Negative assurance i.e., Low Level of assurance, Not anything come to attention)]
Acceptance of Engagement:	Q3. examine the projected FS & give report included in Prospectus. What things you will consider before accepting audit Enmngt ?, what steps to formalize the terms of engmnt? Projected Financial Statements: As per SAE 3400, "The Examination of PF Information" Acceptance of Engagement: As per SAE 3400, →, before accepting an engagement to examine prospective financial information, the auditor would consider, amongst other things: [Trick: ye konsa "Saal" ka h orr "isme Kya hai" ? > ye Sabke "Use" Aaega ya "Limited" logo ke hi sirf ? > "assumption" bhi dikhaao iske]



(Special Trick :-)	(1) The period covered by the information. (2) The elements to be included in the information; [i.e., Asset, Liability, all, etc.] and (3) The intended use of the information; (4) Whether the information will be for general or limited distribution; (5) The nature of the assumptions, that is, whether they are best-estimates or hypothetical assumptions; Further, the auditor should not accept, or should withdraw from, an engagement when the assumptions are clearly unrealistic or when the auditor believes that the prospective financial information will be inappropriate for its intended use To formalize the terms of the engagement, it is essential to agree on the terms with the client by sending an engagement letter, like in other engagements. (SA 210)						
Examination Procedure: (Special Trick :-)	Q4. examine & report on prospective FI (mngt prepared for presentation at an Investor) <u>matters to consider in determining the NTE of procedure to be applied in review (SM)</u> NTE of examination procedures, the auditor should consider matters such as: <i>Trick: Muje dkhna hai ki jo Assumption leke PFI banaya h > Wo assumption sahi h ya nhi > "Meri Khood ki Knowledge & Experience" se dkhunga > "Mngt" ko bhi dkhunga > ki Kis "Source" se Info uthaai > kahi "MMS" to nhi h n Info me</i> a) the knowledge obtained during any previous engagements; b) the engagement team's experience with the business and the industry in which the entity operates and with reporting on PFI c) mgt's competence regarding the preparation of PFI; d) the extent to which the PFI is affected by the mgt's judgment; e) the sources of information considered by the mgt 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 likelihood of MM; g) the stability of entity's business; and <table border="1" data-bbox="318 1209 1529 1507"> <tr> <th colspan="2">For Source of Reliability & Evidence Supporting Mngt:</th></tr> <tr> <td>Best estimate assumptions</td><td>For Best estimate assumption supporting → evidence to obtain → Such Evidence available from varied sources like entity's budgets, debt agreements, etc.</td></tr> <tr> <td>Hypothetical assumptions</td><td>Consider whether all significant implications of such assumptions should have been taken into consideration (eg. If FPI shows Sales grows beyond current plant capacity → check whether in PFI additional cost for plant capacity is taken)</td></tr> </table>	For Source of Reliability & Evidence Supporting Mngt:		Best estimate assumptions	For Best estimate assumption supporting → evidence to obtain → Such Evidence available from varied sources like entity's budgets, debt agreements, etc.	Hypothetical assumptions	Consider whether all significant implications of such assumptions should have been taken into consideration (eg. If FPI shows Sales grows beyond current plant capacity → check whether in PFI additional cost for plant capacity is taken)
For Source of Reliability & Evidence Supporting Mngt:							
Best estimate assumptions	For Best estimate assumption supporting → evidence to obtain → Such Evidence available from varied sources like entity's budgets, debt agreements, etc.						
Hypothetical assumptions	Consider whether all significant implications of such assumptions should have been taken into consideration (eg. If FPI shows Sales grows beyond current plant capacity → check whether in PFI additional cost for plant capacity is taken)						
Presentation & Disclosure: <i>["Info". About "A/cing Policy" > "Assumption" ki "range" & "date"]</i>	Q5. What things you will you consider in assessing the <u>Presentation & Disclosure of Prospective Financial Information</u> & underlying assumption? [OLD & Nov'24] When assessing P&D in PFI & underlying assumption → in addition to specific requirements of any relevant statutes, regulations, it needs to be considered whether: a) The presentation of prospective FI is informative and not misleading b) The accounting policies are clearly disclosed in the notes to the prospective FI; c) If there is any change in the accounting policy of the entity from that disclosed in the most recent historical FS, whether reason for the change and the effect of such change on the prospective financial information has been adequately disclosed. d) Assumptions are adequately disclosed in the notes to the prospective FI. It needs to be clear whether assumptions represent mngt's best-estimates or are hypothetical &, when						



	assumptions are made in areas that are material & are subject to a high degree of uncertainty, this uncertainty & resulting sensitivity of results needs to be adequately disclosed [i.e., Outcome if assumption failed] e) The date as of which the prospective FI 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 f) The basis of establishing points in a range is clearly indicated & the range is not selected in a biased or misleading manner when results shown in the prospective FI are expressed in terms of a range

➤ Reporting

Elements of Report:	Report by an auditor on an examination of PFI should contain the following: - Title; - Addressee; - Identification of the PFI; - Reference to the SAs applicable to the examination of PFI; - Statement that mgt is responsible for the PFI including the underlying assumptions - When applicable, a reference to the purpose and/or restricted distribution of PFI; - 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 - Statement of negative assurance as to whether the assumptions provide a reasonable basis for the PFI - Opinion as to whether the PFI is properly prepared on the basis of the assumptions and is presented in accordance with the relevant FRF; - Appropriate caveats concerning the achievability of the results indicated by the PFI; - Date of report (which should be the date procedures have been completed); - Place of signature; and - Signature.
Reporting:	- State whether, based on the examination of the evidence supporting the assumptions, anything has come to the auditor's attention, which causes the auditor to believe that the assumptions do not provide a reasonable basis for the PFI. - Express an opinion as to whether the PFI is properly prepared on the basis of the assumptions and is presented in accordance with the relevant FRF. - Presentation and disclosure of the PFI not adequate → Qualified or adverse or withdraw - Assumptions do not provide a reasonable basis for the PFI → Adverse opinion or withdraw - Scope limitation → Disclaim or withdraw - State in Report that: ✓ Actual results are likely to be different from the PFI since anticipated events frequently do not occur as expected and the variation could be material, so can be no assurance that actual results will fall within the range ✓ In the case of a projection, the PFI has been prepared for (intended use), using a set of assumptions that include hypothetical assumptions about future events or necessarily expected to occur, Readers are cautioned that the PFI should not be used for purposes other than the abovementioned intended use.

Q6. for an assurance report i.r.o prospective FI → it is noticed that depreciation reflected on proposed fixed assets to be acquired has been calculated as per Income Tax Act. No disclosure is made in this respect too.
Hint: → It's duty of a professional accountant to see that prospective FI is based on a consistent basis with historical FS using appropriate accounting principles.



For company → **historical FS** are prepared as per Companies Act, So, depreciation as per I.T Act → **not proper**.

The fact that the projection has Not been prepared on a consistent basis with the historical FS, using appropriate accounting principles **needs to be stated**.

Further, when **presentation and disclosure are not adequate**, a **qualified or adverse opinion**.

SAE 3402 - Assurance Reports on Controls at a Service Organisation

Scope & Applicability:	Deals with assurance engagement undertaken by a member of ICAI to provide a report on controls at a service organization (SO) for use by user entities (UE) & their auditors. It complements SA 402 SAE 3402 APPLICABLE only when the → SO is responsible for to make an assertion about, the suitable DESIGN of controls. It does NOT APPLICABLE with assurance engagements: - To report ONLY on whether controls at a S.O operated as described, Or, (But applicable, if require testing of Both → Suitable Design + Operating effectiveness) - To report only on controls at a SO other than those related to a service that is likely to be relevant to user entities' internal control as it relates to financial reporting (for example, controls that affect user entities' production or quality control).
What is S.O:	3 rd 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 .
Controls at the S.O:	Controls at the service organization which are relevant to user entities (matter of professional judgment) → include aspects of a service organization's control environment, monitoring, and control activities when they relate to the services provided → However NOT include controls at a S.O that are not related to the achievement of the control objectives stated in the S.O description of its system, for example, controls related to preparation of the service organization's own FS.
Objective:	To obtain reasonable assurance w.r.t. description of its system fairly present S.O controls, designed suitably to achieve objective and operating effectiveness (DDO) of controls established in the service organization, Control Objectives are achieved & to report matters with the service auditor's findings.

➤ How such an Engagement is Proceeded with?

Comply Ethical Requirements:	Service auditor shall comply with relevant ethical requirements, including independence , relating to assurance engagements
Determine mngt & TCWG & communication:	The service auditor shall inquire of, request representations, communicate with, or otherwise interact with S.O wherever required. → So, shall determine the appropriate persons within the service organization's management or governance structure with whom to interact
Acceptance & Continuance:	Before agreeing to accept, or continue, an engagement the service auditor shall: A) Determine whether: - SO's Auditor have capabilities and competence to perform the engagement Criteria to be applied by the SO to prepare system description suitable & will be available to UE & their auditor scope of the engagement will not be so limited (which unlikely to be useful to UE) B) Obtain the agreement of the SO that it acknowledges & understands responsibility: - For the preparation of the description of its system, Including assertion (completeness, accuracy & Presentation of system) - have a reasonable basis for SO's assertion, accompanying description of its system



	• stating in SO's assertion the criteria it used to prepare the description of system • For stating in the description of its system: ✓ The control objectives ✓ Where they are specified by L&R, or another party → party who specified them; (Eg. user group or a professional body) ✓ identifying the risks that threaten achievement of the control objective • To <u>provide the service auditor with</u>: ✓ Access to all information, such as records, documentation and other matters, including service level agreements ✓ Additional information that the service auditor may request ✓ Unrestricted access to persons
Change in the Terms	If the SO requests a change in the scope of engagement before completion of engagement, → SO Auditor shall be satisfied that there is reasonable justification for the change
Assessing the Suitability of the Criteria:	Criteria → Benchmarks used to evaluate or measure a subject matter including, where relevant, benchmarks for presentation and disclosure (It's like FRF in FS Audit) <u>Criterial shall be</u> : • Suitable available to user entities & User auditor Also (MCQ) Service auditor shall assess whether the SO has used suitable criteria in preparing the Description of its system, in evaluating Design & for Type 2 Operating effectiveness also (DDO)
Materiality:	Service auditor shall consider materiality w.r.t. fair presentation of the description, Design & for type 2 operating effectiveness also etc.
Understanding of SO System:	Service Auditor shall obtain an understanding of the service organization's system, including controls that are included in the scope of engagement.
<u>Obtaining evidence</u> for 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 .
<u>Obtaining evidence</u> for Design :	The service auditor shall determine which of the controls at the S.O 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 .
<u>Obtaining Evidence</u> Regarding Operating Effectiveness of Controls	When providing a type 2 report, the service auditor shall test those controls determined as necessary to achieve the control objectives and assess their operating effectiveness throughout the period: ➤ Perform other procedures in combination with inquiry to obtain evidence about: • How the control was applied • The consistency with which the control was applied; and • By whom or by what means the control was applied ➤ Determine whether controls to be tested depend upon other controls (indirect controls), is so, whether evidence require for Other Controls also.
Understanding IAF:	If the S.O has an IAF, 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.
W.R:	Asking for Written Representations from S.O [Refer "Additional PDF booklet"]
Subsequent Events:	Service auditor shall inquire whether the SO is aware of any events subsequent to the period covered by the SO's could have a significant effect on the service auditor's assurance report → shall disclose it in the service auditor's assurance report .

Read Other information:

Included in a document containing the SO's description → Any inconsistency → Discuss matter with SO → If refuse to correct → Take appropriate action

➤ **Reporting [Content/Element of Report]**

Q7. How does auditor report on Description, Design & Operating effectiveness of controls at S.O? [OLD]

Trick: TAD - CU - Mngt Responsb. > Auditor Reponsb. Hai ki > SAE 3402 ke hisaab se Procedure lagaae > par Limitation to unki bhi hogi, > Usse dhyaan me Rakh ke Opinion de > DSP

- 1) **Title:** A title that clearly indicates the report is an independent service auditor's assurance report
- 2) **Addressee.**
- 3) Identification of:
 - a) The SO's Description of its system, and the SO's assertion, which includes the matters described in the definitions of type 1 report and type 2 report.
 - b) Those parts of SO's description of system, if any, that are not covered by service auditor's opinion.
 - c) 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, and that the control objectives stated in the SO's description of its system can be achieved only if complementary user entity controls are suitably designed or operating effectively, along with the controls at the SO.
 - d) If services are performed by a Sub service organisation (SSO), the nature of activities performed by the SSO as described in the SO's description of its system and whether the inclusive method or the carve-out method has been used in relation to them.
- 4) Identification of the Criteria, and the party specifying the control objectives
- 5) In case of Type2 report, For Description of TOC → A statement that the (USE) report is intended only for User Entity (UE) and their auditors, who have a sufficient understanding to consider it, along with other information including information about controls operated by UE themselves, when assessing the ROMM of user entities' FS
- 6) A statement that the SO is responsible for (i.e. Service Organisation responsibility):
 - a) Preparing the description of its system, and the accompanying assertion, including the completeness, accuracy and method of presentation of that description and that assertion;
 - b) Providing the services covered by the SO's description of its system;
 - c) Stating the control objectives (where not identified by L&R, or another party, for example, a user group or a professional body); and
 - d) Designing and implementing controls to achieve the control objectives stated in the SO's description of its system.
- 7) A statement that the service auditor's responsibility is to express an opinion on the SO's description, on the design of controls related to the control objectives stated in that description and, in the case of a type 2 report, on the operating effectiveness of those controls.
- 8) A statement that the engagement was performed in accordance with SAE 3402, which requires that the service auditor comply with ethical requirements and plan and perform procedures to obtain reasonable assurance about whether, in all material respects, the SO's description of its system is fairly presented and the controls are suitably designed and, in the case of a type 2 report, are operating effectively.
- 9) A summary of the service auditor's procedures to obtain reasonable assurance and a statement of the service auditor's belief that the evidence obtained is SAAE to provide a basis for service auditor's opinion, and, in the case of a type 1 report, a statement that service auditor has not performed any procedures regarding the operating effectiveness of controls and therefore no opinion is expressed thereon.
- 10) A statement of the limitations of controls and, in the case of a type 2 report, of the risk of projecting to future periods any evaluation of the operating effectiveness of controls.
- 11) The service auditor's opinion, expressed in the positive form, on whether, in all material respects, based on suitable criteria:



In the case of a type 2 report: **(DDO)**

- (i) **Description fairly presents the SO's system** that had been designed and implemented throughout the specified period;
- (ii) The **controls** related to the control objectives stated in the SO's description of its system were **suitably designed** throughout the **specified period**; and
- (iii) 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

[Service Auditor's assurance report that: -

- a) Conveys **reasonable assurance about the matters in (ii) &**
- b) Includes a **description of the TOC and the results thereof.**]

In the case of a type 1 report: **(DD)**

- (i) The **description fairly presents the SO's system** that had been designed and implemented as at the **specified date**; &
- (ii) The **controls** related to the control objectives stated in the SO's description of its system were **suitably designed** as at the specified date.

*[Service Auditor's assurance report that: Conveys **reasonable assurance about the matters in (ii)**]*

12) The **Date** of the service auditor's assurance report, which shall be no earlier than the date on which the service auditor has SAAE on which to base the opinion.

13) Practitioner's **Signature**

14) The **Place** of signature

In the case of a type 2 report, the service auditor's assurance report shall **include a separate section after the opinion**, or an attachment, that **describes the tests of controls** that were performed and the **results** of those tests.

In Describing TOC

→ **State that which Controls are tested ?**, whether all controls tested or Selected ?

→ Indicate the **nature of tests** in sufficient detail to enable user auditor's to determine the effect of such test on there risk assessment.

In Deviation Identified:

→ Include **extent of testing performed** that led to identification of deviation (including **sample size**) and **Number + Nature of deviation**

→ **Report deviation even if**, on the basis of test performed, the service auditor has concluded that related control objectives were achieved

Q8. Foor Ayurda Ltd. provides cloud-based professional services automation software solutions. They want to engage you to **provide an assurance report for its clients over the controls it operates as a S.O.** Can you provide such an assurance report?

Hint: Yes, Assurance report can be provided under SAE 3402 → **[Refer Above Content of Report : Including TYPE 1 & TYPE 2 Report]** → **[Author's note: ICAI has not given clear answer of this QN, Students are suggested to briefly write about element of above report & Explain about type 1 & type 2 report .. i.e., Point 11]**

Q9. What **Opinion** do auditor require to give in **Type 2 report** ?

Hint: Refer above **point 11** of audit report content: "In the case of a type 2 report: **(DDO)**

Q10. One Easy C.S Qn → Outsourced payroll function → want to Sure about DDO of Control:

- (i) **Why that assurance report needed?** → to obtain **understanding of nature & significance** of service provided by S.O & it's effect on U.E. I.C (relevant for audit), to assess ROMM
- (ii) **On which matters opinion to be provided?** → Refer above point 11 of audit report: "In case of a type 2 report"

➤ **Modified Opinion:**

If the service auditor concludes that:

- The **SO's description** does **not fairly present, in all material respects**, the system as designed and implemented;



- The **controls** related to the control objectives stated in the description were **not suitably designed**, in all material respects;
- In the case of a **type 2 report**, the controls tested, → control objectives stated in the SO's description of its system, did **not operate effectively**, in all material respects; or
- The service auditor is **unable to obtain SAAE**, the service auditor's opinion shall be modified, and the shall contain a clear description of all the reasons for the modification.

Q11. Bansi College outsourced its process of application fees to Easy Ltd. auditors of Bansi want the **design & operating effectiveness of controls** at Easy. What should be the nature of report needed (SA 3402)
Hint: → design and operating effectiveness of controls → **Type 2 report** → It should **also include** details of **TOC performed** and **details of deviations**, if any.

SAE 3420 - Assurance Engagements to Report on the Compilation of Proforma Financial Information Included in a Prospectus

Scope:	Reasonable assurance engagements undertaken by a practitioner to report on the responsible party's (RP) compilation of proforma financial information (PFI) included in a prospectus, where: • Such reporting is required by securities L&R of the securities exchange, Or • reporting is generally accepted practice in such jurisdiction
Not applicable:	• Circumstances where Proforma financial Info → for requirements of applicable FRF. • Non-assurance engagements in which practitioner is engaged by entity to compile its historical FS. [SRS 4410]
Practitioner's Responsibility:	Practitioner has NO responsibility to compile the PFI for the entity → This responsibility rests with the RP → practitioners to report on whether the PFI has been compiled, in all material respects on the basis of the applicable criteria.
Pro Forma Financial Information:	FI shown together with adjustments to illustrate the impact of an event or transaction on Unadjusted Financial Information (PFI) → as if the event had occurred or the transaction had been undertaken at an earlier date selected for purposes of the illustration Adjustment includes the relevant FI of a business that has been, or is to be, acquired ("acquiree"), or a business that has been, or is to be, divested ("divestee"), to the extent that such information is used in compiling the PFI
Why to Include PFI in Prospectus?	to illustrate the impact of a significant event or transaction on unadjusted financial information → As if the event had occurred or the transaction had been undertaken → PFI does not represent the entity's actual financial position , financial performance. to illustrate how the transactions might have affected the assets, liabilities and earnings of the Issuer. (also include notes in relation to the significant aspects of the transactions, assumptions)
Criteria:	Criteria used by the RP when compiling the PFI (Criteria may be established by an authorized or recognized standard-setting organization or by L&R)
Steps for Compilation of PFI	Involves responsible party gathering, classifying, summarizing & presenting FI that illustrates impact of a significant event or transaction on unadjusted financial info of Entity as if event had occurred or transaction undertaken at Selected Date: • Identifying source of Unadjusted FI to be used in compiling PFI & extracting Unadjusted financial info from that source. • Making pro forma adjustments to Unadjusted financial info for which PFI is presented. • Presenting resulting PFI with accompanying disclosures



Q12. Discuss the significance of Pro forma financial information included in prospectus of a company.

Hint: Refer above "Pro Forma Financial Info" & "Why to include Proforma F.I ?"

➤ Engagement Acceptance:

Q13. Mngt requested you to accept an engagement to report on compilation of pro forma financial Info included in prospectus. SAE 3420, **What factors will you consider before agreeing to accept engagement?**

Answer:

SAE 3420: Before agreeing to accept this engagement, the practitioner shall:

Trick: me "Competent" hu and "saamne wale ne apni responsibility" maan li (7th point). → theek hai to ab "Criteria" laga ke evaluate karo and "Opinion" do > "Modified" or "Not Audited"

1. Determine that the practitioner has **Capabilities and competence** to perform the engagement;
2. Determine that the applicable **Criteria** are suitable and that it is **unlikely that the PFI will be misleading** for the purpose for which it is intended;
3. Evaluate the **Wording of the opinion** prescribed by the relevant L&R , if any, to determine that the practitioner will likely be able to express the opinion so prescribed;
4. Where the **sources from which the Unadjusted FI** and any acquiree or divestee FI **have been extracted have been audited or reviewed and a modified audit opinion** or review conclusion has been expressed, or the report contains an EOM paragraph, **consider whether or not the relevant L&R permits the use of**, or reference in the practitioner's report to, the modified audit opinion/review conclusion or the report containing EOM paragraph w.r.t. such sources;
5. **If the entity's historical FI has never been audited/reviewed**, consider **whether the practitioner can obtain a sufficient understanding of the entity and its accounting and financial reporting practices** to perform the engagement;
6. **If the event or transaction includes an acquisition** and the **acquiree's historical FI has never been audited** or reviewed, consider **whether the practitioner can obtain a sufficient understanding of the acquiree and its accounting and financial reporting practices** to perform the engagement and
7. **Obtain the agreement of the RP that it acknowledges and understands its responsibility for:**
 - (i) **Adequately disclosing and describing the applicable criteria** to intended users if these are not publicly available
 - (ii) **Compiling the PFI** on the basis of the applicable criteria; and
 - (iii) Providing the practitioner with:
 - ✓ **Access to all information** relevant to evaluating whether the PFI has been compiled, in all material respects, on the basis of the applicable criteria;
 - ✓ **Additional information** that the practitioner may request for the purpose of the engagement;
 - ✓ **Access to those** from whom the practitioner determines it necessary to obtain evidence relating to evaluating whether the PFI has been compiled, in all material respects, on the basis of the applicable criteria; and
 - ✓ When needed for purposes of the engagement, **access to appropriate individuals within the acquiree(s) in a business combination**

Q14. compilation of pro forma FI to be included in a prospectus → SAE 3420, **what factors you will consider regarding the company acknowledging & understanding its responsibility → before accepting engmnt?**

Hint: The company's responsibility has to be acknowledged for the following matters:-

Refer above (Point no 7 : "in the agreement of the RP that it **acknowledges & understands its responsibility for:** ...

➤ Planning & Performing the Engagement

Criteria:	Practitioner shall assess suitability of applicable criteria. (Exam)



Materiality	When planning and performing the engagement, the practitioner shall consider materiality
How PFI Compiled?	The practitioner shall obtain an understanding of how the responsible party has compiled the pro forma financial Information and other engagement circumstances
Source: (Exam)	- Whether RP has extracted Unadjusted FI from appropriate source If there is no audit/review report on source → perform procedures to satisfy that source is appropriate - The practitioner shall determine whether responsible party has appropriately extracted the unadjusted FI from the source.
Pro-Forma Adjustment: (Exam)	Q15. Discuss the term "Pro forma adjustment" under SAE 3420. The practitioner shall obtain evidence about the appropriateness of the pro forma adjustments. i.r.t unadjusted financial information, Pro forma adjustments include: a) Adjustments to unadjusted F.I 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 FI that are necessary for the pro forma FI to be compiled on a basis consistent with the applicable FRF of the reporting entity and its accounting policies under that framework.
Presentation:	The practitioner shall evaluate the presentation of pro forma financial information .
Other info:	The practitioner shall read the other information included in the Prospectus containing the pro forma FI to identify material inconsistencies , if any, with pro forma financial information.
Opinion:	Whether the PFI has been compiled, in all material respects as per criteria → Conclude whether SAAE obtained → PFI, Compilation & Disclosure is free from material omissions

➤ Form of Opinion

Unmodified:	PFI has been compiled, in all material respects, by the RP basis of applicable criteria.
Modified:	➤ When L&R precludes publication of a prospectus that contains a modified opinion → discuss the matter with the RP. If the RP does not agree to make necessary changes, the practitioner shall: Withdraw from the engagement; or - Consider seeking legal advice. ➤ Where L&R may not preclude publication of a prospectus that contains a modified opinion and the practitioner determines that a modified opinion is appropriate in accordance with the Framework, the practitioner shall apply the requirements in the Framework regarding modified opinions.
EOM Para:	Practitioner may consider it necessary to draw users' attention to a matter presented or disclosed in the PFI → matter is of such importance that it is fundamental to users' understanding → include an EOM (obtained SAAE that the matter does not affect whether the PFI has been compiled, in all material respects) Such a paragraph shall refer only to information presented or disclosed in the PFI or the accompanying explanatory notes



Special Weapon → Let's Compare Quickly:						
SRE 2400	SRE 2410	SAE 3400	SAE 3402	SAE 3420	SRS 4400	SRS 4410
Review Historical FS	Review of IFI	Assurance Prospective FI	Assurance Control at SO	Assurance Proforma FI in Prospectus	Agreed procedure : FI	Compilation engagement
Historical		Other than Historical Info (Moderate Assur)			Agreed Procedure	
Practitioner (not auditor)	Independent Auditor	Independent Auditor	Independent Auditor	Practitioner	Auditor (Practitioner)	Practitioner
Not main auditor of FS	Main Auditor of FS	Not necessary to be a Main auditor of FS			Not necessary to be entity main auditor of FS	
Limited Assurance	Limited Assurance	Limited assurance	Reasonable assurance	Reasonable assurance	NO Assurance	NO Assurance
Independence Require	Independence	Independence	Independence	Independence	NOT REQUIRE	NOT REQUIRE
Consider factor before accepting engagement:						
"Rational" hi kya h iss engt ka .. "Audit" hi kara lete > "Kuch info. to de ni rhe, poora "limitation scope" laga h > de bhi rahe h to "Doubt" h muje to > kyuki wo log "independent" to hai nii		ye konsa "Saal / Period" ka h orr "isme Kya hai" (Element) ? > ye Sabke "Intended Use" Aaega ya "Limited" logo ke hi sirf ? > "assumption" bhi dikhaao iske	capabilities & competence > Criteria > scope > preparation of description > reasonable basis> System description > Provide auditor with all the access to info & person	Competent > mngt reposibility > Criteria > opinion wording > opinion modified > or not audited		
Terms of Engagement						
intended use > applicable FRF > objective and scope > practitioner responsibilities > mgt responsibilities > it's not audit > form content of report	Objective of review > Scope > mngt responsibility for IFI > Mngt repson. For IC > Auditor's respon. > Form & content of report > review report includes				(IMP) • engt Nature • engt purpose • identify FI • NTE of procedure • Limitation on report use	• Intended use • applicable FRF • Objective & Scope of CE • Mngt Responsibility: (FI prepare, IC , accuracy of record) • Form & content of report
Engagement Performance:						
Inquiry,		Trick: Muje dkhna hai ki			Procedure & evidence:	• Obtain Understanding



Analytical Procedure & GROF (Going concern, Related prty, other's work, Fraud/ Non comply L&R)		jo Assumption leke PFI banaya h > Wo sahi h ya nhi > "Meri Khood ki Knowledge & Experience" se dkhunga> "Mngt" ko bhi dkhunga > ki Kis "Source" se Info uthaai > kahi "MMS" to nhi h n Info me			<u>(ICI - OR)</u> • Inquiry, • Confirmation, • Inspection, • Observation, • Recomputation	(Entity Business, Acc System / FRF) • Discuss Mngt/tcwg (significant judgmnt) • Compile the FI • Read the compile FI • If aware : record/Doc is incomplete / inaccurate → request mngt to correct • If unable to complete ,as mngt mngt fail to provide record/doc → withdraw
<u>A Separate Sheet Will be Provided for proper Comparison of above all SAE/SRE/SRS (PW) :-)</u>						

CHAPTER 12: DIGITAL AUDITING

➤ Digital Audit: (Review entity Digital assets)

Meaning:	Digital Audit is placing assurance on the effectiveness of IT systems implemented in an organization. Technology is becoming an integral part of day-to-day business operations. Organization shall review their technology-related controls to identify gaps & risks for continuous improvement and to ensure regulatory compliance → will allow organizations to build trust with their stakeholders
Key Features: (DIN-COST) <i>Costly director laae digital audit k liye...</i>	<i>[Trick: Trick: NSS se accha comprehensive review karo, Reliable decision le paaoge]</i> 1) New Technology & Confidence: Digital audit encourages the auditee to embrace the latest technological advancements and provides confidence to auditee to stay updated in a constantly evolving environment 2) Standardize process: Digital Audit allows to standardize processes and allow controls to be implemented to mitigate risk. 3) Save Time/Cost/effort: Digital Audit leads to savings in time, cost and human effort which can be utilized towards more productive tasks. Many of today's digitally enabled processes can be orchestrated to operate autonomously 24x7, driving real-time transactions 4) Comprehensive review of technology: The digital audit will help organization gain a more comprehensive overview of end-to-end processes and how technologies are utilized, controlled and optimized against standards set 5) Reliable Opinion: A digital audit improves the quality of opinion. This consequently leads to a more reliable audit report 6) Informed decisions: It can help auditee to make informed decisions. 7) Digital Strategy: The digital audit will help create a future for a digital strategy and paves way for adopting new technologies such as AI and Robotic, usage of analytics and automation
Advantages: <i>[Trick: Bhai "kam paiso" and "kam time" me me > "acchi audit" hori h .. kyuki "risk" pahle hi "Analyse" Karli thi]</i> OR (BIBLE)	1) L- Lower Costs of Audit: By automating processes that were previously done manually, technology can assist with cost of auditing. It shortens time to complete audit, Save cost. 2) E- Enhanced Effectiveness & Efficiency: Increased efficiency → With use of tools & automation techniques, auditee can standardize processes & routine tasks can be automated like automating a reconciliation process that increase efficiency & saves time & costs. 3) B- Better Audit Quality: Technology can evaluate massive volumes of data quickly. This can assist auditors in determining the areas that require more testing, lowering the chance that serious misstatements or other problems would go unnoticed. 4) I- Improved Risk Assessment: Creating a number of automations to assist with the audit process and streamlined testing improves the risk assessment procedure. mngt & auditors put their testing efforts on sites with a higher ROMM and make informed decisions. 5) B- Better Analytics: Improved analytics capabilities can aid mngt & auditors in seeing trends and patterns that may be challenging to spot manually. For instance, AI can examine a lot of financial data to spot possible fraud, which is hard for auditors to spot manually.
Consideration & Challenge of Digital audit: <i>[Trick: CPT</i>	Considerations that organization should keep in mind while using digital technique & automation: <i>[Trick: haa maana ki "Change Difficult" hota h > para agar "Sahiii Process" lagya > to Bahot "benefit" hai par saamne wala bolega ... kya benefit h ye koi "Single solution" to nahi hoa > Technology se "Security risk" bhi to hogi]</i> 1) C- Change Difficult: Think people first and do not underestimate change is difficult



me BSR nhi thaa.. so abhi challenge h isse padhna] (Special Trick :-)	2) T- Target the right processes - this is a key for successful automation. 3) P- Process Standardised: Ensure the process works and it is standardised before automating. Bots do not easily adapt to process change 4) B- What Benefit: Know what business benefits organization wants to achieve with automation 5) S- Not standalone solution: Automation is not a standalone solution & should be part of a broader digitalization strategy 6) R- Security Risk: Automation introduces new challenges for organization. Don't forget about governance and data security in the risk framework. Auditors will obtain understanding of mngt's implementation & oversight of new technologies, Area include understanding of following: <i>[Trick: "IC" → "System" & "Process" ki understanding lo]</i> a) The impact the new technology as how the organization obtains or generates and uses relevant, quality information to support the functioning of internal control. b) Changes in the way entity's systems are developed and maintained and whether these changes introduce new risks and require new controls to respond to those risks c) New activities or changes to existing processes due to new technology (e.g., new revenue streams, changes in the roles and responsibilities of entity personnel, automation of manual tasks, changes in staffing levels that affect an entity's internal control environment)

➤ Auditing Digitally : (Doing Audit using Digital tools)

Means:	Using advancements in technology for conducting an effective and efficient audit. With a rapidly growing IT environment it is essential to adapt technology in auditing practices. There are new technologies to help capture data, automate procedures, analyse information and focus on the real risks of the client.
Expectations from an Auditor:	• Involve Expert: Audit teams need to involve the experts on different software applications & technologies. Having right level of expertise of new technology (eg. RPA, AI, blockchain tech) • Automate and enhance existing processes: Investment in technology on developing tools and using tools to automate and enhance existing processes, such as data analytics & collaboration and sharing tools, help to drive quality in audits today • Evolving Scope of audit: Using such technology will also evolve scope of audit
Key Feature / Advantage: (Special Trick :-)	<i>[Trick: ab Jaldi Jaldi kaam koga .. kyuki "Human" to "inefficient" hote h .. "automation" se fatafat kaam ho jaaega > orr "Audit quality" bhi improve hogi.. kyuki "risk" saari "transparent" hogi ab]</i> i) Improved Efficiency: What used to take weeks to learn and programmes using deep experts, is now easily available to auditors after some simple training and digital upskilling. The result may be increased efficiency & fewer errors, but benefits are wider reaching & personal. ii) Decreasing human dependency: Using technology minimizes the manual intervention which ultimately results in reducing the risk of manual errors. decreases the errors which occur from the judgement of different individuals. iii) Automation and Ease: Automating tasks like recording work in repositories, extracting data & sampling have improved quality of audit & reduced the manual error. Using dashboards (e.g., Power BI) for reporting helps in understanding & helps auditor to form opinion. iv) Improved Quality of Audits: The impact on quality is evident, through automation, data analytics techniques we can easily move from sample auditing to full population of transactions being reviewed or re-performed. It free up time for audit teams to analyses the information and better understand the business they audit. v) Increases Transparency: New ERPs and tools have audit trail feature available to trace the



	transaction end to end. like the date on which any change is made, who made the change, what has been changed, all such details are captured and can be used while performing audit. vi) Better risk assessment: With usage of automation in audit, auditor may focus on real challenges & assess potential risk precisely. It gives time to auditors to focus on the bigger picture rather than being involved with repetitive tasks. Dashboards, visual presentations & other tools helps in understanding where the risk lies & what all areas need more attention.									
Considerations in Auditing Digitally:	There are few questions it is important to ask and answer - at all stages of tech journey:									
	What Problem?	What problems are you trying to solve? → Continuously evaluate emerging technologies & latest tools → to see what can benefit the audit (easier or better)								
	Which tech?	Which technology can help you? → There are number of tools available & many vendors using data acquisition, manipulation and visualization tools. Consider how comfortably these solutions will integrate into your current processes and flag any potential implementation issues early on								
	Upskill People:	How will you upskill your people to make best use of the technology available? Technology is only as good as the people using it. Training and development are critical to ensure teams understand how and why they are using the technology								
	Range:	Range of automated solutions: There is a range of automation solutions, from low to high sophistication → helps to standardize the repeatable tasks → using robotics and automation for data gathering → data analytics <table border="1"> <thead> <tr> <th>Macros and Scripts</th><th>Business Process Automation (BPA)</th><th>Robotic Process Automation (RPA)</th><th>Intelligent Process Automation (IPA)</th></tr> </thead> <tbody> <tr> <td>Rules-based automation within a specific application</td><td>Reengineering existing business processes e.g., workflows</td><td>Automating labour intensive, repetitive Activities across multiple systems</td><td>Combining RPA with artificial intelligence technologies to identify patterns learn over time, and optimize workflows</td></tr> </tbody> </table>		Macros and Scripts	Business Process Automation (BPA)	Robotic Process Automation (RPA)	Intelligent Process Automation (IPA)	Rules-based automation within a specific application	Reengineering existing business processes e.g., workflows	Automating labour intensive, repetitive Activities across multiple systems
Macros and Scripts	Business Process Automation (BPA)	Robotic Process Automation (RPA)	Intelligent Process Automation (IPA)							
Rules-based automation within a specific application	Reengineering existing business processes e.g., workflows	Automating labour intensive, repetitive Activities across multiple systems	Combining RPA with artificial intelligence technologies to identify patterns learn over time, and optimize workflows							

Q1. Briefly describe the advantages and challenges of Auditing digitally. [ICAI SM - AMBIGUOUS]

Hint: ICAI has given Hint in ICAI SM answer as Follows: [ICAI Hint seems to be mixture of Above topic "Digital Audit" & "Auditing Digitally". [As per Author, It should be as per Topic "AUDITING DIGITALLY" .. so in exam, Elaborate the answer .. below is just an Hint Given by ICAI]:

Advantages - Improved efficiency, better quality, lower costs, improved risk assessment.

Challenges - Reluctance to change, challenges with data security and governance, choosing the right tool & automating the right process, ensuring standardisation and correct configurations to avoid error and bias, evaluating business benefits the organization wants to achieve with automation and roadmap for digital strategy.

➤ Understand the AUTOMATED ENVIROMENT (IT):

Q2. Auditor is of view that understanding & using the auditee's automated environment is optional and not required. Do you agree? illustrate by giving one example [AUTOMATED ENVIRONMENT] [OLD]

- Understanding the ways in which the entity relies upon IT and how the IT environment is set up to support the business. This allows the auditor to better understand where risks might arise from the entity's use of IT (required as per SA 315).
- Understanding how IT is used by the entity helps in identifying controls over the entity's IT processes.
- Assessing the complexity of the IT environment helps the teams consider whether to involve IT specialists or experts in the planning and/or execution of the audit, including initial consideration of whether to include

specialists in the complexity assessment.

3 Stages as follows:



The auditor's understanding of the **automated environment** should include the following:

- 1) The **applications** that are being used by the company;
- 2) Details of the **IT infrastructure** components for each of the application;
- 3) The **organisation Structure** and governance;
- 4) The **Policies**, procedures and processes followed;
- 5) IT **risks and Controls**.

The auditor is **required to document** the understanding of a company's automated environment as per **SA 230**.

The illustration below is an example of how an auditor can document details of an automated environment:

Application	Used for	Database	Operating System	Network	Server and Storage
SAP ECC/ HANA	Integrated application software	Oracle 19c	HP-UX	LAN, WAN	HP Server and NAS
REVS	Front Desk, Guest Reservations	MS-SQL Server 2018	Windows 2016 Server	In-house developed	HP Server Internal HDD
KOTS	Restaurant and Kitchen Orders	MS-SQL Server 2018	Windows 2016 Server	In-house developed	HP Server Internal HDD
BILLSYS	Billing	Oracle 12c	Windows 2016 Server	Packaged Software	HP Server Internal HDD

➤ Key Areas for an Auditor to Understand IT Environment:

Q3. What are the stages involved in understanding the IT environment and what key considerations auditor should consider? Or explain the key areas for an auditor to understand IT environment

Hint: 3 Stages are → Understand - Identify - Assess

Trick: Konsi Technology, system, & control (TCS) use leti h company h > uska flow Flow & Complexity

Understand flow of transaction:	Auditor's understanding of IT environment may focus on identifying & understanding nature and number of the specific IT applications and other aspects of the IT environment that are relevant to the flows of transactions and processing of information in the info. system. Changes in the flow of transactions, or information within the info. system may result from program changes to IT applications, or direct changes to data in databases involved in processing or storing those transactions or information.
Identification of Significant Systems :	The auditor may identify the IT applications and supporting IT infrastructure concurrently with the auditor's understanding of how info. relating to significant classes of transactions, account balances and disclosures flows into, through and out the entity's info. system.
Identification of Manual and Automated Controls	An entity's system of I.C. contains manual elements and automated elements (i.e., manual and automated controls and other resources used in the entity's system of I.C.). An entity's mix of manual and automated elements varies with the nature and complexity of the entity's use of IT. The characteristics of manual or automated elements are relevant to the auditor's identification and assessment of the ROMM.
Identification of	The need to understand technologies implemented & role they play in entity's info.



the technologies used:	processing or other F.R. activities & consider whether there are risks arising from their use. If complex technology → engage expert to understand whether and how their use impacts the entity's financial reporting processes and may give rise to risks from the use of IT. <u>Some examples of emerging technologies are:</u>			
	Blockchain, including cryptocurrency businesses	Robotics Internet of Things	Artificial Intelligence Biometrics	Drone
Assessing the complexity of the IT environment:	Not all applications of the IT environment have the same level of complexity. The level of complexity for individual characteristics differs across applications . (Complexity is based on Factors such as: automation used in organisation, entity's reliance on system generated reports, customization in IT applications, business model of the entity, any significant changes done during the year and implementation of emerging technologies.)			

➤ IDENTIFYING THE RISKS ARISING FROM USAGE OF IT

How to identify IT Risk?	Consider the nature of identified IT application → may also be identified related to cybersecurity <u>More Risks arising use of IT when:</u> • Volume or complexity of automated application controls is higher • Mngt placing greater reliance on those controls for effective processing of transactions or the effective maintenance of the integrity of underlying information.
Risk arising from use of IT: [Data, IT Application, System, Bande] (Special Trick :-)	• Unauthorized access to data that may result in destruction of data or improper changes to data (recording of unauthorized or non-existent transactions) • Data loss or data corruption (Lack of cyber control → lead to loss of sensitive data/hackers, physical security breach/theft of data) • Unauthorized changes to IT applications • Failure to make necessary update IT applications • There is a risk of system downtime (hardware failures, faulty configurations, cyberattacks or power outage) • System integration risk: companies uses more than one IT systems, integrating one or more systems) and system compatibility → In case of system failure in one system may also lead to widespread failure in integrated systems (or if hardware/software is not compatible → Risk) • Possibility of IT personnel gaining access privileges beyond those necessary to perform their assigned duties (breaking SOD) • Inappropriate manual intervention. • With advancement in usage of IT the risk of regulatory compliances increases → Any change in the law, order, guidelines → (Related cost & investment is higher) [FMCG have different regulatory requirement than Finance company] Scaling: When performance issue arises in IT system due to heavy data load / network issue → IT systems, resources or hardware can be added to an existing nodes, which is known as scaling (However its expensive)

➤ Know how to identify the IT dependencies impacting the Audit

Why to identify IT dependencies?	Identifying and documenting the entity's IT dependencies in a consistent, clear manner helps to identify the entity's reliance upon IT, understand how IT is integrated into the entity's business model, identify potential risks arising from the use of IT, identify related IT General Controls and enables us to develop an effective and efficient audit approach.



How IT dependencies arise? [TYPES] [Trick: SIA - Ram Chandra]	Q4. Auditor should scope in ITGCs to tests when there are IT dependencies identified in the system. Briefly describe the types of IT dependencies. How it arise ? : IT Dependencies are created when IT is used to initiate, authorize, record, process, or report transactions or other financial data for inclusion in FS <table border="1"> <tr> <th colspan="2">5 Types of IT Dependencies: [SIA - Ram Chandra]</th></tr> <tr> <td>Security</td><td>Security including segregation of duties is enabled by the IT environment to restrict access to information and to determine the separation of roles</td></tr> <tr> <td>Interfaces (Qn)</td><td>Interfaces are programmed logic that transfer data from one IT system to another. For example, an interface may be programmed to transfer data from a payroll subledger to the general ledger</td></tr> <tr> <td>Automated Controls</td><td>Automated controls are designed into the IT environment to enforce business rules. For Eg, purchase order approval via workflow or format checks (e.g., only a particular date format is accepted), existence checks (e.g., Duplicate customer number cannot exist), and/or reasonableness checks (e.g., maximum payment amount) when a transaction is entered.</td></tr> <tr> <td>Reports (Qn)</td><td>System generated reports are info. generated by IT systems. These reports are often used in an entity's execution of a manual control, including business performance reviews, or may be source of entity info. used by us when selecting items for testing, performing substantive TOD or performing a SAP. E.g. (Vendor master report, customer ageing report)</td></tr> <tr> <td>Calculations</td><td>accounting procedures that are performed by an IT system instead of a person. (Depreciation by SLM etc.)</td></tr> </table>	5 Types of IT Dependencies: [SIA - Ram Chandra]		Security	Security including segregation of duties is enabled by the IT environment to restrict access to information and to determine the separation of roles	Interfaces (Qn)	Interfaces are programmed logic that transfer data from one IT system to another. For example, an interface may be programmed to transfer data from a payroll subledger to the general ledger	Automated Controls	Automated controls are designed into the IT environment to enforce business rules. For Eg, purchase order approval via workflow or format checks (e.g., only a particular date format is accepted), existence checks (e.g., Duplicate customer number cannot exist), and/or reasonableness checks (e.g., maximum payment amount) when a transaction is entered.	Reports (Qn)	System generated reports are info. generated by IT systems. These reports are often used in an entity's execution of a manual control, including business performance reviews, or may be source of entity info. used by us when selecting items for testing, performing substantive TOD or performing a SAP. E.g. (Vendor master report, customer ageing report)	Calculations	accounting procedures that are performed by an IT system instead of a person. (Depreciation by SLM etc.)
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Understand & respond risk arise from IT dependency:	When auditors identify IT dependencies that are relevant to the entity's flow of transactions and processing of financial information, they need to understand how management responds to the associated risks that may arise from them. ITGC: • Mngt may implement I.T general controls (ITGCs) to address risk related to IT dependency • Auditor should consider IT dependency relevant to audit because → IT dependency affect the entity controls • Auditor should test ITGC • Do not Rely on ITGC (i.e., Do not rely on <u>IT dependency</u>) → <u>When controls around IT environment are not implemented</u> [Refer "Additional PDF Booklet"]												
Q5. IT dependencies also arise due to "system generated reports" and "interfaces". How do such IT dependencies arise? Why it is important to identify IT dependencies for Audit? Hint: refer above → "System generated reports" & "Interfaces" and "Why to identify IT dependency"													
➤ Assessing Cyber Risk:													
Q6. What does cyber risk explain it with some examples. [Length & points of answer will depend on Marks]													
What is Cyber Risk:	A cyber-attack is an attempt to gain unauthorized access to a computing system or network with the intent to cause damage, steal, expose, alter, disable, or destroy data												
Most common types of cyberattacks are:													
Malware:	Malicious software is any program or code that is created with the intent to do harm to a computer, network or server (ransomware, fileless Malware trojans, viruses etc.) <table border="1"> <tr> <th>Type</th><th>Description (RFT-M)</th></tr> <tr> <td>Ransomware</td><td>Adversary encrypts a victim's data and offers to provide a decryption key in</td></tr> </table>	Type	Description (RFT-M)	Ransomware	Adversary encrypts a victim's data and offers to provide a decryption key in								
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		exchange for a payment. (malicious links, phishing emails etc.)
	Fileless Malware	Malicious activity that uses native, legitimate tools built into a system to execute a cyber-attack, unlike traditional malware, fileless malware does not require an attacker to install any code on a target's system, making it hard to detect
	Trojan	legitimate software disguised as native operating system programs or harmless files like free downloads. → installed through social engineering techniques such as phishing or bait websites
	Mobile Malware	designed to target mobile devices. Mobile malware is delivered through malicious downloads, operating system vulnerabilities, phishing, smishing, and the use of unsecured Wi-Fi.
Denial-of-Service (DoS) Attacks:		Malicious, targeted attack that floods a network with false requests in order to disrupt business operations → unable to perform routine and necessary tasks (i.e., accessing email, websites, online accounts or other resources) → not result in lost data and are typically resolved without paying a ransom, they cost the organization time, money and other resources in order to restore critical business operations.
Phishing:		Cyberattack that uses email, SMS, phone, social media, and social engineering techniques to entice a victim to share sensitive information — such as passwords or account numbers — or to download a malicious file that will install viruses on their computer or phone.
(SS - VW)	Type	Description
	Spear Phishing	phishing attack that targets specific individuals or organizations typically through malicious emails. (Steal sensitive info. i.e as login credentials) or infect malware. (Eg, CEO received email from Fake bank, Looks like original, to enter ID/Pass to update the account)
	Whaling	Social engineering attack specifically targeting senior or C-level executive employees (Purpose of stealing money or information)
	Smishing	fraudulent practice of sending text messages purporting to be from reputable companies (Reveal personal info. Like passwords & credit card no.)
	Vishing	voice phishing, is the fraudulent use of phone calls & voice messages pretending to be from a reputable organization (to reveal private info.)
Spoofing:		Technique through which a cybercriminal disguises themselves as a known or trusted source. Engage with target & access their systems or devices with the ultimate goal of stealing info. (Installing malware)
	Type	Description
	Domain Spoofing	Domain appears to be legitimate at first glance, but a closer look will reveal subtle differences.
	Email Spoofing	Email spoofing is a type of cyberattack that targets the businesses by using emails with forged sender addresses. they are more likely to open the email and interact with its contents, such as a malicious link or attachment.
Identity-Based Attacks:		When valid user's credentials have been compromised & adversary is pretend to be that user. For e.g., people often use the same user ID and password across multiple accounts. Therefore, possessing the credentials for one account may be able to grant access to other a/c.
Insider Threats:		When current or former employees that pose danger to an organization because they have direct access to the company network, sensitive data, and intellectual property (IP), as well as knowledge of business processes, company policies that would help carry out such an attack.
DNS Tunneling:		DNS Tunneling is a type of cyberattack that leverages domain name system (DNS) i.e., (Website domain) queries and responses to bypass traditional security measures and transmit data & code within the network. This tunnel gives the hacker a route to unleash malware and/or to extract

(Spoof)	data, IP or other sensitive information by encoding it bit by bit in a series of DNS responses.
IoT-Based Attacks:	An IoT attack is any cyberattack that targets an Internet of Things (IoT) device or network. If compromised, hacker assume control of device, steal data, or join a group of infected devices

Q7. Finance manager received **message** from bank → "**Your account temporary suspended, To reactivate, Visit sendyourinfo-link.com**". → Which type of Phishing is this ? explain other type of phishing too.

Hint: It's **Smishing** (refer other type phishing above)

Stages of Cyber Risks:

Q8. Stages of Cyber Risk ? (MTP'25).

Stage 1 - Assessing the cyber risk:	Different clients will have different levels of risks, even with the same industry. Every organization should consider at least the common threats: <i>[Trick: Inside se sab me 1 common chi h > sab handsome hote h andar se]</i> • Ransomware disabling their organization (including their plants and manufacturing facilities) • Common criminals using email phishing and hacks for fraud and theft • Insiders committing malicious activities or accidental activities resulting in unintended discourse of information theft and frauds.
Stage 2 - Impact of cyber risk: <i>Trick [RIB RIB Fines & Penalty]</i>	Cyber-attack can impact one, two or more types of risks. The impact of the attack would vary from organization to organization, The cyber risks are not an issue of IT alone. Rather, it is a business risk and has an effect on whole business organization. It affects entity's reputation and can lead to many other consequences: <i>[Trick: "Cost" lagegi > "ransomware" ne attack kara to "Privacy" breach ho jaaegi saara "data" uske paas chale jaage, apka main "IP right" bhi > to "business" hi bank ho jaaega]</i> • R - Regulatory costs • Fines and penalties • R- Ransomware - more common these days where entire systems are encrypted • B- Breach of Privacy, if personal data of a consumer is hacked it could have a significant impact on the organization. • Data loss, reputational loss and litigation • I- Intellectual property theft which may not only take the competitive advantage, but we may also result in any impairment/impediment charge because of the loss of IP • B- Business interruptions causing an operational challenge for an organization. • I- Incident response cost which could be for investigations & remediations
Stage 3 - Managing the cyber risk	A strategic approach to cyber risk management can help an organization to: <i>[Trick: "Understand Risk" > uss risk ke against kya "cysbersecurity h" > "security align karo objective se" end me agar fir bhi koi "Risk bache to usse Document karlo .. against Control"]</i> • Gain a holistic understanding of the cyber risks, threats facing their organization and other financial institutions • Assess existing IT & cybersecurity program and capabilities against the relevant regulatory requirements • Align cybersecurity & IT transformation initiatives with strategic objectives and critical risks • Understand accepted risks & documented compensating controls

Q9. Sukanya is of view that **cyber risks are issues of IT** and result only in information loss. → **cyber-attacks are not directly targeted at financial systems** and do **not pose risk of MMS to FS**. Is her view proper?

Hint: **[Mention above "STAGE 2 - IMPACT OF CYBER RISK] & Below Additional Answer**



May cyber-attacks are not directly targeted at financial systems. However, the access gained by the attackers may provide them the ability to:

(1) **modify financial records** (2) **Modify key automated business rules** (3) **Modify automated controls**

Further, auditor should **consider whether cyber risk (like other business risks) represents a ROMM to the FS as part of the audit risk assessment activities.**

➤ Cyber Security Framework (Risk Management Process): - RR - PDI

Q10. Briefly describe the cyber security Framework. [ICAI SM]

Identify the Risk: <u>ABC-G</u>	Determine whether entity's RAP considers cybersecurity risks. • Conduct periodic risk assessment: Entity should Conduct periodic risk assessment & develop a management strategy to identify cyber-risk & loss against it • Asset management: should maintain and periodically reviews an inventory & asset (Intellectual property, patents, copyrighted material) • Governance: Mngt should review how cybersecurity risks affect IC-FR, how mngt will recover financial data & impact on revenue recognition. • Business environment: For cybersecurity establish roles and responsibilities over cybersecurity (CISO, CIO) → Risk asses should also to be discuss with TCWG
Protect the Risk: <u>[DAAI] ko protect krna paani se</u>	Obtained an understanding of the entity's processes for, safeguarding of assets: • Access Control: monitors whether there has been <u>unauthorized access to electronic assets</u> and any related impact on financial reporting • Awareness and Training: To <u>make the teams aware</u> of the <u>risk associated with cyberattacks</u>. • Data Security: <u>implement effective controls</u> for data security • Information Protection Processes and Procedures: for <u>identifying material digital/electronic assets</u> on the balance sheet subject to <u>cybersecurity risk & prioritizing their protection</u> based on criticality
Detect the Risk:	<u>controls and procedures</u> that enable it to <u>identify cybersecurity risks</u> and incidents and to <u>assess</u> and <u>analyse</u> their <u>impact</u> on the entity's business → <u>monitor and detect security breaches</u> . Implemented <u>anti-virus</u> or monitor <u>fire-wall logs</u> on continuous basis • Anomalies and Events (identify karo timely basis pe) • Security Continuous Monitoring • Detection Processes
Respond the Risk: <u>[RCM]</u>	If <u>material cybersecurity</u> or data breach → mngt should <u>capture details of nature of incident</u> and <u>how the incident</u> or data breach <u>was identified</u> → Entity should have <u>response planning</u> • Response Planning (incident response plan) → plan helps in analysing impact & severity of attack, taking the appropriate actions • Communications → same need to communicate to who is responsible for framework & TCWG. • Mitigation & Improvements → Management should assess Litigation costs, investigation costs, Remediation costs, future action plans for safeguard
Recover from Risk: <u>[RIC]over</u>	• Recovery Planning → Should have recovery plan action <u>to recover from the attack</u>, once impact evaluated, <u>communicate with regulator</u>. • Improvements → like <u>patch upgrades</u>, <u>better Controls</u>, <u>improved technology</u> in terms of firewall, anti-virus, etc. • Communications → Communicate to regulatory

➤ Control considerations for Cyber Risks:

Apart from having the cyber security policies, procedures, framework and regular assessment in place, management **should have a strong and updated internal controls** to ensure they are covered from **cyber risks**:



Controls around vendor setup & modifications: <u>NOV'24</u>	Q11. How will you evaluate the controls around the vendor setup and modifications (Nov'24) Cyber schemes exist in which changes to bank account or other critical vendor information are requested through email phishing scams <i>[Trick: agar "Communication" aaya kisika details update karne k liye .. to "Kon" karega ? kis "system" me karega ? hone k baad "Verify" kon karega ?]</i> (i) Are other communication channels, such as email, used to request changes to vendor master data? (If yes, consider if multi-factor authentication is enabled for email). (ii) Who is responsible for making changes to vendor master data? Is the process centralized or decentralized? (iii) What systems and technologies are used to initiate, authorize and process requests related to changes to vendor master data? (iv) Are authentication protocols defined to verify modifications to vendor master data (e.g., call back procedures, multi-factor authentication)?
Controls around electronic transfer of funds:	Wire transfers or electronic funds transfers, similar to vendor changes noted above, cyber schemes pertaining to fraudulent requests for wire transfers → fraudulent requests appearing to come from financial institutions requesting disbursement" <i>[Trick: pai har kisis "system" se har koi transfer nahi karega .. ho "Educated hoga" usse ho ye authority do .. baad me "Authentication review / approval" bhi karo]</i> (i) What systems and technologies are used to facilitate the request/initiation, authorization and release of O wire transfers? (ii) Are personnel responsible for wire transfers educated on the relevant threats and information related to common phishing scams associated with fraudulent requests for wire transfers? (iii) Are authentication protocols defined to verify wire transfer requests (e.g., call back procedures, dual-authentication procedures)?
Controls around patch management:	Cyber and ransomware attacks exploit known security vulnerabilities resulting in the manipulation or the destruction of data. Exploitations of known security vulnerabilities are often caused by unapplied patches or upgrades <i>[Trick: Antivirus/patch lene k liye kon "bolta/notify" karta h ? "scan" karte ho timely basis pe > koi "manage" karne wala h ki nhi...]</i> (i) How is the entity notified of patches by external vendors (e.g., Microsoft for Windows patches)? (ii) Does the entity run periodic vulnerability scans to identify missing/unapplied patches? (iii) Does the entity have a patch management program?

➤ Remote Audit/ Virtual Audit:

Meaning:	• When auditor uses the online or electronic means to conduct the audit. • It could be partially or completely virtual, auditor engages using technology to obtain the audit evidence or to perform documentation review with the participation of auditee • Audit planning and scoping is crucial in every audit → scope and schedule, and ways to conduct audit.
➤ Consideration for Remote Audit:	
Q12. key considerations should CA address to ensure the effectiveness & security of remote audit? (MTP'24 & SM) (Auditors must develop tailored strategies to ensure the remote audit meets the requirements)	

Feasibility & Planning	- Planning should involve agreeing on audit timelines, meeting platform (Zoom calls/ Microsoft Teams/Google Meet) to be used for audit sessions, data exchange mechanisms, any access authorization requests. Ensure feasibility is determining what technology may be used, if auditors and auditees have competencies and that resources are available. - Execution phases of a remote audit involve video/tele conferencing with auditees. Documentation for audit evidence should be transferred through a document sharing platform.
Confidentiality, Security and Data Protection	- To ensure data security and confidentiality, access to document sharing platform should be sufficiently restricted and secured by encrypting the data - information, once reviewed and documented by auditor, is removed from the platform - Auditors should take into consideration legislation and regulations, which may require additional agreements from both sides - Auditors should not take screenshots of auditees as audit evidence (Unless authorized by the audited organization) - Use VPN
Risk assessment	The communication from auditor as well as auditees need to be clear and consistent, and this becomes crucial during remote audit. The assessment to be done that if remote audit would be sufficient to achieve the audit objectives should be done and documented for each audit involving all members of the audit team and the audited organization representative.

Q13. What are the advantages and disadvantages of remote audit?

Trick: kahi aana jaan nhi padega > cost save bhi hogi & flexibility bhi rahegi ...aaram se evidence aa jaaenge .. Globally audit krenge.. dhandha bhi badhega

Advantages and Disadvantages of remote audit	
Advantages (trick - Evidence of Widen CTC)	Disadvantages (trick - Do Not SCN)
Auditor can get first-hand evidence directly from the IT system as direct access may be provided.	<u>Doctored documents</u> → opportunity to present Doctored documents and to omit relevant information is increased. This may call for additional planning, some additional/different audit procedures, Security and confidentiality violation.
Widens the selection of auditors from global network of experts.	<u>Network Issue</u> → Due to network issues, interviews and meetings can be interrupted.
Comfort & flexibility to the audit team as they would be working from home environment,	<u>Sensitive IT Sys may not be allowed</u> → Remote access to sensitive IT systems may not be allowed. Security aspects related to remote access and privacy needs to be assessed
Time required to gather evidence can spread over several weeks, instead of concentrated into a small period that takes personnel from their daily activities	<u>Cultural challenges</u> → Cultural challenges for the auditor. Lack of knowledge for local laws and regulations could impact audit. Audit procedures like physical verification of assets and stock taking cannot be performed.
Cost and time effective: No travel time and travel costs involved	<u>No ability to visualize facility</u> → Limited or no ability to visualize facility culture of the organization, and the body language of the auditees. Time zone issues could also affect

➤ Emerging Technologies in Audit

As the use of emerging technologies in the financial reporting process increases, it becomes important for auditor and the client to upskill on the emerging technologies → evaluate whether management is properly assessing the impact of emerging technologies on internal control over financial reporting (ICFR).

Data Analytic Techniques:



Data Analytics:	Generating & preparing meaningful information from raw system data using processes, tools, and techniques is known as Data Analytics
Audit analytics or audit data analytics:	Involves analyzing large sets of data to find actionable insights, trends, draw conclusions and for informed decision making. The use of audit analytics enables greater efficiencies and more accurate findings from the review process. Allows auditors to more effectively audit the large amounts of data held and processed in IT systems.
Audit Analytics Helps:	- To discover and analyze patterns - Extract other useful information in data - Identifying anomalies
CAAT:	- Data analytics methods used in an audit are known as Computer Assisted Auditing Techniques - Involves use of multiple data analytical tool or visualization tools → can help the auditor to deep dive into the problem statement and hence increase the audit quality - Use various applications & tools that help them to analyze large data sets and obtain insights
Some of the popular tools used across the industry as part of CAATs are listed below: <i>[Trick: AA-BC]</i>	
ACL:	<u>Audit Command Language</u> → Analytics is a data extraction and analysis software used for fraud detection and prevention, and risk management. It samples large data sets to find irregularities or patterns in transactions that could indicate control weaknesses or fraud. Eg. Reconcile TRIAL BALANCE with GENERAL LEDGER to verify COMPLETENESS, it's beyond MS Excel skill to handle such a large data.
Alteryx:	It's used to consolidate financial or operational data to assess controls. A fully transparent audit trail of every action is performed in Alteryx in form of a workflow which makes it easier for the user to learn as no prior knowledge of coding or scripting is required. Alteryx can also be leveraged to automate analytics and perform Machine Learning to search for patterns indicative of fraud or irregularities speed up your processes like accounting close, tax filings, regulatory reporting, forecast creation etc. It can also be used to automate set procedures that are performed periodically like reconciliations, consolidations, marketing workflows, system integrations, continuous audits etc. [i.e., For Hotel: No of room given on rent * Room Rate = Revenue]
Power BI:	Business intelligence (BI) platform that provides nontechnical business users with tools for aggregating, analyzing, visualizing and sharing data. From audit perspective, such visualization tools can be used to find the outliers in the population, it can also be used for reporting purpose (audit reports) in an interactive dashboard to the higher management. [i.e., it's advance version of MS excel, used for Graphs & various reporting's]
CaseWare:	CaseWare is a data analysis software & provide tools that helps in conducting audit and assurance engagements quickly, accurately and consistently. It shares analytical insights which help in taking better informed decisions. It helps in streamlining processes and eliminating the routine tasks. Used by accounting firms, governments and corporations worldwide, this trusted platform integrates everything you need to conduct assurance and reporting engagements. [i.e., Like SAP & Advance version of Tally with many features]

Q14. discuss the meaning of data analytics and example of such data analytics techniques.

Hint: Refer above meaning of "Data analytics" & "Examples" i.e., ACL, alteryx, Power BI etc....

Q15. CA Y is planning to use CAATs extensively in audit of a company-be it for compliance tests or substantive tests. Can you list out examples of few situations (in brief) of tests performed by him using CAATs?

Answer:

[Trick: Payment check karte wqt "Payment" ka RECORD & CALCULATION dekhi hoti h "record" > "Complete" &



"consistent" nahi h ... "calculation" me "Error" & "exception" hai..... > payment "authorisation" se jyada ho gya

- (i) **Duplicate payments:** Establish relationship between two or more tables as required. For example, duplicate payment for same invoice
- (ii) **Existence of records:** Identify fields, which have null values. Eg, invoices which do not have vendor name
- (iii) **Data completeness:** Identify whether all fields have valid data. Eg, null values in any key field such as date, invoice number or value or name.
- (iv) **Data consistency:** Identify data, which are not consistent with the regular format. Eg, invoices which are not in the required sequence
- (v) **Verify calculations:** Re-perform various computations in audit software to confirm the results from application software confirm with the audit software. For e.g.: TDS rate applied as per criteria
- (vi) **Identify exceptions:** Identify exceptional transactions based on set criteria. Eg, cash transactions above Rs. 10,000
- (vii) **Identify errors:** Identify data, which is inconsistent or erroneous. For e.g.: A/c number which is not numeric
- (viii) **Accounts exceeding authorized limit:** Identify data beyond specified limit. For Eg, transactions entered by user beyond their authorized limit or payment to vendor beyond amount due or overdraft allowed beyond limit.

➤ AUTOMATED TOOLS IN AUDIT

Enterprises are adopting emerging technologies → Automation and use of technology often requiring auditors to understand and perform procedures on a larger group of systems that produce information relevant to FS audit's scope may need to include peripheral systems, as well as testing general IT and application controls relative to those systems relevant to F.R (It's based on mngt & auditor Risk assessment)

➤ **Internet of Things (IOT)**

connecting any device (cell phones, coffee makers, washing machines, and so on) to the internet. Key components of IoT are data collection, analytics, connectivity, and people and process. (Change Business model, affect business objective, risk may arise due to new L&R)

Audit Implication	Common risks
<i>(Trick: Manual control nii chalega.. new system chahiye hoga.. auditor ko bhi apni skill badhaani padegi.. kyuki new risk hogi)</i> - may result in auditors not being able to rely only on manual controls. - Instead, auditors may need to scope new systems into their audit. - Audit firms may need to train and upskill auditors to evaluate the design and operating effectiveness of automated controls. - impact the flow of transactions and introduce new risks for management. - payment processing tools that allow users to pay via credit card at a retail location through a mobile device → create a new path for incoming payments that may rely, in part, on a new service provider supplying and routing information correctly (i.e., RazorPay). Auditors would need to consider the volume of those transactions and the processes and controls related to it.	including, device hijacking, data siphoning, denial of service attacks, data breaches and device theft.

Q16. Describe key components & benefits of IoT, risks associated with IoT implementation, and the implications for the company's audit processes. How should company address these concerns? (RTP'24 & SM)

Hint: Refer Above concept IOT Meaning, Audit Implication, Common Risk, And BELOW KEY COMPONENTS:

- **Key components of IoT** are data collection, analytics, connectivity, and people and process. IoT not only changes the business model, but also affects the strategic objectives of the organisation. The risk profile of



the entity changes with exposure to new laws and regulations.

➤ **Example**

- **Connected Cars**, connected manufacturing equipment's, smart home security, users can view video feeds when they are away from home
- **Data from machines** can be used to predict whether equipment will break down → warning to prevent long stretches of downtime
- **Refrigerator** placing an order with a grocery store whenever the supply of eggs falls below a certain number
- **Researchers use IoT devices** to gather data about customer preferences and behavior.

➤ **AI (Artificial intelligence)**

System or a machine that can think and learn. AI systems utilize data analysis and algorithms to make decisions based on predictive methods (Self driving cars, Smart robots, Siri, Google assistant etc.)

Audit Implication	Common risks
• Algorithm: ✓ Logical Flow Process: Given the invisible nature of algorithms, audits must focus on the logical flow of processes ✓ whether unintended bias has been added to the algorithms ✓ assess the effectiveness of algorithms and whether their output is appropriately review & approved • Consider cybersecurity and search for possible bugs and vulnerabilities • confirm their understanding of how the use of AI affects the entity's flows of transactions, generation of report • AI Decision: whether the AI is making decisions or being utilized by management • Oversight by AI: If management shifts its focus on oversight by relying on AI, auditors should understand what shift occurred, how new risks might be addressed & changes in the audit approach	Data privacy - The data used and shared should have the necessary explicit consent from data providers Security: more data the system uses, from more sources, the more entry points and connections are formed Inappropriate configuration: AI may also be used to diagnose medical conditions. If it is badly configured or malfunctions, it could harm people

Q17. What are common risks for Blockchain technology? Also discuss probable audit implications for this. (SM)

Answer:

➤ **BLOCKCHAIN:**

Based on a decentralized and distributed ledger that is secured through encryption. Each transaction is validated by the blockchain participants, creating a block of information that is replicated and distributed to all participants. All blocks are sequenced so that any modification or deletion of a block disqualifies the information. [i.e., Bitcoin, cryptocurrency transactions] security premise rests on cryptography

Audit Implication	Common risks
<i>(Trick: gold ki chain ko Secure & private rakho.. bahar pahen k mat gummo .. tumhe weak samaj ke le jaaenge ... L&R/police bhi kuch nii karegi)</i> • Governance and security transactions: Auditors should consider the appropriate security & governance around the transaction • Confidentiality & Privacy: As blockchain interacts with legacy systems and business partners, concerns related to insecure application programming interfaces (APIs), data confidentiality and privacy cannot be ignored.	• The strengths of blockchain can also be its <u>weaknesses</u> Inability to reverse transactions & access data without the required keys (System is secure) → but also need specific protocols to ensure that they are not locked out and have clear contingency plans • Cyber-attacks and data hacks: (Security issue) • Compliance with Regulation: Auditors should also ensure complies with regulations → regulatory landscape is still evolving for blockchain → ensure that compliance managers are following developments



- **Weak Block chain development protocols** : something auditors cannot overlook
- **Data privacy L&R** : Data are communicated across geographic boundaries, Data put on blockchain will expose the enterprise to liability for noncompliance with applicable laws and regulations.

constantly and adapting processes accordingly

➤ NFT (Non-Fungible Token):

Unlike physical money and cryptocurrencies are fungible (means they can be traded or exchanged for one another)

NFTs are non-fungible tokens. NFTs contains the digital signature which make them unique. NFTs are digital assets, e.g., photos, videos, artwork, sports collectibles etc. → NFT Tokens → used to represent ownership of unique items.

NFTs allow their creators to tokenize things like art, collectibles, or even real estate. They are secured by the blockchain and can only have one official owner at a time. No one can change the record of ownership or copy/paste a new NFT into existence.

Key Features of NFT

- **Digital Asset** - NFT is a digital asset that represents Internet collectibles like art, music, and games with an authentic certificate created by blockchain technology that underlies Cryptocurrency.
- **Unique** - It cannot be forged or otherwise manipulated.
- **Exchange** - NFT exchanges take place with cryptocurrencies such as Bitcoin on specialist sites.

Challenges of NFT

NFTs has its own challenges like ownership and copyright concerns, security risks, market is not that wide, online frauds etc.

NFT audit considerations include comprehensive code review for verifying the safety of a token, valid contract, data privacy and potential cyber threat.

➤ Robotic Process Automation (RPA):

RPA is the automation of the repetitive processes performed by users. It is a software technology that emulate humans' actions interacting with digital systems and software (software bots can interact with any application → the same way people do) → nonstop, much faster and with 100% reliability and precision

Audit Implication

- **Understand RPA processes**, which include data extraction, aggregation, sanitization and cleansing
- A comprehensive assurance process might demand review of the source code
- To perform substantive testing, auditors must have an understanding of the tools used to develop and maintain RPA. This will be helpful when auditors review logs, configuration controls, privileged access controls and the like. General IT controls are applicable as always.

Common risks

- **Operational and execution risks**: Robots are deployed without proper operating model. Buying the wrong tool, making wrong assumptions, taking shortcuts, and jeopardizing security
- **Change management risks**: Not following the change management implementation lifecycle, improper and incomplete testing (not covering all scenarios) leads to inaccurate results
- **RPA Strategy Risk**: Setting wrong expectations, improper KPIs, and unrealistic business goals creates an environment of uncertainty

RPA to check IND AS, IFC-FR and Standards on Auditing.

Incorporating: Standards on Auditing, IFCoFR, IND AS (para-wise details of | Para reference | Accounting policy | Relevant data to be captured | Relevant calculation to be made | Presentation in financial statements | IFCoFR | Audit procedures as per Standards on auditing |) in audit practices ensures accurate financial reporting, effective



internal controls, and reliable audit procedures.

Leveraging RPA in conjunction with these frameworks can significantly enhance audit efficiency, accuracy, and compliance. RPA developers and auditors should collaborate to align RPA workflows with relevant standards and guidelines, ultimately improving the effectiveness of audits and enhancing client assurance

[Refer "Additional PDF Booklet" For Example]

Q18. A company is planning to use Robotics process automation (RPA) to streamline its hiring process. To reduce recruitment costs, efficient hire yield etc. How RPA can be used to automate the hiring process? List out tentative few such steps. What could be likely benefits of using RPA in hiring process?

Answer:

RPA can be used to streamline hiring process in a company. The tentative steps could include: -

- Place advertisements on social media/career advice sites.
- Link redirects candidate to a career site.
- Career site pulls information of candidate.
- An algorithm scans applicants for desired and suitable roles.
- Selected candidates may be asked to play online games to assess their skills.
- A certain percentage of those applicants are called for a video interview using an interview software

The automated hiring process will reduce full time effort involvement, provide with a wider assessment range, reduce the impact of recruiter biases, increase the efficiency of mapping of interested candidates, reduce recruiting costs, increase hire yield, reduce time to hire, increase diversity.

Q19. Enterprises are adopting latest technologies. Give 3 examples of automated tools used as a part of emerging technologies along with the risk and audit considerations associated with these tools. [SM]

Hint: Refer above any 3

➤ CONTROL CONSIDERATIONS OR OBJECTIVES OF AUDITING DIGITALLY

Q20. Give some examples of technology risks of digital system & control considerations while assessing risk.

Emerging technologies can bring great benefits, but they also come with a varied set of substantial risks.

While assessing Risk, Auditor shall consider control:

[Trick: "New technology" ki wjh se jo "change" ho apan ko bhi "skill" badhani hogi]

The strength of the auditing profession is the assessment of risks and controls.

As they address the challenge of assessing technology risk, auditors can and should focus on the following control considerations:

- 1) Auditors should gain a holistic understanding of changes in the industry and the information technology environment to effectively evaluate management's process for initiating, processing, and recording transactions and then design appropriate auditing procedures.
- 2) **Risk From New Technology:** Auditors, as appropriate, should consider risks resulting from the implementation of new technologies and how those risks may differ from those that arise from more traditional, legacy systems
- 3) Auditors should consider whether digital upskilling or specialists are necessary to determine the impact of new technologies and to assist in the risk assessment and understanding of the design, implementation, and operating effectiveness of controls. E.g., cybersecurity control experts, IT specialists in the team etc.

Examples of technology risks

[unauthorise > data> system >]

[Approx Same as "RISK ARISING FROM USE OF IT", Already Discussed Above]

- Unauthorized access to data that might result in destruction of data or improper changes to data, including the recording of unauthorized or non-existent transactions or inaccurate recording of transactions (specific risks arise when multiple users access a common database)

changes > IT personnel doing manual intervention]	• Unauthorized or erroneous changes to data in master files • Potential loss of data or inability to access data as required • Reliance on systems or programs that are inaccurately processing data, processing inaccurate data, or both • Unauthorized changes to systems or programs • Failure to make necessary or appropriate changes to systems or programs • Possibility of info. technology personnel gaining access privileges beyond those necessary to perform their assigned duties, thereby leading to insufficient segregation of duties • Inappropriate manual intervention • Risks introduced when using third-party service providers • Cybersecurity risks

Key Steps for Auditors in a Changing Technology Environment: (Special Trick :-) 	As auditors obtain an understanding of the impact of technology on a company's business, its systems of I.C., and its financial reporting, some important reminders include the following: <u>[Trick: New Technology lagaai mngt ne .. to Control bhi lagao ... > kya effect hoga uska ? > transaction process pe effect padega ?]</u> a) Maintain sufficient professional skepticism when reviewing Mngt risk assessment for <u>new systems</u> . b) Assess the appropriateness of management's processes to select, develop, operate, and maintain controls related to the organization's <u>technology</u> based on the extent the technology is used. c) Understand the direct and indirect effects of <u>new technology</u> and determine how its use by the entity impacts the auditor's overall risk assessment d) Understand how the technologies impact the flow of transactions, assess completeness of the in-scope ICFR systems, and design a sufficient and appropriate audit response.

➤ NEXT GENERATION AUDIT:

The Next Generation Audit is human-led, tech-powered and data-driven. It is based on combining emerging technologies to redefine how audits are performed.

Next Generation Audit aims to the following:

SDM MR. Manual

Sampling population → to Full Population analysis

Disconnected tools → to integrated ecosystem service

Manual work → Automation

Multiple data set → to One data set

Repetitive task → high value work & capacity for grow

Manual risk assessment to → Dynamic, data driven risk assessment

Q21. Give example of emerging technologies available for Next Generation Audit along with the risks associated with it [SM]

[TRICK: AR-VR - Drone Metaver]

Auditing Through:	
Drone Technology:	Also known as (Unmanned Aerial Vehicle) UAV: Using drone technology in the remote locations for stock counts → sensors and cameras, thus they can photograph and physically



	examine the count of large quantities Drone captured audit information can be combined with various alternative sources of information such as QR code readers, handheld bar scanners, manual counts etc
Augmented reality (AR):	The technology allows users to view the real-world environment with augmented (added) elements, generated by digital devices → One famous example was Pokémon Go, a game → catch imaginary Pokémon around physical locations
Virtual reality:	Replaces the real world entirely with a simulated environment, created through digitally generated images, sounds, and even touch and smell Example of AR & VR: • In architecture and engineering businesses → AR-VR → allow architects to see their building plans come to life before being built • Business sector → allow products to be previewed / customized, thus improving productivity • Health sector → AR can provide surgeons with additional information <u>when operating on a patient</u>, such as heartbeat and blood pressure monitoring and virtual x-rays
Metaverse:	Emerging 3-D digital space that uses virtual reality (VR), augmented reality (AR), and other advanced internet technology to allow people to have lifelike personal and business experiences online. It represents a convergence of digital technology to combine & extend the reach & use of Cryptocurrency, Artificial Intelligence (AI), Augmented Reality (AR) & Virtual Reality (VR) mature landscape of virtual spaces with transferable identities and assets enabled by blockchains (NFTs) that are interoperable or interchangeable Some considerations for future: • Digital monetary systems: Beyond cryptocurrencies, coins, and exchanges, players in the Metaverse will need to consider how to build digital monetary systems and apply economic principles to things like digital land. • Governance models: Governance models will become ever more difficult to balance openness and user contribution with strategic direction and innovation • KYC: Identity in the digital world has historically been different based on the platform utilized. The practical challenge of identity will also have to be considered in the Metaverse (e.g., KYC) • Synchronize realtime: Synchronicity is the ability for aspects of the Metaverse to be multiplayer, simultaneous, and real-time. This includes transactions and actions happening in the Metaverse and are dependent on the infrastructure of digital economies, networking and computing power required to operate a digital world.
➤ Common Risks Associated:	
Beyond their potential, these technologies also come with challenges such as public safety, cybersecurity, data privacy, data protection, lack of standards and technical challenges. Since they often track movements and data, massive amounts of data are generated about the whereabouts of users. It also raises questions about taxation, jurisdiction, and customer protection. Regulators and auditors have to think of the controls around privacy, data security, governance to make it more regulated.	
➤ Potential application of the “Metaverse” in the financial domain:	
Virtual Banking and Transactions	A forward-thinking financial institution, establishes a presence in the metaverse to offer virtual banking services → Users can create virtual bank accounts, access personalized financial dashboards, and perform transactions using virtual currencies.

Digital Asset Management	A digital asset management company, recognizes the growing popularity of virtual assets in the metaverse. They launch a virtual asset trading platform within the metaverse, allowing users to buy, sell, and trade NFTs and other digital assets. Investors can diversify their portfolios, participate in virtual auctions
Virtual Financial Education & Training	Aims to enhance financial literacy using the metaverse. They create a virtual classroom environment where participants can attend interactive financial education sessions (learn about budgeting and financial planning etc)
Virtual Meetings and Conferences	For a leading industry even an organisation hosts a virtual conference within the metaverse. Participants from around the world can access the conference through their virtual avatars. They can attend keynote speeches, panel discussions, and networking events in virtual conference halls
Data Visualization and Analytics	A company utilizes the metaverse to offer advanced data visualization and analytics tools to financial professionals. Their virtual analytics platform allows users to visualize complex financial data in interactive and immersive 3D environments. Users can explore data trends, conduct simulations, and analyze financial performance through intuitive interfaces within the metaverse

CHAPTER 13: Group Audit

➤ Introduction

Consolidated Financial Statement (CFS):	- CFS are financial statements of a group presented as those of a single entity. AS-21 & IND AS-110 lays down the principles & procedures for preparation and presentation of CFS. - CFS are presented, to the extent possible, in the same format as adopted by the parent for its separate financial statements - An entity which prepares CFS, might be required to engage the auditor to conduct of audit of CFS. Audit can be conducted by statutory auditor of parent company. - Can be prepare either suo-moto or require by L&R <table><tr><th colspan="5">Consolidated Financial Statements include</th></tr><tr><td>Consolidated balance sheet</td><td>Consolidated statement of P&L</td><td>Consolidated cash flow statement</td><td>Consolidated statement of change in equity (if applicable) and</td><td>Any explanatory notes annexed to, or forming part thereof</td></tr></table>	Consolidated Financial Statements include					Consolidated balance sheet	Consolidated statement of P&L	Consolidated cash flow statement	Consolidated statement of change in equity (if applicable) and	Any explanatory notes annexed to, or forming part thereof
Consolidated Financial Statements include											
Consolidated balance sheet	Consolidated statement of P&L	Consolidated cash flow statement	Consolidated statement of change in equity (if applicable) and	Any explanatory notes annexed to, or forming part thereof							
CFS Mandatory under Companies Act:	- According to Section 129(3) of the Companies Act, 2013, where a company has one or more subsidiaries, including associate company and joint venture, it shall, in addition to its own financial statements prepare a CFS of the company and of all the subsidiaries in the same form and manner as that of its own. - The CFS shall also be approved by the Board of Directors before they are signed on behalf of the Board, along with its standalone FS and shall also be laid before the annual general meeting of the company along with the laying of its standalone financial statement. - The company shall also attach along with its financial statement, a separate statement containing the salient features of the FS of its subsidiary's in Form AOC-1. - According to the Companies (Accounts) Rules, 2014, the consolidation of FS of the company shall be made in accordance with Schedule III to the Act and the applicable A.S. - However, If company which is not required to prepare CFS under Accounting Standards, it shall be sufficient if company complies with provisions of consolidated FS provided in S- III										

➤ **Exemption to prepare CFS:** The requirement related to preparation of CFS shall not apply to a company if it meets the following conditions:-

As per Companies Act:	- It is a Wholly Owned Subsidiary or is a partially subsidiary of another company & All its other members, including those not otherwise entitled to vote Having been intimated in writing for which the proof of delivery of such intimation is available with the company, Do not object to the company not presenting CFS, & - It is a company whose securities are Not Listed or are not in the process of listing on any stock exchange whether in India or outside India, & - Its Ultimate or any Intermediate Holding Co Files CFS with the registrar which are in compliance with the applicable accounting standards
As per AS 21:	<u>Subsidiary be excluded from consolidation when:</u> - Control is intended to be temporary, Or - Operates under severe long-term restrictions which significantly impair its ability to transfer funds to parent
As per IND AS 110:	In accordance with IND-AS 110, parent company has to <u>prepare CFS even if the Control is temporary but,</u>



- **Investment entity** need not present CFS If it is required to measure all of its subsidiaries at fair value through profit & loss (**FVTPL**)
(parent of an investment entity shall consolidate all entities that it controls including those controlled through an investment entity subsidiary unless parent itself is investment entity)

Definition: An Investment Entity is an entity that-

- Obtain funds from **one or more investors** for the purpose of providing those investors with investment management services, &
- Commits to its investors that its business purpose is to invest funds **solely for returns from capital appreciation, investment income**, or both, &
- Measures & evaluate the performance of substantially All of its investments on a **fair value** basis

Q1. Please elaborate on the **situations** wherein **requirement** related to preparation of **consolidated FS may not apply**.

Hint: Refer above "**Exemption as per Companies act**"

Q2. **Whether preparation of consolidated FS is mandatory?** If yes, elaborate the requirements under the statute.,
Q. elaborate the situations wherein the requirement related to preparation of consolidated FS may not apply.

Hint: → refer Above "**CFS Mandatory under Companies Act**" &

Explain Exception to prepare CFS as per Companies Act (As explained in above notes)

Q3. H Ltd is an **Investment Company** following **Ind AS**. Company obtains funds from various investors and commits its **performance for fair return and capital appreciation** to its investors. Company had invested 25% in S1 Ltd., 50% in S2 Ltd. and 60% in S3 Ltd.. Whether there would arise any need to consolidate accounts of any such investee companies with those of H Ltd **as per Sec 129(3)** of Co Act, 2013 which **contains no exclusion from consolidation**.

Hint: → **Explain Sec 129(3)** → where a company has one or more subsidiaries..... in addition to own FS

- **Explain Exception to prepare CFS as per Companies Act (Given in Above notes)**
- Further, the CFS shall be made **as per S-III & applicable AS**. → However, → company which is not required to prepare CFS under AS, it shall be sufficient if company complies with provisions on CFS provided in S-III.
- However, **an investment entity need not present CFS** if it is required, in accordance with Ind **AS 110**.
(Provide "**Definition of Investment Entity**" i.e., **one or more investor, solely for return, fair value.....**)
- **Explain Given case (same as Qn)** → i.e., H Ltd is an investment → **Ind AS** applicable → **Company is not required to prepare CFS** however, for the compliance of Companies Rules, 2014, → **sufficient if company comply S-III**.

Q4. R Ltd. **owns 51% voting power** in S Ltd. It however, holds and discloses all the **shares** as "**Stock-in-trade**" → shares are held **exclusively for subsequent disposal**. → **can it be excluded from the consolidation?** (**Important**)

Hint:

- **CFS As per Ind AS 110**, there is **no such exemption for 'temporary control'**, → It states that "**Consolidation shall begin from the date the investor obtains control of the investee & cease when the investor loses control of the investee**".
- **However, as per Section 129(3)** of Co Act, 2013 → where a company having subsidiary, which is not required to prepare CFS under the AS, it shall be **sufficient if company complies Schedule III** to the Act
- In given case, R Ltd **intention is to dispose off the shares** → **control is temporary**, → R Ltd. is **required to prepare Consolidated FS in accordance with Ind AS 110** as exemption for 'temporary control' is not available in Ind AS 110.

Q5. M Ltd. **acquired 51 % shares of S Ltd. on 01-04-2020** and sold 25% of these shares **during the financial year 2020-21**. Not preparing Consolidated FS on plea that the **control was only temporary**..

Hint: → **Refer Above Qn, Same Answer**

Q6. A Ltd. holds the **ownership of 10% of voting power** and **control over the composition of Board of Directors** of B Ltd. → what factors would be considered by the statutory auditors of A Ltd for the audit of CFS as per Ind AS?

Hint:



- **10% Voting Power and Control over the composition of Board of Directors**
- In such a case, → it would consolidate B Ltd in its consolidated FS as a **subsidiary**.
- The auditor should **verify A Ltd's management's assessment of having control in B Ltd despite having only 10% voting power** as per the requirements of Ind AS 110. → how A Ltd controls the composition of the BOD.
- **There can be various means by which such kind of control can be established.** → the auditor may verify **minutes of Board meetings, shareholder agreement, parent might have provided any technology or know how**, etc
- Further, → **verify that the adjustments warranted by Ind AS 110 have been made** and have been **properly authorised by the mngt of the parent**. → permanent & current period **consolidation adjustments**. → make plan for the understanding of **a/cing policies** of the A Ltd and B Ltd & determining **NTE of the audit procedures** etc.
- Further, Follow **SA 550 on Related Parties**. → the auditor should review information provided by the mngt of the entity identifying the names of all known related parties.
- In forming an opinion on the FS → the auditor shall evaluate whether the **identified related party (RPR/RPT) have been appropriately accounted for and disclosed in accordance with Ind AS 110 and Schedule III**

Q7. S Ltd. is an intermediate subsidiary of JRS Ltd in Surat. → Explain any 2 reasons which are considered by Auditor for exclusion of components from the consolidated FS and reporting of reasons of exclusion [Old]

Hint:

- Reason For Exclusion:
 - Under A.S → 2 reasons for exclusion → i.e., **temporary Control Or, long-term restrictions**.
 - Similarly, under the Companies Act, 2013, **intermediate subsidiary** in India is not required to present CFS.
 - Ind AS 110 also prescribes certain criteria where CFS are not required.
- In such cases, the auditor should satisfy himself that the exclusion made by the management falls within these categories, (i.e., If **temporary Control** → the auditor should verify that the **intention of the parent, to dispose off the shares**, in the near future, **existed at the time of acquisition**)
- The auditor should also **verify that the reasons for exclusion are given in the notes of CFS**. If an entity is excluded from the CFS for reasons other than those allowed by the applicable FRF, → Affect auditor's report

➤ **Responsibility of Parent & Auditor for CFS**

Responsibility of Parent: (Special Trick :-)	Q8. Write a short note on: Responsibility of holding company for preparation of CFS. The responsibility for preparation & presentation of CFS, is of the mngt of parent. This includes: Identifying components, and including the financial information of the components to be included in the consolidated financial statements; Obtaining accurate and complete financial information from components; - Identifying related parties and related party transactions for reporting; - Where appropriate, identifying reportable segments for segmental reporting; - Making appropriate consolidation adjustments; Harmonization of accounting policies and accounting framework; and GAAP conversion, where applicable
Responsibility of Auditor: (Auditor's Objective) (Special Trick :-)	Q9. Write short note on Auditor's objectives in an audit of CFS. The auditor's objectives in an audit of consolidated financial statements are: - The auditor should also validate the requirement of preparation of CFS for the company as per applicable financial reporting framework. - To satisfy himself that the consolidated financial statements have been prepared in accordance with the requirements of applicable financial reporting framework; - to enable himself to express opinion on true and fair view presented by the CFS; - to enquire into the matters as specified in section 143(1) of the Companies Act, 2013; - to report on the matters given in the clauses (a) to (i) of section 143(3) of the Companies Act, 2013, for other matters under section 143(3)(j) read with rule 11 of the Companies



	(Audit and Auditors) Rules, 2014, to comment on the matters specified in sub-rule (a),(b) and (c), (d), (e), (f), (g) to the extent applicable;
Responsibility of Auditor to Follow SA's, Guidance Note:	Follow SA, Statements and Guidance Notes on auditing matters issued by ICAI in the same manner to audit of consolidated financial, Means Auditor is expected to: plan work to enable them to conduct an effective audit in efficient & timely manner; obtain an understanding of the accounting and internal control systems including IT system like consolidation tool, sufficient to plan the audit and determine the nature, timing and extent of his audit procedures. Such an understanding would help the auditors to develop an effective audit approach; use professional judgement to assess audit risk and to design audit procedures to ensure that the risk is reduced to an acceptable level, etc.

Consideration because:	- CFS is prepared using SFS → which may be audited by another auditor. - CFS also include some "other Financial Information" (i.e., some additional disclosure in CFS, proportion of item of SFS, different a/cing policy, subsequent events) which are not covered in SFS - Component auditor sometime request to assist principal auditors → that assignment will be consider as separate assignment than component audit.
Materiality Consideration:	Q10. Describe the relevance of SA 600 while auditing consolidation of Financial Statements. Q. 3 subsidiaries, Other Auditors appointed for the subsidiaries. W.r.t determination of materiality during CFS audit, what should be considerations of Principal Auditor? (May'22 - Old) <u>Answer:</u> CA. H should consider the requirement of SA 600, "Using the Work of Another Auditor", if he decides to use the work of another auditor i.r.t audit of CFS, comply with SA 600. For audit of standalone FS, the computation of materiality for the purpose of issuing an opinion on the standalone FS of each component would be done component-wise on a standalone basis. However, with regard to <u>determination of materiality during the audit of consolidated financial statements (CFS), the auditor should consider the following:</u> - The auditor is required to compute the materiality for the group as a whole. This materiality should be used to assess the appropriateness of the consolidation adjustments (i.e. permanent consolidation adjustments and current period consolidation adjustments) that are made by the management in the preparation of CFS. - The principal auditor also computes materiality for each component and communicates to the component auditor, if he believes is required for true and fair view on CFS. - The parent auditor can also use the materiality computed on the group level to determine whether the component's FS are material to the group to determine whether they should scope in additional components, and consider using the work of other auditors as applicable. - The principal auditor also obtains certain confirmations from component auditor like independence, code of ethics, certain information required for consolidation and disclosure requirements etc. However, while considering the observations (for instance modification and /or emphasis of matter in accordance with SA 705/706) of the component auditor in his report on the standalone FS, the principles of SA 600 need to be considered, the parent auditor should comply with the requirements of SA 600. Therefore, the concept of materiality would be considered while considering the observations of the component auditor



Q11. T Ltd. is holding 68% share of B Ltd, statutory auditors of B Ltd. qualified the report of B Ltd. due to material discrepancies in standalone FS. While framing the opinion on Consolidated FS of T Ltd., RS & Co. (Principal Auditor) have ignored the qualification of B Ltd. as it not material at Group Level. (Old- May'22)

Hint: → Refer Above "Materiality Consideration" (Write full topic & all the points)

In case principal auditor is satisfied that It's not material at Group level, then Yes, Can Ignore. (Otherwise RS & Co. cannot ignore the qualification of B Ltd. while framing the opinion on CFS of T Ltd.)

➤ Auditing The Consolidation

Completeness of Component: (Special Trick :-)	Q12. Auditor has to verify that all the components have been included in the Consolidated FS. State the procedures to be followed by Auditor i.r.o completeness of this information. <u>Procedures to be followed by CA. Vimal in respect of completeness of this information:</u> - Review the parent's procedures for identification of various components; - make inquiries of the management to identify any new components or any component which goes out of consolidated financial statements; - Review the investments of parent as well as its components to determine the shareholding in other entities; - Review the joint ventures and joint arrangements as applicable; - Review the other arrangements entered into by the parent that have not been included in the consolidated financial statements of the group; - Identify the changes in shareholding that might have taken place during reporting period. - Review his working papers for the prior years for the known components - Review the statutory records maintained by the parent, for example registers under section 186, 190 of the Companies Act, 2013;
If any Component Excluded:	Auditor should obtain a listing of all the components included in CFS → verify that all the components have been included in the CFS unless these components meet criterion for exclusion (i.e., Component exception criteria of AS 21, Ind As 110, S-III) → auditor should satisfy himself that the exclusion made by the management falls within these categories → if criteria not satisfied → it will affect audit report.
Plan Audit of CFS: [Jis "PC/IT system" pe "accounting" hoti hai, Uspe "Auditor" apne "Audit Procedure" lagaega]	Before commencing an audit of consolidated financial statements, the auditor should plan his work, The auditor should make plans, among other things, for the following: Understanding of the group structure and group-wide controls including assessment of Information Technology (IT) system and related general and applications IT related controls (manual and automated) for consolidation process; understanding of accounting policies of the parent and its components as well as of the consolidation process including the process of translation of FS of foreign components; Determining and programming the NTE of the audit procedures to be performed based on the assessment of the risk of material misstatement in consolidation process; Determining the extent of use of other auditor's work in the audit; and coordinating the work to be performed.
Some Points to Note:	CFS are prepared using the separate FS of the parent and its components and also other financial info., which might not be covered by the separate FS of these entities. - It may happen that while working out the permanent consolidation adjustments, in the case of one subsidiary, goodwill arises and in the case of another subsidiary, capital reserve arises. The parent may choose to net off these amounts to disclose a single amount in the consolidated balance sheet where permitted by the applicable financial reporting framework. In such cases, the auditor should verify that the gross amounts of goodwill and capital reserves arising on acquisition of various subsidiaries have been disclosed in the notes to the



consolidated financial statements to reflect the excess/shortage over the parents' portion of the subsidiary's equity.

- 3) **In Case of NCI Share of Loss is more than NCI Equity:** Apart from verifying that the calculation and disclosures regarding minorities/NCI have been made appropriately, any further losses applicable to the minority interest, have been **accounted for in accordance with the relevant accounting standards**.
- 4) **Verify that the adjustments** as required by AS/Ind AS → **approved by Parent's mngt**
- 5) The auditor should **also pay attention to off balance sheet entities** which **sometimes do not qualify for the definition of subsidiary**, **de-facto control should also be considered** [means an investor with less than majority of the voting rights has the practical ability to direct the relevant activities unilaterally]
- 6) **Goodwill arises due to consolidation** → Need to **test for impairment at every B/s date**
- 7) **Loss on Goodwill arise is on Foreign Currency** → Need to be **adjusted from currency translation reserve**
- 8) **In case Harmonization of A/cing policy** for CFS preparation is **Not Possible:**
Under AS 21 → Adequate Disclosure require
Under Ind-AS 110 → Adjustment require in CFS

➤ Special Considerations

Permanent Consolidation Adjustments:

Q13. Write short note on Permanent Consolidation adjustment

Permanent consolidation adjustments are those adjustments that are **made only on the first occasion or subsequent occasions in which there is a change in the shareholding** of a particular entity which is consolidated. Permanent consolidation adjustments are:

- (i) Determination of **goodwill or capital reserve** as per applicable accounting standards
- (ii) Determination of **amount of equity attributable to minority/NCI**

Auditor Shall Verify above calculations have been made appropriately:

- Auditor should pay particular attention to determination of **pre-acquisition reserves** of the components. **Date(s) of investment** in components assumes importance for this.
- The auditor should also examine whether the **pre-acquisition reserves** have been **allocated appropriately** between the parent and the minority interests/ non-controlling interests of the subsidiary.
- The auditor should also **verify the changes** that might have taken place in these permanent consolidation adjustments on account of **subsequent acquisition** of shares in the components, **disposal of the components** in the subsequent years

Current Period Consolidation Adjustments:

Q14. During CFS Audit, which current period consolidation adjustments are to be Consider?

Current period adjustments are those adjustments that are made in the accounting period for which the consolidation of financial statements is done.

Current period consolidation adjustments primarily relate to elimination of intra-group transactions and account balances including:

- (a) **intra-group interest** paid and received, or management fees, etc.;
- (b) **intra-group indebtedness**;
- (c) **unrealised intra-group profits on assets acquired/ transferred** from/ to other subsidiaries;
- (d) **record deferred taxes** on unrealised intercompany profits elimination as per Ind AS 12;
- (e) **adjustments of deferred tax on account of temporary differences** arising out of



- elimination of profit and losses resulting from intragroup transactions and undistributed profits of component in case of CFS prepared under Ind AS.
- (f) adjustments to the financial statements (of the parent and the components being consolidated) for recognized **subsequent events or transactions** that occur between the balance sheet date and the date of the auditor's report on the consolidated financial statements of the group.
- There are two types of subsequent events:**
- (i) The first type of subsequent events consists of events or transactions that provide additional evidence about conditions that existed at the date of the FS, including the estimates inherent in the process of preparing FS (**i.e. adjusting events**).
- (ii) The second type of subsequent events consists of events that provide evidence about conditions that did not exist at the date of the financial statements but arose subsequent to that date (**i.e. non-adjusting events**).
- (g) adjustments for the effects of significant transactions or other events that occur between the date of the components balance sheet and not already recognised in its financial statements and the date of the auditor's report on the group's consolidated financial statements when the financial statements of the component to be used for consolidation are not drawn upto the same balance sheet date as that of the parent;
- (h) adjustments related to **harmonising the different accounting policies** being followed by the parent and its components;
- (i) **In case of a foreign component, adjustments to convert** a component's audited **financial statements** prepared under the component's **local GAAP** to the GAAP under which the consolidated financial statements are prepared;
- (j) **determination of movement in equity attributable to the minorities interest**/non controlling interest since the date of acquisition of the subsidiary. It should also be noted that under Ind AS, non-controlling interest can also result in negative balance. Unlike earlier AS, as per paragraph 28 of Ind AS 27, if the net worth of subsidiary is negative, non controlling interest could have deficit balance;

The **adjustments required for preparation of CFS are made in memorandum records** kept for the purpose by the parent. The auditor should review the memorandum records to verify the adjustment entries done for CFS.

➤ **Difference Between CFS Date & Component FS Date**

- The **financial statements of the components** used in the consolidation should be **drawn up to the same reporting date as that of the parent**.
- **If it is NOT practicable** to draw up the financial statements of one or more components **to such date** and, accordingly, those financial statements are **drawn up to different reporting dates**, adjustments should be made for the effects of significant transactions or other events that **occur between those dates** and the date of the parent's financial statements

Difference between reporting dates should **not** be **more than 6 months** in case of financial statements **under AS** and

And **3 months** in case of financial statements under **Ind AS**

- **Auditor of the CFS is responsible** to **review other components' results** between its
 - ✓ Financial reporting date of component and
 - ✓ that of the parent

For significant transactions or other events that **have taken place during the period** and, therefore, need to be reflected in the consolidated financial statements

➤ **Disclosure which is Not Required in Case of CFS:**

Q15. In Subsidiary FS, many information is given. The principal auditor is of the view that only those info should form part of the notes to the consolidated FS which are relevant at group level. Please mention any 5 aspects which are given in notes to the separate FS, need not be included in consolidated FS

Answer: Ind AS 110 does not give a list, However Sec 129(4) & circular issued by MCA Provides → information which is part of the separate FS but that need NOT be reported in the notes of consolidated FS, in consolidated FS under Ind AS, only those disclosures should be given which are relevant to consolidated FS.

Following given in notes to separate FS of parent/subsidiary, need not be included in the consolidated FS:

[Trick: aajkal to Chote chote "MSME" bhi "Shares Issue" karke "Money" le lte .. "Foreign Investor" se bhi hai, Fir unhe "Foreign Currency me "Dividend" bhi Dena padta h, Par uss Paise se apan "Foreign Currency me hi Expenditure" "Import" & "Export karke foreign currency earn bhi karte hai]

- (i) Disclosure required under **Micro, Small and Medium Enterprises** Development Act, 2006.
- (ii) Source from which **bonus shares** are issued, e.g., capitalization of profits or reserves or from securities premium account.
- (iii) Disclosure of all **unutilized monies out of the issue** indicating the form in which such unutilized funds have been invested
- (iv) A **statement of investments** (whether shown under "financial assets or non-financial assets as stock-in-trade) separately classifying trade investments and other investments, showing the names of the bodies corporate (indicating separately the names of the bodies corporate under the same management) in whose shares or debentures, investments have been made (including all investments, whether existing or not, made subsequent to the date as at which the previous balance sheet was made out) and the nature and extent of the investment so made in each such body corporate.
- (v) The **amount remitted during the year in foreign currencies** on account of **dividends**, with a specific mention of the number of non-resident shareholders, the number of shares held by them on which the dividends were due and the year to which the dividends related.
- (vi) **Expenditure in foreign currency** during the financial year on account of royalty, knowhow, professional and consultation fees, interest, and other matters.
- (vii) Value of **imports calculated on C.I.F.** basis by the company during the financial year in respect of:
 - a) raw materials;
 - b) components and spare parts;
 - c) capital goods.
- (viii) **Value of all IMPORTED raw materials**, spare parts and components **consumed** during the financial year and the **value of all INDIGENOUS** (Non-Imported) **raw materials**, spare parts and components similarly **consumed** and the **percentage of each to the total consumption**.
- (ix) **Earnings in foreign exchange** classified under the following heads, namely:
 - (a) export of goods calculated on F.O.B. basis;
 - (b) royalty, know-how, professional and consultation fees;
 - (c) interest and dividend;
 - (d) other income, indicating the nature thereof.

➤ **Additional Disclosure/Info Require in Case of CFS (w.r.t Component):**

Following information is also required to be disclosed in the consolidated financial statements separately for the parent and each of its components (including foreign component) which has been consolidated:

- a) amount of **net assets and net assets as a percentage** of consolidated net assets;
- b) amount of **share in profit or loss** and the % share in P&L as a percentage of consolidated P&L;



- c) amount in **other comprehensive income (OCI)** and the % of OCI as a percentage of Consolidated OCI

➤ **Management Representation:**

Q16. CA. Kajal Gupta is nearing completion of audit of CFS. She requires WR from the parent → What matters ?

Answer: → Examples of such representations include:

SA 580, Mngt of parent acknowledges its responsibility for a true & fair presentation of CFS in accordance with FRF. In addition, the auditor of CFS obtains W.R from parent mngt on matters material to the CFS.

[har "segment identify" karke "complete" FS banare ho n? kyuki ye sab "R.P" h To "adjustment" risky ho sakte h...]

- 1) **Completeness** of components included in the CFS
- 2) **Identification of reportable segments** for segmental reporting;
- 3) Identification of **related parties** and related party transactions for reporting;
- 4) Appropriateness and **completeness of permanent and current period consolidation adjustments**, including the elimination of intra-group transactions.

➤ **Audit Considerations & Reporting**

Q17. As an auditor, how will you draft the report in case:

- (a) When the Parent's Auditor is also the Auditor of all its Components?
- (b) When the Parent's Auditor is not the Auditor of all its Components?
- (c) When the Component Auditor Reports on FS under an Accounting Framework Different than of the Parent?
- (d) When the Component(s) Auditor Reports under an Auditing Framework Different than that of the Parent?
- (e) Where the financial statements of one or more components is not audited?

Answer: Different cases of Drafting the Report

When the Parent's Auditor is also the Auditor of all its Components (AS & T/F)	<u>While drafting the audit report, the auditor should report :</u> - Whether principles and procedures for preparation and presentation of consolidated FS as laid down in the relevant accounting standards have been followed. - In case of any departure or deviation, the auditor should make adequate disclosure in the audit report so that users of the CFS are aware of such deviation. - Auditor should issue an audit report expressing opinion whether the consolidated FS give a true and fair view of the state of affairs of the Group as on balance sheet date and as to whether consolidated P&L statement gives true and fair view of the results of consolidated profit or losses of the Group for the period under audit. - Where the CFS also include a cash flow statement, the auditor should also give his opinion on the true and fair view of the cash flows presented by the consolidated cash flow statements.
When the Parent's Auditor is not the Auditor of all its Components:	Q18. Reporting in case parent company's auditor is not auditor of all components. - In a case where parent's auditor is not the auditor of all the components included in the CFS, the auditor of the CFS should also consider the requirement of SA 600. - As prescribed in SA 706 "EOM & OM Para", if the auditor considers it necessary to make reference to the audit of the other auditors, the auditor's report on the CFS should disclose clearly the magnitude of the portion of the FS audited by the other auditor(s). - This may be done by stating aggregate rupee amounts or % of total assets, revenues and cash flows of components included in the CFS not audited by the parent's auditor. Total assets, revenues and cash flows not audited by the parent's auditor should be presented before giving effect to permanent and current period consolidation adjustments. Reference in the report of the auditor on the CFS to the fact that part of the audit of the group was made by other auditor(s) is not to be construed as a qualification of the



	opinion but rather as an indication of the divided responsibility between the auditors of the parent and its subsidiaries.
When the Component(s) Auditor Reports on FS under an Accounting Framework Different than that of the Parent:	The parent may have components located in multiple geographies outside India applying an accounting framework (GAAP) that is different than that of the parent in preparing its FS. (such as US GAAP or IFRS) or the local GAAP of the jurisdiction of the component. → Local component auditors may be unable to report on FS prepared using the parent's GAAP because of their unfamiliarity with such GAAP. - When a component's FS are prepared under an accounting framework that is different than that of the framework used by the parent in preparing group's CFS, the parent's mngt perform a conversion of the components' audited FS from the framework used by the component to the framework under which the CFS are prepared. The conversion adjustments are audited by the principal auditor to ensure that the financial information of the component(s) is suitable and appropriate for the purposes of consolidation. - A component may alternatively prepare FS on the basis of the parent's accounting policies, as outlined in the group accounting manual, to facilitate the preparation of the group's consolidated FS. The group accounting manual would normally contain all accounting policies, including relevant disclosure requirements, which are consistent with the requirements of the financial reporting framework under which the group's CFS are prepared. The local component auditor can then audit and issue an audit report on the components FS prepared in accordance with "group accounting policies". - When applying the approach of using group accounting policies as the financial accounting framework for components to report under, the principal/parent auditors should perform procedures necessary to determine compliance of the group accounting policies with the GAAP applicable to the parent's financial statements. This ensures that the information prepared under the requirements of the group accounting policies will be directly usable and relevant for the preparation of CFS by the parent entity, eliminating the need for auditing by the auditor, the differences between the basis used for the component's FS and that of the CFS. The principal auditor can then decide whether or not to rely on the components' audit report and make reference to it in the auditor's report on the CFS.
When the Component(s) Auditor Reports under an Auditing Framework Different than that of the Parent:	Normally, audits of financial statements, including consolidated financial statements, are performed under auditing standards generally accepted in India ("Indian GAAS"). In order to maintain consistency of the auditing framework and to enable the parent auditor to rely and refer to the other auditor's audit report in their audit report on the consolidated financial statements, the components' financial statements should also be audited under a framework that corresponds to Indian GAAS
Components Not Audited:	Generally, the FS of all components included in CFS should be audited or subjected to audit procedures in the context of a multi-location group audit. Such audits and audit procedures can be performed by the auditor reporting on the CFS or by the components' auditor. Where the FS of one or more components continue to remain unaudited, the auditor reporting on the CFS should consider unaudited components in evaluating a possible modification to his report on the CFS. The evaluation is necessary because the auditor (or other auditors, as the case may be) has not been able to obtain SAAE in relation to such consolidated amounts/balances. In such cases, the auditor should evaluate both qualitative & quantitative factors on the possible effect of such amounts remaining unaudited when reporting on the consolidated financial statements using the guidance provided in SA 705, "Modifications to the Opinion in

➤ Integrated Qns:

Q19. R Limited is a listed company. The company is having investment in the following components:

2 Subsidiary Companies	1 Joint Venture (JV)	2 Associate	3 Business entities under common control
Interest in assets , liabilities, revenues, and expenses in a joint operation with 1 Company			

While preparing **consolidated FS as per Ind As**, R Limited consolidated its components on a **line-by-line** basis by adding together like items of assets, liabilities, income, expenses, and cash flows. (SM & Old Exam)

Hint: For consolidation of subsidiaries in accordance with Companies (IND-ASs) Rules, 2015:

- Ind AS 110 → FS of parent & **subsidiaries** are combined as, "CFS" on a **line-by-line** basis by adding together
- Ind AS 103 → Calculate **goodwill/ capital reserve** (or gain on bargain purchase) and non-controlling interest
- Ind AS 103 → Business combinations of entities under **common control**, accounted using **pooling of interest**
- Ind AS 110 → Adjustments like **elimination of intra-group** transactions, balances, unrealised profits & DTA etc
- Ind AS 28 → **Associates & JV's** are accounted for using the **Equity Method** (Ind AS 28).
- Ind AS 111 → **Interests in assets, liabilities**, revenues, & expenses in a **joint operation** are accounted for as **part of separate FS** of the entity in accordance with Ind AS 111, "Joint Arrangements".
- Ind AS 103 → in a business combination achieved in stages, the acquirer shall **remeasure its previously held equity interest** in the acquiree at its acquisition-date **fair value** and recognise the resulting gain or loss, if any, in profit or loss or other comprehensive income

In given Case, R Ltd have Subsidiary, JV's, Associate, common control etc..... → **In view of above, R Limited consolidated its components on a line-by-line basis**, which is correct for the subsidiaries, however for other companies, It is **not correct**.

Q20. CA.MV Chitale is auditor of consolidated FS of "D and D Limited". The consolidated FS consist of **8 subsidiaries** audited by other auditors. Following further info. is also available i.r.o these 8 subsidiaries:

Total assets → Rs. 1500 crore	Total revenues → Rs. 1000 crore	Net cash outflows → Rs. 10 Crore

Out of above, **2 Subsidiaries** are located outside India (whose FS have prepared as per **A/cing principles of respective countries** & audited by other auditors under auditing standards of respective countries.

Where & how such info should be included in auditor's report on consolidated FS? draft a suitable para (SM)

Answer:

Where parent's auditor is not the auditor of all the components included in the consolidated FS, Then → **SA 706**, → **Make reference to the audit of the other auditors**, the auditor's report on consolidated FS should disclose clearly the magnitude of the portion of the FS audited by the other auditors. This may be done by stating aggregate rupee amounts or % of total assets, revenues & cash flows of components included in the consolidated FS not audited by the parent's auditor.

It should be included in "**Other Matter paragraph**" of auditor's report:

Other Matter Paragraph

We did not audit the FS and other financial information, in respect of eight (8) subsidiaries, whose financial statements include total assets of Rs.1500 crores as at March 31, 2023, and total revenues of Rs.1,000 crores and net cash outflow of Rs. 10 crores for the year ended on that date. These FS and other financial information have been audited by other auditors and such FS, other financial information and auditor's reports have been furnished to us by the mngt of the Holding Company.

Our opinion on the consolidated FS, in so far as it relates to the amounts and disclosures included in respect of these subsidiaries and joint ventures, and our report in terms of sub-sections (3) of Section 143 of the Act, in so far as it relates to the aforesaid subsidiaries is based solely on the reports of such other auditors.

Two of these subsidiaries are located outside India whose FS and other financial information have been prepared



in accordance with accounting principles generally accepted in their respective countries and which have been audited by other auditors under generally accepted auditing standards applicable in their respective countries. The Holding Company's management has converted the FS of such subsidiaries from accounting principles generally accepted in their respective countries to accounting principles generally accepted in India.

We have audited these conversion adjustments made by the Holding Company's management. Our opinion in so far as it relates to the balances and affairs of such subsidiaries is based on the report of other auditors and the conversion adjustments prepared by the Mngt of the Holding Company and audited by us. Our opinion on the consolidated FS, and our report on Other Legal and Regulatory Requirements is not modified in respect of the above matters w.r.t our reliance on the work done and the reports of the other auditors and the FS and other financial information certified by the Management.

CHAPTER 14.1: Audit of Banks

➤ Introduction:

Banks have certain characteristics distinguishing them from most other commercial enterprises: <u>(RV-Cold)</u> <u>Bank have AC..lead to cold</u>	• Regulatory requirements by governmental authorities often influence accounting and auditing practices in the banking sector. • Custody of large Volumes of monetary items, including cash and negotiable instruments, whose physical security has to be ensured • Engagement in a large volume and variety of transactions in terms of number and value which necessarily require Complex accounting and internal control systems and widespread use of Information Technology (IT) • Assumption of significant commitments without any transfer of funds. These items, called 'Off-balance sheet' items, may at times not involve accounting entries and the failure to record such items may be difficult to detect. • Engagement in transactions that are initiated at one location, recorded at a different location and managed at yet another location. • Direct Initiation and completion of transactions by the customer without any intervention by the bank's employees. For example, over the Internet or mobile or through automatic teller machines (ATMs).
Special audit considerations arise in the audit of banks because of: <u>(Dr. VPN)</u>	Q1. Banks, because of certain characteristics, are distinguished from other commercial enterprises and hence it needs special audit consideration ? • the extensive Dependence on IT to process transactions • the effect of the statutory and Regulatory requirements; • Voluminous: the scale of banking operations and the resultant significant exposures which can arise within short period of time; • the Particular nature of risks associated with the transactions undertaken; • Continuing development of New products and services and banking practices which may not be matched by the concurrent development of accounting principles & auditing practices. Evolution of technology and providing services through Net Banking and Mobiles has exposed banks to huge operational and financial risk
Special Considerations in IT Environment: <u>(Special Trick :-)</u>	Overall review of IT Environment & Computerised accounting system has to be taken care at HEAD OFFICE level, as branch auditor do not have access to IT Policy & processes implemented by bank, Hence Central statutory auditor is responsible for it (i.e, Obtain understanding of IT Environment & evaluate that Controls are operating effectively, Hence based on the guidance from SCA, Branch auditor should perform data analysis & CBS review by TOC & substantive sample checking & share the results to SCA) Technological developments have brought new challenges for auditors as audit is required to be conducted through the system, The key security control aspects that an auditor needs to address when undertaking audit in a computerised bank include: • Verify that the account master and balance cannot be modified/amended/alterd except by the authorised personnel • Ensure that the system prevents unauthorised amendments to the programmes • Verify that segregation of duties is ensured while granting system access to users and that the user activities are monitored by performing an activities log review • Verify whether "access controls" assigned to the staff-working match with the



	responsibilities as per manual - Ensure that <u>authorised, accurate and complete data</u> is made available for processing - Verify that charges calculated manually for accounts when function is not regulated through parameters are properly <u>accounted for and authorised</u> - Verify that exceptional transaction reports are being <u>authorised and verified on a daily basis</u> by the concerned officials. It is important for auditor to understand the nature of exception and its impact on financials
Legal Framework for Banks in India:	- Banking Regulation Act, 1949 - Reserve Bank of India Act, 1934 - State Bank of India Act, 1955 - Regional Rural Banks Act, 1976 - Companies Act, 2013 - Information technology act 2000 - Prevention of money laundering act 2002 - Securitization and reconstruction of financial assets & enforcement of security interest 2002, Etc.

➤ FORM AND CONTENT OF FINANCIAL STATEMENTS:

Third Schedule:	Banking company is <u>required to prepare a Balance Sheet and a Profit and Loss Account</u> in the forms set out in the Third Schedule to the Act Form A of the Third Schedule contains the form of: <u>Balance Sheet</u> Form B of the Third Schedule contains the form of: <u>Profit and Loss Account</u>
A.S:	- Needs to <u>comply with the disclosure requirements</u> under the various <u>Accounting Standards</u>, as specified under section 133 of the Companies Act, 2013, Ind AS has been deferred by RBI for all scheduled commercial banks presently.
Branch Audit:	In case of private banks , the processes of accounting are centralized and there is no concept of mandatory branch audit in accordance with RBI guidelines

➤ Audit of Accounts & Appointment of Auditor:

No. of auditor:	Most banks, especially those in nationalized banks or public sector appoint : 4 or more firms of chartered accountants to act jointly as statutory central auditors (SCAs).		
Authority appointing the Auditors?	Generally at:	AGM by shareholder (RBI approval also require)	
	Nationalised bank:	Board of Directors (RBI approval also require)	
	State Bank of India:	Appointed by the Comptroller and Auditor General of India	
	Regional rural banks:	by the concerned bank (With approval of CG)	

➤ CONDUCTING AN AUDIT:

- 1) **Initial Considerations:** Acceptance & Continuance, Declaration of Indebtedness, Terms of Audit Engagements
- 2) **Understanding:** Understanding the Bank and Its Environment including Internal Control
- 3) **Risk Assessment:** Identifying and Assessing the Risks of Material Misstatements
- 4) **Execution**
- 5) **Reporting:** Independent Auditor's Report, Long Form Audit Report etc

Understanding involves - **Understanding the Risk Management Process** :An effective risk management system in a bank generally requires the following:

1) Monitoring activities:	<u>Risk management models, methodologies</u> and assumptions used to measure and manage risk <u>should be regularly assessed</u> and updated.



2) Reliable info. systems:	Banks require reliable information systems That provide adequate financial, operational and compliance information on a timely and consistent basis
3) Oversight by TCWG:	Those charged with governance written risk management policies . The policies should be consistent with the bank's business objectives and strategies, capital strength, management expertise, regulatory requirements and the types and amounts of risk it regards as acceptable.
4) Identification, measurement and monitoring of risks:	Risks that could significantly impact the achievement of bank's goals should be identified, measured and monitored against pre-approved limits and criteria
5) Control activities:	A bank should have appropriate controls to manage its risks, including effective segregation of duties (particularly, between front and back offices) , accurate measurement and reporting of positions, verification and approval of transactions, reconciliation of positions and results, setting of limits, reporting and approval of exceptions, physical security and contingency planning

➤ **Risk-based Internal audit:**

(Chief audit executive is responsible for RBIA) → Risk-based Internal audit is conducted based upon the **risk assessment of business and control risks** of branches. The risk assessment process includes: -

- Identification of **inherent business risks** in various activities undertaken by branches (**Business risk**)
- Assessment of **effectiveness of control systems** for monitoring inherent risks of business activities of branch (**Control risk**)
- Making an assessment of level and direction of various **risk areas** and assess level and direction of overall business risk and control risk
- Drawing up of risk matrix taking into account factors viz. Risk of branch

➤ **INTERNAL CONTROL IN CERTAIN SELECTED AREAS:**

Clearings:	• Under the Cheque Truncation System (CTS) implemented by RBI, an electronic image of the cheque is transmitted to the paying branch through the clearing house, along with relevant information like data on the MICR band, date of presentation, presenting bank, etc. This effectively eliminates the associated cost of movement of the physical cheques, reduces the time required for their collection. • As per RBI guidelines, the branch is required to either call the customer (Payer) or email him for any cheque received for the amount of ₹ 5 lakh and above in respect of inward clearings. The Auditor may verify the compliance on test check basis. • The Auditor is to check whether signature of the drawer of the cheque is being verified by the staff or not as else there will be liability of the paying bank under all circumstances • The unpaid cheques received in outward clearing should be either sent to the customers at their recorded address or the customers be informed to collect the same from bank branch
Loans and Advances: (Special Trick :-)	<u>Before giving loan:</u> • Bank should make advances only after satisfying the creditworthiness of borrowers and after obtaining sanction from the proper authorities of the bank • All the necessary documents (e.g., agreements, demand promissory notes, letters of hypothecation, etc.) should be executed by the parties before advances are made • All the securities should be received • All securities requiring registration should be registered in the name of the bank or otherwise accompanied by the documents sufficient to give title of the bank • Sufficient margin should be kept against securities taken to cover any decline in the value thereof and to comply with Reserve Bank directives.



	<u>After giving loan:</u> - All accounts should be kept within both the "drawing power" and the "sanctioned limit" as per prescribed norms. Additional <u>temporary limit may be sanctioned</u>, for a maximum of 20% of existing limit and 90 days maximum tenure - The operation (in each advance account) should be reviewed at least once every year.
Credit Card Operation: <i>(banda shopping pe gaya)</i>	Q2. How will you evaluate the I.C System in the area of Credit Card operations of a Bank? - There should be effective screening of applications with reasonably good credit assessments - There should be strict control over storage and issue of cards - There should be a system whereby a merchant confirms the status of unutilised limit of a credit-card holder from the bank before accepting the settlement. - All reimbursement (gross of commission) should be immediately charged to customer's A/c Reimbursement to merchants should be made only after verification of the validity of merchant's acceptance of cards - There should be a system to ensure that statements are sent regularly to the customer - There should be a system to monitor and follow-up customers' payments - There should be a system of periodic review of credit card holders' accounts. On this basis, the limits of customers may be revised, if necessary. The review should also include determination of doubtful amounts and the provisioning

➤ COMPLIANCE WITH CRR AND SLR REQUIREMENTS:

Cash Reserve Ratio (CRR):	Minimum fraction of the total deposits of customers (Demand and Time Liabilities-DTL) , which commercial banks have to hold as reserves either in cash or as deposits with the central bank (RBI). (Liquidity situation - minimum cash reserve.)
Statutory Liquidity Ratio (SLR):	- Every scheduled commercial bank in India is required to maintain in the form of certain liquid assets such as gold, cash and government approved securities <u>before providing credit to the customers</u>. [Kept by Bank themselves, Not With RBI] - Statutory central auditors of banks to verify the compliance with SLR requirements of 12 odd dates in different months of a fiscal year not being Fridays.

➤ **Audit Approach and Procedure to check Compliance with CRR and SLR requirements:**

Q3. As statutory central auditors of a Nationalized bank, what special points are to be borne in mind in the audit of compliance with "Statutory Liquidity Ratio" (SLR) requirements?

General Points: <i>(Special Trick :-)</i> (Margin is security / Deposit taken by bank from borrower, not freely withdrawable) (Since Bills Sold, so risk is already T/F) (DICGC settle claim on Behalf of Failed Bank, so it's temporarily lying with bank)	- Obtain an understanding of the relevant circulars/ instructions of the RBI, particularly regarding composition of items of DTL. - Request the branch auditors to send their weekly trial balance as on Friday and these are consolidated at the head office. Based on this consolidation, the DTL position is determined for every reporting Friday. The statutory central auditor should request the branch auditors to verify the correctness of the trial balances relevant to the dates selected by him/her. The branch auditors should also be specifically requested to examine the cash balance at the branch on the selected dates. - Examine, on a test basis, the consolidations regarding DTL position prepared by the bank with reference to the related returns received from branches. ➤ While examining the computation of DTL, specifically examine that items have been excluded from liabilities as per RBI guidelines. Some items are:- (IC-BUM-DICE - BAD BI) Amounts received in Indian currency <u>against Import bills and held in sundry deposits pending receipts of final rates</u> - Paid up Capital, reserve, any credit balance in profit & loss account of bank, amount of loan



(When exporter failed to repay Loan to bank, ECGC organisation repay it to bank)

(Bank raised some insurance claim, Final amt is Pending to be determine by Court, but In between some adhoc amt paid by insurer to bank)

(Borrower defaulted laon → bank reached to court for Mortgage property dispute, So Bank appointed court receiver to manage property till case is resolved, if any rent income generated, it's temporarily with bank)

(BAF → Bill (like Cheque), issued by Drawer, & bank is liable to pay to Bill Holder on due date .. it's only C.L of bank)

Eg. Saving bank a/c (1 lacs * 3.5% interest)/365 days = Rs. 9.65 Per day int. So, Fortnight Int added = 14 * 9.65 = 134

(During Derivative/ swaps etc. trn. Bank takes some Cash as collateral from party, to mitigate risk, it's refundable when trn. End)

taken from RBI and amount of refinance taken from EXIM bank, NHB, SIDBI and NABARD

- 3) Part amounts of recoveries from the borrowers in respect of debts considered **Bad and doubtful of recovery**.
- 4) **Un-adjusted deposits/balances lying** in link branches for agency business like dividend warrants, interest warrants, refund of application money, etc., in respect of shares/debentures to the extent of payment made by other branches but not adjusted by the link branches.
- 5) **Margins held and kept in sundry deposits** for funded sundry deposits for funded
- 6) Amount received from **DICGC** towards claims held by banks pending adjustments thereof.
- 7) Net **Income tax provision**
- 8) Amount received from **Court receiver**.
- 9) Amount received from **ECGC** by invoking the guarantee.
- 10) **Bills discounted** by a bank with eligible financial institutions as approved by the RBI.
- 11) **Income flows received in Advance** such as annual fees and other charges which are not refundable
- 12) **Net unrealized gain/loss** arising from **Derivatives transactions** under trading portfolio.
- 13) Liabilities on account of utilisation of limit under **Bankers' Acceptance Facility** (BAF)
- 14) Amount received from **Insurance companies** for ad hoc settlement of claims pending judgement of court.

➤ Similarly, specifically examine that the items have been **included in liabilities** as per RBI guidelines. Some of these items are:- **(BAN - IC)**

- 1) **Net credit balance in Branch adjustment accounts** (credit entries in branch adjustment A/c which are O/S for more than 5 years are required to be considered at **gross**)
- 2) **Borrowings from Abroad by banks** in India needs to be considered as 'liabilities to other', the adverse balances in Nostro Mirror Account needs to be considered as 'Liabilities to other'.
- 3) The **reconciliation of Nostro accounts** (Adverse balance) (with Nostro Mirror Accounts) needs to be scrutinized carefully to analyze and ascertain if any inwards remittances are received on behalf of the customers and have remained unaccounted and are pertaining to any liabilities for the bank
- 4) **Interest accrued** on deposits should be **calculated on each reporting fortnight** (as per the interest calculation method applicable to various types of accounts), whether or not such interest is accounted for in books of accounts (included in NDTL)
- 5) **Cash collaterals received** under **collateralized derivative transactions** as these are in the nature of 'outside liabilities'.

➤ While examining the computation of DTL, the auditor may specifically **examine the details of exempted categories** of the following items:

- 1) **Minimum Eligible Credit (EC)** and outstanding **Long-Term Bonds (LB)** → to finance **Infrastructure loans and affordable housing loan**, as per RBI Circular.
- 2) Eligible **Incremental amount of Deposit under FCNR**(Bank) and **NRE A/c** → of **maturities of 3 years & above**. (i.e., Only increased amt of deposit is excluded, but existing is included)
 - ✓ Auditor shall Also **verify** → **Loans given out of funds from FCNR(B)** deposits & inter-bank Foreign Currency (**IBFC**) deposits → **for reporting in Form A** return.
- 3) **Banks should convert their foreign exchange assets/liabilities (including borrowings):**
 - 🌐 in **USD, GBP, JPY and Euro** into → **INR at RBI reference rate**.



- ✚ For other currencies → **New York rate** for converting to **USD** (then USD to INR as above)
- 4) What is Reference rate as per RBI Circular ? :
 - ✚ for INR/USD and other major currencies → reference rate from **FBIL** should be taken.
 - ✚ If rate is not available from **FBIL**, → use **New York** closing rate for converting to **USD**
- Whether, balances of "Branch Adjustment A/c of Foreign branches" are also included in arriving "Net Branch adjustment A/c".
- The auditor should **examine the correctness of data** on sample basis:
 - ✓ in **Form A return** for → CRR and
 - ✓ **Return in Form VIII** for → SLR purposes.
- To check compliance of SLR requirement by SCA, a Considerable part of information required/flow from Branch:
 - ✓ Branch provide required information → then it **consolidated at the regional level**.
 - ✓ **Regional auditor verifies** the accuracy of this consolidated data and reports on it.
 - ✓ The **regional manager** shall Also counter-sign the consolidated statement.
 - ✓ Then the **Central Auditor** will apply the Audit procedure on above Conso. Statement (for bank as whole)
 - ✓ **Where such a procedure is followed → SCA should adequately describe the same in his certificate**
- While reporting on compliance with SLR requirements, the auditor should **specify the number of unaudited branches and state that he/she has relied on the returns received from the unaudited branches** in forming an opinion.
- The auditor at the central level should apply the audit procedures listed above to the overall consolidation prepared for the bank as a whole. Where such procedure is followed, the central auditor should adequately describe the same in the report.

➤ VERIFICATION OF ASSETS:

1) Cash, Balance with RBI, Balance with Other Bank, Money at Short Call:

These items needs to check **existence and completeness** as on date of balance sheet, in most of the branches of bank, there will be **no bank account requiring reporting except in branches with treasury operations**.

Cash:	• Carry out the physical verification of cash, cash at ATM and cash at cash deposit machines) as close to the balance sheet date as possible. • The cash balance as physically verified should be agreed with the balance shown in cash register /balance in CBS
Balance with RBI:	• Verify the ledger balances in each account with reference to the bank confirmation certificates and reconciliation statements as at the year-end. • Review the reconciliation statements: ✓ Cash transactions remaining unresponded (i.e., Reco. Items un-answered by Bank staff) ✓ Revenue items requiring adjustments/write-offs ✓ Other credit and debit entries originated in the statement provided by RBI remaining unresponded for more than 15 days
Balance with Other Banks (Other than Reserve	• Examine that no debit for charges or credit for interest is outstanding and all the items which ought to have been taken to revenue for the year have been so taken. • Examine that no cheque sent or received in clearing is outstanding. • Examine that all bills or outstation cheques sent for collection and outstanding as on the closing date have been credited subsequently. • Examine large transactions in inter-bank accounts to ensure that no transactions have been put through for window-dressing particularly towards the close of year



Bank of India)	The balances with banks outside India should also be verified in the manner described above. These balances should be converted into the Indian currency at the exchange rates prevailing on the balance sheet date

2) Investment: Special-purpose Certificates Relating to Investments:

- Auditor to Examine whether the bank is maintaining separate accounts for the investments made by it on their **own Investment Account**, on **PMS (Portfolio management service) clients'** account, and on behalf of other constituents (including brokers).
- As per the RBI guidelines, banks are required to get their investments under PMS separately audited by external auditors → So, Bank need to prepare separate record for PMS & → external auditor to give Separate certificate for that
- Banks should undertake **half-yearly reviews** (as of 30th Sept and 31st Mar) of their investment portfolio
- Internal auditors should separately conduct the concurrent audit of treasury transactions & its report should be placed before the CMD (Currency management dept) **once every month**. (No need not forward copies of the internal audit report to RBI). However, major irregularities observed in shall be incorporated in the half yearly review of the investment portfolio

Q4. Bank was engaged in providing PMS to its customers. You are statutory auditors of Bank. While verifying PMS transactions you noticed that the bank has **not maintained separate record for PMS transactions?**

Hint: Refer above Point (a) & Point (b) of "Investment" (i.e., Separate account, PMS separately audited)

In the above case the auditor should not verify the PMS transactions and advise the bank to segregate the PMS transactions from its own investments and provide the certificate of external auditor as described above. In case SSP Bank does not provide the same the auditor may report accordingly." **[ANSWER ENDS]**

Examine classification:	- Examine that entire investment portfolio of bank is classified under three categories i.e. HTM, HFT and AFS & shifting of securities is as per regulatory norms & laid down policy - Examine whether the shifting of the investments 'available for sale' to 'held to maturity' is duly approved by the Board of Directors of the bank.

Income recognition norms : Investment	
Performing investment:	On Accrual basis provided that interest rate is pre-defined on instrument (i.e., Debenture, Not equity)
NPI:	Income should be recognised on realization
Dividend:	Accrual basis if same has been declared by corporate body in AGM & shareholder's right to rec payment is established
Units of MF's:	Income from mutual fund should be accounted only on Cash basis

Q5. Statutory Auditors of a Nationalised Bank, Which has **recognised on accrual basis** income from **dividends on securities & Units of Mutual Funds (MF)**. Dividends on securities & Units of MF were **declared after end of FY**.

Hint:

As per AS 9 → Income from dividend to recognize when → dividend declared by company in its AGM & Owner's right to receive payment is established → So in Given Case Accrual Basis is Not in orders (As declared after Yr end) i.e. Income from Govt Securities & Bond/Debenture (Int. rates predetermined) → could be booked on Accrual Basis

3) Advances: Audit procedure In carrying out audit of advances, concerned with obtaining evidence about the following:



Q6. A. procedures for evaluation of I.C over advances, substantive audit procedures & recoverability of advances.

Answer:

Sr.	Area of Focus	Suggested Audit Procedures
1	Evaluation of Internal Controls over Advances: (DAS - UCO bank)	<u>Before giving loan:</u> - Examine area of credit appraisal and verify whether laid down procedures regarding credit appraisals including loan applications, preparation of proposals, obtaining satisfaction about Credit worthiness of borrowers are being followed; - Examine all necessary loan Documents have been executed after sanction but before disbursements are made to borrowers; - Examine advances are sanctioned according to delegated Authority; - Examine existence, enforceability and valuation of Securities. In respect of securities requiring registration, examine this area also; <u>After giving loan:</u> - Examine compliance with stipulated terms of sanction and end Use of funds more particularly in case of term loans - Review whether drawing power is being calculated properly on basis of stock/book debt statements received from borrowers as stipulated in respective sanction letters; Review Operations of A/c and look for adverse features like unauthorised over drawings beyond limits
2	Substantive Audit Procedures:	Examine all large advances while other advances may be examined on a sample basis Verify correctness of master data of loan accounts updated in CBS. Check parameters like instalments, EMI, rate of interest, tenure of loans etc - Verify completeness and accuracy of interest being charged <u>Gande A/c (A-QRS):</u> Examine accounts which have been Adversely commented upon by concurrent auditors/bank's internal inspection/RBI inspection team - Examine accounts identified to be problem accounts but which have not yet slipped into NPA category. This can be done by obtaining list of: ✓ SMA1 → (Special mention a/c i.e. Loan overdue between 30 to 60 days) & ✓ SMA2 → (Loan overdue between 60 to 90 days) borrowers from the bank and same can be considered for selection of problematic accounts. - Examine Quick/early mortality accounts. (advance which become NPA within 12 months of its sanction is called as quick/early mortality case. - Examine list of restructured a/c's to ensure that Restructure as per RBI guidelines - Carry out appropriate analytical procedures. - Examine each customer have single customer ID for all the facilities granted
3	Recoverability of Advances	- Review latest financial statements of borrowers - Review auditor's reports in case of borrowers having credit facilities from the banking system beyond a cut-off limit fixed by board of directors of bank - Review reports on inspection of security - Review periodic statements submitted by the borrowers indicating the extent of compliance with terms and conditions

Q7. If due date of Loan is 31/03/2023, & not paid →

Overdue date should be	SMA 1 Date should be	SMA 2 Date should be	NPA Date should be
31 Mar 2023 (not 1st April)	30 Apr 2023	30 May 2023	29 June 2023

as overdue/SMA by banks as part of their day-end processes for due date.



4) NPA's: Verification of asset classification, income recognition and Provision for Non-performing

assets: Nonperforming investments are those where **interest/principal** is in arrears and remains **unpaid for more than 90 days**. (Or, "Out of Order")

Area of Focus	Suggested Audit Procedures
Classification & Provision:	1) Examine whether the classification made by the branch is appropriate. Particularly, examine the classification of advances where there are threats to recovery 2) Verify whether bank has a system of ongoing identification and classification of advances through CBS without manual intervention and its accuracy in crystallising date of NPA. 3) Examine whether the secured and the unsecured portions of advances have been segregated correctly and provisions have been calculated properly 4) Review and compare the date of NPA of loan accounts mentioned in current year statements with that of previous year. Reasons for any change should be ascertained
Accounts regularized near Balance sheet date:	if an account has been regularized before the balance sheet date by payment of overdue amount through genuine sources, the account need not be treated as NPA. Where, subsequent to repayment by the borrower (which makes the account regular), the branch has provided further funds to the borrower (including by way of subscription to its debentures or in other accounts of the borrower), the auditor should carefully assess whether the repayment was out of genuine sources or not. Where the account indicates inherent weakness based on the data available, the account should be deemed as NPA. In other genuine cases, the banks must furnish satisfactory evidence to the Statutory Auditors about the manner of regularization of the account to eliminate doubts on their performing status. It is to be ensured that the classification is made as per the position as on date and hence classification of all standard accounts be reviewed as on balance sheet date. The date of NPA is significant to determine the classification and hence specific care be taken in this regard. NPA should be recognized only based on concept of Past Due/ Overdue concept, and not based on the Balance Sheet date.
Drawing Power Calculation:	• Ensure that the drawing power is calculated as per the guidelines by BOD • Special consideration should be given to proper reporting of sundry creditors and stocks covered under LCs/guarantees for the purposes of calculating drawing power • drawing power needs to be calculated carefully in case of working capital advances to companies engaged in construction business. (WIP Inventory valuation) • stock audit including audit of book debts should be carried out by the bank for all accounts having funded exposure of more than stipulated limit
Accounts with temporary deficiencies:	• Banks should not classify an advance account as NPA merely due to the existence of some deficiencies which are temporary in nature such as: - o non-availability of drawing power based on latest stock statement, - o balance o/s exceeding the limit temporarily & - o non-renewal of limits on the due date. However, stock statements relied upon by the banks for determining drawing power should not be older than 3 months The outstanding in the account based on drawing power calculated from stock statements older than 3 months are considered as irregular.
Limits not reviewed:	Accounts where regular/ad hoc limits are not Renewed/reviewed within 180 days from the due date/date of ad hoc sanction, should be considered as NPA .
Classification	o Ensured that all the facilities granted by a bank to borrower will have to be treated as NPA



to be borrower wise and not facility wise:	and not particular facility which has become irregular o if debits arising out of devolvement of LC or invoked guarantees are kept in separate account the outstanding balance should be treated as part of borrower's principal account, for purpose of application of prudential norms on asset classification, income recognition and provisioning
Government Guaranteed Advances become NPA:	- o Income Recognition → If government guaranteed advance becomes NPA, then for the purpose of income recognition, interest on such advance should not to be taken to income unless interest is realized - o Asset Classification → However, for purpose of asset classification credit facility backed by: ✓ Central Government Guarantee, though overdue, can be treated as NPA only when the Central Government repudiates its guarantee, when invoked. (However, income will be recognized on receipt basis only) ✓ State Government: This exception is not applicable for State Government Guaranteed advances, where advance is to be considered NPA if it remains overdue for more than 90 days. - o In case the bank has not invoked the Central Government Guarantee though the amount is overdue for long, the reasoning for the same should be taken and duly reported in LFAR
Agricultural Advances:	- o For Priority Sector as per Circular: Ensure that NPA norms have been applied in accordance with the crop season, determined by the State Level Bankers' Committee in each State Depending upon the duration of crops - short term/ long term - raised by an agriculturist, the NPA norms would also be made applicable to agricultural term loans availed of by them, Also ensure that these norms are made applicable to all direct agricultural advances listed in Master Circular on lending to priority sector. - o For Other than Priority sector: In respect of agricultural loans, other than those specified in the circular, ensure that identification of NPAs has been done on the same basis as non-agricultural advances. Remember CA Inter: - o For short term crops: Account will be treated as NPA if loan remain o/s for more than 2 season - o For Long term crops: Account will be treated as NPA if loan remain o/s for more than 1 season
Restructured Advances:	- o Restructuring is an act in which a lender, for economic or legal reasons relating to borrower's financial difficulty, grants concessions to the borrower. It may involve modification of terms of advances including alteration of amount of instalments/alteration of repayment period/rate of interest/sanction of additional credit facilities etc. to help in curing of default. - o Banks cannot restructure accounts with retrospective effect. - o On restructuring, the account will be downgraded from Standard to substandard. - o A/c's which are NPAs will remain in the same category. (Note: Loss asset can't be restructure)
Upgradation of Account:	- o Examine all the accounts upgraded from NPA to standard category during the year - o possibility of incorrect upgradation of account on the basis of partial recoveries made in the account and overdue portion might not have wiped out completely - o There can also be a possibility of recoveries being made in the account after cut-off date and account being upgraded as on date of balance sheet
Sale/ Purchase of NPAs:	Q8. During audit of Skip Bank Ltd., you found that the Bank had sold certain of its nonperforming assets. Draft the points of audit check that are very relevant to this area of checking. • In case of Sale/Purchase of NPA by Bank, the auditor should examine: - o the policy laid down by the Board of Directors in this regard relating to procedures,

(kon bech sakta h, kisko bech sakta hai, kese, wapas chahiye to nhi hoga n?)

(sale kara to books me se remove karo and P&L me sahi treatment karo)

(Risky asset kharidi hai tumne, provision bana lna, pata nii recover ho nii ho)

valuation and delegation of powers

- o only such NPA has been sold which has remained NPA in Bank books for at least 2 years
- o the assets have been sold/ purchased "without recourse" only .i.e., the entire credit risk associated with non-performing asset should be transferred to purchasing bank.
- o the NPA has been sold at cash basis only (Not at contingent price, whole consideration should be upfront only)
- o bank has not purchased an NPA which it had originally sold
- In case of sale of an NPA, the auditor should also ensure that:
 - o on the sale of the NPA, the same has been removed from the books of the account of selling bank on transfer
 - o If the sale is at a price below the net book value (NBV) (i.e., book value less provisions held), the shortfall should be debited to the profit and loss account of that year
 - o If the sale is for a value higher than the NBV, the excess provision shall not be reversed (don't credit to P&L) but will be utilized to meet the shortfall/ loss on account of sale of other non-performing financial assets
- Similarly, in case of purchase of NPAs, the auditor should verify that:
 - o For the purpose of capital adequacy, banks have assigned 100% risk weights to the NPAs purchased from other banks.
 - o The NPA purchased has been subjected to the provisioning requirements appropriate to the classification status in the books of the purchasing bank
 - o any recovery in respect of an NPA purchased from other banks is first adjusted against its acquisition cost and only the recovered amount in excess of the acquisition cost has been recognised as profit.

Q9. Bank Mngt want to sell on April 2023, NPA of Books → (i) Fin Pvt Ltd → Became NPA in 2020-21 (ii) Dairy works → Become NPA in 2022-23, being an auditor scrutinize the above case & mention specific points to consider.

- Hint: Refer above Sale/purchase of NPA → "In case of Sale/Purchase of NPA by Bank, the auditor should examine" & "In case of sale of an NPA, the auditor should also ensure that",
- Considering the facts given in the Qn all the NPAs, except for Dairy Works, are prior to April 2021 i.e., 2 yrs prior to April 2023, so other than Dairy Works, can sale NPA's.

Q10. Audit of a nationalized bank for the year, verify the following areas:

- (i) NPA norms for Govt guaranteed advance. (ii) NPA norms for the advances given for agricultural purposes.
- (iii) Drawing power calculation from stock. (iv) A/c's where regular/ad hoc limits are not reviewed within 180 days (SM)

Hint: Refer relevant answer in above notes

Q11. In course of audit of Good Samaritan Bank as at 31st March, 19 you observed the following:

- a) In a particular account there was no recovery in the past 18 months. The bank has not applied the NPA norms as well as income recognition norms for that. Bank mngt replied that this account was guaranteed by the central govt and norms were not applicable. Please respond. Would your answer be different if guaranteed by a State Govt?
- b) bank's advance portfolio comprised of significant loans against Life Insurance Policy. Write suitable audit program(SM)

Hint:

a) Government Guaranteed Advance: → Refer above Notes "Government Guaranteed Advances become NPA" Exemption is not available i.e. income recognition norms. Hence the income not recovered should be reversed.

b) The Audit Programme to Verify Advances against Life Insurance Policies is as under-

- i. The auditor should inspect the policies and see whether they are assigned to the bank and whether such assignment has been registered with the insurer.
- ii. The auditor should also examine whether premium has been paid on the policies and whether they are in force.



- iii. Certificate regarding **surrender value** obtained from the insurer should be examined.
- iv. The auditor should particularly see that **if such surrender value is subject to payment of certain premium**, the amount of such premium has been deducted from the surrender value.

Q12. Bank is Consortium member of Cash credit facility of Rs.50 crore (bank own share is 10 Crore), In last 2 Qtr, interest debited was Rs.1.75 crore, But Credit was Rs.1.25 Crore, **Based on the certificate of lead bank**, the bank has **classified the account of X Ltd as performing**. (SM)

Hint: Explain given case (same as question) → each bank may classify the advance given by it according to its own **experience of recovery** (so last two Qtr interest should be reversed) → Amount should show as NPA

Q13. Audit for Year 31/03/2020 → Cash Credit limits renewal was due on 1st Sept 2019. → **Renewal has not been done even though 180 days are over.** → account is operated regularly & within drawing power. It shows a **letter from Client** stating that → "sudden death of FS auditor, a new auditor appointed, so it took time". The audited FS are received on 10/04/2020 & **renewal done immediately**. Whether it's NPA ? as limit was not renewed on 31/3/2020.

Hint: (SM) → RBI Guideline → Classify as NPA if renewal is not done in 180 days.

Given case → Account operation is excellent, **a letter from company that audited FS are delayed**, Further limit has been **renewed before signing audit report**. → it is an **adjusting event under AS 4** → Classify as **standard asset**.

Q14. Company have **CC limit of ₹25 crores**. The limit availed **remained less than ₹5.00 crores in all days**. The company has **not done any credit in CC A/c during Yr**. Company have **sufficient security of stocks**. Whether it's NPA (SM)

Hint: **classified as NPA** if → It **ceases to generate income** for bank Or, **Interest/principal remain overdue or out of order** for a specified period of time

• **'Out-of-order:**

- ✓ If O/S balance continuously in **excess of the sanctioned limit/drawing power** or
- ✓ if there are **no credits continuously for 90 days as on the balance sheet date** or
- ✓ the **credits are not enough to cover the interest debited** during the same period.
- Conclusion: - Cash credit facility with U bank **need to be classified as NPA** as there are no credit

Q15. Company is enjoying **cash credit facility from "Mumbai branch of KNB Bank"** for ₹ 250 crore. However, **various sub-limits have been fixed for company for operation at Solapur, Pune & Nashik branches**. In **Solapur branch** → **no credit transactions in sub-limit A/c for more than 90 days on 31/03/23**. CA. Muni, statutory auditor of Mumbai branch of KNB Bank, in the matter of **asset classification** & also Solapur branch. (SM)

Hint: → Customer is sanctioned a cash credit limit at 1 branch but authorised to utilise such overall limit at other branches also, → **NPA should be determined based on overall sanctioned limit** → not by each sub-limit.

- Auditor of limit-sanctioning branch should examine whether → all transactions in the account at sub-limit branches and status of the account is determined considering the **total position**. (standalone matter is irrelevant)
- CA. Muni should consider **classification considering the total position at all concerned branches**. & Regarding branches (Like Solapur), the same classification as adopted by the limit-sanctioning branch should be followed.

Q16. Interest on **State Govt Guaranteed** advance has taken to income → remained **overdue for more than 90 days**. (old)

- 1) A/c for which an **ad hoc limit has not been reviewed for 180 days** from the date of such ad hoc sanction.
- 2) **NPA's was sold for a value higher than the net book value**, excess provision i.e. same has been reversed.
- 3) an **additional temporary limit has been sanctioned for 25% of the existing limit** and for **120 days** tenure.
- 4) outstanding **forward exchange contracts** → 'net position' not squared and was uncovered by a substantial amount

Hint:

- 1) Reverse the interest income & recognize income when it's realized, It's Non-performing assets
- 2) Cancel the Entry for reversal of provision & such excess provision will be retained to meet shortfall of other NPA
- 3) Additional temporary limit would be revised to 20% of existing limit and for max 90 days
- 4) **Net position should be Squared off** & and **get covered by a substantial amount**.

Q17. Some borrower account **regularised before B/S date by payment** of overdue amount. Narrate audit procedures to be carried out with special focus on **Classification of advances & Provisioning for NPA** (Old)

Hint: → Audit procedures to be carried out for **Classification of advances & Provisioning for NPA** of the Branch:

- Examine **whether the classification made by the branch is appropriate**.



- Examine whether **secured & unsecured portions of advances segregated** correctly & provisions calculated properly.

Now refer & mention above Notes → "Accounts regularized near Balance sheet date"

Q18. CA Prachi → Bank statutory auditor 2021-22, A borrower enjoying overdraft (O/D)s credit facilities of ₹50 crore (availed against security of stocks and book debts), following observations:

- Balance in O/D credit facility on 31/03/22 → ₹55.65 crore. Balance exceeded sanctioned limit in Mar'22
- Based on Latest stock/debt of Feb'22 → DP of ₹48.50 Cr only. However previous months showed adequate DP.
- Stock audit report 31/12/22 showed adequate DP, But, it has commented adversely on declining turnover.
- The **renewal of O/D was due on 20th October, 2021**. The account was short renewed by competent authority for a period of 3 months pending submission of complete papers.

However, borrower has not submitted complete renewal papers till 31st March, 2022. There is a request letter from borrower on record stating that valuation report of a property located at a faraway location was taking time. (OLD)

Hint: → Feb'2022 showed inadequate DP, there was adequate DP available throughout Yr.

- Mar'2022 inadequate drawing power → temporary deficiencies → not require NPA Classification.
- Credit limits need to be reviewed not later than 3 months from the due date. → Hence, an account where the credit limits have not been reviewed/ renewed within 180 days from the due date will be treated as NPA
- 180 days from the date of original due date for renewal and not from date of expiry of short reviews. In given case, original date of renewal was 20th Oct 2021 and period of 180 days has still not expired as on B/S date.
- Keeping in view all above factors, CA Prachi should accept classification of account as 'Standard Asset'

Q19. Statutory audit of branch of Bank. examining large advances, finds that in 5 cases, loan applications have been filled up scantily with important details left out. Also cash credit limits to the borrowers were enhanced, but there are no records pertaining to assessment of enhanced working capital requirements in files. However, all 5 accounts are operating satisfactorily. These accounts have been classified as standard assets. Would auditor to suggest change in asset classification of above accounts? What does depicted situation reflect? (SM)

Answer: → An account becomes NPA when it ceases to generate income for bank. In the given situation, all the examined 5 accounts are operating satisfactorily. There is no reason for suggesting changes in classification

The matter of scantily filling up loan applications and lack for record for assessment of enhanced working capital requirements shows that internal control over advances in branch is not proper. The above said situation shows **deficiencies in "credit appraisal"** at branch level. Such deficiencies need to be **highlighted by auditor in LFAR**

➤ VERIFICATION OF ASSETS:

Banking Regulation Act, 1949 requires fixed assets to be **classified into two categories** in Balance Sheet

- (1) "**Premises**" (including residential premises used by employees)
- (2) **Other Fixed Assets**

Section 9 of banking regulation act: **prohibits a banking company from holding any immovable property**, howsoever acquired (i.e., **whether acquired by way of satisfaction of claims or otherwise**), for a **period exceeding 7 years** from the date of acquisition, **except such as is required for its own use**.

➤ VERIFICATION OF OTHER ASSETS:

Inter-Office Adjustments	• Examine whether Inter-branch accounts are normally reconciled at the central level • auditor should report on the year-end status of inter-branch accounts indicating the dates up to which all or any segments of the accounts have been reconciled. • auditor should also indicate the number & amount of O/s entries in the inter branch A/c's • ensure that any discrepancies found in inter-branch accounts have been properly dealt with in the books • auditor can obtain the relevant information primarily from branch audit reports.
Non-Banking Assets Acquired in	• Verify such assets with reference to the relevant documentary evidence, e.g., terms of settlement with the party, order of the Court



Satisfaction of Claims:

(Ownership dekho, Jyada tym tak Hold nahi kar sakte ... bechna padega)

- Check that the **ownership of the property** is legally vested with the bank. [in case of Dispute, Provision as per AS 29]
- **Ensure compliance** with Section 9 of Banking Regulation Act, on **holding period** of such assets [Max 7 Yrs]
- Ensure that the heading includes those immovable properties/tangible assets which the bank has acquired in satisfaction of debts due or its other claims and **these are being held with intention of being disposed off**
- Ensure that as **at date of acquisition, the assets should be recorded at lower of:**
 - **net book value of advance** or
 - **net realisable value** of asset acquired

➤ VERIFICATION OF CAPITAL ADEQUACY:

Capital Adequacy:	Term 'capital adequacy' is used to describe the adequacy of capital resources of a bank in relation to the risks associated with its operations
Capital Adequacy Measures: (Calculation MCQ)	• Tier I capital → consist of share capital + disclosed reserves + bank's highest quality capital (because it is fully available to cover losses) • Tier II capital → certain reserves + certain types of subordinated debt (loss absorption capacity of Tier II capital is lower than that of Tier I capital) Tier II capital ≤ tier I capital
Capital Risk Adequacy Ratio (CRAR):	$\frac{\text{Eligible Total Capital Funds}}{\text{Risk weighted assets and oFFbalance sheet items}} * 100$ ✓ Maintain a minimum CRAR of 9% ✓ Example: R. Weight for Housing loan in 50%, then Loan given 60 lacs, then denominator will be 60 lacs * 50% = 30 lacs
Stress Testing:	RBI has required that all commercial banks (excluding RRBs and LABs) shall put in place a Board approved 'Stress Testing framework' Stress tests are designed to understand whether a bank has enough capital to survive plausible adverse economic conditions and to maintain enough buffer to stay afloat under extreme scenarios.
BASEL III framework: <u>[TAR]</u>	• Basel III norms relate to the Capital Adequacy requirement compliance. • Basel capital adequacy norms are meant for the protection of depositors and shareholders by prescriptive rules for measuring capital adequacy, thereby evolving methods of determining regulatory capital and ensuring efficient use of capital. • It is global regulatory standard on capital adequacy of banks, stress testing as well as market liquidity risk. • The Basel III accord, aims at: (a) Improving the banking sector's ability to Absorb shocks arising from financial and economic stress, irrespective of reasons thereof; (b) Improving Risk management and governance practices; and (c) Strengthening banks' Transparency and disclosure standards

➤ VERIFICATION OF DEPOSITS:

Current and saving accounts (CASA):

Q20. For CASA Suggest a few audit procedures he should follow. (SM & MTP)

- Verify on a sample basis current account and saving **accounts opened during the year** for **adherence to KYC norms**. (For business transaction, open Current a/c, Not saving a/c)
- Verify the **balances** in individual accounts on a **sample basis**.
- Check the calculations of **interest on a test check basis**. Remember that no interest is paid generally on current accounts by banks



A/C <u>open</u> (KYC), <u>Balance</u> (Sample, EC) <u>Interest</u> <u>Close</u>	- Examine whether the procedure for obtaining balance confirmation periodically has been followed consistently. Examine, on a sampling basis, the confirmations received. - Ensure that debit balances in current accounts are not netted out on the liabilities side but are appropriately included under the head 'advances' Inoperative accounts (both current and saving) are a high-risk area of frauds in banks (treated as inoperative/dormant if there are no transactions in the account for over a period of 2 years), Ensure that inoperative A/c's are revived only with proper authority
Term deposits: <u>RD/FD</u> jo li uspe <u>Serial no.</u> the → uspe <u>interest</u> milla → fir <u>close</u> karadi	- Verify on sample basis some of recurring deposit accounts opened during the Yr. - Verify in case of bulk deposits (Rs. 2 crore and above for scheduled commercial banks presently), correct rate of interest has been offered - Examine whether the deposit receipts and cash certificates are issued serially and all of them are accounted for in the registers - In case of closure of term deposit, test check whether required foreclosure penalty has been deducted from applicable rate of interest payable - Verify correctness of rate of interest on term deposits on sample basis.

➤ VERIFICATION OF OTHER LIABILITIES AND PROVISIONS

Bills Payable: <u>Mne Form</u> bhara → <u>sign</u> kara → Employee ko diya jiske pass <u>Reliable Pvt code</u> hai	Q21. As an auditor of nationalized bank, your assistant found irregularities in telegraphic transfer & demand draft. Guide him Drafts, mail transfers, traveler's cheques, etc. should be in standard printed forms. Unused forms relating to drafts, traveler's cheques, etc. should be kept under the custody of a responsible officer - The signatures on a demand draft should be checked by an officer with the specimen signature book - The bank should have a reliable private code known only to the responsible officers - All the telegraphic transfers & demand drafts etc. issued by a branch should be immediately confirmed by advices to the branches concerned
Telegraphic transfer or Demand Draft:	- The bank should have a reliable private code known only to the responsible officers - The signatures on a demand draft should be checked by an officer with the specimen signature book - All the telegraphic transfers and demand drafts issued by a branch should be immediately confirmed by advices to the branches concerned - If the paying branch does not receive proper confirmation of any D.D. from the issuing branch or does not receive credit in its account with that branch, it should take immediate steps to ascertain the reasons

➤ CONTINGENT LIABILITIES

CL Include: (O-CPA-GF)	Q22. Provide disclosure requirement of Contingent Liabilities for Banks. Other items for which the bank is contingently liable Claims against the bank not acknowledged as debts - Liability for partly paid investments Acceptances, endorsements and other obligations (i.e., LC) Guarantees given on behalf of constituents (within India; outside India) - Liability on account of outstanding Forward exchange contracts & Derivative Contracts
Audit Procedure for contingent	Ensure that there exists a system whereby the non-fund based facilities or additional/ad hoc credit facilities to parties are extended only to their regular constituents, etc



Guarantees Given on Behalf of Constituents	Acceptances, Endorsements and Other Obligations (i.e. LC)
• Ascertain whether there are adequate internal controls over issuance of guarantees • Ascertain whether there are adequate controls over unused guarantee forms, e.g., whether these are kept under the custody of a responsible official • Check the relevant guarantee registers with the list of outstanding guarantees to obtain assurance that all outstanding guarantees are <u>included</u> in the amount disclosed in this behalf • <u>Examine</u> the guarantee register to seek evidence whether the <u>prescribed procedure of marking off the expired guarantees</u> is being followed or not.	• Evaluate the adequacy of internal controls over issuance of letters of credit and over custody of unused LC forms in the same manner as in the case of guarantees • Verify the balance of letters of credit <u>from</u> the register maintained by the bank. • Examine whether the bank has incurred a potential financial obligation in respect of letters of comfort and if such obligation has been cast, ensure the amount to be disclosed under contingent liability.



- (iv) all year end **contingent liabilities** have been **disclosed**;
- (v) Estimated amounts of financial effect of **contingent liabilities** are based on **best estimates as per AS 29**, including consideration of the possibility of any reimbursement;
- (vi) the disclosed **contingent liabilities** do **not include any crystallised liabilities** which are of the nature of loss/expense and which, therefore, **require creation of a provision**/adjustment in the financial statements;
- (vii) such **contingent liabilities** which have **not been disclosed** on account of the fact that the possibility of their outcome is remote **include the mngt's justification** for reaching such a decision i.r.o those CL.
- (viii) in case of **guarantees issued on behalf of the bank's directors**, the **bank has taken appropriate steps to ensure that adequate and effective arrangements** have been made so that the commitments would be met out of the party's own resources and that the bank will not be called upon to grant any loan or advances to meet the liability consequent upon the invocation of the said guarantee(s) and that no violation of section 20 of the Banking Regulation Act, 1949 has arisen on account of such guarantee; and

➤ **AUDITOR'S REPORT**

Auditor report address to:	• Nationalised bank → Central Government • State Bank of India → Central Government
Unaudited branches:	Not only the information relating to number of unaudited branches is given but quantification of advances, deposits, interest income and interest expense for such unaudited branches has also been disclosed in the audit report
Format of Audit Report:	<u>Explain Rule 11</u> [as explained in Sec 143(3) - Company audit chapter i.e., Any pending Litigation, provision for material foreseeable loss]
Long Form Audit Report: (30th June)	• Applicable to all banks (including branches) • given by statutory branch auditors as well as statutory central auditors • LFAR of Branch → is in form of questionnaire where observations/comments have to be provided on range of matters including cash, balance with banks, investments, advances, deposits etc. These are submitted to statutory central auditors. • Consolidation is done at head office level and LFAR for bank is submitted by statutory central auditors to management. • The LFAR, after due examination, should be placed before the ACB (Audit committee board) of the bank <u>indicating the action taken/proposed</u> to be taken for rectification of the irregularities, if any, mentioned therein; • Copy of the LFAR & relative agenda note, together with the Board's views or directions, is submitted to RBI within 60 days of submission of LFAR by statutory auditors.
Other Reporting Requirements:	• Circular relating to Bank Frauds applicable to all scheduled commercial banks (excluding Regional Rural Banks). → need to report fraud. Also Sec 143 (12) fraud reporting
Reports and certificates:	Q25. Write short note on: Special purpose certificates relating to investments required to be issued by Central Statutory Auditors of a bank. Besides, as part of statutory audit process, statutory central auditor provides reports and certificates mainly consisting of following:- • Certificate on reconciliation of securities by the bank (both on its own investment account as well as PMS Banks' account). • Report on adequacy and operating effectiveness of ICFR in case of banks • Long form audit report (LFAR) • Report on compliance with SLR requirements • Report on whether the income recognition, asset classification and provisioning have been



- made **as per the guidelines** issued by the RBI from time to time.
- Authentication of **capital adequacy ratio**, including disclosure requirements and other ratios reported in the notes to accounts
- Asset liability management (**ALM**)

➤ **CONCURRENT AUDIT:**

Meaning:	Audit or verification of transactions or activities of an organisation concurrently as the transaction/activity takes place. It is not a pre-audit
Scope:	Q26. Explain scope of concurrent audit of bank with reference to RBI guidelines Detailed scope of the concurrent audit should be clearly and uniformly determined for the Bank as a whole by the Bank's Central Inspection and Audit Department in consultation with the Bank's Audit Committee of the Board of Directors (ACB). In determining the scope, importance should be given to checking high-risk transactions having large financial implications as opposed to transactions involving lesser amounts.  <pre> graph LR Deposit --> Cash Cash --> ADVANCE Cash --> INVESTMENT ADVANCE --> HOUSE_keeping[HOUSE keeping] ADVANCE --> FOREIGN_EXCHANGE[FOREIGN EXCHANGE] INVESTMENT --> FOREIGN_EXCHANGE </pre>
Concurrent Audit System:	System such as selection of branches/coverage of business operations, appointment of auditors, rectification processes Etc. → bank should Once in a year review the effectiveness of the system
Coverage of Business/ Branches	Scope left to the discretion of the head of internal audit of banks with the due prior approval of the Audit Committee of the Board of Directors (ACB) Broad areas of coverage under concurrent audit shall be based on the identified risk of the unit and must include random transaction testing of sufficiently large sample of such transactions wherever required.
Appointment & Accountability:	- Left to the discretion of individual banks (Internal staff or external) In case of Staff engaged on concurrent audit must be independent of the "branch" as well as Experienced, trained & senior In case of External auditor: any serious acts of omissions noticed in their working → appointments may be cancelled & reported to RBI & ICAI. - ACB of the bank shall decide the maximum tenure of external concurrent auditors ✓ Shall not be more than 5 years on continuous basis for Bank ✓ Shall not be more than 3 years on continuous basis for a single branch
Reporting System:	- A quarterly review containing key features brought out during the concurrent audits should be placed before the ACB zone-wise reporting of the findings Minor irregularities pointed by concurrent auditors are to be rectified in a timely manner. Serious irregularities should be reported to the controlling offices/ Head Offices for immediate action - Whenever fraudulent transactions are detected, they should immediately be reported to Inspection & Audit Department (Head Office) as also the Chief Vigilance Officer as well as Branch Managers concerned (unless the branch manager is involved). Follow on action on the concurrent audit reports should be given high priority by controlling office/Inspection and Audit Department
Audit procedure for ADVANCES:	Q27. Concurrent auditor procedure to verify Advances <u>Loan dete waqt:</u> Ensure that loans and advances have been sanctioned properly in accordance with

	delegated authority - Ensure that securities and documents have been received <u>Dene ke baad:</u> - Ensure that post disbursement supervision and follow-up is proper, such as receipt of stock statements, instalments, recovery/ renewal of sanction limits - whether there is any misutilisation of the loans & diversion of fund <u>Accounting</u> - Whether the classification of advances has been done as per RBI guidelines <u>LC/BG</u> - Whether the letters of credit issued by the branch are within the delegated power Bank guarantees issued, whether they have been properly worded & recorded in register of the bank
Audit procedure for FOREIGN EXCHANGE:	Q28. Concurrent Auditor → foreign exchange transactions of branch under concurrent audit. <u>A/c:</u> - Check FCNR and other non-resident accounts whether debits and credits are permissible under rules - Ensure verification/reconciliation of Nostro and Vostro account transactions/balances. - Ensure that balances in Nostro accounts in different foreign currencies are within the limit as prescribed by the bank <u>Paisa aana jaana:</u> - Check whether inward/outward remittance have been properly accounted for - Check foreign bills negotiated under letters of credit - Examine extension and cancellation of forward contracts for purchase and sale of foreign currency. Ensure that they are duly authorised and necessary charges have been recovered <u>Other Points:</u> - Ensure that the overbought/oversold position maintained in different currencies is reasonable, considering the foreign exchange operations - Ensure adherence to the guidelines issued by RBI/HO of the bank about dealing room operations

Q29. concurrent audit → branch having advances of about Rs. 500 crores including export advances, LCs issued.
Discuss 5 areas pertaining to Branch advances, which you would verify to ensure no revenue leakage. [SM]

Answer:

Kya kya income ho sankti h Loan dene se > Processing fees (dete time) > fir interest > fir overdue pe Interest, Charges & penal action

- Processing fees** in respect of freshly sanctioned advances and renewed limits need to be levied in accordance with bank guidelines and these need to be verified. Any revision in processing fees from time to time has to be given effect to in accordance with circulars/manual of bank.
- Interest rates fed in the system** need to be verified with respect to corresponding sanction letters. It would help ensure that correct rate of interest is fed into the system and interest is applied properly at stipulated intervals on advances.
- Verification of **overdue interest on export bills** purchased and packing credit facilities for overdue period.
- Verification of **charges/commission** in respect of letters of credit issued in accordance with Bank's circulars/manual
- Sanction of cash credit limits** is generally accompanied with stipulation to submit stock statements. Non-submission of stock statements can involve levying of penal interest. Verification of this aspect is required



Q30. Stock auditor just physically counted the Rice Bags (Stock) and Calculated DP → After a week, internal inspector also visited premises of borrower & found that 5000 Rice bags was fungus ridden. The company was holding this stock for last 15 months. → How do you view the above situation? Discuss (SM)

Answer: → The above situation reflects that **professional work of stock audit** was **not performed diligently** by stock auditor. It is one of the important responsibilities of stock auditor to verify condition of stocks. The auditor's role is not limited to verify physical quantities only.

In given case, **she should have got opened rice bags on test check basis**. Value of such rice should have been excluded while arriving at value of stocks for purpose of computation of drawing power.

It shows that she has **failed to perform her work diligently & drawing power calculated in report is not proper**

Q31. Audit of Small Bank Branch, have only Manager, Cashier & 3 Staff (S1, S2, S3) → S1 is a Peon who opens incoming mail & forward it to concern person (he don't have signature book to check mail signatures), S2 has possession of all bank form (cheque book, Currency cards, DD etc.) and he only maintain record & do test check. No one among staff regularly test check (as it's a small branch with shortage of manpower). (SM)

Hint: Bank is required to maintain a System of I.C for mitigating risk, good governance etc. Given case, IC are violated:

- S1 is Peon. **Mail should be always opened by a Responsible person** & that person should check sign as per **Sign Book**
- All **bank forms** (Cheques, DD etc.) should be **kept in possession of Officer** & **another responsible officer should verify the same** (Currently S2 is only maintaining it, and verifying it on test basis)
- Being a small branch so not able to check records regularly is not tenable (as lapse in I.C pose risk of fraud)
- Auditor should **report the same**

Q32. Statutory audit of Branch → at year end Cash credit is fully utilised, to make fixed deposit from that amount, and that Deposit again liquidated in First week of April. (Old)

Hint: → Explain given case as it is → This is an example of **window dressing** → **artificially boosting its advances and deposits. Utilization of advances and placing of fixed deposits at end of year.**

The auditor has to verify whether the unavailed portion of the credit facilities are used to boost the loans and deposits which might tantamount to window dressing. → these might **involve penal action**

Report this in **audit report & commented in LFAR** also. may require **qualification in the main audit report**

Q33. Central Statutory Auditors of a **nationalized bank** → Co. Act, 2013 & CARO, 2020 → Audit Report: (OLD)

- To which **authority auditors** should **submit their audit report**? → **Central Govt** (as it's Nationalised Bank)
- List the matters covered under Companies Act → **report matters U/s 143 of Co. act [explain whole Sec 143(3)]**
- Reporting under Companies (Auditor's Report), Order, 2020. → **Not Applicable**

Q34. Meaning of "Gross NPAs" & "Net NPAs" of a Bank? Ratio of Net NPAs to Net advances: for KNO Bank 3.97%, CNI Bank 2.65%, what inference would you draw by comparing "Ratio of net NPAs to net advances"? [MTP'24]

Answer:

- **Gross NPAs** → opening balances of NPAs (+) fresh NPAs during the year (-) reduced by upgradations, recoveries and write-offs during the year
- **Net NPAs** are arrived at Gross NPA (-) [total provision held against NPAs + balance in interest suspense A/c to park accrued interest on NPAs] i.e., **it's Gross NPA asset minus provision for that asset**
- **Net Advance:** Total advances (-) Provisions created for advances
- **Net NPAs ÷ Net advances** ratio → is **higher in the case of KNO Bank** as compared to other public sector banks. It shows that there is a **risk that the bank could not have made the required provisions** in accordance with RBI guidelines. → indicates the probability and risk of under-provisioning.

Q35. Write a short note on **reversal of income** under bank audit. [OLD]

Answer:

- If any **advance, including bills purchased & discounted, becomes NPA** → the entire **interest accrued & credited to income account in the past periods**, should be **reversed** or provided for if the same is not realised. This will **apply**



to Government guaranteed accounts also.

- For NPAs, fees, commission & similar income → be reversed or provided for w.r.t past periods, if uncollected.
- Further, in case of banks which have wrongly recognised income in the past should reverse the interest if it was recognised as income during the current year or make a provision for an equivalent amount if it was recognised as income in the previous year(s).

NOTE:

- Interest Accrued on Deposit (But not Due) → "Shown in Other Liability & Provision" (Not included in Deposit)
- Interest Rate Swaps → "Contingent Liability"



CHAPTER 14.2: Audit of NBFC's

➤ Some Abbreviations:

SI - Systematic Important	NSI - Non Systematic Important	D- Deposit taking
ND- Non Deposit Taking	ML/UL - Middle Layer/Upper Layer	BL- Base Layer

➤ Introduction:

Definition of NBFC:	As per 45I(f) of RBI (Amendment) Act, 1997, Non-Banking financial institution are: 1) A financial institution which is a company 2) A non-banking institution which is a company a non-banking institution and which has as its principal business the receiving of deposits, under any scheme or arrangement or in any other manner, or lending in any manner; 3) Other non-banking institution or class of such institutions, the Bank may, with previous approval of the Central Government and by notification in the Official Gazette, specify;"
Deemed NBFC:	Q1. A trading Company, has made investments in shares & advanced loans → to more than 50% of its total assets. However, trading income constitutes majority of its total income. To identify a particular company as NBFC, it will consider both assets and income pattern as evidenced from the last audited balance sheet of the company to decide its principal business: 1) Company's Financial Assets constitute > 50% of the total assets (netted off by intangible assets), AND 2) Income from financial assets constitute > 50% of the gross income. A company which fulfils both these criteria shall qualify as an NBFC and would require to be registered as NBFC by RBI. In given case, Company not fulfilling the criteria on income side, company is not Deemed NBFC.
Registration & Regulations of NBFC:	➤ Under Section 45-IA of the Reserve Bank of India (Amendment) Act, 1997, no non-banking financial company is allowed to commence or carry on the business of a non-banking financial institution without 1) Obtaining a certificate of registration issued by the Reserve Bank of India. 2) Having a net owned fund (NOF) of ₹ 2 crore (→ However for Certain NBFC's Minimum NOF is ₹10 Crore prescribed, For those Certain Existing NBFC's, RBI has prescribed timeline to meet NOF amount of 10 crore in phased manner by 31/03/2027), as the RBI may, by notification in the Official Gazette, specify. [However, for NBFC-P2P, NBFC-AA, and NBFCs with no public funds and no customer interface, the NOF shall continue to be ₹ 2 Crore.] [However, for NBFC-IFC, NBFC-IDF, the NOF shall continue to be ₹ 300 Crore.] ➤ Company Can apply to the Reserve Bank of India in prescribed form along with necessary documents for registration. The RBI issues Certificate of Registration after satisfying itself that the conditions as enumerated in Section 45-IA of the RBI Act, 1934 are satisfied. ➤ The Reserve Bank of India has issued directions to non-banking financial companies on acceptance of public deposits, prudential norms like capital adequacy, income recognition, asset classification, provision for bad and doubtful debts, risk exposure norms and other measures to monitor the financial solvency and reporting by NBFCs ➤ Auditors to report non-compliance with the RBI Act and the Regulations to the RBI, Board of Directors and shareholders.



Exempted from registration: (To Obviate Dual Registration)	Companies exempted from registration under RBI: 1) Housing Finance Institutions (regulated by National Housing Bank); 2) Merchant Banking Companies (regulated by SEBI); 3) Stock Exchanges (regulated by SEBI); 4) stock-broking/sub-broking (regulated by SEBI); 5) Venture Capital Fund Companies (regulated by SEBI); 6) Nidhi Companies (regulated by Ministry of Corporate Affairs, Government of India); 7) Insurance companies (regulated by Insurance Regulatory and Development Authority); 8) Chit Companies (as defined in clause (b) of section 2 of the Chit Funds Act, 1982) 9) Micro Finance Companies 10) Securitisation and Reconstruction Companies 11) Mutual Benefit Companies 12) Mortgage Guarantee Companies 13) Alternative Investment Fund (AIF) Companies 14) Core Investment Companies with ✓ Asset size of < ₹ 100 crore, Or ✓ Asset size $\geq$ ₹ 100 crore but not accessing public funds

The following glide path is provided for the existing NBFCs, viz., NBFC-ICC, NBFC-MFI5 and NBFC-Factor to achieve the NOF of ₹ 10 crore:

NBFC	Current NOF	By 31/03/2025	By 31/03/2027
NBFC-ICC →	₹ 2 crore	₹ 5 crore	₹ 10 crore
NBFC-MFI →	₹ 5 crore (₹ 2 crore in NE Region)	₹ 7 crore (₹ 5 crore in NE Region)	₹ 10 crore
NBFC-Factor →	₹ 5 crore	₹ 7 crore	₹ 10 crore

Q2. You are required to **explain the requirements related to registration and regulation** of NBFCs which an auditor needs to keep in his mind while planning the audit of NBFC which would help this firm

Hint: → Refer "**Registration & Regulations of NBFC**" & Some points of "**Exemption from registration**"

i.e., (to obviate dual regulation, certain categories of NBFCs which are regulated by other regulators are exempted from the requirement of registration with RBI viz. Venture Capital Fund/Merchant Banking /Stock Broking registered with SEBI, Insurance Company, Nidhi Companies, Chit Companies, 1982 or Housing Finance Companies regulated by National Housing Bank)

Q3. ABC Ltd. is a company registered under the Companies Act, 2013 following are some extracts from the FS (In Crores)

Paid-up share capital: ₹40.53	Non-Current Assets - Advances : ₹55.90	Current Assets -Advances: ₹344.47 Cr
Total assets of the company: ₹530 (Intangible assets = ₹3)		
Profit for the Year: ₹7.25	Income from interest & dividends: ₹52	Gross income: ₹102.57

Is registration of NBFC Section 45-IA of the RBI (Amendment) Act, 1997 needed ?. Advise

Hint: Mention 50-50 Criteria as given in Above Notes (> 50% of Assets & Income) & Below In the given case of,

its Financial Assets are = ₹55.90 + ₹344.47 = ₹400.37 Cr	Total Assets (-) intangible assets = ₹527 Cr (530-3)
Income from financial assets = ₹52 Cr	Gross Income = ₹102.57 Cr

Hence, 50%-50% Criteria is Fulfilled, to qualify as an NBFC. → Thus ABC Ltd. can apply for registration U/s 45-IA.

➤ **TYPES OF NBFC's (For Compliance & Regulatory Perspective):**

Sec 45-I (f)	Company registered under the Companies Act, engaged in the <u>business of loans and advances, acquisition of shares/stocks/bonds/ debentures/ securities issued by Government or local authority or other marketable securities of a like nature, leasing, hire-purchase, insurance business, chit business</u> but does not include any institution whose principal business is that of <u>agriculture activity, industrial activity, purchase or sale of any goods (other than securities) or</u>



providing any services and sale/purchase/construction of immovable property.

- A) In Terms of Deposit acceptance → Deposit and Non-Deposit accepting NBFCs
 B) Non-Deposit NBFC → Base Layer, Middle Layer, Upper Layer & Top Layer (Earlier It was systemically important and non-systemically [NBFC-NDSI or NBFC-ND])
 C) by the kind of activities, they conduct (as given below in table)

I	M	Financing	House
<u>Investment:</u> 1) Investment and Credit Company (ICC) 2) Core Investment Company (CIC) <u>Infrastructure:</u> 3) Infrastructure Finance Company (IFC) 4) Infrastructure Debt Fund Non-Banking Financial Company (IDF-NBFC)	5) Non-Banking Financial Company <u>Micro Finance</u> Institution (NBFC-MFI)	6) Non-Banking Financial Company - <u>Factors</u> (NBFC Factors)	7) NBFC- Non Operative Financial Holding Company (NOFHC)

Some Brief Explanation of Above NBFC's (Not Given in New ICAI SM)

ICC:	principal business of asset finance (& is not any other category of NBFC as defined by RBI)
CIC:	<u>satisfies the following conditions as on the date of the last audited balance sheet:</u> - Invest in securities of group companies only AND, - Investment in Equity + Preference Debt+ Loan ≥ 90% of its Net assets, AND - Investment in Equity + Compulsory convertible within 10 yr ≥ 60% of Net asset, AND, - Not trade in Investment and Not carry any other financial activities Can do investment in: Bank deposits, money market instruments (including money market mutual funds and liquid mutual funds), government securities
Systematic CIC:	CIC + Asset ≥ 100 Crore (individually or in aggregate along with other CICs in the group)
Micro Finance:	Loan to lower income person i.e., annual income of ₹ 1 Lacs in rural areas and ₹ 1.6 Lacs in urban (minimum 24 Month Loan, Max amt 1L, without collateral) (Consist 85% asset of that loan)
NBFC Factor:	Whose financial asset in factoring business consist at least 75% of total asset & income
Non-Operative Holding Co.	Its an inactive NBFC, just form to hold/acquire Shares of group companies
Inf Finance (IFC):	NOF ≥ 300 crore + 75% of total assets is this loan + Credit rating A & Above + CRAR ≥ 15%
Inf Debt Fund (IDF):	NOF ≥ 300 Crore + Invest in public pvt partnership (which has completed atleast 1 year of satisfactory commercial operation)

Q4. Define NBFC. Also give a brief description about types of NBFCs covering any five NBFCs. (SM)

Hint: → Refer "Definition of NBFC: 45 I(f)" & "Types of NBFC's" as explained in above notes

(In Answer → ICAI Has explained → ICC, Systematic CIC, Micro Finance, IFC & IDF)

Q5. What is CIC under RBI regulations? & specific reporting requirements by auditor i.r.o CIC under CARO 2020? [OLD]

Hint: → Refer above "ICC" & Refer CARO 2020 Chapter: Paragraph 3(xvi) (c) For CARO reporting

➤ Four Layers of NBFC's – Scale Based Regulation (SBR):

Effective from 01 October 2022: RBI has revised different facets of existing NBFC Classification and regulation like Capital Requirements, Governance Standards, Prudential Regulations, etc. based on four layers that are defined based on their size, activity, and perceived riskiness:



1) Base Layer (NBFC-BL): Trick: "PAN" ka "No Consumer"	a) NBFC - ND: asset size < ₹1000 crore and b) NBFC undertaking the following activities- (i) NBFC-Peer to Peer Lending Platform (NBFC-P2P), [online mediator to Lender & borrower] (ii) NBFC-Account Aggregator (NBFC-AA), [accumulate & distribute F.I. of Persons] (iii) Non-Operative Financial Holding Company (NOFHC) and (iv) NBFCs not availing public funds & not having any customer interface.																
2) Middle Layer (NBFC-ML) "Dealer" of "Infrastructure" & "House" is my "Core" Activity	<table border="1"> <tr> <td>a) NBFC-D, irrespective of asset size</td><td>[Can be in Mid Layer Or Upper]</td></tr> <tr> <td>b) NBFC - ND, with asset size ≥ ₹1000 crore</td><td></td></tr> <tr> <td>c) NBFCs undertaking the following activities:</td><td></td></tr> <tr> <td>(i) Standalone Primary Dealers (SPDs), [authorized in buying and selling govt. securities]</td><td>[Always remain in MID LAYER]</td></tr> <tr> <td>(ii) Infrastructure Debt Fund - NBFC (IDF-NBFCs)</td><td>[Always remain in MID LAYER]</td></tr> <tr> <td>(iii) Infrastructure Finance Companies (NBFC-IFCs)</td><td>[Can be in Mid Layer Or Upper]</td></tr> <tr> <td>(iv) Housing Finance Companies (HFCs)</td><td>[Can be in Mid Layer Or Upper]</td></tr> <tr> <td>(v) Core Investment Companies (CICs)</td><td>[Can be in Mid Layer Or Upper]</td></tr> </table>	a) NBFC-D, irrespective of asset size	[Can be in Mid Layer Or Upper]	b) NBFC - ND, with asset size ≥ ₹1000 crore		c) NBFCs undertaking the following activities:		(i) Standalone Primary Dealers (SPDs), [authorized in buying and selling govt. securities]	[Always remain in MID LAYER]	(ii) Infrastructure Debt Fund - NBFC (IDF-NBFCs)	[Always remain in MID LAYER]	(iii) Infrastructure Finance Companies (NBFC-IFCs)	[Can be in Mid Layer Or Upper]	(iv) Housing Finance Companies (HFCs)	[Can be in Mid Layer Or Upper]	(v) Core Investment Companies (CICs)	[Can be in Mid Layer Or Upper]
a) NBFC-D, irrespective of asset size	[Can be in Mid Layer Or Upper]																
b) NBFC - ND, with asset size ≥ ₹1000 crore																	
c) NBFCs undertaking the following activities:																	
(i) Standalone Primary Dealers (SPDs), [authorized in buying and selling govt. securities]	[Always remain in MID LAYER]																
(ii) Infrastructure Debt Fund - NBFC (IDF-NBFCs)	[Always remain in MID LAYER]																
(iii) Infrastructure Finance Companies (NBFC-IFCs)	[Can be in Mid Layer Or Upper]																
(iv) Housing Finance Companies (HFCs)	[Can be in Mid Layer Or Upper]																
(v) Core Investment Companies (CICs)	[Can be in Mid Layer Or Upper]																
3) Upper Layer (NBFC-UL)	These are specifically identified by the RBI as warranting enhanced regulatory requirement based on a set of parameters and scoring methodology (as per Circular). The top 10 eligible NBFCs in terms of their asset size shall always reside in the upper layer, irrespective of any other factor																
4) Top Layer (NBFC-TL)	- The Top Layer will ideally remain empty. - RBI will add NBFCs in this layer if is of the opinion that there is a substantial increase in the potential systemic risk from specific NBFCs in the Upper Layer. Such NBFCs shall move to the Top Layer from the Upper Layer.																
- NBFCs like, viz., Investment and Credit Companies (NBFC-ICC), Micro Finance Institution (NBFC-MFI), NBFC-Factors and Mortgage Guarantee Companies (NBFC-MGC) could lie in any of the layers of the regulatory structure depending on the parameters of the scale based regulatory framework. - Government owned NBFCs shall be placed in the Base Layer or Middle Layer, as the case may be. They will not be placed in the Upper Layer till further notice.																	

From Oct 2020

All Below will be old references, Get replaced By →	New Meaning
NBFC - ND (Non SI) & NBFC - NDSI (Asset Size Between Rs.500 Crore & below Rs.1000 Crore), except those necessarily featuring in Middle Layer	NBFC - BL
NBFC D & NBFC - ND SI	NBFC - ML & UL, as case may be

Q6. Write a short note on the following: Categorization of NBFCs carrying out specific activity (SM)

Answer:

As the regulatory structure envisages scale based as well as activity-based regulation, the following prescriptions shall apply in respect of the NBFCs

- NBFC-P2P, NBFC-AA, NOFHC and NBFCs without public funds and customer interface always → Base Layer
- NBFC-D, CIC, IFC and HFC → in Middle Layer or the Upper Layer (and not in the Base layer), SPD and IDF-NBFC always → Middle Layer.
- The remaining NBFCs, viz., Investment and Credit Companies (NBFC-ICC), Micro Finance Institution (NBFC-MFI), NBFC-Factors and Mortgage Guarantee Companies (NBFC-MGC) could lie in any of the layers of the regulatory structure depending on the parameters of the scale based regulatory framework.
- Government owned NBFCs → Base Layer or Middle Layer, as the case may be. (not placed in Upper).



➤ **DIFFERENCES BETWEEN BANKS AND NBFCs:**

Basis	NBFC	Bank
Demand Deposit	NBFC cannot accept demand deposits, however some NBFCs can accept Term Deposits	Can accept
Cheque	No , NBFCs do not form part of the payment and settlement system and cannot issue cheques drawn on itself;	Yes
DICGC	No , deposit insurance facility of Deposit Insurance and Credit Guarantee Corporation (DICGC) is not available to depositors	Yes
Priority Sector	No Minimum Exposure to Priority Sector required by NBFCs	Yes

➤ **PRUDENTIAL NORMS:**

Capital Requirements: $\frac{\text{Capital}}{\text{Assets} * \text{Risk Weight}}$	NBFC : ND-SI (Sys. Imp) & NBFC - D taking: - Shall maintain a minimum capital ratio (Tier I +Tier II capital) which shall ≥ 15 % of its aggregate risk weighted assets on-balance sheet and of risk adjusted value of off-balance sheet items. Tier I capital ≥ 10% (Except NBFC MFI or Primarily engaged in lending against Gold Jw) - NBFC NBFCs primarily engaged in lending against gold jewellery Tier I capital ≥ 12% (Such Loan comprised 50% or More of there financial assets) - Note: For Fixed Assets : Risk weightage is "100" For Cash - Risk weightage is "0"													
	Calculation: ➤ <u>Formula:</u> $\frac{\text{Capital}}{\text{Assets} * \text{Risk Weight}} = \text{Risk Weighted Asset}$ (Above Asset will also include off-balance sheet items) ➤ <u>Tier 1 Capital (Except NBFC-BL):</u> <table border="1"> <tr> <td>Owned Fund</td><td>xxx</td></tr> <tr> <td>(-) Below Investments → <u>Exceeding 10% of owned fund</u></td><td>(xxx)</td></tr> <tr> <td> a) Investment in shares of Other NBFC's b) Investment in shares / debentures / bonds/ outstanding loans & advances/ Hire purchase Lease Finance/ Deposit with Subsidiaries & Group Company </td><td></td></tr> <tr> <td>(+) Perpetual debt instruments issued by NBFC-ND (Max to the extent of 15% of Tier 1 capital of <u>Previous Year 31st Mar</u>)</td><td>xxx</td></tr> </table> <u>Owned Fund =</u> PU Equity SC + Pref share Compulsory convertible to equity + Free reserve (including retained earning & share premium etc) + capital reserve (excluding revaluation reserve) (-) accumulated loss (-) deferred revenue expenditure (-) other intangible assets (Tier 1 Capital for NBFC-BL → Same as Above, Except → not eligible to include perpetual debt instruments) ➤ <u>Tier 2 Capital (Except NBFC-BL):</u> <table border="1"> <tr> <td>Preference shares (other than which are compulsorily convertible into equity)</td><td>xxx</td></tr> <tr> <td>Revaluation reserves x 45% i.e., (Revaluation reserve is Discounted at 55%)</td><td>xxx</td></tr> <tr> <td>Lower of (A) or (B)</td><td>xxx</td></tr> </table>	Owned Fund	xxx	(-) Below Investments → <u>Exceeding 10% of owned fund</u>	(xxx)	a) Investment in shares of Other NBFC's b) Investment in shares / debentures / bonds/ outstanding loans & advances/ Hire purchase Lease Finance/ Deposit with Subsidiaries & Group Company		(+) Perpetual debt instruments issued by NBFC-ND (Max to the extent of 15% of Tier 1 capital of <u>Previous Year 31st Mar</u>)	xxx	Preference shares (other than which are compulsorily convertible into equity)	xxx	Revaluation reserves x 45% i.e., (Revaluation reserve is Discounted at 55%)	xxx	Lower of (A) or (B)
Owned Fund	xxx													
(-) Below Investments → <u>Exceeding 10% of owned fund</u>	(xxx)													
a) Investment in shares of Other NBFC's b) Investment in shares / debentures / bonds/ outstanding loans & advances/ Hire purchase Lease Finance/ Deposit with Subsidiaries & Group Company														
(+) Perpetual debt instruments issued by NBFC-ND (Max to the extent of 15% of Tier 1 capital of <u>Previous Year 31st Mar</u>)	xxx													
Preference shares (other than which are compulsorily convertible into equity)	xxx													
Revaluation reserves x 45% i.e., (Revaluation reserve is Discounted at 55%)	xxx													
Lower of (A) or (B)	xxx													



a) **General provisions (including that for Standard Assets) & Loss Reserves**

- ✓ that are Not Linked to any specific asset's value reduction,
- ✓ Not for any identifiable potential loss,
- ✓ Available for covering unexpected Losses

b) **1.25% of risk weighted assets**

Hybrid debt capital instruments;

xxx

Subordinated debt

xxx

Excess perpetual debt instruments (PDIs that couldn't be included in Tier 1 due to 15% limit)

xxx

xxx

TOTAL (To the extent the aggregate does not exceed Tier 1 capital)

(Tier 2 Capital for NBFC-BL → Same as Above, Except → not eligible to include perpetual debt instruments)

Q7. (MTP'25) → Practical Qn is asked ... w.r.t CRAR/Tier 1 & 2 calculation → refer QN Bank

Income Recognition:

The income recognition (interest/ discount/ hire charges/ lease rentals or any other charges etc.) shall be **based on recognised accounting principles**.

- Income on **NPA** shall be recognised **only when it is actually realised**.
- **Any such income recognised before** the asset became nonperforming and remaining unrealised shall be **reversed**.

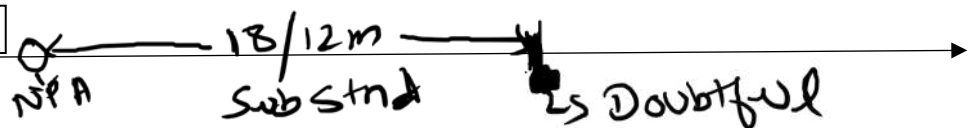
Asset Classification & Provisioning Norms:

The asset classification & Provisioning norms as given below shall apply to **every applicable NBFC (except NBFC-MFIs)**:

Note: The class of assets referred to above shall **not be upgraded merely** as a result of **rescheduling**, unless it satisfies the conditions required for the upgradation

Due date

180 days



(Nov'24 Practical Qns)

	Meaning	Provision										
Standard Assets:	No default in repayment of principal or payment of interest	<u>Except NBFC-ML & Above:</u> 0.25% <u>NBFC-ML & Above:</u> 0.4% <i>(Not Applicable for NBFC-UL)</i>										
Sub-Standard Assets:	• <u>Except NBFC-ML & Above</u> → [i.e, BL] An asset which has been classified as NPA for a period not exceeding 18m • <u>NBFC-ML & Above</u> i.e., [ML or UL] An asset which has been classified as NPA for a period not exceeding 12 m	10% of total outstanding										
Doubtful	• <u>Except NBFC-ML & Above</u> → [i.e, BL] Remains a sub-standard asset for a period 'exceeding 18 months • <u>NBFC-ML & Above</u> i.e., [ML or UL] Remains a sub-standard asset for a period 'exceeding 12 months	• 100% Provision: Unsecured or Non-Realizable securities • For Secured Portion:<table><tr><th>Asset</th><th>Provision</th></tr><tr><td>Doubtful for:</td><td></td></tr><tr><td>Upto 1 Yr</td><td>20%</td></tr><tr><td>1 to 3 Yr</td><td>30%</td></tr><tr><td>≥ 3 yrs</td><td>50%</td></tr></table>	Asset	Provision	Doubtful for:		Upto 1 Yr	20%	1 to 3 Yr	30%	≥ 3 yrs	50%
Asset	Provision											
Doubtful for:												
Upto 1 Yr	20%											
1 to 3 Yr	30%											
≥ 3 yrs	50%											
Loss Assets:	• An asset which has been identified as loss asset by the applicable "NBFC" or	100% Should be Written Off (If										



	its "internal" or "external auditor" or by the Bank during the inspection an asset which is adversely affected by a potential threat of non-recoverability due to either erosion in the value of security or non-availability of security or due to any fraudulent act or omission on the part of the borrower	For any reason it remain in Books, provide for 100% provision)
	Substandard Asset also include: an asset where the terms of the agreement regarding interest and / or principal have been renegotiated or rescheduled or restructured after commencement of operations, until the expiry of 1 year of satisfactory performance under the renegotiated or rescheduled or restructured terms; Provided that → classification of "infrastructure loan" as "a sub-standard asset" shall be in accordance with the provisions of Para 17 of master direction - RBI (NBFC- Scale Based Regulation) Directions, 2023;	
Treatment of Provision:	Generally, provision <u>Netted-Off against advance</u>, However, in case of Standard assets provision it separately shown as "Contingent Provisions against Standard Assets" Further, NET NPA = Gross NPA - Provision for NPA (except Provision on Standard assets)	

➤ What is NPA ?

		Other NBFC's (including NBFC ND NSI)
a)	For an Asset	interest has remained overdue for > 180 Days
b)	Term Loan	Interest or installment overdue for > 180 Days
c)	Demand or call loan	Interest or Loan from call date overdue for > 180 Days
d)	Bill	Remain overdue > 180 Days
e)	Short term loan/adv	Interest Remain overdue > 180 Days
f)	Any Due:	any dues on account of sale of assets or services rendered or reimbursement of expenses incurred, Remain overdue > 180 Days
g)	lease rental	lease rental and hire purchase instalment Remain overdue > 180 Days
h)	Credit Facilities	in respect of loans, advances and other credit facilities (including bills purchased and discounted), the balance outstanding under the credit facilities (including accrued interest) made available to the same borrower/beneficiary when any of the above credit facilities becomes non-performing asset. But, for lease and hire purchase transactions → Classify EACH ACCOUNT on basis of recovery

Above 180 days will shift to 90 Days → as per Below Path:

NPA Norms	Timeline
>150 days overdue	By March 31, 2024
>120 days overdue	By March 31, 2025
> 90 days	By March 31, 2026

Note: The glide path will not be applicable to NBFCs which are already required to follow the 90-day NPA norm



➤ General Audit Procedures for All NBFC's:

Q8. During Statutory Audit of NBFC, M. Mr. O is of the opinion that evaluation of I.C system and verification of registration with RBI should not be the part of audit procedure. Briefly state what broad areas should mandatorily become part of the audit procedure? Also comment whether contention of Mr. O is correct?

Answer:

Following are broad areas that should be mandatorily part of the audit procedure for conducting the audit of NBFC:

Trick: R - BC - PC hi nii chalra Audit kese karu

1	Ascertaining the Business of the Company:	- The first step in carrying out the audit of a NBFC is to <u>scan through the Memorandum and Articles of Association</u> of the company, so as to acquaint oneself with the type of business that the company is engaged into. - The task of <u>ascertaining the principal business activity</u> of any NBFC is of paramount importance since the very classification of a company.
2	Evaluation of Internal Control System:	- An auditor should <u>gain an understanding of the accounting system and related internal controls</u> adopted by the NBFC to determine the NTE of his audit procedures. - An auditor should also ascertain whether the I.C are being effectively followed. In particular, an auditor should <u>review the effectiveness of the system of recovery</u> prevalent at the NBFC. The absence of a periodical review system could result in non-detection of sticky advances at their very inception which may ultimately result in the NBFC having an alarmingly high level of NPAs.
3	Registration with the RBI:	- Section 45-IA of the RBI Act, 1934, has made it incumbent on the part of <u>all NBFCs to comply with registration requirements and have minimum net owned funds</u>. - An auditor should <u>obtain a copy of the certificate of registration</u> granted by the RBI or if registration has not been granted, a copy of the application form filed with the RBI. - NBFCs are <u>not entitled to commence business without first obtaining a registration certificate</u> from the RBI. - An auditor should, therefore, verify whether the dual conditions relating to registration with the RBI <u>and</u> maintenance of minimum net owned funds have been duly complied with by the concerned NBFC.
4	Proper Classification:	The auditors must ascertain whether the company <u>properly classified</u> as per the requirements of various regulations. In case, the NBFC has not been classified by the RBI, the classification of a company will have to be determined after a careful consideration of various factors such as particulars of earlier registration granted, if any, particulars furnished in the application form for registration, company's MOA and its financial results
5	NBFC Prudential Norms Directions:	Check compliance with prudential norms encompassing <u>income recognition, income from investments, accounting standards, accounting for investments, asset classification, provisioning for bad and doubtful debts, capital adequacy norms</u> , prohibition on granting of loans by a NBFC against its own shares, prohibition on loans and investments for failure to repay public deposits and norms for concentration of credit/investments.

In the given situation → While planning the audit procedures → there was difference of opinion between O and his partner M → As discussed above NBFCs are not entitled to commence business without first obtaining a registration certificate from the RBI. An auditor should, therefore, verify whether the dual conditions relating to registration with the RBI and maintenance of minimum net owned funds have been duly complied → Further, auditor should gain an understanding of the accounting system and related I.C adopted by the NBFC to determine the NTE of his audit procedures. An auditor should also ascertain whether the internal controls put in place by the NBFC are adequate and being effectively followed. Accordingly, **contention of Mr. O is not correct.**

➤ Audit Procedures for Specific NBFC's:



NBFC Acceptance of Public Deposit Directions: [ML/UL] Trick: Its Process, Credit Rating > Written application > BR to accept > Deposit register > Invest that money > at year end, Give Interest & File return	The auditors must ascertain whether the company properly classified as per the requirements of various regulations: 1) Ceiling on quantum of public deposits has been linked to its credit rating. Obtain a copy of the credit rating assigned to NBFC and check whether the public deposits accepted/held by it are in accordance with the level of credit rating assigned to it. 2) Ascertain whether the NBFC has accepted or renewed any public deposit only after a written application form the depositor in the form to be supplied by the company 3) In case of NBFCs not accepting/holding public deposits, check whether a board resolution has been passed by the NBFC to the effect that it has neither accepted any public deposits nor would it accept any public deposits during the year 4) Verify the deposit register maintained by a NBFC and test check the particulars 5) Check whether the investments made in approved liquid assets by a NBFC holding public deposits have been lodged in safe custody with a designated scheduled commercial bank 6) Test check the interest calculations in respect of public deposits mobilised by a NBFC to ascertain that the NBFC has not paid interest in excess as per specification 7) Check whether the NBFC has filed its prescribed returns in a timely manner 8) In the case of Group Holding Investment Companies, check whether the NBFC has passed a board resolution to the effect that company has invested or would invest/hold its investments in share and securities of group companies specifying the names of companies.
P2P NBFC: [Understand karo uske business ko > ki wo business krne k liye RBI ki chize copy kari (i.e., <u>licence liya</u> ?, <u>reporting</u>, <u>lending</u> <u>borrowing</u> guideline) > board ki policy bhi (3)]	Q9. "Fin crazy" is a P2P online platform registered with RBI. Where does such NBFC fit into in accordance with scale-based regulations? Suggest few audit procedures for above NBFC-P2P falls in base layer, Following are few audit procedure: 1) Gaining an understanding of business conducted by NBFC-P2P. It should be verified that company undertakes only permissible activities applicable to such type of NBFCs like providing online marketplace to participants for lending and borrowing. It should not be engaged in business of lending funds on its own. 2) Verify certificate of registration obtained from RBI for carrying P2P platform 3) Compliance with reporting requirements of RBI 4) Verification of adherence to lending and borrowing guidelines prescribed by RBI 5) Verifying Board approved policy setting out eligibility criteria for participants i.e lenders and borrowers. 6) Verifying board approved policy for pricing of services provided by P2P platform 7) Verifying board approved policy for grievance redressal and complaints 8) Verifying appropriate arrangements entered into among participants & NBFC-P2P
NBFC Prudential Norms:	Q10. How auditor of NBFC would proceed to ensure compliance of Prudential Norms directions. 1) Check compliance with prudential norms encompassing income recognition, income from investments, accounting standards, accounting for investments, asset classification, provisioning for bad and doubtful debts, capital adequacy norms, prohibition on granting of loans by a NBFC against its own shares, prohibition on loans and investments for failure to repay concentration of credit/investments. 2) An auditor should assess on the basis of examinations conducted by him whether the NBFC has complied with the prudential norms. In particular, he should verify that advances and other credit facilities have been properly classified as standard/ substandard/ doubtful/ loss and that proper provision has been made in accordance with the Directions. 3) An auditor should ensure that the Board of Directors of every NBFC granting/intending to grant demand/call loans shall frame and implement a policy for the company. 4) In respect of Non-Performing Assets, an auditor should check whether the unrealised income in respect of such assets has not been taken to the Profit & Loss Account on an accrual basis.



	Income from NPAs should be accounted for on realisation basis only. 5) Check whether all accounts which have been classified as NPAs in the previous year also continue to be shown as such in the current year also. If the same is not treated as an NPA in the current year, auditor should specifically examine such accounts to ascertain whether the A/c has become regular & same can be treated as performing as per the Directions.
Auditors Checklist in General: [Eg., NBFC ICC - Investment & Credit Company]	Q11. audit of NBFC in case Investment companies / NBFC Investment & Credit Company (ICC)? In addition to audit points that may be covered for companies in general, Follow given below: <u>Trick: Shares related point</u> 1) Physically verify all the shares & securities held by a NBFC. Where any security is lodged with an institution or a bank, a certificate from the bank/institution to that effect must be verified. 2) Verify whether NBFC has not advanced any loans against the security of its own shares. 3) In respect of shares/securities held through a depository, obtain a confirmation from the depository regarding the shares/securities held by it on behalf of the NBFC <u>Trick: AS & Income recognition</u> 4) Ascertain whether the requirements of AS 13 "Accounting for Investments" or other accounting standard, as applicable, (to the extent they are not inconsistent with the Directions) have been duly complied with by the NBFC. 5) Verify that dividend income wherever declared by a company in AGM has been duly received by an NBFC and interest wherever due <u>[except in case of NPAs]</u> has been duly accounted for. <u>Trick: Asset related points</u> 6) Physically Check the classification of loans and advances made by a NBFC into Standard Assets, Sub-Standard Assets, Doubtful Assets and Loss Assets and the adequacy of provision for bad and doubtful debts as required by NBFC Prudential Norms 7) Check whether the investments have been valued in accordance with NBFC Prudential Norms and adequate provision for fall in the market value of securities, wherever applicable, have been made there against, as required by the Directions <u>Other Points:</u> 8) Verify the Board Minutes for purchase and sale of investments. Ascertain from the Board resolution or obtain a management certificate to the effect that the investments so acquired are current investments or Long-Term Investments. 9) Test check bills/contract notes received from brokers with reference to the prices vis-à-vis the stock market quotations on the respective dates 10) Check whether the NBFC has not lent/invested in excess of the specified limits to any single borrower or group of borrowers as per NBFC Prudential Norms

➤ **CLASSIFICATION OF FRAUDS BY NBFC:**

Q12. Write a short note on Classification of Frauds by NBFC

Trick: SA 240 wale 2:

- Misappropriation and criminal breach of trust.
- Fraudulent encashment through forged instruments, manipulation of books of account or through fictitious accounts and conversion of property.

Trick: CC-GF

- Unauthorised credit facilities extended for reward or for illegal **G**ratification.
- Negligence and **C**ash shortages.
- C**heating and forgery



- (f) Irregularities in Foreign exchange transactions.
- (g) Any other type of fraud not coming under the specific heads as above.

Cases of 'negligence and cash shortages' and 'irregularities in foreign exchange transactions', reported as fraud if the intention to cheat/ defraud is suspected/ proved.

However, the following cases where fraudulent intention is not suspected/ proved, at the time of detection, will be treated as fraud and reported accordingly:

- (a) Cases of cash **shortages** > ₹10,000/- and
(b) Cases of cash **shortages** > ₹5000/- if detected by management/ auditor/ inspecting officer and not reported on the occurrence by the persons handling cash

➤ **AUDITOR'S DUTY: Compliance with NBFC Auditor's Report - RBI Directions**

In case of NBFC's, Following Persons are also need to be reported in additional to normal reporting requirements to the shareholders under section 143 of the Companies Act, 2013:

- 1) Reporting to the **Board of Directors** on certain **specified matters** and
- 2) To the **RBI** on an **exception basis** has been imposed upon him

Material to be included in the Auditor's report to the Board of Directors: The auditor's report on the accounts of a non-banking financial company shall include a statement on the following matters, namely -

A) For Every NBFC:	1) Auditor shall examine whether the company has obtained a Certificate of Registration (CoR) from the RBI 2) In case of a company holding CoR issued by the RBI, whether that company is entitled to continue to hold such CoR in terms of its Principal Business Criteria (Financial asset/income pattern) as on March 31 of the applicable year 3) Whether non-banking financial company is meeting the required net owned fund requirement as laid down in Master Direction of RBI (NBFC-Scale based regulation 2023) Every NBFC shall submit a Certificate from its Statutory Auditor that it holding a CoR under Section 45-IA of the RBI Act and is eligible to hold it, It shall be submitted to the Regional Office of the Department of NonBanking Supervision, within 5 Working Days from the date of Signing of Auditor's report (as per Sec 134 of Co. Act) and in any case not later than December 31st of that year
B) NBFC accepting/ holding public deposits: [ML/UL] (Special Trick :-)	Q13. NBFC, which is accepting public deposits. Please explain what points are required i.r.o separate report to Board of Directors of NBFC. Apart from the matters enumerated in (A) above, the auditor shall include following matters: <u>Trick: Deposit lene ki aukaad hai ?</u> 1) Whether the non-banking financial company is accepting "public deposit" without minimum investment grade credit rating from an approved credit rating agency as provision of NBFC-Acceptance of PD (RBI) Direction 2016 2) Whether the credit rating, for each of the fixed deposits schemes that has been assigned by one of the Credit Rating Agencies listed in NBFC Acceptance of Public Deposits (Reserve Bank) Directions, 2016. 3) Whether the capital adequacy ratio as disclosed in the return submitted to the Bank in terms of Master Direction of RBI (NBFC - Scale based regulation) 2023 has been correctly determined and whether such ratio is in compliance with the minimum CRAR prescribed therein <u>Trick: Deposit lii ? Exceed to nahi kari limit? Default to nahi kara payment me ? :</u> 4) Whether the public deposits accepted by the company together with other borrowings indicated below viz.



	a) From public by issue of unsecured non-convertible debentures/bonds; b) From its shareholders (if it is a public limited company); and c) Which are not excluded from the definition of 'public deposit' in the NBFC-PD (RBI) Directions, 2016, are within the limits admissible to the company as per the provisions of the NBFC-PD (RBI) Directions, 2016; 5) whether the aggregate amount of deposits outstanding as at any point during the year has exceeded the limit specified by the such Credit Rating Agency 6) Whether company has defaulted in paying to its depositors the interest & /or principal <u>Trick: Some Compliance & Norms to follow:</u> 7) Principal amount of the deposits after such interest and/or principal became due; 8) Whether the company has complied with the prudential norms on income recognition, accounting standards, asset classification, provisioning for bad and doubtful debts, and concentration of credit/investments as specified in the Directions issued by the Bank in terms of the Master Direction of RBI (NBFC - Scale based regulation) 2023. 9) Whether the company has furnished to the RBI within the stipulated period the quarterly return on prudential norms as per Direction of RBI (NBFC - Scale based regulation) 2023 10) Whether the company has furnished to the RBI within the stipulated period the return on deposits specified in DNBS-01 11) Whether, in the case of opening of new branches or offices to collect deposits or in the case of closure of existing branches/offices or in the case of appointment of agent, the company has complied with the requirements contained in the NBFC - Acceptance of PD (RBI) Directions, 2016 12) Whether the company has complied with the liquid asset's requirement (details of the designated bank in which approved securities held is communicated in NBS 3)
C) NBFC Not accepting public deposits: [BL]	Apart from the aspects enumerated in (A) above, the auditor shall include a statement on: 1) Whether the BOD has passed a resolution for non-acceptance of any public deposits; 2) Whether the company has accepted any public deposits during the relevant period 3) Whether the company has complied with the prudential norms relating to income recognition, accounting standards, asset classification and provisioning for bad and doubtful debts as applicable to it in terms of Master Direction of RBI (NBFC - Scale based regulation) 2023; 4) (a) Whether the capital adequacy ratio as disclosed in the return submitted to the RBI in form NBS - 7, has been correctly arrived at and whether such ratio is in compliance with the minimum CRAR prescribed by the RBI; [NBS 7] (b) Whether the company has furnished to the RBI the annual statement of capital funds, risk assets/exposures and risk asset ratio (NBS-7) within the stipulated period 5) Whether the NBFC has been correctly classified as NBFC Micro Finance Institutions (MFI) as defined in Master Direction of RBI (NBFC - Scale based regulation) 2023
D) Reasons to be stated for unfavorable:	unfavorable or qualified, the auditor's report shall also state the reasons for such unfavourable or qualified statement, as the case may be. Where the auditor is unable to express any opinion, his report shall indicate such fact together with reasons therefor
E) Exception report to RBI:	Q14. Auditor of NBFC → exceptions which are required to be reported in the audit report. Q. Krishna Pvt Ltd have business of selling computer parts. However, is fulfilling the Principal Business Criteria → F.A & F.I is more than 50%. What shall be obligation of the Statutory Auditor? In the given case, company qualify as an NBFC & hence is required to obtain Certificate of Registration with RBI. So, statutory auditor has an obligation to submit exception report to the RBI: Obligation of auditor to submit an exception report to the RBI:



- 1) Where, in the case of a NBFC, the statement regarding any of the items referred to in paragraph 3 above, is unfavorable or qualified, or in the opinion of the auditor the company has **not complied with**:
- The provisions of **Chapter III B** of RBI Act (Act 2 of 1934); or
 - NBFC **Acceptance of Public Deposits** (Reserve Bank) Directions, 2016; or
 - Master Direction - **RBI (NBFC - Scale Based Regulation)** Directions, 2023.
- It shall be the obligation of the auditor to make a report containing the **details of such unfavourable or qualified statements** and/or about the non-compliance, as the case may be, in respect of the company **to the concerned Regional Office of the Department of Non-Banking Supervision of the RBI** under whose jurisdiction the registered office of the company is located as per first Schedule to the NBFC Acceptance of Public Deposits (Reserve Bank) Directions, 2016.
- 2) The duty of the Auditor under sub-paragraph (I) shall be to **report only the contraventions** of the provisions of RBI Act, 1934, and Directions, Guidelines, instructions referred to in sub-paragraph (1) and such report shall **not contain any statement with respect to compliance** of any of those provisions.

Q15. Karma is a **Non-Deposit Taking Non-Systemically Important** NBFC → content of the Auditor's Report to the Board.

Hint: Refer Above Auditor's duty -

(A) For Every NBFC & (C) NBFC Not accepting public deposits: Point 1,2,3 Only & (D) Reasons to be stated for unf

Q16. Super Non-Bank Limited, a "Systemically Important Non-Deposit Taking NBFC", Net owned fund of last 4 yrs,

FY 2019-20	FY 20-21	FY 21-22	FY 22-23
Rs. 15 Crore	Rs. 6 crore	Rs. 4 Crore	Rs. 1.5 Crore

Net Owned Funds is **less than ₹ 2 Crore since June 2022**, Auditor reporting requirements? (Old)

Hint: → Sec 45-IA(1)(b) of RBI Act → specifies **INR 2 Cr** as NOF for a NBFC

- NOF of which **currently falls below ₹200 lakh, to submit a statutory auditor's certificate certifying compliance with the prescribed levels by the end of the period as given above**
- NBFCs failing above, shall **not be eligible to hold the CoR** as NBFCs.
- **Refer Above Notes → "For Every NBFC" i.e., whether company has obtain CoR, eligible to hold, till 30th Dec.**
- Hence, in the current case, it is the responsibility of Auditor, to report where NOF has fallen below ₹ 200L.

➤ **CARO 2020:**

- I. 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,
- 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;
 - 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**;
 - If the amount is overdue, state the total amount **overdue for more than 90 days, and whether reasonable steps** have been taken by the company for recovery of the principal and interest;
 - 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; **[Paragraph 3(iii)]**

- II.
- Whether the company is **required to be registered under section 45-IA** of the Reserve Bank of India Act, 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; [Paragraph 3(xvi)]

Q17. for NBFC → **CARO, 2020 reporting, whether registration obtained ? state audit procedure** for this.

Q. NBFC → having NOF of Rs. 1.5 Crore, & was not having registration certificate from RBI & applied for it on 30th Mar 2022. Advise Auditor w.r.t auditor procedures to be taken & reporting requirements of **CARO 2020?** (SM & MTP Nov'24)

Answer: → Audit Procedure for reporting under **CARO, 2020** w.r.t. registration u/s 45-IA of RBI Act, 1934:

- i) **Clause (xvi)** of Paragraph 3 of **CARO 2020**, Requires the company auditor to report:-
- Whether** the company is **required to be registered** under Section 45-IA of the RBI Act, 1934 and if so,
 - Whether** the registration has been **obtained**.
- ii) The auditor is required to examine **whether the company is engaged in the business** which attract the **requirements of the registration**. The registration is required where the financing activity is a principal business of the company. The RBI restrict companies from carrying on the business of a non-banking financial institution without obtaining the certificate of registration.

iii) **Audit Procedure and Reporting:-**

- The auditor should **examine the transactions of the company** with relation to the activities covered under the RBI Act and directions related to the Non-Banking Financial Companies.
- Auditor should examine the FS to ascertain **whether company's financial assets constitute more than 50% of the total assets and income** from financial assets constitute more than 50% of the gross income.
- Ascertain whether the **net owned funds of the company exceeds such amount so as to require** the company to get itself registered as NBFC with RBI.
- Ascertain **whether the company has obtained the registration** as NBFC, **if not, the reasons** should be sought from the management and documented.
- Auditor's **Report under CARO, 2020** shall incorporate the following:
 - Whether the registration is required under section 45-IA** of the RBI Act, 1934.
 - If so, **whether it has obtained** the registration.
 - If the registration **not obtained, reasons** thereof

Conclusion: - net owned funds of Rs. 1,50,00,000/-, which is less in comparison to the prescribed limit i.e. 2 crore rupees and was also not having registration certificate from RBI (though applied for it on 30th March 2022). The auditor is required to report on the same as per Clause (xvi) of Paragraph 3 of **CARO 2020**.

Q18. Sugam Finance is in business of housing finance activities (asset size Rs. 800 Cr). → **not identified by RBI in upper layer**. Under scale-based regulations, what should be **appropriate classification?** **CARO 2020** reporting ? (SM)

Hint: → It's "**middle layer**". (asset size is not relevant in such case).

There is specific reporting requirement under **CARO, 2020 under clause 3 (xvi)(b)** which requires auditor to report: "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"

➤ **IND-AS Applicability on NBFC's:**

01/04/2018	NBFC's having ≥ Rs. 500 Net Worth (Net worth on the basis of "Standalone FS")
01/04/2019	NBFC's having ≥ Rs. 250 Net Worth (Net worth on the basis of "Standalone FS")

On **Group companies** also or in process of listing



➤ **Differences between Division II (Ind- AS- Other than NBFCs) and Division III (Ind- AS- NBFCs) of Schedule III:**

Q19. Differences between Division II (Ind- AS- Other than NBFCs) & Division III (Ind- AS- NBFCs) of S- III

[P&L → (a)&(b), B/S → (c),(d),(e), Cash Flow →(f)]

- a) **OCI:** NBFCs are also required to disclose items comprising 'revenue from operations' and 'other comprehensive income' on the face of the Statement of profit and loss instead of showing those only as part of the notes
- b) **Other Expenditure:**
 - ✓ An NBFC is required to separately disclose by way of a note any item of 'other income' or 'other expenditure' which exceeds 1% of the total income.
 - ✓ Division II, on the other hand, requires disclosure for any item of income or expenditure which exceeds 1% of the revenue from operations or ₹10 lakhs, whichever is higher
- c) **LLP Receivable:** NBFCs are required to separately disclose under 'receivables', the debts due from any LLP in which its director is a partner or member
- d) **Credit Impaired TR:** Separate disclosure of trade receivable which have significant increase in credit risk & credit impaired
- e) **Statutory reserves:** The conditions or restrictions for distribution attached to statutory reserves have to be separately disclose in the notes as stipulated by the relevant statute
- f) **Liquidity:** NBFCs have been allowed to present the items of the balance sheet in order of their liquidity which is not allowed to companies required to follow Division II.

Q20. Listed NBFC audit, disclosure requirements of Schedule III of Companies Act, 2013:

- 1) disclosure of any of item of income or expenditure exceeds 1% or revenue or 10 lacs w.e.higher
- 2) Verification of disclosure reg. Return on Capital Employed Ratio, return on Equity Ratio and NP ratio [Old]

Answer: → Above is applicable to Division II of S-III (companies), Not pertain to Division III of S-III (For NBFC's), → Hence, Need revision as per Division III of S-III, as follows:

- 1) Any item of other income or other expenditure which exceeds 1% of total income
- 2) Disclosure of the following ratios: -

Capital to risks-weighted assets ratio (CRAR)	Tier I CRAR	Tier II CRAR	Liquidity coverage ratio

Q21. NBFC Rating was cut to D from A4 (due to default in repayment of interest), implying that the company was in default or expected to be in default soon. What aspects Auditor should look into in relation to the activity of mobilization of public deposits (particularly in relation to downgrading of credit facilities) by RHL Ltd? (Imp.)

Answer:

Following aspects should be looked in relation to the activity of mobilization of public deposits (particularly in relation to downgrading of credit facilities):

- 1) The ceiling on quantum of public deposits has been linked to its credit rating as given by an approved credit rating agency. Obtain a copy of the credit rating assigned to NBFC and check whether the public deposits accepted/held by it are in accordance with the level of credit rating assigned to it.

In the event of a upgrading/downgrading of credit rating, the auditor should bear in mind that the NBFC will have to increase/reduce its public deposits in accordance with the revised credit rating assigned to it within a specified time frame and should ensure that the NBFC has informed about the same to the RBI in writing.

- 2) In the event of downgrading of credit rating below the minimum specified investment grade, a non-banking financial company, being an investment and credit company or a factor, shall regularise the excess deposit as provided hereunder:



- (a) With immediate effect, **stop accepting fresh public deposits** and renewing existing deposits;
- (b) all **existing deposits shall run off to maturity**; and
- (c) **report the position within 15 working days**, to the concerned **Regional Office of RBI** where the NBFC is registered.
- (d) Provided **no matured public deposit shall be renewed without the express and voluntary consent** of the depositor.

Q22. NBFC (NBFC-D) → following Ind-AS → Extract of P&L is given as per Division III of S-III, in that P&L, Total Income was shown as 10000 Crore. And in schedule of "Other Expenditure", manpower outsourcing cost of Rs. 99.5 Crore is included. (SM)

Hint: 99.5 Crore is not exceeding 1% of Total income → hence it's meeting Division III, S-III requirements.

CHAPTER 15: Overview of Public sector undertaking

➤ INTRODUCTION:

PSU:	Public sector undertakings in India are fundamentally owned or controlled by central Govt , or any state govt or govt's, or partly by the central govt and one or more state govt's
Govt Co. U/s 2(45):	"Government Company" is a company in which: • ≥ 51% of the paid-up share capital is held by the Central Govt or by any State Govt or Govt's or partly by the Central Govt and partly by one or more State Govt's, and • includes a company which is a subsidiary company of such a Government company

Q1. BT Ltd, a company **wholly owned by Central Govt** was **disinvested** → resulting in **40% of shares being held by public**. → Sam is saying that since it's a Listed company, So in Audit, C&AG will not have any role to play. (SM)

Answer: Mention definition of Govt. Co. U/s 2(45) of Co. Act (as given in Above notes)

The auditors of Govt. companies are firms of CA's, appointed by the C&AG, who gives the auditor directions on the manner in which the audit should be conducted. The **listing of company's shares is irrelevant** → Sam's is not correct.

➤ ROLE OF C&AG (Framework of Govt. Audit):

Audit of the above government companies is performed by an independent constitutional authority, i.e. Comptroller and Auditor General of India (C&AG), (**Trick: Appoint kon karega, Remove kon karega, wo Kaam kya krega**)

Article 148:	• Appointment → of C&AG by the President. • Removal → for removal of C&AG, only on the ground of proven misbehaviors or incapacity. • Salary → and other conditions of service to be determined by the Parliament
Article 149:	• Perform such duties & exercise such powers in relation to accounts of Union & States and of any other authority or body as may be prescribed by or under any law made by the Parliament. • C&AG's (Duties, Powers & Conditions) Act, 1971 defines these functions and powers in detail.
Article 150:	• On the advice of the C&AG, President to prescribe such form in which accounts of the Union and States shall be kept
Article 151:	• Audit reports of the C&AG relating to the accounts of the Central/ State Government should be submitted to the President/Governor of the State who shall cause them to be laid before Parliament/State Legislative Assemblies
Hold Office:	• C&AG shall hold office for a term of 6 years or upto the age of 65 years, whichever is earlier. • He can resign at any time through a resignation letter addressed to the President.

➤ Categories for organisation of PSUs

Category for Organisation of PSU	Example:
Departmentally managed undertakings which form part and parcel of Govt. activities →	Eg., Indian Railways , Postal Services , Security Printing Press , Canteen Stores Department , etc.
Govt companies (Inc. deemed government Co. Act, 2013)	
Corporations set up under specific Acts of legislature	Eg., LIC , Unit Trust of India , etc.

➤ Organisations subject to the audit of C&AG Includes i.e. TYPES OF PSU's

1) All the Union and State Government departments and offices including the Indian Railways and Posts and Telecommunications	2) Public commercial enterprises controlled by the Union and State governments, i.e. government companies and corporations (BPCL/IOCL etc)
3) Non-commercial autonomous bodies and authorities owned or controlled by the Union or the States.	4) Authorities and bodies substantially financed from Union or State revenues.



Etc. other organisation is also....

➤ **Audit of Govt Companies (Commercial Audit) (C&AG Role in it):**

Q2. Write a short explanatory note on Role of C&AG in the Audit of a Government company, Or,
 Q. 54% of S/C is held by Govt. → During audit, lot of intervention done by C&AG. → role of C&AG in Govt Co Audit.
 Q. C&AG appointed a CA to conduct supplementary audit u/s 143(6)(a) of Co, Act, 2013. Directors did not think it necessary to discuss supplementary auditor's report and comment of the C&AG. (SM)

1) Appointment- Sec 139(5), 139(7) & 143(5):	Statutory auditors of Government Companies are appointed or reappointed by the C&AG. <u>Sec 143(5)</u> → The C&AG has power to direct the appointed auditor on the manner in which the accounts of the Government company are required to be audited and the auditor so appointed has to submit a copy of the audit report to the C&AG → include the directions , if any, issued by the C&AG the action taken thereon and its impact on FS of company
2) Supplementary audit - Sec 143(6)(a):	C&AG shall within 60 days from the date of receipt of the audit report have a right to conduct a supplementary audit of the FS by such person or persons as he may authorize in this behalf and for the purposes of such audit, require information to be furnished to any person, so authorised.
3) Comment or supplement such Audit Report - Sec 143(6)(b):	Any comments given by the C&AG upon, or in supplement to, the audit report issued by the statutory auditors shall be sent by company to every person entitled to copies of audited FS under sub-section (1) of section 136 of the said Act i.e. every member of the company, to every trustee for the debenture-holder of any debentures issued by the company, and to all persons other than such member or trustee, being the person so entitled and also be placed before the AGM of the company at the same time and in the same manner as the audit report.
4) Test audit: section 143(7):	C&AG may , in case of any company covered under Sec 139(5) / (7), if he considers necessary, by an order, cause test audit to be conducted of the accounts of such company.

In view of above provisions, the approach of directors is not correct. They are required to mandatory send the Supplementary Audit Report and comments of C&AG to every member of company etc. as prescribed, also be placed before the AGM of company in the same manner as in case of audit report. Since in given case neither the report has been distributed nor discussed in the AGM, the directors of company will be liable for contravention of aforesaid sections.

Q3. Statutory auditors of Govt. owned were required to examine, provide replies & report on following:

1. Whether company has system in place to process all accounting transactions ? If yes, financial implications
2. Whether there is any restructuring of an existing loan or cases of waiver by lender If yes, the financial impact
3. Whether funds (grants/subsidy etc.) specific schemes from Central government properly accounted.

Can you gauge likely nature of such responsibility thrust upon auditors of above PSU? (SM)

Hint: → The above areas were **required to examine, report and indicate impact** of these matters in FS → are likely to relate to directions issued by C&AG to statutory auditors under section 143(5).

Now explain Sec 143(5) as given in Above notes → i.e., C&AG has power to direct the appointed auditor etc..etc.

➤ **Audit Board Setup in Commercial Audit (Of Govt. Companies):**

Constitution of Audit Boards for conducting comprehensive audit appraisals of the working of Public → engaged in diverse sectors → Audit Boards associate with them experts in disciplines relevant to the appraisals → they discuss their findings and conclusions with the mngt of the enterprises → to ascertain their view points before finalization → The results of such comprehensive appraisals are incorporated by the C&AG in his reports → Audit Boards have no separate legal entity and work under the supervision and control of the C&AG

➤ **Specialised Committee's to Scrutinise Annual Accounts and the Audit Reports:**

- **Action on Audit Reports** → Parliament have Limited Time to review report → So they have constituted 3



committees to review the audit reports

- **Final User** of Report's are **Parliament & State Legislature** → So They have set-up some committee's which evaluate the report of C&AG & then committee ask further info. From ministries

Public Accounts Committee (PAC) → check Following:	Estimates Committee (check whether policies give improvement as estimated)	Committee on Public Undertakings
1) That the moneys were disbursed/Spent legally on the service or purpose to which they were applied 2) That the expenditure incurred was authorized 3) That re-appropriation has been made in accordance with the provisions made (i.e. distribution of funds) . (Eg., Money allocated to built school, but excess money left, so t/f that fund to built hospital... this is done by following Rules)	The Committee examines the estimates with a view to: 1) Report what economies, improvements in organization, efficiency or administrative reform, consistent with the policy underlying the estimates may be effected ; 2) Suggest alternative policies ; 3) Examine whether the money is well laid out within the limit ; and 4) Suggest the form in which the estimates (Budgets/Forecast) shall be presented to Parliament .	Examine Financial control on PSU's: 1) to examine the reports and accounts of public undertakings 2) to examine the reports of the C&AG on public undertakings 3) to examine the autonomy and efficiency of public undertakings and to see whether they are being managed in accordance with sound business principles and prudent commercial practices 4) to exercise other functions vested in the PAC & the Estimates Committee as are not covered above & as may be allotted by the Speaker from time to time .

* It's duty of **PAC committee** → to **examine** the **statement of accounts** of **autonomous and semi autonomous** bodies (whose audit is **conducted by C&AG** under the **directions** of the **President** or by a **Statute of Parliament**)

** **Estimate committee** → **Not comment on policy** approved by **Parliament** → Unless have an evidence that policy not giving desired result or leading waste

*** Financial Committees, in doing so, is to **focus not only on the individual irregularity, but also on the defects in the system** which led to such irregularity, and the need for **correction** of such systems and procedures

Q4. C&AG of India plays a key role in the functioning of the financial committees of Parliament & State Legislatures. He has come to be recognised as a 'friend, philosopher and guide' of the Committees. W.r.t above, → list down role of C&AG. → Also, briefly discuss the functions of "Estimates Committee" of Parliament

Answer:

(Author's Gyaan: C&AG Conduct audit through IAAD.. Indian audit and a/c's department → report is evaluated by 3 Committees → committee report to Parliament / State Legislature → Parliament will issue notes to Committees & scold on Railway ministry & → Railway ministry will take action, then → Inform to 3 Committees → committee will again give it to C&AG to recheck it)

- His Reports generally **form the basis of the Committees' working**, although they are not precluded from examining issues not brought out in his Reports;
- He **scrutinises the notes which the Ministries submit to the Committees** and helps the Committees to check the correctness of submissions to the Committees and facts and figures in their draft reports;
- The Financial Committees **present their Report to the Parliament/ State Legislature** with their observations and recommendations. The various **Ministries / Department** of the Government are required to **inform the Committees of the action taken by them** on the recommendations of the Committees (which are generally accepted) and the Committees present Action Taken Reports to Parliament / Legislature;
- In respect of those Audit Reports, which could not be discussed in detail by the Committee's, written answers are obtained from the Department / Ministry** concerned and are sometimes incorporated in the Reports presented to the Parliament / State Legislature.



This ensures that the Audit Reports are **not taken lightly by the Government**, even if the entire report is not deliberated upon by the Committee.

[Refer Above table : Function of "Estimate Committee"]

Q5. Of PSU → One of the financial committees has **decided to examine its physical & financial performance.** also examined audit findings of C&AG. **Which financial committee** is this ? its main functions. (SM)

Hint: It's "**Committee on Public Undertakings (COPU)**", refer above notes to discuss it's function

➤ **OBJECTIVE AND SCOPE OF PUBLIC ENTERPRISES AUDIT** (End me krte h ;0)

Trick: FM subject ka banda ho ya PCM ka, Govt ko help karna Decision lene me & Issue highlight karne me, jisse EEE achieve ho

- 1) **Fiscal and Managerial Accountability:** Two main elements, viz.,
 - (a) **Fiscal Accountability:** It includes audit of provisions of funds, sanctions, compliances and propriety; and
 - (b) **Managerial Accountability:** It includes audit of efficiency, economy and effectiveness (Also referred as efficiency-cum-performance audit)
- 2) **Propriety Audit:**
 - This audit is directed towards an examination of management decisions in sales, purchases, contracts, etc. to see whether these have been taken in the best interests of the undertaking and conform to accepted principles of financial propriety.
- 3) **Comprehensive Audit:** Under comprehensive audit, the C&AG do **not really cover again the field which has already been covered.**
 - He conducts an appraisal or an efficiency-cum-performance audit.
 - He sees whether the undertakings have fulfilled the objectives for which they have been established,
 - Whether value-for-money spent has been obtained, whether the targets have been achieved, etc.
 - He locates the areas of weakness including review of the decisions taken by the management and a comprehensive appraisal of the performance of the undertaking
- 4) **Helping Government:**
 - Bringing out financial and operational deficiencies, inadequacies or ineffectiveness of systems, shortfalls in performance, etc. and by analysing the causes of shortfall from acceptable standards of performance.
- 5) **Organisation's Decision to be taken by Competent Authority:**
 - In examining the decisions of a management, the auditor examines that these were taken by the competent authority after examination of all aspects (economic, technological, public interest) on the basis of all the relevant information available at that time and taking into consideration the different alternatives available to management and that the decisions were consistent with the aims and objectives of the enterprise.
- 6) **Highlighting Issues of Efficient and Economic Operations:** Financial performance is linked with physical performance and issues of efficient and economic operations and management of resources are highlighted.
- 7) **Audit of PSUs not constrained to Financial and Compliance Audit:** Audit of public enterprises in India is not restricted to financial and compliance audit; it extends also to performance (**efficiency, economy and effectiveness** with which these operate and fulfill their objectives and goals).

➤ **ELEMENTS OF PSU AUDITS:**

Three Parties:	1) Auditor: The role of auditor is fulfilled by Supreme Audit Institution (SAI), India and by its personnel delegated with the duty of conducting audits. [C&AG & the Indian Audit and Accounts Department (IAAD) <u>function under SAI</u>] Senior functionaries of SAI representing C&AG in the state are called Accountants General. 2) Responsible Party: Generally, auditable entities and those charged with governance of the



	auditable entities would be the responsible parties. 3) Intended Users : Intended users are the individuals, organizations or classes thereof for whom the auditor prepares the audit report.
Variance:	1) Subject matter : This refers to the information, condition or activity that is measured or evaluated against certain criteria (eg, Financial Information) 2) Criteria : These are the benchmarks used to evaluate the subject matter (eg, FRF) 3) Subject matter information : This refers to the outcome of evaluating or measuring the subject matter against the criteria. (eg, Financial Statement)
Types of engagement	1) Attestation Engagements : The "responsible party" measures the subject matter against the criteria and presents the subject matter information, on which the auditor then gathers sufficient and appropriate audit evidence to provide a reasonable basis for expressing a conclusion • Example: Financial audits 2) Direct Reporting Engagement : In direct reporting engagements, it is the "auditor" who measures or evaluates the subject matter against the criteria. • Example: Performance audits and compliance audits

➤ Principles of PSU Audits:

General Principles: (Special Trick :-)	Trick: IPCC me padh liya tha, Audit risk & Materiality ka Documentation Audit team hi karegi 1) Ethics & Independence 2) Professional Judgement, due care and skepticism 3) Communication 4) Quality Control 5) Audit Risk 6) Materiality 7) Documentation 8) Audit Team Management & Skill	
Principles related to the Audit Process:	Planning the Audit:	- Establish the terms of the audit. - Obtain understanding of the entity. - Conduct Risk assessment of problem analysis. - Identify risks of fraud. - Develop an audit plan.
	Conducting the Audit:	- Perform the planned audit procedures to obtain audit evidence. - Evaluate audit evidence and draw conclusions.
	Reporting & Follow-up	- Prepare a report based on the conclusions reached. - Follow-up on reported matters as relevant.

➤ Type of Audits:

1) Financial Audit 2) Compliance Audit 3) Comprehensive Audit 4) Propriety Audit 5) Performance Audit

1) Financial Audit:

Meaning:	Financial audit is primarily conducted to: 1) Express an audit opinion on the financial statements; and 2) Enhance the degree of confidence of intended users in the financial statements. The C&AG shall express an opinion as to whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.



2) Compliance Audit:

Meaning: (i.e., To Comply with Something)	Compliance audit is the independent assessment of whether a given subject matter is in compliance with the applicable criteria . Assessing whether activities, financial transactions and information comply in all material respects , with the regulatory and other rules i.e., Comply with: <table border="1" data-bbox="277 317 1469 483"> <tr> <td data-bbox="277 317 472 401">Regularity:</td><td data-bbox="472 317 1469 401">adherence of the subject matter to the formal criteria emanating from relevant laws, regulations and agreements applicable to the entity.</td></tr> <tr> <td data-bbox="277 401 472 483">Propriety:</td><td data-bbox="472 401 1469 483">Observance of the general principles governing sound financial management and the ethical conduct of public officials.</td></tr> </table>	Regularity:	adherence of the subject matter to the formal criteria emanating from relevant laws, regulations and agreements applicable to the entity.	Propriety:	Observance of the general principles governing sound financial management and the ethical conduct of public officials.
Regularity:	adherence of the subject matter to the formal criteria emanating from relevant laws, regulations and agreements applicable to the entity.				
Propriety:	Observance of the general principles governing sound financial management and the ethical conduct of public officials.				
Conducted:	Compliance Auditing is generally conducted either: - With audit of financial statements, or - Separately as individual compliance audits - In combination with performance auditing				
Non-comply	compliance auditing is part of a performance audit (EEE Evolution) → Noncompliance may lead to performance audit				

Q6. During **Audit of State Govt. Dept**, C&AG observed that Prescribe law of state defined Flat based on 2 criteria in premises : (1) → Dwelling units exceeding a threshold limit (2) → Buildings with a total area surpassing a threshold limit. However, relevant database do not include column for entering Area of Building → So some buildings were identified as flat, even though they have less dwelling (Wrong classification).

Identify **type & nature of audit** performed above, and to whom to submit report. (SM & OLD)

Hint: Subject matter should comply Applicable criteria → "**Compliance audit**" → refer above "**MEANING**".

As per Article 151 → C&AG report to submit to **President/Governor of the State** who shall cause them to be laid before Parliament/State Legislative Assemblies.

Current case → report relate to **State G. dept** → Submit to **Governor of state** to laid before **State legislative assembly**

3) Comprehensive Audit:

Q7. A PSU engaged in production of electricity. It had commissioned a new project for a cost of ₹ 5,750 crore. **State the matters that a Comprehensive Audit by C&AG may cover in reporting on performance & efficiency.**

Hint: Refer below - Issues examined

Meaning:	Assists the legislature in reviewing the performance of public undertakings . He conducts an efficiency-cum-performance audit other than the field which has already been covered either by the internal audit of the individual concerns or by the professional auditors. He locates the area of weakness for managements' information Auditor combine all aspects : Financial , Compliance and Performance audits to get holistic approach
Issues Examined: (Special Trick :-)	Some of the issues examined in comprehensive audit are: <u>Trick: Investment Related - Investement karne k pahle R&D kar lena ki.</u> - Does the enterprise have research and development programmes? What has been the performance in adopting new processes, technologies, improving profits and in reducing costs through technological progress? - How does the overall capital cost of the project compare with the approved planned costs? Were there any substantial increases and, if so, what are these and whether there is evidence of extravagance or unnecessary expenditure? - Has the planned rate of return been achieved? - If the enterprise has an adequate system of repairs and maintenance?



Trick: Poore project ki planning acche se karna , chaai iske liye koi accha saa Project formulation system purchase karna pade

- 5) Is there any poor or insufficient or inefficient **project planning**?
- 6) Are the **systems of project formulation and execution sound**? Are there inadequacies? What has been the effect on the gestation period and capital cost?

Trick: Production & Purchase Policy related:

- 7) Have the **planned production** or operational outputs been **achieved**? Has there been under utilisation of installed capacity or shortfall in performance and, if so, what has caused it?
- 8) Are the **purchase policies adequate**? Or have they led to piling up of inventory resulting in redundancy in stores and spares?

Are **cost control measures adequate** and are there inefficiencies, wastages in raw materials consumption, etc.?

4) Propriety Audit:

Q8. What are the **principles** involved regarding "Propriety audit" in the case of Public Sector Undertaking?

Hint: Refer Meaning & Principles below

Meaning: (Special Trick :-)	Audit of public enterprises in India is not restricted to financial and compliance audit; it extends also to efficiency, economy and effectiveness and fulfill their objectives and goals Propriety audit stands for verification of transactions on the tests of Public interest, Commonly accepted customs and standards of Conduct. (PCC) • Tests boil down to tests on economy, efficiency and faithfulness. • Its emphasis to the substance of transactions and looks into the appropriateness thereof on a consideration of financial prudence, public interest and prevention of wasteful expenditure. • It is also seen whether every officer has exercised the same vigilance in respect of expenditure incurred from public money, as a person of ordinary prudence would exercise in respect of expenditure of his own money under similar circumstances
Principles:	<u>Propriety requires the transactions, and more particularly expenditure, to conform to certain general principles. These principles are:</u> (i) That the expenditure is not prima facie more than the occasion demands and that every official exercises the same degree of vigilance in respect of expenditure as a person of ordinary prudence would exercise in respect of his own money; (ii) That the authority exercises its power of sanctioning expenditure to pass an order which will not directly or indirectly accrue to its own advantage; (iii) That funds are not utilised for the benefit of a particular person or group of persons and (iv) That, apart from the agreed remuneration or reward, no other avenue is kept open to indirectly benefit the management personnel, employees and others.
Functions of Auditor in case of Propriety audit:	Q9. You are appointed by C & AG to conduct the propriety audit and report on the funds utilized by the state government. What functions as an auditor will be performed by you? (Nov'24) <u>Trick: Substitute the wrong expense habits ... Plan the Right Expense > which give maximum & optimum result → I'm saying for your interest only</u> • see that any substitute plan of action can bring about an improvement on current operation and as well as return from capital expenditure • see that all expenditure incurred are properly planned.



	• see that the size & channels of <u>expenditure</u> are rightful & expected to give maximum results. • appraise whether those <u>expenditure</u> are likely to give optimum result. • examine the actions and decisions of the management to see that they are conducive to public interests and that they meet the standards of conduct	
Problems in Propriety Audit:	• "propriety" is a moral term and can be understood by reference to the concept of morality accepted by the society at a given time • Audit of financial accounts by reference to financial and legal requirements, propositions are existence, accuracy, title, ownership, compliance etc., which are all verifiable, But In propriety audit the formulation of verifiable auditing propositions poses the problem. • Propriety audit has an inherent element of subjectivity because it is very difficult to establish standards of public interest, commonly accepted customs, standards for conduct which are not firm basis for audit evaluation • The norms so developed is for Government departments. Can-Not ipso facto apply to transactions of private sector which have distinct and more limited, objectives suited to them. • if the management of each entity, irrespective of any legal requirements, formulates norms of propriety for the entity, The element of subjectivity in propriety evaluation will get reduced. • Propriety as a moral element should be a matter of evaluation based on objectives and prevailing circumstances. For example, a travel by air as such should not be considered wasteful unless it is proved that a travel by rail would have been feasible in the circumstances and would have brought the same results brought by the air travel.	
Propriety Elements:	Mentioned in Companies Act:	<i>Refer Section 143 (1) of company audit chapter</i>
	Mentioned in CARO 2020:	<i>Refer Clause 3(b),(c),(d),(f) Clause 4, 8, 9, 10, 11, 13, 15, 18 in CARO 2020 Chapter</i>

➤ Performance Audit:

Q10. Briefly discuss the issues addressed by Performance Audits.

Hint: Refer Below - Meaning, Economy, Efficiency, Effectiveness

Meaning:	A performance audit is an objective and systematic examination of evidence for the purpose of providing an independent assessment of the performance of a government organization, program, activity, or function in order to provide information to improve <u>Public accountability</u> and facilitate <u>Decision-making</u> by parties with responsibility to oversee or initiate <u>Corrective action</u> (PDC). → conducted by the C&AG through various subordinate offices of IAAD (Indian audit & a/c dept) → Accountability → Whether EEE received → tax payers/citizens have received value for money According to the guidelines issued by the C&AG, Performance Audits usually address issues of: <table><tr><td>1) Economy</td><td>2) Efficiency</td><td>3) Effectiveness</td></tr></table>	1) Economy	2) Efficiency	3) Effectiveness
1) Economy	2) Efficiency	3) Effectiveness		
Economy:	It is minimising the cost of resources used for an activity, having regard to appropriate quantity, quality and at the best price . (Resources e.g., human, financial and material))			
Efficiency:	Q11. In carrying out efficiency audit of a PSU, what important aspects to be looked into? It is the input-output ratio. In the case of public spending, efficiency is achieved when the output is maximised at the minimum of inputs, or input is minimised for any given quantity and quality of output. <u>Auditing efficiency embraces aspects such as whether:</u> <u>Trick: Efficient procedure</u> banao for resources Procure, Use & remaining ko Protect > Jisse apne <u>Program ka objective Cost Effectively & efficiently achieve</u> ho jaae			
(Special Trick :-)				



	1) Efficient operating procedures are used; and 2) sound procurement practices are followed; 3) human, financial and other resources are efficiently used; 4) optimum amount of resources (staff, equipment, and facilities) are used in producing or delivering the appropriate quantity and quality of goods or services in a timely manner 5) resources are properly protected and maintained; 6) the objectives of public sector programmes are met cost-effectively. 7) public sector programmes, entities and activities are efficiently managed, regulated, organised and executed;
Effectiveness:	It is the extent to which objectives are achieved and the relationship between the intended impact and the actual impact of an activity. <u>In auditing effectiveness, performance audit may, for instance:</u> <u>Trick: Desired result achieve ho kya?</u> 1) Determine the extent to which a program achieves a desired level of program results; <u>Trick: Nahi, Itni satisfactory performance to nahi lag rhi?</u> 2) Identify factors inhibiting satisfactory performance or goal-fulfilment; <u>Trick: Kya aapne dusre alternative nahi dekhe more effective karne k liye?</u> 3) Determine whether management has considered alternatives for carrying out the program that might yield desired results more effectively or at a lower cost; 4) Identify ways of making programmes work more effectively. <u>Trick: haa dekhe the, kisi me L&R bich me aara tha, kiski me Duplicacy thi?</u> 5) Assess compliance with laws and regulations applicable to the program 6) Assess whether the programme complements, duplicates, overlaps or counteracts other related programmes; <u>Trick: Accha chalo Effectiveness monitor karte rhna timely?</u> 7) Assess the effectiveness of the program and/or of individual program components 8) Assess the adequacy of the management control system for measuring, monitoring and reporting a programme's effectiveness;
C&AG Audit:	The supplementary or test audit conducted by the Comptroller and Auditor General is in the nature of efficiency-cum-performance appraisal .
Planning for Performance Audit: Trick: ...	1) Understanding the entity/programme Source of understanding the entity: a) <u>Documents of the entity</u>: Annual reports, budget documents, accounts, minutes b) <u>Documents of Legislative</u>: Legislation (Law), parliamentary questions and debates (over that Law), reports of the Public Accounts Committee c) <u>Policy documents</u>: Documents of Planning Commission, Ministry of Finance etc. d) <u>Academic or special research</u>: Independent evaluations on the entity, academic research and similar work done by other governments e) <u>Past audits</u> f) <u>Media coverage</u>: Print and electronic media g) <u>Special focus groups</u>: Audit Advisory Committee concerns, annual and special reports of World Bank, Reserve Bank of India reports 2) Defining the objectives and the scope of audit 3) Determining audit criteria: Audit criteria are the standards used to determine whether a program meets or exceeds expectations. Audit criteria are reasonable and attainable standards of performance against which economy, efficiency and effectiveness of programmes and activities can be assessed

Audit Criteria (SOP's & Policies) may be sought to be obtained from following sources:

Q12. You as auditor of a AKY Ltd → After determined the audit objectives, now you have been requested to **draft audit criteria**. What are the **sources** that you will use?

Trick: Internal Manual & Policy, External Criteria or Expert

- 1) Procedure **manuals** of the entity.
- 2) **Policies**, standards, directives and guidelines.
- 3) **Criteria used by the same entity or other entities** in similar activities or programmes.
- 4) **Independent expert opinion** and know how.
- 5) New or established **scientific knowledge** and other reliable information
- 6) General management and **subject matter literature** and research papers.

4) Deciding **audit approach**

Q13. In PSU → **delay in completion of work due to failure of timely decision** → what kind of Audit ? and describe method of conducting such audit

Hint: (Define Performance Audit → and Below approach/Method)

There is no uniform audit approach, Some of the methods:

- 1) **Analysis of procedures**: Review of the systems in place for planning, conducting, checking and monitoring the activity
- 2) **Quantitative analysis**: It involves examination of available data relating to financials like earnings, revenue, or data relating to programme implementation like details of beneficiaries etc. → However, it may **not be possible for the auditor to work with complete data due to its high volume**. In such cases, **sampling techniques are required** to be used (**MCQ**)
- 3) **Analysis of results**: It requires the auditor to carry out actual output-input analysis to determine the efficiency
(Below are points related to collecting Data for Audit)
- 4) **Use of existing data**: The audit staff should investigate the data held by entity management and by other relevant sources
- 5) **Surveys**: Survey is a method of collecting information from members of a population to assess the interrelation of events and conditions
- 6) **Case studies**: Descriptive analysis of an entity, scheme or a programme. It involves analysis of a particular issue

5) Developing **audit questions**

- 6) Assessing **audit team skills** and whether outside expertise required
- 7) Preparing **Audit Design Matrix** [*Refer Additional PDF Booklet*]
- 8) Establishing **time table and resources**
- 9) **Intimation of Audit programme** to audit entities

PQR:

**ICAI
Example:
Minimum
Wages Act**

Performance Audit of enforcement mechanism for administering the provision of Minimum Wages Act (a social welfare legislation):

- 1) Auditors **must possess knowledge** of the **industries or labor contracts** where these provisions are applicable
- 2) He shall **evaluate the standard of living before implementation & after implementation** of Act
- 3) Evaluate the evidence available as to **nature of returns** prescribed
- 4) Auditor shall also have to **evaluate the economy, efficiency and effectiveness** in the welfare systems to be audited
- 5) Study the **shortcomings in the coordination between different agencies** like labor department, EPF and ESI organization



- 6) study actual level of compensation required in each area keeping in mind the local living conditions and where the minimum wages prescribed

Q14. ICAI Illustration: The objectives of audit in connection with a State Electricity Distribution Company were to ascertain whether the:

- a) total cost of providing electricity is being recovered by timely submissions to State Electricity Regulatory;
- b) tariff orders, sales circulars and sales instructions were issued timely, without any ambiguity. They were implemented in time;
- c) metering, billing and collection was managed efficiently and effectively;
- d) monitoring and internal controls were efficient.

Q15. Refer Above Question (Illustration). → What kind of audit is this? any two sample observations for audit report. → Also briefly discuss the steps suggested to the auditors for planning such an audit.

Hint: → This is a performance audit. Sample observations could be:

- (i) **Non replacement of defective/ burnt meters:** Large number of meters, much in excess of the permitted limit of 1% of the total meters were defective and their replacement was not completed within the stipulated time of 1 month. This resulted in billing on average basis for a continuous period of several months. This could result in losses as well as administrative hassles and disputes with consumers.
- (ii) **Under charging of meter rent:** As per Schedule of Charges, the Company is required to charge meter rent of ₹30 per month for a single phase meter and ₹40 per month for three phase meter. It was observed that the Company had short charged meter rent of ₹60 lakh from 3 lakh consumers in 5 lakh bills during the period.

For Steps of Planning, "Refer Planning for Performance Audit" as given in above notes

Q16. ABG & Co., a Chartered Accountant firm has been appointed by C & AG for performance audit of a Sugar Industry. What factors should be considered by ABG & Co., while planning a performance audit of Sugar Industry?

Answer:

- Understanding the entity/programme
- Defining the objectives and the scope of audit
- Determining audit criteria
- Deciding audit approach
- Developing audit questions
- Assessing audit team skills and whether outside expertise required
- Preparing Audit Design Matrix
- Establishing time table and resources
- Intimation of Audit programme to audit entities

Q17. C&AG appointed Sambhav & Ass., a CA firm, to conduct Performance audit of MAP Ltd., a PSU. Firm conducted the audit with view to check all the expenses of unit are in conformity with public interest & publicly accepted customs. Audit report submitted by audit firm was rejected by C&AG. Give your opinion on action of C&AG. (SM)

Hint: Explain the given case (CA appointed to check all expenses in conformity with) → is not Performance Audit

- Mention Meaning/Definition of Performance Audit (As given in above notes)
- Performance is conducted by C&AG through various subordinate offices of Indian Audit & A/c Department (IAAD).
- Therefore, the objectives of performance auditing are evaluation of economy, efficiency, and effectiveness of policy, programmes, organization and mgnt. → Performance auditing focuses on areas in which it can add value which have the greatest potential for development. (Responsible party are also required to define intermediate and final outputs and outcomes in measurable and monitorable terms, standardise the unit cost of delivery and benchmark quality of outputs and outcomes)
- Thus, **rejection of audit report** (submitted by audit firm) by C&AG is in order as audit with a view to mere check all the expenses in conformity to the public interest and accepted customs is not performance audit in all aspects.

Q18. Direct Benefit Transfer (DBT) is a major reform initiative of the Government of India to ensure better and timely delivery of benefits from Govt to people. It marks a paradigm shift in the process of delivering benefits like wage payments, fuel subsidies, food grain subsidies, etc. directly into the bank accounts of the beneficiaries removing leakages and enhancing financial inclusion.
C & AG is likely to undertake a performance audit for selected social security pension schemes & scholarship schemes under DBT. Objectives of such performance audit? Explain "audit criteria", how these can be determined in above case. (SM & MTP 2024).

Answer:

The likely objectives of performance audit of some selected social security pension schemes and scholarship schemes:

- 1) Whether proper planning and process were in place to capture data of beneficiaries under above schemes
- 2) Whether necessary steps were taken for implementation of DBT like preventing delay in payments to the intended beneficiaries and pilferage and duplication
- 3) Whether the infrastructure, organization and management of DBT were adequate and effective

➤ **AUDIT CRITERIA:** standards used to determine whether a programme meets or exceeds expectations. It provides a context for understanding the results of the audit. Audit criteria are reasonable and attainable standards of performance against which economy, efficiency and effectiveness of programmes and activities can be assessed.

So Criteria in above situation, various documents issued by Govt of India and state government like circulars, instructions, Standard operating procedure manuals, guidelines of schemes on identification and authentication of beneficiaries etc, general management and subject matter literature can be used to determine "audit criteria".

➤ **AUDIT REPORT OF THE COMPTROLLER AND AUDITOR GENERAL:**

Q19. PSU Audit report → Enumerate the contents of Audit Report presented by C&AG.

To facilitate a proper consideration, the reports of the C&AG on the audit of PSUs are presented to the Parliament in several parts consisting of the following: (GAAR)

- 1) Introduction containing a General review of the working results of Government companies, deemed Govt companies and corporations;
 - 2) Results of comprehensive Appraisals of selected undertakings conducted by the Audit Board;
 - 3) Resume of the company Auditors' reports submitted by them under the directions issued by the C&AG and that of comments on the accounts of the Government companies; and
 - 4) Significant Results of audit of the undertakings not taken up for appraisal by the Audit Board
- For certain specified states, the C&AG submits a separate audit report (commercial) to the legislature,
 - while for other States/Union Territories with legislature, there is a commercial chapter in the **main audit report**.
 - The State audit reports, contains both the results of audit appraisal of performance of selected companies/corporations as well as important individual instances of financial irregularities, wasteful expenditure, system deficiencies noticed by the statutory auditors, and a general review of the working results of Government companies and corporations.



CHAPTER 16: INTERNAL AUDIT

NOTE: Some topics of this chapter is already covered in SA-610, refer that also

➤ INTRODUCTION:

Definition:	Internal Audit provides independent assurance on the effectiveness of internal controls and risk mgnt processes to enhance governance and achieve organisational objectives																				
Scope Objective of IAF (SA 610):	May go beyond assurance to include an advisory (consulting) → provided this does not compromise the independence → include review of operational activities, IC, L&R [Refer SA 610: GIR - IC-FR - O]																				
IASB & SIA:	ICAI constituted IASB (Internal Audit Standards Board) → with the object of formulating Standards on Internal Audit (SIAs) → for guidance of the members, [Recommendatory in nature]																				
Applicability:	As per section 138 of the Companies Act, 2013, read with Rule 13 following companies shall be required to appoint an internal auditor: 1) Every Listed company 2) Every unlisted public company having: <table><tr><td>O/s deposits</td><td>≥ Rs.25 Crore</td><td>at any point of time during the preceding FY</td></tr><tr><td>Paid up S/c</td><td>≥ Rs.50 Crore</td><td>during the preceding FY ,Or,</td></tr><tr><td>O/s loans or borrowings from banks or public F.I</td><td>> Rs.100 Crore</td><td>at any point of time during the preceding FY, Or,</td></tr><tr><td>Turnover</td><td>≥ Rs.200 Crore</td><td>during the preceding FY ,Or,</td></tr></table> 3) Every Private company having: <table><tr><td>O/s loans or borrowings from banks or public F.I</td><td>> Rs.100 Crore</td><td>at any point of time during the preceding FY, Or,</td></tr><tr><td>Turnover</td><td>≥ Rs.200 Crore</td><td>during the preceding FY ,Or,</td></tr></table>			O/s deposits	≥ Rs.25 Crore	at any point of time during the preceding FY	Paid up S/c	≥ Rs.50 Crore	during the preceding FY ,Or,	O/s loans or borrowings from banks or public F.I	> Rs.100 Crore	at any point of time during the preceding FY, Or,	Turnover	≥ Rs.200 Crore	during the preceding FY ,Or,	O/s loans or borrowings from banks or public F.I	> Rs.100 Crore	at any point of time during the preceding FY, Or,	Turnover	≥ Rs.200 Crore	during the preceding FY ,Or,
O/s deposits	≥ Rs.25 Crore	at any point of time during the preceding FY																			
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Turnover	≥ Rs.200 Crore	during the preceding FY ,Or,																			
Who can be I. Auditor? [Sec 138]	- chartered accountant or a cost accountant (whether engaged in practice or not), or - such other professional as may be decided by the Board. - The internal auditor may or may not be an employee of the company.																				

Q1. Prateek → A post graduate in Law → career in Indian Audit & Accounts Service for about 25 years, After Retirement → He wants to take responsibilities as Chief internal auditor (in one of Listed Company). The Board of company is keen on him due to his impressive credentials. Can he be appointed? (SM)

Hint: Refer Above notes "Who can be I. Auditor?" [Sec 138]

The Board can appoint any professional as may be decided by it. The applicant in question is a law post graduate and has 25 years' experience (has necessary experience and skills required) → So Board can appoint

Q2. JKT Pvt. Ltd. → ₹40 lacs paid-up capital, ₹9.50 Cr reserves, Turnover of last 3 consecutive FY, immediately preceding the FY under audit → ₹49 Cr, ₹145 Cr and ₹260 Cr, but does not have any internal audit system.

Hint: Explain applicability of internal audit (as explained above),

Given Case → turnover of ₹260 crores during the preceding FY (more than 200 Cr) → Internal Auditor mandatory.

Q3. One of the independent directors sought Info reg. the appointment of internal auditors for below companies:

Figures are in ₹ crore and correspond to the previous year

Name	Nature	Equity Share	Turnover	Loan from	Public



		Capital		Bank and PFI	Deposits
AADI Ltd.	Listed	100	190	50	24
AJIT Ltd.	Unlisted Public	60	190	50	24
NEMI Ltd.	Unlisted Private	60	190	50	0

Hint:

- Explain "applicability of I.Audit" & "Who can be internal auditor"
- AADI Ltd. is a listed company : Applicable
- AJIT Ltd. is unlisted public company, 60 crore as equity share capital
- NEMI Ltd. is unlisted private company : No condition fullfill
- AADI Ltd. and AJIT Ltd. is required to appoint the internal auditor.

IMPORTANT → In Few Qns → ICAI will confuse you by Giving Current Year Data, as well as Previous Year Data → So to check Internal audit applicability → Just check the Previous Year Data ... Ignore Current Year Data

➤ Consideration in Internal Audit Plan:

Q4. What approach would Mr. A follow to prepare the internal audit plan for next year?

The internal auditor **should, in consultation with TCWG**, including the audit committee, **develop and document a plan** for each internal audit engagement to help him conduct the engagement in an efficient and timely manner.

Internal audit plan should be developed in such a manner that all the business processes **covering both financial as well as operational activities** are reviewed by internal audit function within a defined time cycle. Also,

Ensuring that appropriate consideration is made and adequate balance is ensured to the following:

Trick: "Risk", "Risk appetite" ko dkh k decide karo ki kis "Area" pe kitne "efforts" daalne h > fir valuable input do managerial f(x) ko

- **Risk** underlying the business process
- **Risk Appetite** of the organization
- Coverage of **all auditable areas** within the defined time range
- **Effort** involved in conducting the internal audit for a particular business process
- **Value** that the internal audit can provide to the organization
- In addition, each of the **managerial functions** should be reviewed by the internal auditor

➤ SCOPE OF INTERNAL AUDITING:

Scope of Internal Auditor Work include review of:	Trick: FOLI > SIR 1) Custodianship & Safeguarding of Assets (Fixed assets) 2) Accomplishment of Goals & Objectives 3) Compliance with Policies, Plans, Procedures & Regulations (L&R) 4) Internal Control System & Procedures 5) Organisational Structure 6) Relevance & Reliability of Information 7) Utilisation of Resources
Review of the Organisation Structure:	Q5. Internal auditor makes an appraisal of organization structure to ensure that it is in harmony with the objectives of the entity. Elaborate. The internal auditor should conduct an appraisal of the organisation structure to ascertain: Whether it is in harmony with the objectives of the enterprise and whether the assignment of responsibilities is in consonance therewith.



<i>Trick: 1&2 points are similar, 3,4,5 are similar</i> <u>(Special Trick by :-)</u>	1) He should review the manner in which the activities of the enterprise are grouped for managerial control. It is also important to review whether responsibility and authority are in harmony with the grouping pattern 2) The internal auditor should examine the organisation chart to find out whether structure is simple and economical and that no function enjoys an undue dominance over the others 3) He should particularly see that the responsibilities of managerial staff at headquarters do not overlap with those of chief executives at operating units. Examine whether there is a satisfactory balance between the authority & responsibility of important executives. 4) Internal auditor should examine the reasonableness of the span of control of each executive (number of subordinates that an executive controls). He should examine whether there is a unity of command i.e., whether each person reports only to 1 superior. 5) Where dual responsibilities cannot be avoided, the primary one should be specified and specific responsibility to each senior fixed. This must be made known to all concerned. 6) Finally, he should evaluate the process of managerial development in enterprise.
Review of Utilisation of Resources: <i>(It's Like Variance Analysis)</i> <u>(Special Trick by :-)</u>	Q6. Internal auditor observed that company gym is used only 2 days in a week by employees, there is huge bank balance but company is not investing it, there is downtime of 1 hour for machines. Manager is saying that it's not in scope of internal audit. (Nov'23) Answer: Scope of internal auditor include Review of Utilisation of Resources • Whether proper operating standards and norms have been established for measuring the economical and efficient use of resources • Detailed enough to be identifiable with specific operating responsibilities to monitor & evaluate performance • Review the methods of establishing operating standards and norms, carefully examine the assumptions made while setting the standards • Where there is a wide divergence between actual performance and the corresponding standards, reasons may be considered (Over utilisation / Under utilisation) [For example, it may consist of under-utilized machines, unoccupied storage space, huge cash or bank balances, idle manpower, etc. staff non-productive work being performed] Now explain given Case (i.e., Gym not used, Bank balance idle, Downtime.....) All above issues fall under utilization of Resources, Auditor must highlight the weakness observed & Give suggestion for improvement of the same. Opinion of Manager is not Tenable.
Review of Internal Control System and Procedures <i>(Less Imp)</i>	• assessing the design and operational efficiency and effectiveness of the internal control system to strengthen the overall internal control environment of the entity [Review of three-way matching internal control involves matching of Purchase Orders, Goods Receipt Notes and Invoice] • As far as possible, Built the controls in the Operating function itself, to timely prevent & detect fraud. [Eg. Control can be implemented in Accounting software only for approving PO, instead of Separate physical approvals] • IC should be reviewed considering the limitations of internal controls, i.e., cost- benefit comparison, human errors etc. • whether the internal controls were in use throughout the period

➤ INTEGRITY, OBJECTIVITY AND INDEPENDENCE OF INTERNAL AUDITOR

There is a set of core principles fundamental to the internal audit function and activities. These basic principles of internal audit are critical to achieving the desired objectives.

1) Independence:	• The Internal Auditor shall be free from any undue influences which force him to deviate from the truth. Independence shall be not only in mind but also in appearance.



	- the internal auditor shall resist any undue pressure or interference in establishing the scope of the assignments. - The independence of the internal audit function as a whole, and the Internal Auditor within the organisation, plays a large part in establishing the independence of the Internal Auditor. The overall organisation structure of key personnel, <u>the position and reporting of the Chief Internal Auditor within this structure, along with the powers and authority</u> which is derived from superiors further establishes the independence of the Internal Auditor.
2) Integrity:	The Internal Auditor shall be honest, truthful and be a person of high integrity. He shall operate in a highly professional manner and seen to be fair in all his dealings. He shall avoid all conflicts of interest and not seek to derive any undue personal benefit or advantage from his position.
3) Objectivity:	The Internal Auditor shall conduct his work in a highly objective manner, especially in gathering and evaluation of facts and evidence. He shall not allow prejudice or bias to override his objectivity, especially in arriving at conclusions or reporting his opinion

- Example:** To avoid any conflict of interest → internal auditor **should not review an activity for which he was previously responsible**.
- Example:** Internal auditor shall report directly to:
 - ✓ For **Listed Company**: **TCWG**, such as the **Audit Committee / Board**
 - ✓ **Other**: **CEO/CFO / Managing Director**
 - ✓ **Any actual or apparent conflict of interest** → attention of the appropriate level of mngt for necessary corrective action

Q7. Suggest **ideal reporting structure of CIA (Chief Internal Auditor)** [SM]

Hint: → HR should evaluate different option for **Administrative reporting & Functional reporting** of CIA

- Possible options include **BOD, Audit Committee, Managing Director, CEO, CFO**.
- Sec 138** → I.Auditor **can be CA or Cost accountant** (in Practice or not) or other as may be decided by Board.
- Definition of I.Audit:** I.Audit provides independent assurance on the effectiveness of I.C & risk mngt processes to enhance governance and achieve organisational objectives
- Internal Auditor shall be free from any undue influences**, independence shall be **not only in mind but also in appearance**
- CIA needs** to be **independent from Operation activities** & report to → **Audit Committee/BOD** (for independent)
- He may administratively report to CEO or Managing Director**

Q8. How independence of Internal auditor can be established? (Old)

Hint → He shall be free from any undue influence → not only mind, but also appearance. Resist any undue pressure.

Firstly → overall organisation structure should allow him to operate independently/objectively (Access to A.C/BOD)

Secondly → reporting line of CIA should be to highest level of authority (CEO/A.C)

Third → I.Auditor shall have necessary resources, budget & support to work without undue influence /pressure

➤ **QUALITIES OF INTERNAL AUDITOR: (CA-TMOC)**

- Expertise in Control Systems** → The internal auditor should have the special **expertise necessary for evaluating management control systems**, especially **financial and accounting controls**
- Accounting and Finance Knowledge** → Accounting and finance functions provide basic data for management control of an enterprise. Therefore, the internal auditor must have **accounting and financial expertise to be able to discharge his duties**.
- Technical Skills** → He should also have a **basic knowledge of commerce, laws, taxation, cost accounting, economics**, quantitative methods and EDP systems.
- Management and Communication Skills** → An understanding of management principles and techniques is



another essential qualification of an internal auditor as also the **ability to deal with people**.

- 5) **Operational Knowledge** → The internal auditor is also expected to evaluate **operational performance and non-monetary, operational controls**. This requires a basic knowledge of the technology and commercial practices of the enterprise.
- 6) **Confidentiality** → I.A. should provide an assurance to the management that the **confidentiality** maintained.

➤ **Who Define Objectives of Internal Audit:**

For companies covered under Rule 13 (Sec-138):	Audit Committee or the Board , in conjunction with mngt & Chief of Internal Audit, → is expected to exercise the responsibility to formulate the objectives of internal audit .
Other Organisation:	Those who appoint the Internal Auditor (e.g., the owners, the promoters, the Board of Trustees, etc.) would generally define the objectives of internal audit.

➤ **SIA 210 “Managing the Internal Audit Function”**

Function performs a number of activities to achieve its objectives, as outlined in Terms of Engagement:

Critical activities are as follows:	Trick: Plan karo > staff & expert hire karo > unke kaam ko monitor karo > fir saare kaam report ko karo to all stakeholders > nd “Quality improve” karo a) Define overall plan, scope & methodology of Internal Audit Function on a periodic basis. b) Plan, acquire, engage & review the performance, training & development of professional staff, talent and other resources to achieve its objectives c) Identify, source, engage & manage external experts and technical solutions, if required. d) Oversee and monitor various audit assignments, <u>their proper planning, execution, reporting of findings</u> and subsequent closure of reported observations e) Communicate & engage with all key stakeholders regarding progress & achievement of objectives. f) Develop and maintain a quality evaluation and improvement program.

W.r.t. Accounting function and financial Records: Trick: Independently (3), Evaluate IC, if any deficiency found, Update the management	Q9. responsibilities I.Auditor w.r.t accounting function & financial records of organisation? (SM) Main Responsibilities of I.Auditors are: With respect to the accounting function and financial records of the organisation, the responsibilities of an Internal Auditor include: 1) to operate independently of the accounting staff and must not in any way divest with any of the responsibilities placed upon him. 2) At all times, the internal auditor must enjoy an independent status. 3) Not to involve in the performance of executive functions in order that the objective outlook does not get obscured by the creation of the vested interest. 4) to maintain an adequate system of internal control by a continuous examination of accounting procedures, receipts and disbursements, and to provide adequate safeguards against misappropriation of assets. 5) to observe facts and situations and bring them to notice of authorities who would otherwise never know them; also, critically appraise various policies of the management and draw its attention to any deficiencies, wherever these require to be corrected. 6) to associate closely with management and keep knowledge up to date by being informed about all important occurrences and events affecting the business, as well as the changes that are made in business policies.

Q10. Company asks its internal auditor to manage its compliance tracking system including directly corresponding with regulator. agreed at time of appointment for “compliance with L&R? (SM)

Hint:



The Internal Auditor does **NOT assume any responsibility to manage or operate the compliance framework** or to take compliance related decisions. It is **Not responsibility of the Internal Auditor** to execute or resolve compliance related risks (e.g., engaging directly with regulators, etc.).

Although IAF provides independent assurance to enhance governance (which includes compliance with L&R), → it does NOT assume operational responsibility → It is responsibility of management. He is responsible for auditing the compliance framework and not managing it. Similarly, he does not accept compliance related risks.

➤ 5 Steps to Perform Internal Audit Engagement:

Q11. requested Internal auditor to **perform detailed analysis of their expenses** in previous year & report all risks and underlying gaps? **Elucidate the steps Internal auditor should take to identify such gaps?**

Step 1	<u>Obtain knowledge of the Business and its Environment:</u> (i) Obtain info by conducting meeting with Mngt. TCWG etc. (ii) Read business documents (SOP's , FS) (iii) IT System, Application & ERP used etc.
Step 2	<u>Perform Audit Planning:</u> - Plan as per SIA 310, Audit scope must be approved by Audit Committee & BOD, - Once approved → share detailed Audit Plan with the KMP and plan in advance detailed schedule. - do opening meeting with key stakeholder before audit, share detail of Info & System access required. - Detailed Work plan is prepared by Audit managers & approved by Head / Chief internal auditor
Step 3	<u>Gather required information:</u> → obtain the required info. & perform checks to ensure correctness and integrity of Info. Received → Obtain directly from Source → Adequate planning should be done & Intimate in advance for any interim info needed for audit checks
Step 4	<u>Perform audit checks:</u> collate all data and perform analytical procedures to identify key trends → Audit (SIA) 6 , Analytical Procedures → select the sample → Audit (SIA) 5, Sampling → adequate evidences must be collected (SIA) 320, Internal Audit Evidence → Adequate document → (SIA) 330
Step 5	<u>Reporting of Internal Audit Issues:</u> Must prepare a draft report of Internal Audit issues comprising of: ✓ the business process/ function reviewed as per scope, ✓ detailed audit coverage and exclusions ✓ Period Covered ✓ Summary of gaps noted along with implication of the business and recommendation. Management Action Plan should be agreed along with responsibility of action and timelines Internal Auditor must also review the status of actions taken by the management against. actions agreed during previous audits & report status of such follow up in the audit report. Internal Auditor should thereafter circulate Final Report and presentation his findings [(SIA) 360, Communication with Management and Standard on Internal Audit (SIA) 370, Reporting Results while sharing the result of internal audit with the stakeholders]

➤ INTERNAL AUDIT REPORT:

However, in case internal auditor comes **across any actual or suspected fraud** or any other **misappropriation of assets**, it would be more appropriate for him to bring the same immediately to the attention of the mngt

Q12. Write a short note on Internal Audit Report. [ICAI SM]



SIA: 370 – Reporting in Two Stages:	As per Standard on Internal Audit (SIA) 370 Reporting Results, reporting of internal audit results is generally undertaken in two stages: 1) <u>At the end of a particular audit assignment</u>, an “Internal Audit Report” covering a specific area, function or part of the entity is prepared by the Internal Auditor highlighting key observations arising from those assignments. This report is issued to the auditee, with copies shared with local and executive management, as agreed during the planning phase. 2) <u>On a periodic basis, at the close of a plan period</u>, a comprehensive report of all the internal audit activities covering the entity and the plan period is prepared by the Chief Internal Auditor (or the Engagement Partner, in case of external service provider). Such reporting is normally done on a quarterly basis and submitted to the highest governing authority responsible for internal audits, generally the Audit Committee. This Standard on Internal Audit (SIA) deals with the internal auditor's responsibility to issue only the first type of reports, the Internal Audit Report pertaining to specific audit assignments and not to the periodic (e.g., Quarterly) reporting for the whole entity as per the Annual/Quarterly audit plan.
Key “ELEMENTS” of Audit report:	On the basis of the internal audit work completed, the Internal Auditor shall issue a clear, well documented Internal Audit Report which includes the following key elements: (a) An overview of the objectives, scope and approach of the audit assignments; (b) The fact that an internal audit has been conducted in accordance the Standards of I.A.; (c) An executive summary of key observations covering all important aspects, and specific to the scope of the assignment; (d) A summary of the corrective actions required (or agreed by mngt) for each observation; (e) Nature of assurance, if any, which can be derived from the observations.
CONTENT & Form: <i>(Same as Step 5 of above Topic → this one is more relevant for exam)</i>	The content and form of report will be based on auditor best professional judgement, in consultation with the auditee and, if necessary, with inputs from other key stakeholders. No internal audit report shall be issued in final form unless a written draft of the report has previously been shared with the auditee. <u>Accordingly, a typical internal audit report should include the following:</u> • Audit Scope performed; • Audit period Covered; • Executive Summary; • Summary of the critical findings; • Detailed audit findings with elaboration on business impact and root cause of such issues; • Rating of the highlighted issues (E.g High / Medium / Low) in accordance to the rating criteria approved by Audit Committee • Audit recommendation to improve control environment and address the highlighted finding; • Response received from the responsible functional authority containing action plan and target timelines for action
Follow-up: (SIA 390) [Action taken Report]	Q13. CA Sanjana is recently appointed as Chief Internal auditor. He come to know that many prior issues are still opened, does she have any responsibility in this regard ? (SM) • As per SIA 390 Monitoring and Reporting of Prior Audit Issues, the Chief Internal Auditor is responsible for continuously monitoring the closure of prior audit issues through timely implementation of action plans included in past audits. • The responsibility to implement the action plans remains with the management. • In monitoring and reporting of prior audit issues, the responsibility of the Internal Auditor is usually in the form of an “Action Taken Report (ATR) of previous audits”.



- monitoring and reporting means the periodic tracking of issues raised during prior audits and evaluation of the corrective actions undertaken by the auditee to resolve them and to report any open and pending matters to the mngt & TCWG
- If no action is taken within a reasonable time he should draw the management's attention to it [report any open and pending matters to the mngt and TCWG (e.g. the Audit Committee).]. Where the management has not acted upon his suggestions or not implemented his recommendations, the internal auditor should ascertain the reasons thereof.

(Above Answer Ends)

Typical Action Taken Report may include the following: (V. Easy... just see Flow)

- Reference to the previous audit reporting containing the reported issues
- Implementation Action agreed by the management along with target implementation date
- Status of action taken by management. Same may be classified under Implemented / Not Implemented
- Residual risk and rating for any unimplemented action
- Audit findings not implemented for long period of time
- Any critical audit finding that require immediate action for action or implementation

Q14. Audit committee requested I.auditor to present detailed report on their finding & areas where immediate action is needed to mitigate critical risks? **What should be the content of I.A audit report ? (SM)**

Hint: Refer above notes: "**SIA: 370 - Reporting in Two Stages**" & "**CONTENT & Form**"

Q15. The XYZ Ltd has appointed Mr. A to conduct their internal audit. The Audit committee requested Mr. A to present their analysis on the implementation of recommendation of previous audit report and highlight critical areas which need immediate attention of Audit Committee? What should be the steps followed by internal auditor to address this requirement of Audit Committee? **(SM) [Action Taken Report]**

Answer:

As per SIA 390 Monitoring and Reporting of Prior Audit Issues,

- the **Chief Internal Auditor** is responsible for continuously monitoring the closure of prior audit issues through timely implementation of action plans included in past audits. This shall be done with a formal monitoring process, elements of which are pre-agreed with management and TCWG.
- The **responsibility to implement the action plans remains with the mngt.**

In monitoring and reporting of prior audit issues, the responsibility of the Internal Auditor is usually in the form of an "**Action Taken Report (ATR) of previous audits**".

Now refer the Above Topic → "Typical Action Taken Report may include the following"

➤ **Difference Between Internal & External Auditors:**

Sr.	BASIS	INTERNAL AUDIT	EXTERNAL AUDIT
1	Meaning	It refers to an ongoing audit function performed within an organization by a separate internal auditing department.	It is an audit function performed by the independent body which is not a part of the organization.
2	Examination	The Internal auditor examines the Operational efficiency of the organisation	The External auditor examines the Accuracy and Validity of Financial Statements.
3	Appointment	The Internal auditor is appointed by the Management	The External auditor is appointed by the Members
4	Users of Report	User of internal audit report is Management	The user of external audit report is Stakeholders
5	Period	Internal audit is a Continuous Process	An External audit is done once in a year



		throughout the year.	
6	Opinion	The opinion is provided on the effectiveness of the operational activities of the organization	The opinion is provided on the truthfulness and fairness of the financial statement of the company
7	Status of Auditor	The Internal auditor could be an employee of the company	External auditor is mandatorily not an employee of the company

➤ AUDIT TRAIL (Edit Logs)

Meaning:	Audit Trail (or Edit Log) is a visible trail of evidence enabling one to trace information contained in statements or reports back to the original input source . Audit trails are a chronological record of the changes that have been made to the data. Any change to data including creating new data, updating or deleting data that must be recorded.
Records Include:	Records maintained as audit trail may include the following information: a) when changes were made i.e., date and time (timestamp) b) who made the change i.e., User Id c) what data was changed i.e., data/transaction reference; success/failure
Software:	Audit trails may be enabled at the accounting software level depending on the features
Internal Control: [UD-CAB] (Special Trick by :-)	Q16. mngt is concerned with the reporting requirement cast through Rule 11 of Companies (Audit) Rules, 2014 w.r.t Audit Trail (edit log). → suggest list of I.C which may be required to be implemented & operated to demonstrate that Audit trail (Edit Log) feature was functional. (May'24 & SM) In order to demonstrate that the audit trail feature was functional, operated and was not disabled , a company would have to design and implement specific internal controls (predominantly IT controls) which in turn, would be evaluated by the auditors , as appropriate. An illustrative list of I.C which may be required to be implemented and operated are given below: a) Controls to ensure that User IDs are assigned to each individual & that User IDs are not shared. b) Controls to ensure that the audit trail feature has not been Disabled or deactivated. c) Controls to ensure that Changes to configurations of audit trail are authorized and logs of such changes are maintained d) Controls to ensure that Access to the audit trail (and backups) is disabled or restricted and access logs, whenever the audit trails have been accessed, are maintained e) Controls to ensure that periodic Backups of the audit trails are

Q17. Company is concerned about **high employee attrition rate** in his company. As the **internal auditor** of company he requests you to analyze the causes for the same. What factors would you consider in such analysis? (SM)

Answer:→ The factors responsible for high employee attrition rate are as under:

- 1) Low monetary benefits;
- 2) Lack of labour welfare schemes;
- 3) Limited opportunities for promotion
- 4) Wrong policies of the Management;
- 5) Job Stress & work life imbalance;
- 6) Unbearable behaviour of Senior Staff;
- 7) Whether the organization has **properly qualified and experienced** personnel for the various levels of works?
- 8) Is the number of **people** employed at various work centres excessive or **inadequate**?
- 9) Does the organization provide facilities for staff **training** so that employees and workers keep themselves abreast



of current techniques and practices?
10) Safety factors;

Q18. demand of products declined drastically. The statutory auditor question going concern assumption of company. Its internal auditor has helped mngt in devising a strategy to come out of situation., internal auditor has also prepared estimates of revenue & cash flows. Can statutory auditor place total reliance on I.A (SM)

Answer:

The **greater the judgment needed to be exercised in planning and performing** the audit procedures and evaluating the audit evidence, the external auditor will need to perform more procedures directly because using the work of the **internal audit function alone will not provide the external auditor with SAAE.**

The appropriate use of going concern assumption requires **significant judgment** on part of statutory auditor.

Therefore, **statutory auditor cannot place total reliance on internal auditor's work** in this regard and he should perform more procedures directly

Q19. State important aspects to be considered by External auditor in the evaluation of the I.Audit Function. (SM)

Answer: [SOP-T]

Evaluation of IAF by External Auditor, will assist him in determining the extent to which he can place reliance upon the work of the I. auditor. The important aspects to be considered in this context are:

- (a) **Scope of Function** - The external auditor should ascertain the nature and depth of coverage of the assignment which the internal auditor discharges for management..
- (b) **Organisational Status** - Whether internal audit is undertaken by an outside agency or by an internal audit department within the entity, the I.auditor reports to mngt. → He reports to the highest level of mngt & are free of any other operating responsibility. I.auditor should be free to communicate fully with the external auditor.
- (c) **Due Professional Care** - The external auditor should ascertain whether internal audit work appears to be properly planned, supervised, reviewed and documented. An example of the exercise of due professional care by the internal auditor is the existence of adequate audit manuals, audit programmes and working papers.
- (d) **Technical Competence** - The external auditor should ascertain that internal audit work is performed by persons having adequate technical training and proficiency. This may be accomplished by reviewing the experience and professional qualifications of the persons undertaking the internal audit work.

CHAPTER 17.1: DUE DILIGENCE

➤ Introduction:

Q1. "Due diligence is different from audit" - Explain the difference between due diligence and audit.

Meaning & Difference:	Due Diligence - Due diligence refers to an examination of a potential investment to confirms all material facts of the prospective business opportunity - It involves review of financial and non-financial records as deemed relevant and material. - Simply put, due diligence aims to take the care that a reasonable person should take before entering into an agreement or a transaction with another party.	Audit Audit is an independent examination and evaluation of the financial statements on an organization with a view to express an opinion thereon
More about Due Diligence:	<u>When can be performed?</u> → analysis carried out before acquiring a controlling interest in a company → corporate restructuring, venture capital financing, lending, leveraged buyouts, public offerings, disinvestment etc. <u>Who can perform?</u> → Anyone (CA or Non-CA)	
Importance:	Identify → To identify potential 'deal killer' defects in the target company & avoid a bad business transaction Verify → To verify that the transaction complies with investment or acquisition criteria Confirm → To confirm that the business is what it appears to be - To gain information that will be useful for valuing assets, defining representations and warranties, and/or negotiating price concessions; and	
Classification of due diligence: (CPT-FILE) (Special Trick :-)	Q2. What are the areas in which Due Diligence can take place? <u>Or</u>, Classification of DD ? Commercial or Operational Due Diligence: It is generally performed by the concerned acquire enterprise involving an evaluation from commercial, strategic and operational perspectives. For example, whether proposed merger would create operational synergies Personnel Due Diligence: It is carried out to ascertain that the entity's personnel policies are in line or can be changed to suit the requirements of the restructuring. Tax Due Diligence: it is generally included in the financial due diligence. The accountant has to look at the tax effect of the merger or acquisition. Financial Due Diligence: It involves analysis of the BOA & other information pertaining to financial matters of the entity. It should be performed after completion of commercial due diligence. Information Systems Due Diligence: It pertains to all computer systems and related matter of the entity. Legal Due Diligence: This may be required where legal aspects of functioning of the entity are reviewed i.e. Compliance of various laws, legal aspects of property owned Environmental Due Diligence: It is carried out in order to study the entity's environment, its flexibility and adaptiveness to the acquirer entity	

➤ FINANCIAL DUE-DILIGENCE:

Meaning:	Financial due diligence commences only after a price has been agreed for the business or a restructuring plan is framed. The initial price and other decisions are taken on the basis of net worth as well as trend of profitability of the target company, with an assumption that all



- contingent liabilities that may impact the future of the business have been recorded.
- The principal objective of financial due diligence, therefore, is usually to look behind the veil of initial information provided by the company and to assess the benefits and costs of the proposed acquisition/merger by inquiring into all relevant aspects of the past, present and future of the business to be acquired/merged with.

In order to achieve its objective, the due diligence process can include any or all of the following objectives for individual areas of the verification:

- Brief description of the history of business
- The background and standing of promoters
- Details of management structure
- Trading results both past and the recent past
- The projection of future profitability
- Assets and liabilities as per latest balance sheet
- Cash flow patterns
- Accounting policies and practices followed by the organization
- Management information systems
- Current status of Income tax assessments including appeals pending against tax liabilities assessed by tax authority.
- Brief description of commercial and/or other activities carried out by the organization

Scope:

If a full-fledged financial due diligence is conducted, it would include following matters, scope:
(Bando ka dhyaan rakho, kyuki wo Cash lera h, to accounting kare Law & Taxation ko dhyan me rakh kar)

a) Brief history of the target company and background of its promoter;	b) Management and employees;	c) Cash flow;
d) Financial Projection;	e) Accounting policies;	f) Taxation;
g) Statutory Compliance	h) Review of financial statements;	

Review of Financial Statements:

- Whether the financial statements of the target company have been prepared in accordance with the Statute governing & FRF (AS/Ind As)
- Make an evaluation of the operating results/ profit reported by the target company
- consider the presence of an extraordinary item of income or expense
- the trading results for the past 4 to 5 years are compared and the trend of normal operating profit arrived at.
- If Required Expert assistance for valuation of assets (As Valuation of company are mostly based on Net Worth) → yes can take

Q3. State in brief major areas you would examine for hidden liabilities & overvalued assets. (Imp)

Answer:

Hidden Liabilities:

Tax

- Tax liabilities under direct and indirect taxes
- Long pending sales tax assessments.
- Pending final assessments of customs duty where provisional assessment only has been completed

Contingent liability:

- The company may not show any show cause notices which have not matured into demands, as

(Special Trick :-)



- contingent liabilities. These may be material and important
- 5) The company may have given "**Letters of Comfort**" to banks and Financial Institutions. Since these are not "guarantees", these may not be disclosed in the Balance sheet of the target company.

Customer liability, Labour liability, Employee liability, Society liability:

- 6) **Product and other liability claims**; warranty liabilities; product returns/discounts; liquidated damages for late deliveries etc. and all litigation
- 7) Unresolved **labour litigations**
- 8) Huge **labour claims** under negotiation when the labour wage agreement has already expired.
- 9) Unfunded gratuity/superannuation/leave **salary liabilities**; incorrect gratuity valuations
- 10) **Environmental problems**/claims/third party

Other:

- 11) **Future lease liabilities**.
- 12) **Agreement to buy back shares** sold at a stated price
- 13) The Company may have sold **some subsidiaries/businesses** and may have agreed to take over and indemnify all liabilities and contingent liabilities of the same prior to the date of transfer. These may not be reflected in the books of accounts of the company

Q4. due diligence State what areas of analysis to ensure that the assets are not stated at overvalued

Answer:

Over-Valued Assets::

Current assets:

- 1) Uncollected/uncollectable **receivables**
- 2) Obsolete, slow non-moving **inventories** or inventories valued above NRV; huge inventories of packing materials etc. with name of company

Fixed Assets:

- 3) Underused or obsolete **Plant and Machinery** and their spares; asset values which have been impaired due to sudden fall in market value etc.
- 4) **Litigated assets and property**

Intangible assets:

- 5) Intangible assets of no value.

Investment:

- 6) Investments carried at cost though realizable value is much lower.
- 7) Investments carrying a very low rate of income / return

Fictitious asset:

- 8) Infructuous project expenditure/**deferred revenue expenditure** etc.
- 9) Assets carried at much more than current market value due to **capitalization of expenditure/foreign exchange fluctuation**, or capitalization of expenditure mainly in the nature of revenue.
- 10) Group Company balances under reconciliation etc.

Review of Cash Flow:

Q5. conducting due diligence to check Cash generating ability. What points to check in order to ensure that manufacturing unit of SV Ltd. will be able to meet the cash requirements internally?

Answer:



	A review of historical cash flows and their pattern would reflect the cash generating abilities of the target company and should highlight the major trends. to know if company is able to meet its cash requirements through internal accruals or does it have to seek external help. 1) Is the company able to honor its commitments to its trade payables, to the banks, to government and other stakeholders? 2) How well is the company able to turn its trade receivables and inventories? 3) Are there any funds lying idle or is the company able to reap maximum benefits out of the available funds? 4) How well does it deploy its funds? 5) What is the investment pattern of the company and are they easily realisable?
Management & employees:	How much of the labour force has to be retained → administrative and managerial staff to gauge which of these matches the requirements → face protracted litigation from its workforce → assumptions regarding increase in salaries, interest rate, retirement (PF ESI payment etc) → how much ESOP / deferred compensation is pending

Q6. Sri Rajan wishes to sell his proprietary business. Ceta Ltd. wants to buy the business and appoints you to carry out a due diligence audit. What procedures you would adopt before you could render any advice to Ceta Ltd.? Or, Q. A German Company is interested in acquiring a listed Indian Company. Request you to conduct a "Due Diligence" of this Indian Company and submit your report. discuss the key areas you will cover in your review

Answer:

- Brief history of the target company and background of its promoters** :The accountant should begin the financial due diligence review by looking into the history of the company and the background of the promoters. The details of how the company was set up and who were the original promoters has to be gone into, before verification of financial data in detail. An eye into the history of the target company may reveal its turning points, survival strategies adopted by the target company from time to time, the market share enjoyed by the target company and changes therein, product life cycle and adequacy of resources.
- Accounting policies** - The accountant should study the accounting policies being followed by the target company and ascertain whether any accounting policy is inappropriate. The accountant should also see the effects of the recent changes in the accounting policies.
- Review of Financial Statements**: Before commencing the review of each of the aspect covered by the FS, the accountant should examine whether the FS of the target company have been prepared in accordance with the Statute governing the target company, Framework for Preparation and Presentation of the FS and the relevant Accounting Standards. If not, the accountant should record the deviations from the above and consider whether it warrant an inclusion in the final report on due diligence. After having an overall view of the FS, as mentioned in the above paragraphs, the accountant should review the operating results of the target company in great detail. It is important to make an evaluation of the profit reported by the target company. The reason being that the price of the target company would be largely based upon its operating results
- Taxation**: Tax due diligence is a separate due diligence exercise but since it is an integral component of the financial status of a company, it is generally included in the financial due diligence. It is important to check if the company is regular in paying various taxes to the Government. The accountant has to also look at the tax effects of the merger or acquisition
- Cash Flow** - A review of historical cash flows and their pattern would reflect the cash generating abilities of the target company and should highlight the major trends. It is important to know if the company is able to meet its cash requirements through internal accruals or does it have to seek external help from time to time. It is necessary to check that: (a) Is the company able to honor its commitments to its trade payables, to the banks, to government and other stakeholders? (b) How well is the company able to turn its trade receivables and inventories? (c) How well does it deploy its funds? (d) Are there any funds lying idle or is the company able to reap maximum benefits out of the available funds? (e) What is the investment pattern of the company and are they easily realisable?
- Financial Projections** - The accountant should obtain from the target company the projections for the next 5 years with detailed assumptions and workings. He should ask the target company to give projections on optimistic,



pessimistic and most likely base

- g) **Management and Employees** - In most of the companies which are available for take over the **problem of excess work force** is often witnessed. It is important to work out **how much of the labour force has to be retained**. It is also important to judge the job profile of the administrative and managerial staff to gauge which of these matches the requirements of the new incumbents. **Due to complex set of labour laws applicable** to them, companies often have to **face protracted litigation from its workforce** and it is important to gauge the likely impact of such litigation
- h) **Statutory Compliance** - During a due diligence this is one aspect that has to be investigated in detail. It is important therefore, to **make a list of laws/ statutes that are applicable** to the entity as well as to make a checklist of compliance required from the company under those laws. If the company has **not been regular in its legal compliance** it could lead to punitive charges under the law. These may have to be **quantified and factored** into the financial results of the company

➤ **WORK APPROACH TO DUE-DILIGENCE:**

- 1) Reviewing and **reporting on the financials** submitted by the target company
- 2) Assessing the business first hand by a **site visit** (if applicable).
- 3) Working through the due diligence process with the acquisition company or investor by **defining the key areas**
- 4) **Helping prepare an offer** based on completion of due diligence

➤ **CONTENTS OF A DUE DILIGENCE REPORT:**

Q7. List out the contents of your Due Diligence Review Report that you will submit to your USA based Client

1) Introduction	2) Executive Summary	3) Objective of due diligence
4) Terms of reference and scope of verification	5) Brief history of the company	6) Share holding pattern
7) Assessment of management structure	8) Observations on the review	9) Assessment of valuation of assets
10) Assessment of financial liabilities	11) Assessment of operating results	12) Assessment of net worth
13) Assessment of possible liabilities on account of litigation	14) Comments on properties, terms of leases	15) SWOT Analysis
16) Comments on future projections	17) Status of charges, liens, mortgages	18) Suggestions on various aspects to be taken care of before and after merger/acquisition

Q8. A company has approached Sangana (Bank mgr) to sanction credit facilities worth ₹ 10 crore. She checks past history of the company, back ground of promoters & directors, financial results and SWOT etc.

(a) Identify activity being performed. (b) Would your answer be different if it was performed by a Non-CA?

(c) Name any three other areas where identified activity can be undertaken. (SM)

Hint:

- a) It is **Due diligence**. → Due diligence is a measure of prudence activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a **reasonable and prudent person** under the particular circumstance. It's a **process of investigation**, performed by investors, into the details of a **potential investment such as an examination of operations and management and the verification of material facts**. Or While Acquiring controlling interest. It involves a **careful study of the financial as well as non-financial possibilities** Also, due diligence can apply to **recommendation for an investment or advancing a loan/credit**.
- b) There would be **no difference in answer** if above activity was performed by Non- Chartered Accountant..
- c) The areas where due diligence may be undertaken are:
- (i) **Corporate restructuring** (ii) **Venture capital financing** (iii) **Public offerings**

Q9. CA. Y is Employee of BDFP Bank. One of existing borrower approached bank for proposal to sanction fresh term loan of Rs.5 crore → While performing due diligence, he notices → Its sales have increased from Rs.25 crores in first year to Rs.45 crores in year, generating cash profits and is timely servicing its debts.



- Now Company planning for The expansion plans are in line with development in area of marketing relating to exports.
- However, there are a large number of units catering to domestic and export market of garments in NOIDA,
- relies upon marketing skills of its main promoter. There is lack of well-paid qualified staff with the borrower

Identify what he is trying to do as part of due diligence **(SM)**

Hint: → As part of due diligence exercise, he is performing **SWOT analysis of borrower.**

<u>rise in sales, generation of cash profits & timely service</u> → Strength	<u>Lack of well-paid qualified staff</u> → Weakness	<u>Entering into export market</u> → Opportunity	<u>large number of competitors</u> → Threat



CHAPTER 17.2: INVESTIGATION

➤ Meaning:

The term investigation implies a **systematic and indepth examination** or inquiry **to establish a fact** or to evaluate a specific situation.

➤ Difference:

Q1. Brief out the difference between Audit & Investigation

Answer: (Trick: **O NEAR IPO**)

Sr.N	Basis	Investigation	Audit
1	O bjective	An investigation aims at establishing a fact or a happening or at assessing a particular situation.	The main objective of an audit is to verify whether the financial statements display a true and fair view of the state of affairs and the working results of an entity.
2	Scope	The scope of investigation may be governed by statute or it may be non-statutory	The scope of audit is wide and in case of statutory audit the scope of work is determined by the provisions of relevant law
3	P eriodicity	The work is not limited by rigid time frame . It may cover several years, as the outcome of the same is not certain	The audit is carried on either quarterly, half-yearly or yearly
4	N ature	Investigation is voluntary in nature.	It is mandatory for companies.
5	I nherent Limitations	No inherent limitation owing to its nature of engagement	Audit suffers from inherent limitation
6	E vidence	It seeks conclusive evidence	Audit is mainly concerned with prima- facie evidence (Persuasive)
7	O bservance	It is analytical in nature and requires a thorough mind, capable of observing, collecting and evaluating facts	Is governed by compliance with generally accepted accounting principles , audit procedures and disclosure requirements.
8	A ppointing Agency	Even third party can appoint Investigator	Auditor is appointed by owner/ shareholders of company/ enterprise
9	R eporting	The outcome is reported to the person(s) on whose behalf investigation is carried out	The outcome is reported to the owners of the business entity.

- An **auditor** does not suspect unless circumstances are there to arouse suspicion, while an **investigator** approaches the work with a frame of mind to suspect, verify and satisfy.
- **Auditor** has to see whether the method of valuation and other accounting policies have been properly made in the FS or not [**Investigator** not bound by accounting conventions, policies and disclosure requirements]
- sometimes investigation results from the prima facie findings of the auditor.

➤ SPECIAL ISSUES IN INVESTIGATIONS:

Can investigator use sampling ?	• Depends on the circumstances of the case under investigation. ✓ For Cash defalcated by the cashier → Have not option but to no option but to carefully



	examine all the cash vouchers ✓ <u>To Establish Profitability</u> → transactions on a selective basis it is always safer to go by statistically recognised sampling methods than to depend on the so-called "test checks" where circumstances permit selective verification.
Can he rely on audited FS?	<u>Covered in Question section (Below questions)</u>
Can he take expert assistance?	Investigator should get the written general consent of his client, to refer special matters for views of different experts at the beginning of investigation and he should settle the question of costs for obtaining the views and other related implications.
Can he make futuristic statements?	- Investigator should refuse to be futuristic - For Trend also, he should assume that trend will continue in future, Should not project the trend into any future years to establish a value
Basis of opinion of an investor:	If the facts, as conveyed through the books, records, papers and other evidence, are not capable of being properly established, he should NOT express an opinion <u>or</u> qualify the opinion by clearly stating the reasons
Can He retain Working Paper:	Q2. Whether an investigator can retain working papers or not? [Old] - Investigating accountant should retain in his files full notes of the work carried out, copies and all working papers, annexures, facts, figures, record of conversations and the like. - If required, investigator should take representation letter from appointing authority In the absence of working paper, he would not be able to explain the figures when he is called upon to give evidence in a court of law to support his figures when he is called upon to give evidence in a court of law Many times, the conclusions of the accountant are challenged by parties whose interest is adversely affected by his findings, for example, when the value of shares of a company taken over by the Government has been determined by him. This will also be of immense help to the investigator in correlating facts and events and later in drafting the report
Investigation out of disputes and conflicting claims:	- When Investigation arise Due to Dispute between Two or more parties. - Then he must be appointed of any of the Party → he should not be Biased. - should remain above disputes or conflicting claims and be alert to the possibilities of the information or documents made available to him to be prejudiced.

Q3. PV Associates was appointed as Investigator. Investigator were of the view that they need to take an expert's opinion on the price of land. Whether PV Associates is authorized to take assistance of expert? (Old)

Answer: Yes, they are allowed to do so → get the written general consent of his client, to refer special matters for views of different experts at the beginning of investigation and he should settle the question of costs for obtaining the views and other related implications

Q4. Investor appointed You to investigate the audited FS and ensure that the valuation of shares. What process will be used for checking and whether you can put reliance on already audited statement of accounts?

Hint: "Process used for checking and reliance on already audited statement of accounts -

- If account were **not audited by a qualified accountant**, → a **natural duty to get figures properly checked**
 - If accounts is **specially prepared by a professional accountant**, who knows that these were prepared for the investigation, → he could **accept them as correct relying on the principle of liability to 3rd parties**.
 - Nevertheless**, → **see first that such accounts were prepared with objectivity** and that **no bias**
- **Can Not rely** : → **If the investigation has been launched because of some doubt** in the audited statement of account, no question of reliance on the audited statement of account arises.
- **Yes can rely** : → **However, if the investigator has been requested to establish value of a business or a share or goodwill payable by an incoming partner**, ordinarily the investigator would be entitled to put



reliance on audited materials made available to him unless, in the course of his test verification,

It is, therefore, **desirable for the investigator to ascertain from the client, in advance, in writing,** whether the audited statements of account produced to him should be taken as correct

➤ **SPECIAL ASPECTS IN CONNECTION WITH BUSINESS INVESTIGATIONS:**

Studying the overall picture:	In such a business investigation, it is of utmost importance first to have an overall picture of the position of the business which is being investigated before the details are gone into.
Economic & financial position: <i>[Capital daalo > Production capacity badhaao > Sales hogi > Profit hoga]</i>	Q5. AB Ltd wants to acquire a unit of CT Ltd, How he can investigate Economic & Financial position of Business ? [Old] - The adequacy or otherwise of fixed and working capital. Are these sufficient for the growth of the business? - Whether the business is operating at its 100% capacity or improvements can be made to reach at full productivity? - What will be the trend of the sales and profits in the future? Establishing the trend of sales, product-wise and area-wise will ordinarily help in drawing a conclusion on whether the trend will be maintained in the future. - Whether the profit which the business could be expected to maintain in the future would yield an adequate return on the capital employed?
Statement of Profit and Loss:	In foregoing summary, <u>in the place of figures of opening and closing inventories, the figures of inventory consumed</u>, for each product, <u>in different years should be entered</u>. Consider each item, included therein, a summary, in a columnar form, should be prepared for a period, say of 5 to 7 years. Turnover: Sales should be broken down between the various products, identify fictitious sales Managerial Remuneration: not excessive Wages: method of computing wages and the rates of wages examine, any strike Depreciation: consistent basis and that it is adequate Repairs and maintenance: heavy in some of the years, while quite low in some others. Exceptional Item: adjust exceptional items in the summary of Statement of P&L
Balance Sheet:	Fixed Assets: values are not in excess of the value of service that they could be expected to render to the business Investments: Valuation should be as per accounting standard (Market value) Inventories: due allowance for damaged, obsolete and slow-moving inventories Trade Receivables: Provision for bad debts have been made in the years Other liquid assets: assets so described are readily realizable Idle assets: the duty of the investigating accountant to eliminate these idle assets Liabilities: whether those are stated fully or understated or overstated. Taxation: adequate provision has been made in respect of liabilities for taxes Capital: capital is well balanced between equity, preference, debentures etc
Interpretation of figures: Future Maintainable Turnover:	Q6. factors would you consider in assessing the future maintainable turnover? For Turnover: In assessing the turnover which the business would be able to maintain in the future, the following factors should be taken into account Marketability: Is it possible to extend the sales into new markets or that these have been fully exploited? Product wise estimation should be made Competition: What is the likely effect on the business if other manufacturers enter the same field or if products which would sell in competition are placed on the market at



(MC-PT)

cheaper price? Is the demand for competing products increasing? Is the company's share in the total trade constant or has it been fluctuating?

- 3) **Political and economic considerations:** Are the policies pursued by the Govt likely to promote the extension of the market for goods to other countries? Whether the sales in the home market are likely to increase or decrease as a result of various emerging economic trends?
- 4) **Trend:** Whether in the past sales have been increasing consistently or they have been fluctuating. A proper study of this phenomenon should be made.

➤ TYPES OF INVESTIGATION:

1) Statutory	a) Investigation of ownership of a company (Section 216) b) Investigation into the affairs of a company - By inspector through an order of the Central Government (Section 210) - By Serious Fraud Investigation Office: SFIO (Section 212) - Other cases (Section 213)
2) Non-statutory	a) Investigation on behalf of an incoming partner b) Investigation for valuation of shares in private companies c) Investigation on behalf of a bank / Financial Institution proposing to advance loan to a company d) Investigation of frauds e) Investigation on behalf of an individual or a firm proposing to buy a business f) Investigation in connection with review of profit / financial forecast

➤ INVESTIGATION INTO AFFAIRS OF COMPANY:

Section 210 (CG)	Section 212 (SFIO)	Section 213 (Tribunal)
Where the CG is of the opinion, that it is necessary to investigate into the affairs of a company: 1) on the receipt of a report of the Registrar or inspector; 2) special resolution by company 3) in public interest, it may order an investigation into the affairs of the company.	The CG may, by an order, assign the investigation, to the Serious Fraud Investigation Office, when it considers necessary: 1) on receipt of a report of the Registrar or inspector; or 2) special resolution by a company; or 3) in public interest; or 4) on request from Department of the CG, or a SG	Tribunal may order investigation into affairs of the company on an application received by specified number of members or on an application made to it by any other person or otherwise, if it is satisfied that there are circumstances like, the business of the company is being conducted with intent to defraud its creditors, or that the company was formed for any fraudulent or unlawful purpose etc.

- ❖ **Who can be appointed as an Inspector:** **Only Individual** (A firm, body corporate or other association cannot be appointed as an inspector. Thus, a firm of professional accountant cannot be appointed as inspector but an individual accountant can be so appointed.)

[ICAI have not given above Co Act Section in Audit ICAI SM, they have mentioned "Sections 210, 212, 213 and 216 of the Companies Act" discussed in details in Self-Paced Module Set A"]

➤ General Approach/Steps for investigation under Sections 210 and 213:

Q7. What will be your approach in investigation under Section 210 and 213 of Companies Act, 2013? **[OLD]**

Answer:

TRICK : TSP-PER



- 1) **Clarity of Terms of Reference:** Inspector should ensure that the terms of reference are clear, unambiguous and in writing. If he has any doubt about any item in the terms, he should obtain clarification in writing
- 2) **Scope of Investigation:** he may need to stretch his inquiry into the books and records of allied and associated persons and concerns and may require to arm himself with the powers given under the Co.Act.
- 3) **Period for investigation:** He should also have regard to the period over which the investigation can stretch
- 4) **Framing of Programme:** The next step is the investigator/inspector should frame his programme for investigation in a systematic manner
- 5) **Using the work of Experts:** He should also consider whether assistance of other experts like engineers, lawyers, etc., is necessary in the interest of a comprehensive and full proof examination of the documents and information
- 6) **Legal requirements and investigation Report:** Only after he has completed the steps in the investigation programme and has marshaled all the information that he needed should he prepare his report

➤ Non-Statutory Investigation:

Investigation on behalf of an Incoming Partner: (Special Trick :-)	Q8. What are steps involved while conducting Investigation on behalf of an Incoming Partner? <u>why are they inviting me as partner?</u> 1. Reasons for the offer of admission to a new partner should be ascertained 2. Whether any special clause exists in the deed of partnership to allow admission in future of a new partner, who may be specified, on concessional terms. <u>About partnership firm Growth, History:</u> 3. Ascertainment of the history of the inception and growth of the firm. 4. Study of the provisions of the deed of partnership, particularly for composition of partners, their <u>capital contribution, drawing rights, retirement benefits</u>, job allocation, financial management, goodwill, etc. <u>check Balance sheet & P&L items of Firm:</u> 5. Scrutiny of the record of profitability of the firm's business over a suitable no. of years, with usual adjustments that are necessary in ascertaining the true record of business profits 6. Examination of the asset and liability position to determine the tangible asset backing for the partner's investment, appraisal of the value of intangibles like goodwill, know how, patents, etc. impending liabilities including contingent liabilities. 7. Position and terms of loan finance would call for careful scrutiny to assess its usefulness and implication for the overall financial position; reason for its absence or (-)ve impact should be studied. 8. Various important contractual and legal obligations should be ascertained and their nature studied. It may be the case that the firm has standing agreement with the employees as regards salary and wages, bonus, gratuity and other incidental benefits. Full impact of such standing agreements would be gauged before a final decision is reached 9. Appraisal of the record of capital employed and the rate of return. It is necessary to have a comparison with alternative business avenues for investments and evaluation of possible results on a changed capital and organisation structure, if any, envisaged along with the admission of the partner. <u>Inquire about client & staff:</u> 10. Position of orders at hand & the range and quality of clientele should be thoroughly examined, 11. Whether the incomplete contracts which will be transferred to the reconstituted firm will be a liability or a loss. 12. It would be interesting to study the composition and quality of key personnel employed by



	the firm and any likelihood of their leaving the organisation in the near future
Valuation of Shares in Private Companies:	The different bases on which valuation is possible and the variety of economic factors, on a consideration whereof the price so determined needs to be adjusted. 1) Net Worth method: amount of net worth is divided by the number of shares (i.e., Value per share) → goodwill of the business, and non-trading assets (like investments) based on the estimated future maintainable profit, is included among the assets to arrive at the amount of net worth. • Each asset should be revalued (based on GC assumption) • value of goodwill of a business is primarily dependent on its capacity to earn super-profit and the period over which these are expected to arise 2) Yield basis: average profit earned by the business during the preceding 5 to 7 years is computed. Afterwards, on the assumption that the same would continue to be earned in the future, the value of business is calculated by capitalising it at a reasonable rate_[For Preference share → yield on preference shares of companies engaged in a similar trade or industry after making appropriate adjustment] • present value of the right to receive dividends in the future. (So dividend will also paid out of profit → so while estimating profit → consider that dividend will be paid out) • rate at which the amount of dividends should be capitalised is decided on taking into account the risk that shareholders are taking, similar shares trading (stock exchange)
On behalf of a Bank:	Q9. Nationalised bank received an application from a company seeking sanction of a term loan. Banker has appointed you for investigation List out points you will cover in your investigation Investigation on behalf of a Bank/ Financial Institution Proposing to Advance Loan to a Company: ➤ <u>Investigating accountant, in the course of his enquiry, should attempt to collect information on the under-mentioned points:</u> 1) The purpose for which the loan is required and the manner in which the borrower proposes to invest the amount of the loan 2) The financial standing and reputation for business integrity enjoyed by directors and officers of the company. 3) history of growth and development of company and its performance during the past 5 years 4) The schedule of repayment of loan submitted by the borrower 5) Whether the company is authorised by the Memorandum or the Articles of Association to borrow money for the purpose for which the loan will be used. 6) Whether any loan application to any other Bank or Financial Institution was made, and if so, the reasons for rejection thereof. 7) How the economic position of the company would be affected by economic, political and social changes that are likely to take place during the period of loan. ➤ <u>To investigate the profitability of the business for judging the accuracy of the schedule of repayment furnished by the borrower, as well as the value of the security in the form of assets of the business already possessed and those which will be created out of the loan, the investigating accountant should take the under-mentioned steps:</u> a) Prepare a condensed income statement from the Statement of Profit and Loss for the previous 5 years, showing separately therein various items of income and expenses b) Compute the under-mentioned ratios separately and then include them in the statement to show the trend as well as changes that have taken place in the financial position of the company: (i) Current Assets to Current Liabilities



- (ii) Quick Assets to Quick Liabilities
 - (iii) Equity to Long Term Loans
 - (iv) Sales to Book Debts
 - (v) Return on Capital Employed
 - (vi) Sales to Average Inventories held
 - (vii) Sales to Fixed Assets
 - (viii) Equity to Fixed Assets
 - c) Enter in a separate part of the statement the **break-up of annual sales** product-wise to show their trend
- **Steps involved in the verification of assets and liabilities included in the Balance Sheet of the borrower company which has been furnished to the Bank:**
- a) **Fixed assets:**
 - A full description of each asset its gross value, the rate at which depreciation has been charged and the total depreciation written off
 - In case any asset is encumbered, the amount of the charge and its nature should be disclosed
 - In case an asset has been revalued recently, the amount by which the value of the asset has been decreased or increased on revaluation should be stated along with the date of revaluation
 - b) **Inventory:** The value of different types of inventories held (raw materials, work-in-progress and finished goods) and the basis on which these have been valued.
 - c) **Trade Receivables, including bills receivable:** Their composition should be disclosed to indicate the nature of different types of debts, whether any debts are considered bad or doubtful
 - d) **Investments:** The schedule of investments should be prepared. It should disclose the date of purchase, cost and the nominal and market value of each investment
 - e) **Secured and Unsecured Loans:** Debentures and other secured loans should be included together in a separate schedule. Against the debentures and each secured loan, the amounts outstanding for payments along with due dates of payment should be shown
 - f) **Provision of Taxation:** The previous year's up to which taxes have been assessed or assessment order received should be ascertained
 - g) **Other Liabilities:** It should be stated whether all the liabilities, actual and contingent, are correctly disclosed
 - h) **Contingent Liabilities:** The investigating accountant should ascertain particulars of any contingent liabilities which have not been disclosed. In case, there are any, these should be included in a schedule and attached to the report.
 - i) **Insurance:** A schedule of insurance policies. Risks covered, the date.

Q10. A nationalized bank received an application from a company, seeking **sanction of a term loan**. What major steps an investigating accountant **would keep in mind while verifying assets & liabilities** shown in B/S.

Hint: Refer above "**Steps involved in the verification of assets and liabilities included in the Balance Sheet of the borrower company which has been furnished to the Bank**"

Q11. Investigation on behalf of bank for loan, **investigate the profitability of the business for judging the accuracy of the schedule of repayment** furnished by Core Limited, as well as the **value of the security?**

Hint: Refer above "**To investigate the profitability of business for judging the accuracy of the schedule of repayment furnished by the borrower, as well as the value of the security in the form of assets of the business already possessed and those which will be created out of the loan, the investigating accountant should take the under-mentioned steps**"



➤ Investigation on behalf of an Individual or Firm Proposing to Buy a Business:

In case of proprietary concerns or partnerships: (Special Trick :-)	Q12. Mr. Clean who proposes to buy the proprietary business of Mr. Perfect, engages you as investigating accountant. Specify the areas which you will cover in your investigation. <u>Why is he selling:</u> (i) Reasons for the sale of the business and the effect on turnover and profits that there would be on retirement of the present proprietor (or partners). <u>Customer & Staff:</u> (ii) The age of the present managerial staff and the prospects of continuing in service under the new proprietorship and the possible liability, not already provided for that would arise as regards payment of pensions or gratuities in case of old and aged employees/ retrenched employees. (iii) If the bulk of sales are made to customers whose number is small, the profitability of the business would be greatly shaken on withdrawing their support. This would be an element of weakness which should be investigated as it might affect future profitability. <u>Resources:</u> (iv) The length of lease under which the premises are held, the prospects of its renewal or extension. (v) The unexpired period of any patents owned by the vendors. (vi) The valuation that could be placed on goodwill to determine whether that appearing in book is less or more; if none is included to determine the amount that should be included, if at all.
In Case of Limited companies:	(i) The authorised and issued capital of the company (ii) if the capital is divided into different classes of shares - the rights that are attached to each class. (iii) Whether there is any uncalled liability on the shares (iv) The price at which the shares are being offered. (v) Particulars of dividends paid in the past and the amounts thereof which are in arrear (on cumulative preference shares) (vi) If there are any mortgages/ charge created on the assets appearing in the company's books, a search should be made in the Register of Charges

➤ Investigation in connection with review of Profit/Financial Forecasts

There are many investigations which involve an examination of future profits like,

- 1) Profit reports can be required as part of a **general investigation into the purchase of a business** OR,
- 2) **By banks and financial institutions** with regard to project **cash flow and profitability statements** for appraisal of loan applications submitted by the intending borrowers.

All forecasts depend, to a large extent, on the nature of the business with its numerous and substantial **uncertainties**. Therefore, such forecasts **are not capable of verification** by the reporting accountants in the same way as financial statements which present the results of a completed accounting period.

Normally, such situations involve special review as these depart from the auditor's traditional role of expressing an opinion in relation to past events.

➤ Investigation of Frauds (Link with SA 240, Sec 143(10), Sec 447 Punishment)

Q13. In a Company, it is suspected that there has been **embezzlement in cash receipts**. As an investigator, **what are the areas that you would verify?** (Refer Investigation procedure & way of committing fraud)



Q14. In a Public Limited Company, it is suspected by the Management that there has been **embezzlement in supplier's ledger**. As an auditor of the Company, you have been asked to investigate. What are the **major areas that you would verify** in this regard? *(Refer Investigation procedure & way of committing fraud)*

	Way of committing fraud	Investigation Procedure
Cash receipts	1) Showing a larger cash discount than actually allowed 2) Adjusting a fictitious credit in the account of a customer for the value of goods returned by him. 3) Adjusting a cash sale as a credit sale, and raising a debit in the account of the customer. 4) Writing off a good debt as bad and irrecoverable to cover up 5) Issuing a receipt to the payee for the full amount collected and entering only a part of the amount on the counterfoil 6) the amount collected which has been misappropriated. 7) Under-casting the receipts side of the Cash Book or over-casting the payment side.	1) Income received from different sources should be scrutinized, e.g., inventory, sales summaries, rental registers, correspondence with customers 2) Cash sales should be vouched in detail 3) Recoveries from customers and sundry parties should be checked with the copies of receipts issued to them 4) paying-in-slips from the bank the details of cash deposited on each day should be compared with those shown in the Cash Book. 5) All withdrawals from the bank should be checked by reference to corresponding entries in the bank pass book. 6) Carbon copies of receipts marked 'duplicate', should be scrutinized to confirm that they are in fact copies of receipts issued earlier
Inflate Cash payment	1) Making double payment of an invoice or paying a false invoice. 2) Paying personal expenses out of the business by falsifying details. e.g., showing betting losses as advertisement charges. 3) Withdrawing unclaimed credit balances of customers or amounts falsely credited in the accounts of parties. 4) Wrong totalling of the wage sheets and misappropriating the excess amount withdrawn from the bank for payment of wages.	1) The system of recording of wages should be reviewed, specially as regards possible over-totalling of wage sheets, and entries in them of dummy workmen. <i>Payment ya to CASH se hoga Ya BANK se ...</i> 2) All the evidence as regards cash payments made, including acknowledgement by parties, should be carefully scrutinized. 3) All payments by bearer cheques should be examined. 4) The Petty Cash Book should be vouched and totaled. Bank 5) All the withdrawals from the bank should be checked by reference to entries in the bank's pass book. All the bills receivable or payable should be checked by reference to the Bills Books.
Suppliers' ledger (Nov' 24)	1) Double: Adjusting fictitious or duplicate invoices as purchases in the accounts of suppliers and subsequently misappropriating the amounts when payments are made to the suppliers in respect of these invoices 2) Price: Accepting purchase invoices at prices higher than their market prices and collecting the excess amount, paid in cash, from the suppliers.	1) The Purchase Journal should be vouched by "Goods Inward Book" and "suppliers' invoices". 2) All the suppliers should be requested to furnish statements of their accounts to see whether or not any balance is outstanding or due so as to confirm that allowances and rebates given by them have been correctly adjusted and were duly authorized by the authorized person/ officer 3) Examine internal control i.r.t purchase orders issued and identify possibilities of collusion with



	3) Qty: Suppressing the Credit Notes issued by suppliers and withdrawing the corresponding amounts not claimed by them. 4) Withdrawing amounts unclaimed by suppliers, for one reason or another by showing that the same have been paid to them.	suppliers.
Customers' ledger	(i) By the 'teeming and lading' method, i.e., misappropriating the amount collected from a customer and crediting his account by the amount paid by him only when an amount is subsequently collected from another customer; repeating this practice with several items collected and depositing back the amount or amounts so misappropriated before the close of the year. (ii) Misappropriating the amount collected from a customer and subsequently adjusting his account by crediting the amount on account of allowance or a rebate for excess price charged.	1) To confirm that the accounts of customers have been debited in respect of goods supplied to them, entries in the Order Book should be cross-checked with those in the Sales Day Book where the same is kept. 2) Special attention should be paid to allowances adjusted on account of goods returned or difference in price or on any other account as well as to amounts written off as bad debts. 3) The investigating accountant should obtain confirmation of customers i.e. the amounts standing in their accounts. Those of them who have no balance in their accounts should be requested to confirm the statement of their account (which should be sent to them) for ascertaining that the entries shown therein were genuine.

➤ INVENTORY FRAUD:

Q15. areas of verification and the procedure to be followed for verification of defalcation of inventory? how inventory fraud occurs and the verification procedure. (SM & RTP May 25)

Answer:

❖ Way of committing fraud:

- 1) **Employees** may simply **remove goods** from the premises
- 2) **Theft** of goods may be concealed by writing them off as damaged goods, etc.
- 3) Inventory **records may be manipulated by employees who have committed theft** so that book quantities tally with the actual quantities of inventories in hand.
- 4) **Inflating the quantities issued for production** is another way of defalcating raw materials and store items.
- 5) Stocks actually **dispatched but not entered in sales/ debtor's account**

❖ Investigation Procedure:

- 1) Thefts usually are possible through collusion among a number of persons. Therefore, for their detection, the **entire system of receipts, storage and dispatch of all goods**, etc. should be **reviewed to localise the weakness** in the system
- 2) The **determination of factors which have been responsible for the theft** and the establishment of guilt would be **difficult in the absence of:**
 - (a) a system of inventory control, and existence of detailed record of the movement of inventory, or
 - (b) availability of sufficient data from which such a record can be constructed.
- 3) The first step in such an investigation is to establish the different items of inventory defalcated and their quantities by **checking physically the quantities in inventory** held and those **shown by the Inventory Book**.
- 4) Identify the **excessive control in the hands of a single person**, without any supervision as it will widen the



scope of investigation.

- 5) Verify all the **receipts and issues** of inventory recorded in the **Inventory Book** should be **verified** by reference to entries in the **Goods Inward and Outward Registers** and the documentary evidence as regards purchases and sales.
- 6) Afterwards, the shortages observed on physical verification of inventory should be reconciled with the discrepancies observed on checking the books in the manner mentioned above
- 7) This would reveal the particulars of **inventory not received but paid** for as well as that issued but not charged to customers.
- 8) **Defalcations of inventory, sometimes, also are committed by the management, by diverting a part of production and the consequent shortages** in production being **adjusted by inflating the wastage** in production; similar defalcations of inventories and stores are covered up by inflating quantities issued for production. **For detecting such shortages, the investigating accountant should take assistance of an engineer.**
- 9) Correctly determine the extent to which the **shortage in production has been inflated**. In this regard, **guidance can also be taken from past records** showing the extent of wastage in production in the past. Similarly, he would be able to better judge whether the material issued for production was excessive and, if so to what extent. The per hour capacity of the machine and the time that it took to complete one cycle of production, also would show whether the issues have been larger than those required.

Q16. the top management has grown suspicious over manpower expenditure. There is a system in the company where time cards are punched by all employees to mark attendance → **Suggest any one procedure you would perform as an investigator to bring out the facts.**

Answer:

The **attendance record of employees** pertaining to that **section can be analysed** with regards to **in and out** time. Further, surprise visit to the site can be conducted to see the **actual number of workers** at a point of time. **It may reveal ghost workers.** Discrepancies in attendance records vis-à-vis actual number of workers present could reveal dummy workers.

Such a **visit** also give indication of **actual work done in the area & give an inkling of productivity** of employees.

➤ **REPORTING:**

Q17. Important issues to be kept in mind by the investigator while preparing his report

Trick: Nature/scope/objective/limitation : Only *relevant chize likhna*, and *Wording ka dhyaan rakhna*, Jo bhi *assumption liye hai conclusion ke liye*, vo likh dena, Then Finally *Opinion de dna last Para me*

"The important issues to be kept in mind by the investigator while preparing his report are as follows:

- (i) The report should **not contain anything** which is **not relevant** either to highlight the nature of the investigation or the final outcome thereof.
- (ii) Every **word or expression used should be properly considered** so that the possibility of arriving at a **different meaning or interpretation** other than the one intended by the investigator can be minimized.
- (iii) Bases and **assumptions made should be explicitly stated**. Reasonableness of the bases and assumptions made should be well examined and care should be taken to see that none of the bases and assumptions can be considered to be in conflict with the objective of the investigation. For example, in an investigation into over-stocking of raw materials, inventories and spares etc. it should not be assumed that the ordering levels indicated on bin cards provide fair guidance about acquisition of further materials. Also, since investigation is a fact -finding assignment, assumptions should be made only when it is unavoidably necessary
- (iv) **Relevant facts and conclusions** should be properly **linked with evidence**.
- (v) The **opinion** of the investigator should appear in the **final paragraph of the report"**

- (vi) The report should be made in **paragraph form with headings** for the paragraphs. Any detailed data and figures supporting any finding may be given in Annexures
- (vii) The report should clearly spell out the **nature and objective of the assignment** accepted its scope and limitations, if any.
- (viii) The report should also **state restrictions or limitations**, if any, imposed on the instructions given by the client. Preferably the reasons for placing such restrictions and their impact on the final result should also be stated.



CHAPTER 17.3: FORENSIC ACCOUNTING

➤ Meaning:

Forensic Accounting:	Definition 1
	The integration of accounting, auditing and investigative skills yields the specialty known as Forensic Accounting. It is the study and interpretation of accounting evidence . It is the application of accounting methods to the tracking and collection of forensic evidence , usually for investigation and prosecution of criminal acts such as embezzlement or fraud .
	Book Definition by by Hopwood, Leiner, and Young
	- Forensic accounting is the application of investigative and analytical skills for purpose of resolving financial issues in a manner that meets standards required by courts of law. - Forensic accountants apply special skills in accounting, auditing, finance, quantitative methods, certain areas of the law, research and investigative skills to collect, analyse and evaluate evidential matter and to interpret and communicate findings
Forensic:	The word forensic comes from the Latin word forensis, meaning "of or before the forum." - It is Relating to, used in, or appropriate for courts of law or for public discussion or argumentation. Relating to the use of science or technology in the investigation and establishment of facts or evidence in a court of law.
Red Flag:	Red flags are indicators or warning of any impending danger or inappropriate behavior. Red flag does not necessarily indicate the existence of fraud however are indicators that caution needs to be exercised while investigating the situations. Red flags are classified in categories such as financial performance

➤ Difference:

Q1. ABC Ltd. is a listed company & plans expansion by incurring Following Cost:

Rs. 10 Crore for Building, Rs. 8.5 Crore for Machine, Rs. 1.5 Crore for Working Capital = **Total 20 Crore Rs.**

Director is suspicious transactions are noticed in purchase of building material. But Mngt is confused as to whether do an audit or Forensic Audit done for the same. Advise **difference in forensic accounting and audit**.

Answer:

Forensic accountant professional will often look for indications of fraud that are not subject to the scope of a FS audit. Forensic Accounting has **Investigative mentality**" → A forensic accountant professional may focus more on seemingly immaterial transactions.

However auditing is done with "**professional skepticism**". A forensic accountant professional will often require more extensive corroboration.

(Trick: **OTP** diya tha **Stock purchase ke liye..isne to OFF kar diya mera bank balance adversely**)

Sr	Basis	Other Audits	Forensic Accounting
1	Objective	Express an opinion as to 'True & Fair' presentation	Whether fraud has actually taken place in books
2	Techniques	Substantive & Compliance. Sample based	Investigative, substantive or in-depth checking
3	Period	Normally for a particulars accounting period .	No such limitations



4	Verification of stock , Estimation realisable value of assets, provisions, liability etc	Relies on the management certificate/Management Representation	Independent/verification of suspected/selected items where misappropriation in suspected
5	Off balance sheet items (like contracts etc.)	Used to vouch the arithmetic accuracy & compliance with procedures.	Regulatory & propriety of these transactions/ contracts are examined .
6	Adverse findings if any	Negative opinion or qualified opinion expressed with/without quantification	Legal determination of fraud impact and identification of perpetrators depending on scope

➤ About Forensic Auditor/ Forensic Accountant:

Forensic Accounting Services: [FM-DT-IVT] <i>Saari subject me jarurat h uski:</i>	Q2. What are the areas where the services of forensic accountants are generally required? An indicative list of services that can be provided by the Professional in this area are as follows: 1) Financial Statement manipulations 2) Anti-Money laundering 3) Fund Diversions/Asset tracing 4) License Fees/Dues/Tax Evasion 5) Suspicious transactions in IBC (Insolvency & Bankruptcy Code) (eg., Fund diverted just before IBC process) 6) Valuations/Estimations of loss/damage 7) Related party transactions/valuations		
Who Retains Forensic Accountant?	1) Police Forces 2) Courts 3) Lawyers	4) Banks 5) Insurance Companies 6) Business Community	7) Government Agencies 8) Other organisation
Forensic Accountant involved in: <i>Trick: Expert in prevention & detection of fraud using computer</i>	Q3. What do you understand by the word "Forensic" and why the need for forensic audit arises? <u>Refer "Forensic" word definition, as given in 1st page</u> 1) Providing Expert Testimony: Assisting in legal proceedings, including testifying in court as an expert witness and preparing visual aids to support trial evidence. 2) Fraud Prevention: Either reviewing internal controls to verify their adequacy or providing consultation in the development and implementation of an internal control framework aligned to an organization's risk profile 3) Fraud Detection: Investigating and analyzing financial evidence, detecting financial frauds and tracing misappropriated funds 4) Computer Forensics: Developing computerized applications to assist in the recovery, analysis and presentation of financial evidence		
Skills of F. Accountant:	In order to properly perform these services a Forensic Accountant Professional must be familiar with legal concepts and procedures and have expertise in the use of IT tools and techniques that facilitate data recovery and analysis . In addition, a Forensic Accountant Professional must be able to identify substance over form when dealing with an issue		

Q4. X Ltd manufacturer has taken a **Product Liability Insurance policy (PLI)**. Policy covers risk of liabilities for damages for bodily injury resulting from sale and distribution of floor. The policy is also subject to "**claim series**" clause. A **Claims Series event is a series of two or more claims arising from one specific common cause** which are attributable to the same fault in design or manufacture of products or to the supply of the same products showing the same defect. forensic accountant **appointed by insurance company, what special issues** you would keep in mind while dealing with claims involving PLI policy covering such matters? (SM)



Answer:

Trick: "3rd party" se "kitne Rs. ki Legal liability" & "Kab aai"? ... ohhoo .. y to bahot bada loss hai .. "reputation" issue hoga apna ... "independence" rkhna

- (i) In claims involving product liability insurance policies, many documents are required from 3rd parties. The third party may be unwilling to provide relevant documents to forensic accountant concerning the very organization responsible for causing damages
- (ii) Quantification of legal liability under the policy can prove to be a challenging task and it has to be determined in accordance with policy terms & conditions.
- (iii) Careful analysis of date of loss when first claim occurred in accordance with "claim series" clause and whether the same falls under the policy
- (iv) Company might be willing to negotiate it to salvage its reputation. It can lead to additional complexities
- (v) Independence of forensic accountant become paramount in such types of assignments because it involves engagement with parties who are not directly claiming from insurance company. Forensic accountant needs to resist any pressure or interference in establishing the scope of the assignments or the manner in which the work is conducted and reported.

➤ PROCESS OF FORENSIC ACCOUNTING: (Trick: IPE-ARC)

Q5. Enumerate the steps to be undertaken in case of forensic Accounting process.

1	Initialization	Clarify all doubts as to the real motive, purpose and utility of the assignment
2	Develop the Plan	Plan will take into account the knowledge gained by meeting
3	Obtain Relevant Evidence	• In order to gather detailed evidence, the investigator must understand the specific type of fraud that has been carried out, and how the fraud has been committed. • Evidence should be sufficient to Prove Identity of Fraudster, Mechanism/Method of fraud, amount of financial loss incurred. (Kisne, Kaise, and kitne ka) • Investigating team is skilled in collecting evidence that can be used in a court case within the stipulated time period, and in keeping a clear chain of custody until the evidence is presented in court. If any evidence is inconclusive or there are gaps in the chain of custody, then the evidence may be challenged in court, or even become inadmissible
4	Perform Analysis (Special Trick :-)	Q6. You have been appointed as a forensic accountant → Specify the various analysis which might have to be carried out by you to arrive at your result. a) calculating economic damages b) summarizing a large number of transactions; <u>Statistics related point:</u> c) performing present value calculations utilizing appropriate discount rates; d) performing a regression or sensitivity analysis; e) utilizing charts and graphics to explain the analysis f) utilizing a computerized application such as a spread sheet, data base or computer model; g) performing a tracing of assets;
5	Reporting	• Issuing an audit report is the final step of a fraud audit. Auditors will include information detailing the fraudulent activity → Findings of Investigation (Evidences & Conclusion) → Amount of loss suffered & identity of those involved in fraud. • May include nature of assignment, Scope, approach, limitation, finding/opinion • Report will include schedules & graphics necessary to proper support & explain findings. • The report will also discuss how the fraudster set up the fraud scheme, and which



		controls, if any, were circumvented. It is also likely that investigative team will recommend improvements
6	Court Proceedings	The investigation is likely to lead to legal proceedings against the suspect, and members of the investigative team will probably be involved in any resultant court case. team members may be called to court to describe the evidence they have gathered

Q7. Forensic accountant extracted Evidence → but team has failed → keeping record of each person in team gathering relevant evidence, date and time of collection and storage of such evidence (MTP'24 & SM)

Hint: → In Forensic Engagement → Undertake Scrutiny & detailed examination of all relevant transaction, so that evidence gathered is Suitable in court of Law. (comply legal requirement where it can be challenged by defending party) Team should be Skilled in Collecting evidence → Keep Clear chain of custody of evidence → if any gap in chain → evidence can be challenged in court/even become inadmissible by defending party.

Hence, Explain Given case → it defeat objective of forensic a/cing → evidence can be challenged in court of law.

➤ FORENSIC ACCOUNTING & INVESTIGATION REPORT:

This **Forensic Accounting and Investigation Standard (FAIS or "Standard") 510** deals with the responsibility of the Professional to issue a written report to the stakeholders at the conclusion of the assignment.

Reporting results of the work procedures completed and the findings from those procedures, is the concluding part of the assignment. Since one engagement may include multiple assignments, multiple reports may have to be issued; one for each assignment.

Q8. Briefly discuss the key content of Forensic Accounting and Investigation Report.

[Trick: there is no trick See the answer ... it's very basic thing about audit report... "Timely basis" pe "written" m "kya kya content" likh k dna h .. "like assumption" etc..final ke phle draft share karo]

Written Report:	Written report → conveys the results of the assignment clearly and accurately. precise and unambiguous.
Report addressee & distribution:	shall be addressed to the Primary Stakeholders and shared with other stakeholder(s) if required or otherwise permissible
Format or Content of Report:	No fixed form or content of the report is mandated by this standard. Where the form and content of the report is mandated by the stakeholders, or specified by the statutory or regulatory requirements, the Professional shall report in line with those requirements, while keeping in mind the key elements. Key Elements of the Report: The Professional shall consider the inclusion of the following key elements in the report (indicative list): 1) Title, addressee and distribution list (if any) 2) Scope and objectives of the assignment 3) Approach and broad work procedures undertaken 4) An Executive Summary of the results, covering all important aspects and the essence of the findings 5) Reference to use of an expert, where applicable 6) The fact that the assignment has been conducted in accordance with FAIS, or any material departures therefrom 7) List of findings supported by key evidences, sources of evidences, and other relevant matter; 8) Assumptions, limitations and disclaimers of the assignment 9) Conclusions (if any) drawn from the assessment undertaken
Discussion of	Mandate of the engagement requires a discussion of the findings with the subject party prior to



Draft report:	finalization , a summary of the responses received from them shall be included in the report . Further, Principles of Natural Justice requires a discussion of observations with subject party.
Assumptions & Limitations:	List any relevant assumptions → significant bearing on the subject matter. Professional may encounter limitations that restrict the methodologies or procedures → lack of (or limited) management support, restricted (or denied) access to required records. The report shall not express an opinion or pass any judgement on the guilt or innocence → Determination of culpability is either a disciplinary process internal to the organization under review, or a judicial process
Reporting Timelines:	shall be issued within reasonable time frame as per the engagement terms . The Professional may be required to provide interim reports as per the engagement terms which can be given to the extent practicable without compromising the progress of the investigation. Such interim reports are also subject to this Standard

➤ OVERVIEW OF FORENSIC ACCOUNTING & INVESTIGATION STANDARDS (FAIS)

Issued by:	ICAI
Framework:	Framework Governing Forensic Accounting and Investigations ("Framework") lays down the underlying principles and boundaries for undertaking such services → This Framework needs to be read in conjunction with the Preface to the FAIS.
Objective of Framework:	1) Provide a overall understanding of Forensic Accounting & Investigations & its key components. 2) Outline the manner in which these components come together in an inter-related cohesive manner when providing such services 3) Maintain and improve the quality of forensic accounting and investigation services
Mandatory:	4 components given are MANDATORY (Except Guidance Note is recommendatory.)
4 key Component:	The four key components (forming the pillars) of the Framework are: 1) Basic Principles of Forensic Accounting and Investigations 2) Key Concepts 3) Standards on Forensic Accounting and Investigations 4) Guidance. Code of Ethics forms the foundation of the Framework
FAIS seek to provide:	Forensic Accounting & Investigation Standards ("FAIS" or "Standards") seek to provide: a) The Professionals with the minimum standards for undertaking forensic accounting and investigation (FAI) assignments; b) The Users of FAI services with an indication of the quality of service that can be expected from such engagements c) The Regulators and Governmental agencies with an appreciation of what can be expected from FAI services; and d) To everyone, guidance on matters of implementation and related practical issues.
Principle Based:	The Standards are intended to be principle-based , rather than rule based , thereby providing ample room for professional judgment when applying such principles to unique situations and under specific circumstances .
Unable to Comply FAIS:	If, for any reason , a member is unable to comply with any of the requirements of the FAIS, or if there is a conflict between the Standards and other mandates , such as a statutory or regulatory requirement, the FAI report (or such similar communication) should draw attention to the material departures therefrom along with appropriate explanation.
	<u>"Refer Additional PDF Booklet"</u>



CHAPTER 18: Sustainable Development Goals (SDG) & Environment, Social and Governance (ESG) Assurance:

➤ Sustainable Development & It's 3 Pillars:

Sustainability:	• Development of products, goods and services that involves meeting our present needs without compromising the ability of future generations to fulfil their own needs. (As resources are Limited i.e., exhaustible resource) • It's named after Brundtland report, which reports sustainable consumption in developed countries.												
Sustainable Development:	As per Brundtland report, Sustainable development is development that strives to meet the needs of developing countries seeking to achieve a more sustainable world . Sustainable development addresses the needs of the present moment without compromising current and future generations to meet their own sustainable lifestyles.												
❖ Sustainable development can be applied to corporate policy: 3 Pillars of sustainability (ESG):													
Environment(E): <i>[natural resources khatam kar diye.. pollution fela diay.. us wjh se Climate change hora h .. ab thik karo usse]</i>	Environmental stands for corporate climate policies, energy use, waste, pollutions, natural resource conservation, and treatment of animals. It includes the natural resources that every entity absorbs → like that of coal, electricity, water and so on. Processing this energy into products / services which will leave behind certain wastes like that of carbon emissions, water discharges, e-wastes and so on. <table><tr><th colspan="4">Elements of Above Pillar:</th></tr><tr><th>Climate Change:</th><th>Natural Resources:</th><th>Pollution & Waste:</th><th>Environment Opportunity:</th></tr><tr><td> • Carbon Emissions • Product Carbon FootPrints • Financing Environmental Impact • Climate Change Vulnerability </td><td> • Water Stress • Bio-diversity & land use • Raw Material sourcing </td><td> • Toxic emission and waste • Packing Material & waste • E- Waste </td><td> • Clean Tech • Green Building • Renewable Energy </td></tr></table>	Elements of Above Pillar:				Climate Change:	Natural Resources:	Pollution & Waste:	Environment Opportunity:	• Carbon Emissions • Product Carbon FootPrints • Financing Environmental Impact • Climate Change Vulnerability	• Water Stress • Bio-diversity & land use • Raw Material sourcing	• Toxic emission and waste • Packing Material & waste • E- Waste	• Clean Tech • Green Building • Renewable Energy
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Climate Change:	Natural Resources:	Pollution & Waste:	Environment Opportunity:										
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Social(S): <i>[Human apni capital lagaake product banaata h> fir koi n koi social worker aake usse oppose karta h]</i>	It addresses the relationships the entity has and the reputation it fosters with people and institutions in the communities where you do business and the value chain involved. It further includes labour relations, diversity, and inclusions. (Society) <table><tr><th colspan="4">Elements of Above Pillar:</th></tr><tr><th>Human Capital:</th><th>Product Liability:</th><th>Stakeholders Opposition:</th><th>Social Opportunity:</th></tr><tr><td> • Labour Management • Health & Safety • Human Capital Development • Supply Chain Labour Standards </td><td> • Product Safety & Quality • Chemical Safety • Financial Product Safety • Privacy and Data Security • Responsible Investment </td><td> • Controversial Sourcing </td><td> • Access to Communication • Access to Finance • Access to Health Care • Opportunities in Nutrition & Health </td></tr></table>	Elements of Above Pillar:				Human Capital:	Product Liability:	Stakeholders Opposition:	Social Opportunity:	• Labour Management • Health & Safety • Human Capital Development • Supply Chain Labour Standards	• Product Safety & Quality • Chemical Safety • Financial Product Safety • Privacy and Data Security • Responsible Investment	• Controversial Sourcing	• Access to Communication • Access to Finance • Access to Health Care • Opportunities in Nutrition & Health
Elements of Above Pillar:													
Human Capital:	Product Liability:	Stakeholders Opposition:	Social Opportunity:										
• Labour Management • Health & Safety • Human Capital Development • Supply Chain Labour Standards	• Product Safety & Quality • Chemical Safety • Financial Product Safety • Privacy and Data Security • Responsible Investment	• Controversial Sourcing	• Access to Communication • Access to Finance • Access to Health Care • Opportunities in Nutrition & Health										
Governance(G):	It is the internal system of practices, controls , and procedures entity adopts in order to												



govern itself, make effective investment decisions, comply with the law, and meet the needs of all stakeholders.

Elements of Above Pillar:

Corporate Governance:	Corporate Behaviour
- Broad Diversity - Executive Pay - Ownership - Accounting	- Business Ethics - Anti - Competitive Practices - Corruption & Instability - Financial system and stability - Tax Transparency

➤ ESG Reporting: (it's sub-part of Sustainable reporting)

Added Value: Environmental, Social and Governance (ESG) reporting is all about disclosure of information, data, metrics that **explain the added value in these three areas.**

Q & Q: ESG reporting can be both **quantitative** and **qualitative** in nature.

Qualitative report:	describe a company's strategy or policy around the relevant topics,
Quantitative approach:	includes metrics , and key performance indicators (KPIs) linked to each area in order to measure progress against goals and report on achievements

Mixed approach that makes use of both qualitative and quantitative information tends to add the **maximum value to the quality of disclosures**

Q1. SEBI has mandated BRSR for certain listed companies. Discuss the nature of ESG reporting. How can corporates contribute to Sustainable Development Goals (SDGs)? (RTP'24 & SM)

Hint: → Refer Above Topic "**3 Pillars of (ESG)**" → "**Environment, Social & Governance**" → **Explain about them ..** (However, **Do Not mention** , "**ELEMENTS of Pillars**") → Also explain "**ESG Reporting**" (as mentioned in above notes)

- UN members states adopted Sustainable Development → Sustainable Development Goals (SDGs). They recognized that ending poverty & other deprivations, strategies that improve health & education, reduce inequality, & tackling climate change etc. **Corporates can contribute to SDGs due to their capacity to provide solutions necessary for meeting SDGs.** Companies can lead in innovation & contribute to achievement of SDG.

Q2. What is your understanding of "Sustainability reporting"? Can you list some of its expected benefits?

➤ Sustainability reporting:

Meaning:	- Sustainability reporting is an organization's practice of reporting publicly on its Economic, Environmental, and/or Social impacts [ESG], and hence its contributions - positive or negative → towards the goal of sustainable development - Sustainability reporting refers to the info. that companies provide about their performance to the outside world on a regular basis in a structured way. It is the comprehensive mechanism of measuring & disclosing sustainability data with performance indicators and mngt disclosures
Expected Benefits:	Stakeholder: It can help stakeholders to understand organizations performance vis a vis sustainability and impacts. The reporting process emphasizes the link between financial and non-financial performance. Investors: Such reporting help entities to focus on long-term value creation, by addressing environmental, social and governance (ESG) issues. Since investors are increasingly recognizing that environmental and social issues provide both risks and opportunities in respect of their investments and are seeking disclosures on environmental and social performance of businesses, they can use ESG performance of companies to make investment decisions. Own Business & Customer: Investing in social and environmental issues will not only improve own



business continuity of companies but also put them in a better position with their B2B (Business to Business) customers as well as enable them to acquire new ones.

➤ Sustainable Development Goals [SDG]:

About:	- In 2015, Sustainable Development was adopted by all United Nations Members states to provide a blueprint, which mentioned the Sustainable Development Goals (SDGs) 17 SDGs which are considered as an urgent call for action by all countries, whether developed or developing countries. - SDG plays a key role in the evaluation of UN systemwide implementation of the 2030 Agenda → broad ownership of the SDGs must translate into a strong commitment by all stakeholders to implement the global goals [For more Details: Refer Additional PDF Booklet]	
17 SDG's:	1) No Poverty	10) Reduced Inequalities
<u>PHHEE WE WI</u>	2) Zero Hunger	11) Sustainable Cities & Communities
<u>IS CC LLP</u>		12) Responsible Consumption & Production
Gareebi / inequality (4)	3) Good Health & Well Being	
Sabko health & education (har gender ko) 3	4) Quality Education	
Paani/Bijli (2)	5) Gender Equality	
Growth ki wjh se sab jgh ka climare kharab hora h (6)	6) Clean Water & Sanitization	
	7) Affordable & Clean Energy	
	8) Decent Work & Economic Growth	13) Climate Action
	9) Industry Innovation & Infrastructure	14) Life Below Water
		15) Life on Land
	16) Peace, Justice & Strong Institutions	17) Partnership for the Goals

➤ GLOBAL TRENDS IN SUSTAINABLE REPORTING

Q3. What are the global trends in sustainable reporting? [ICAI SM]

Mandatory reporting:	The mandatory reporting requirements are mostly associated with: public sector or government companies, large corporations, multi-national business conglomerates, and listed companies in the stock exchanges → Furthermore, sector-specific, and thematic reporting provisions
➤ Worldwide Frameworks for Reporting Sustainability Performance	
Global Reporting Initiative (GRI)	Helps the organizations to report on Economic, Environmental, and Social impacts [EES]. This report is addressed to all the stakeholders of the entity. It's most widely used framework in the world (100 countries, 250 Large corporation (Amsterdam, Netherlands, Brazil, India, China, US etc)
Carbon Disclosure Project (CDP)	Captures the environmental performance data which is related to GHG emissions, water, forests, and supply chain. Major details required to be reported are climate change, Forest, and Water security. addressed to all the investors, buyers, and other stakeholders of the entity.
International Integrated Reporting Framework	has established guiding principles and content elements in order to allow the companies to produce integrated reports. This report consists of Organisational overview, Governance structure, Business model, risks and opportunities, strategy, performance, outlook etc.



Below are Some Timelines innovations:

Comprehensive corporate reporting system	In Sept 2020 → these framework & standard setting institutions came together to set → comprehensive corporate reporting system, Intent of Collaboration: - Joint guidance on how frameworks & standards can be applied in complementary way - how these elements could complement financial generally accepted accounting principles (Financial GAAP) (coherent, comprehensive corporate reporting system)
ISSB	International investors with global investment portfolios are increasingly calling for high quality, transparent, reliable, and comparable reporting by companies on climate and other environmental, social and governance (ESG) matters Nov 21, IFRS Foundation Trustees created new standard board → the International Sustainability Standards Board (ISSB) —to help meet this demand. Intent of IISB: to deliver a comprehensive global baseline of <u>sustainability-related disclosure standards</u> that <u>provide investors and other capital market participants with information</u> about <u>companies' sustainability-related risks and opportunities</u> to help them make informed decisions.
TCFD:	Task Force on Climate-Related Financial Disclosures: Created by Financial stability board (FSB) in 2015: with the goal of helping companies create consistent climate-related disclosures . [Unlike GRI which focus on wide range of organization → TCFD target only → Companies that predominantly handle financial-related interests , such as banks and insurance firms]
CDSB:	The Climate Disclosure Standards Board: International group of business and committed to making climate-rated disclosures in the mainstream global corporate reporting . → disclose climate related risks and opportunities . → approach on for reporting environmental info.
VRF	The Value Reporting Foundation: a non-profit organization which was a result of the merger between SASB Foundation and the International Integrated Reporting Council (IIRC). The International Accounting Standards Board (IASB) and the ISSB has agreed to work together in order to build an Integrated Reporting Framework .

➤ **INTEGRATED REPORTING (6 C's) i.e., 6 capitals:**

Q4. What are the 6 C's of Integrated reporting? Or,

Q. how would you explain the essential components of Integrated Reporting to the board?

Trick: FS M NHI (FS Me show krna hai ? NHI)

Financial Capital:	- Pool of funds that is available to the organization for use in the production of goods or provision of services. - Obtained through financing, such as debt, equity, or grants, or generated through operations or investments
Social Capital:	- Institutions & relationships established within and between each community, group of stakeholders and other networks to enhance individual and collective well-being Common values and behavior. key relationships, the trust and loyalty that an organization has developed and strives to build and protect with customers, suppliers, and business partners. - an organization's social license to operate.
Manufactured	Seen as human-created, production-oriented equipment and tools.

Capital	Available to the organization for use in the production of goods or the provision of services, including buildings, equipment, infrastructure (such as roads, ports, bridges & waste, and water treatment plants).
Natural Capital:	- Is an input to the production of goods or the provision of services. - An organization's activities also impact, positively or negatively, on natural capital. - Includes water, land, minerals and forests, biodiversity, and ecosystem health.
Human Capital:	People's skills and experience, their capacity, and motivations to innovate, including their: - Alignment with and support of the organization's governance framework & ethical values such as its recognition of human rights - Ability to understand and implement an organization's strategy. Loyalties and motivations for improving processes, goods, and services, including their ability to lead and to collaborate
Intellectual Capital:	Key element in an organization's future earning potential, with a tight link and contingency between investment in R&D, innovation, human resources, and external relationships , which can determine the organization's competitive advantage.

Q5. Listed company → sustainability report based on "Integrated Reporting" on a voluntary basis, identify which capitals of "Integrated Reporting" are being referred above respectively? (SM)

- i) It has increased the No. of customers using digital customer mobile app for collection → **Intellectual Capital**
- ii) It has increased the number of beneficiaries under its flagship CSR programmes. → **Social & Relationship Capital**
- iii) It has secured a loan to expand its operations & invests funds in purchasing machinery → **Financial Capital**

➤ GLOBAL SCENARIO IN VARIOUS COUNTRIES

United States [RR-SM]	In March 2022, the US Securities and Exchange Commission (SEC) proposed climate-risk disclosure requirements , which would expand the annual reporting requirements of publicly traded companies . In their SEC filings, companies would be required to discuss financially material, climate-related risks guided by the TCFD recommendations. <u>Reporting would include:</u>	
	- The company's climate Risk management processes - How the Risks identified would impact financial performance - Any Scenario analysis, transition plans, and publicly announced climate goals - How these risks are Managed and mitigated	
	UK ESG disclosures is the Co. Act of 2006 , which includes requirements for annual reporting .	
	Applicable:	These rules apply to large companies that are either Listed, or Exceed £500 million in annual turnover, or - have more than 500 employees.
United Kingdom	Non-financial information include sustainability matters , align with the recommendations from the Task Force on Climate-Related Financial Disclosure (TCFD) .	
	Required to discuss strategy, processes, and due diligence regarding matters of:	- The environment (including the company's impact on the environment) - The company's employees Social matters - Respect for human rights Anti-corruption and anti-bribery
	Specific Climate Related Disclosure (Under	- Climate change-related risks and opportunities - How these risks & opportunities are managed through targets & KPIs - How climate change is addressed in corporate governance



Environment):

- How climate risk impacts **strategy**

Additionally, large UK companies are required to report on their **UK energy use and carbon emissions** within their annual reports through the Streamlined Energy and Carbon Reporting

➤ EVOLUTION OF ESG IN INDIA

2009	MCA Issued : Corporate Social Responsibility VOLUNTARY Guidelines 2009 element (element focus on Ethical functioning, Rights and welfare of workers, environmental)
2011	National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business' (Comprehensive principles: adopted by companies as part of their business practice.)
2012	SEBI Mandates top 100 listed companies to file Business Responsibility Report (BRR) (ESG principles)
2015	BRR became part of SEBI LODRS → in respect of reporting on ESG → Top 500 Listed entities (market capitalization)
2017	SEBI recommend Integrated Reporting to prepare BRR for top 500 listed companies (Voluntary)
2019	MCA formed National Guidelines on Responsible Business Conduct (NGRBC).
2019	BRR became mandatory for top 1,000 listed companies
2021 (BRSR) Voluntary	SEBI Introduced → New reporting requirements on ESG parameters called the Business Responsibility and Sustainability Report (BRSR) → It seeks disclosures from listed entities on their performance against the 9 principles of 'National Guidelines on Responsible Business Conduct' (NGRBCs) and Reporting under each principle is divided into 1) Essential Indicators: Mandatory Reporting 2) Leadership indicators: Voluntary basis BRSR is intended towards having quantitative & standardized disclosures
2022	Top 1000 listed companies → to File BRSR along with Annual report (Mandatory)

Q6. What type of companies are required to mandatorily furnish BRSR as per SEBI circular w.e.f FY 2022-23?

Hint: Top 1000 listed companies

➤ BUSINESS RESPONSIBILITY AND SUSTAINABILITY REPORT (BRSR)

The reporting questionnaire is divided into 3 sections :				
Section A: General Disclosures	Section B: Management Process and disclosures	Section C: Principle-wise performance disclosures		
contains the details of the listed companies, its products, services, operations, employee related details, its	It contains questions related to policy and management processes, governance, leadership, and oversight	Companies are required to report upon Key performance indicators (KPIs) in alignment with the nine principles of the NGRBC. The section <u>classifies KPIs into two categories</u> that companies are required to report upon: <table><tr><td>I] Essential indicators (Mandatory disclosures)</td></tr><tr><td>include data on training programs conducted, environmental data on energy, emissions, water, waste management, anti-corruprtion etc.</td></tr></table>	I] Essential indicators (Mandatory disclosures)	include data on training programs conducted, environmental data on energy, emissions, water, waste management, anti-corruprtion etc.
I] Essential indicators (Mandatory disclosures)				
include data on training programs conducted, environmental data on energy, emissions, water, waste management, anti-corruprtion etc.				

holding, subsidiary, associate companies etc.		II] Leadership indicators (Optional disclosures) include life cycle assessments, details of conflict management policy, additional data, on biodiversity, energy consumptions, supply chain managements , awareness program etc.

Nine Principles of BRSR

[Its' based on ESG component: 2 of Environment, 3 of Social, 4 of Governance → interlinked to each other in some way → Eg. environmental protection is closely linked to the stakeholder engagement and inclusive growth]

Principle 1: Ethics, Transparency & Accountability <u>(May'24)</u> <u>(Special Trick :-)</u>	Q7. One of the principles emphasizes that the business decisions in an organization should be open to disclosure and accessible to the relevant interested parties. (May 2024 & SM) <u>Answer:</u> Business decisions in an organisation should be open to disclosure and accessible to the relevant interested parties. <u>[Trick: "Policy" & "Governance structure" hai ? "stakeholder" ko d rkha h ? agar kuch "adverse" ho to "repond" kese karoge ?]</u> Policies & procedures: The entities' governing structure should develop policies, procedures, and practices for their offices, factories, and work areas, ensuring that ethics is not compromised. Governance Structure: The entities in the value chain should be encouraged to adopt these principles by governance structure. Available to the stakeholders: The information relating to the policies, procedures, and practices along with the performance should be made available to the stakeholders. Adverse: In case of adverse effects, more care to be taken for transparent disclosures. Violation Response: The entities should proactively respond to outside entities that violate the 9 principles of the BRSRs. This includes their suppliers, distributors, sub-contractors, or regulatory officers that may engage with the business concern.
Principle 2: Safe and Sustainable Goods and Service: (Product banana k phle, banana k baad, bechne k baad)	The entities should make sure that goods, services, and operations → will result in better life for the consumers and end-users. Production method & technology: When a product is designed by the entity, the production methods and technologies have to be devised in such a way so as to minimize the resource usage to make it sustainable. Reduce/Reuse/Recycle: The entities should take measures that reduce the over exploitation of the nature's resources by consuming sustainably and encourage methods for reduce, reuse and recycling of the resources. Customer Rights: The entities are also responsible to educate and make aware their consumers and clients about their rights.
Principle 3: Promote well-being of all employees including those in the value chain:	Q8. Employees raised issue reg delay in salary, work life balance → BRSR ?. (RTP May'25) All the initiatives an entity has to take for the benefit of its employees from the point of view of their dignity, health, well-being. Regulatory requirements: The entity should ensure compliance with all regulatory requirements as far as employees are concerned. Dignity of People: The entities are to respect the dignity of employee as a human being & should not restrict their freedom of associations, unions, & other participatory mechanism for collective bargaining of their rights & redressal of issues they face at workplace Child Labor: The entities should prevent all kinds of child labour, bonded labour, and any



	other forms of involuntary labour. 4) Work Life Balance: The entities should have a system in which the work-life balance of the employees is not compromised. 5) Timely Wages Payment: The businesses have to ensure timely payment of the worker's wages and compensation. 6) Wages as per Living & Security: Payment of the wages has to be as per the living wages, that can take care of the basic needs and provide economic security to the employees. 7) Workplace safe & comfortable: Entities are responsible to create a workplace and work environment that is safe, hygienic, & comfortable for people to work for long durations. 8) Training: The skill development, career development and training of the workforce is another responsibility of the entities employing them. 9) No Harassment & Violence: The creation of a workplace which is free of harassment and violence is also a responsibility of the entity.
Principle 4: Respect for stakeholders' interests and responsiveness:	Interested party or stakeholders to a business has been a point of discussion in all the regulatory & voluntary systems that relate to the management system of any organisation, be it related to the quality, environment or the occupational health and safety of the workers. <i>[Trick: stakeholder ko identify karo > unse communicate karo > fir benefit aadan pradan karo]</i> a) Identify Interested parties (Stakeholder): The entities have to systematically determine the context of their operation and identify their interested parties. b) Transparent & communicate with Stakeholder: The entities have to be transparent & communicate with stakeholders about the impacts of their operations and business decisions on the people & nature. Policies, decisions, & impact of operations of organisation to stakeholders have to be disclosed transparently with no ambiguity. c) Share Benefit with Stakeholder: Entities should fairly share benefits to stakeholders or give an opportunity to them to benefit from the operations in an equitable manner.
Principle 5: Respect and promote human rights: <i>(Special Trick :-)</i>	Vast topic that covers wide variety of violence & belligerent abusive issues faced by people. <i>[Trick: Understand human right of all stakeholders > fir usse system me daalo]</i> a) Understand Human Rights: Entities should have clear understanding of human rights & various ways by which human rights can be violated from perspective of the Constitution of India, national laws and policies and the content of International Bill of Human Rights. b) Rights of All Stakeholders: Businesses should recognize and respect the human rights of all relevant stakeholders and groups within and beyond the workplace, including that of communities, consumers, and vulnerable and marginalized groups c) System to integrate with Human Policy: Entities when developing their mngt systems, should integrate the human rights element into their policies, procedures, and practices.
Principle 6: Protection and restoration of Environment:	Environmental responsibility as basic requirement for economic prosperity & sustainability. <i>Trick: "Policy" banao ki "pollution" jyada ni karna > means plastic jyada use mat lo .. lo to "recycle reuse" karo ... jisse "nature" & "climate" shi rahi ...</i> a) Policy to assess Impact on Environment: The entities should have policies, procedures, and practices in place to assess and rectify impacts to the environment. This should cover the whole life cycle of the product. b) Performance of Preventing Pollution: The entities have to measure their performance relating to the prevention of pollution, destruction of forests, waste generation, energy use, land use, etc. c) Reduce/Reuse/Recycle: The entities should explore the comparison of its activities with industry best practices to reduce, reuse and recycle/ recover materials, resources.



	d) Natural & Manmade resources optimum: The entities have to make use of natural and manmade resources in an optimum manner to ensure their sustainability by taking feedback from the stakeholders. e) Climate change: The entities have to contribute towards climate change resilience in line with India's commitment to various international mechanisms such as, Paris Agreement and National Action Plans for Climate Change. f) Avenue to improve Environmental: The companies have to look out for avenues by which they can improve their performance towards various environmental responsibilities.
Principle 7: Influence on Public and Regulatory Policy:	Influencing the policy formulation positively recognizes that the businesses operate within the framework of statutory and legislative policies of the governing authority. a) Policy Formulation: The core elements of BRSR are to have met holistically when the organisation go ahead with their contributions to policy formulation and policy advocacy. b) Collective associations such as, the trade groups and industry chambers have to be utilized when moving ahead with the policy advocacy and formulation. c) Encourage Fair competition & Human rights: Role in policy advocacy by the organisation should be in such way that it encourages fair competition & prevents human rights abuses.
Principle 8: Promote Inclusive Growth and equitable development:	This can work only with close participation & collaboration amongst entities, authorities, the civil associations contributing to one another for a better livelihood & assistance to the marginalized communities. <i>Trick: "people pe impact" hoa kya ? > "adverse impact" that ? > to bhai galat hogya .. ab "Marginalized society" ki helo karo ... "CSR" karo unpe ... unko pareshan mat karna ab "reallocate" krke</i> a) Impact on People (Social, Cultural & Economic): The entities should have systems in place to identify and address impacts of their activities on the social, cultural, and economic aspects of the people. This includes business created issues like, land acquisition and use and construction activities for new facilities b) Adverse impact on Society: The entities should review, measure, and track the adverse impacts of their activities on the society and environment and make action plans to mitigate them adequately c) Creative to help Marginalized: The entities should make efforts to bring up creative products, technologies, and business concerns that help the marginalized communities to have well-being and a better quality of life. d) CSR: Entities when designing their CSR activities should review the local and regional development priorities to help the marginalized groups and communities. e) Not Reallocate Communities: The entities should take care to ensure that business induced displacement or relocation of communities does not happen, and in unavoidable cases, should make sure to have mutually agreed, participative, and informed negotiations to provide fair compensation to the affected people. f) Intellectual Property: All forms of intellectual property & traditional knowledge should get the deserved respect from the organisation, and efforts should be made to ensure that benefits derived from their knowledge are shared equitably.
Principle 9: Provide value to the consumers in a responsible manner:	Q9. Company Misleading Advertisement, lack of grievances redressal system → BRSR. (MPT'25) The primary purpose of any business is to create or provide useful products and services to the customer in exchange of reasonable profits. <i>Trick: product banaate wqt > "koi adverse impact hoa" > to "disclose" karo bechne k liye "advertise" karte wqt mislead mat krna & "fair competition" hi krna > ab product bech diya to jo customer ka data h wo "Privacy" me rkhna .. or usse bataao ki "use" kse karte h product > use karne k baad koi complaint aai to "redressal mechanism"</i>

- a) **Reduce negative impact on consumer & Nature:** Entities should put in their efforts to reduce the negative impacts of their products and services on consumers, natural environment, and society at large.
- b) **Disclose all kind of adverse impact:** The entities should transparently and accurately disclose all kinds of adverse impacts to the user, planet, society, on the biodiversity from their products.
- c) **Advertise not mislead:** When advertising about their products, the organisations should ensure that misleading & confusing information is not exposed to the customers about their products or its usage.
- d) **Fair Competition & Freedom Choice:** When conceptualizing, designing, and marketing their products, the organisation should not in any manner prevent the freedom of choice and fair competition.
- e) **Privacy of data:** When handling customer data, the right to privacy of the customer needs to be maintained.
- f) **Inform customer usage/recycle/reuse:** Entities should inform the customers on the safe and responsible ways of usage, reuse, recycling, and disposal of their products, and ways to eliminate over-consumption.
- g) **Grievance redressal system:** Business enterprises should make available transparent and accessible grievance redressal and feedback management system for their customers to raise their voices or to seek clarifications.
- h) **Essential goods to everyone:** Entities, when in the business of providing essential goods and services (e.g., Utilities), should enable universal access, including to those whose services have been discontinued for any reason, in a non-discriminatory and responsible manner.

(Special Trick :-) → **Trick of 9: T SESH EP EC**

- P-1: Ethics, **T**ransparency & Accountability
P-2: **S**afe and **S**ustainable Goods and Service
P-3: Promote well-being of all **E**mployees including those in the value chain
P-4: Respect for **S**takeholders' interests and responsiveness
P-5: Respect and promote **H**uman rights
P-6: Protection and restoration of **E**nvironment
P-7: Influence on Public and Regulatory **P**olicy
P-8: Promote Inclusive Growth and **E**quitable development
P-9: Provide value to the **C**onsumers in a responsible manner

Q10. What are the nine principles of BRSR? How are the nine principles of BRSR linked with the 17 UN SDG's ? (SM)

Hint: Refer above notes for 9 principles & Below Linkage Table

➤ **Linkage / Alignment of BRSR Principles with SDG's:**

SDG's	P1	P2	P3	P4	P5	P6	P7	P8	P9
SDG 1			✓	✓				✓	
SDG 2		✓				✓	✓	✓	✓
SDG 3			✓					✓	
SDG 4			✓					✓	✓
SDG 5			✓	✓	✓			✓	
SDG 6		✓				✓		✓	



SDG 7		✓				✓	✓		
SDG 8		✓	✓		✓			✓	
SDG 9		✓					✓		
SDG 10		✓					✓		
SDG 11			✓	✓			✓	✓	
SDG 12		✓				✓			✓
SDG 13		✓				✓	✓	✓	
SDG 14		✓				✓	✓	✓	✓
SDG 15		✓				✓	✓	✓	✓
SDG 16	✓		✓	✓	✓			✓	
SDG 17	✓						✓	✓	

Q11. BRSR reporting → Company is engaged in Fintech business; he has submitted input on Draft of "Digital personal data protection bill" to concerned Ministry during year 2022-23. → During the same year, he has also submitted on application to one industry chambers, for inputs related to "how to we can work together to improve/leverage India's digital public infrastructure, for Bank solutions ". → discuss how above information would likely be disclosed by company in "Principle-wise performance disclosures" as part of BRSR for year 2022-23 ?

Whether information discussed above is mandatory to disclose ? (SM & MTP'24)

Hint: Such info to be disclosed in **Principle 7** of Principle wise disclosure → **influencing public & regulatory policy**.

Info. under each principle, disclosed under either Essential (Mandatory) or Leadership (Optional) indicator.

- **Mandatory Disclosure** → **Information relating to membership of Chamber/associations** is in the nature of Essential Indicators and requires mandatory disclosures
- **Optional Disclosure** → Below are in nature of leadership positions taken by the company, optional disclosures
 - ✓ Information relating to inputs provided **by company to the Ministry** on legislative bill
 - ✓ **inputs provided to one of the prominent chambers** on leveraging India's digital public infrastructure

➤ **ASSURANCE in BRSR**

Assurance in BRSR: [ESG Audit]	➤ The top 1,000 listed companies → need to comply with the provisions of BRSR.
	➤ BRSR is expected to be used as a single means for disclosing sustainability related information in India . This would be the main document which the stakeholders, investors would review and do industry analysis
	➤ ESG audit would be a process that would help the companies to evaluate Environmental & Social risks for Company's products , services, operations etc. Conducting an ESG audit also helps businesses look at their supply-chain risks , risk management capabilities and transparency with shareholders.
	ICAI: Standard on Sustainability Assurance Engagements (SSAE) 3000 Assurance Engagements on Sustainability Information
	Deals with: Assurance engagements on an entity's sustainability information
	Intended users of SSAE: • Assurance providers providing assurance on sustainability info. • Entities seeking to engage a professional auditor. • Regulators, investors, & other users of Sustainability Reporting data
	assurance: providing reasonable or limited assurance on sustainability information.
	Effective date: • Voluntary basis for reports covering periods ending on 31st March 2023. • Mandatory basis for reports covering periods ending on or after 31 Mar24.
	SSAE 3410, Assurance Engagements on Greenhouse Gas Statements
	Deal with assurance engagements on entity's sustainability info. including assurance of BRSR.



Methodology to provide assurance on BRSR: [POI - RSP]	Q12. What is the methodology of providing assurance in BRSR? (SM & RTP) • Preliminary Review of ESG report, parameters • On-site Assessment / Verification of ESG Report • Issuance of Assessment Report and Assessment Statement • Review of the responses and clarifications on the findings • Submission of findings of the onsite assessment and document review • Preparation Assessment of / Verification report including final results of Assessment/ Recommendation										
Social Audit Standards (SAS):	The Sustainability Reporting Standards Board (SRSB) of the ICAI has recently issued Social Audit Standards (SAS 100 to 1600). It Aim to provide Social Auditor with the necessary guidance i.r.t independent impact assessment engagement of Social Enterprises engaged in various areas & audit steps and procedures that should be applied while conducting the social impact assessment. The Standard sets out the minimum requirements to be followed while conducting impact assessment. L&R may establish additional requirements which should be followed, as applicable. <table border="1" data-bbox="297 682 1510 917"> <thead> <tr> <th>SAS</th><th>Particulars</th></tr> </thead> <tbody> <tr> <td>100</td><td>Eradicating hunger, poverty, malnutrition and inequality</td></tr> <tr> <td>200</td><td>Promoting health care including mental healthcare, sanitation and making available safe drinking water</td></tr> <tr> <td>300</td><td>Promoting Education, Employability, and Livelihoods</td></tr> <tr> <td colspan="2">Etc. etc. (Refer Additional PDF Booklet) for Full List of "SAS"</td></tr> </tbody> </table>	SAS	Particulars	100	Eradicating hunger, poverty, malnutrition and inequality	200	Promoting health care including mental healthcare, sanitation and making available safe drinking water	300	Promoting Education, Employability, and Livelihoods	Etc. etc. (Refer Additional PDF Booklet) for Full List of "SAS"	
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➤ ROLE OF AUDITOR -Consideration of Climate related risk in an "Audit of F.S".

Q13. What is the auditor's role on ESG aspects in an audit of financial statements of Company? (SM & Nov'24)

FS is Free from MMS:	Role of auditor is to obtain reasonable assurance about whether the FS as a whole are free from MMS, whether due to fraud or error, to report whether the FS are prepared and presented fairly, in all material respects, in accordance with the applicable FRF.
Understand Climate Risk:	In developing understanding of an entity, auditor should consider climate related risks & how these risks may be relevant to the audits. Climate-related risks could be more relevant in certain sectors or industries, e.g., banks and insurance, energy, transportation, materials and buildings, agriculture, food, & forestry products.
Audit Report:	Investors and stakeholders are seeking information from auditor's reports about how climate related risks were addressed in the audit increasing pressure for transparency about climate matters in our auditor's reports.
EOM:	Sometimes, it may warrant inclusion of an EOM paragraph to draw attention to disclosures that are of fundamental importance to users' understanding of the FS. The auditor should also determine whether the entity has appropriately disclosed relevant climate-related information in the FS in accordance with the applicable FRF e.g., Ind-AS or AS ,when relevant before considering climate-related matters in the auditor's report.
Read Other Info:	The auditor should also read the other information for consistency with information disclosed in the F.S and information that may be publicly communicated to stakeholders outside the FS, such as management report narratives in the annual report, press releases, or investor updates. This is a requirement under ISA 720 and SA 720, The Auditor's Responsibilities Relating to Other Info.

Q14.

C.S. Qn: The agrochemical sector is about a \$35 billion industry in India. The Indian agrochemicals market is

segmented by product type (fertilizers, pesticides, adjuvants, and plant growth regulators). The continuous and increased use of agrochemicals seems to have an adverse effect on humans, animals, and nature in whole.

The toxicity levels of the agrochemicals are harmful, not only to the workers in the manufacturing process but also to farmers, the soil, and the end consumers. The Central Insecticide Board (CIB) of India has categorized agrochemical toxicity levels based on a labeling system—using red, yellow, blue, and green labels—where red is the most toxic and green is the least. Most of the red-labeled products are banned abroad but are being sold in India due to the lack of a strong regulatory environment.

In India, it is estimated that almost 25% of the total amount of agrochemicals sold are counterfeit products (Duplicate). The quality and the efficacy of these counterfeit products differ from the original products, which can lead to reputational damages for the companies. Agrochemical companies need to add barcodes or other identifying technologies to their product packaging, to allow enduse consumers to check for authenticity. Also, since India is a multilingual country, the companies will have to publish the usage instructions in multiple languages.

Company A and B are both listed companies and part of top 1000 listed companies. They are engaged in the production of agrochemicals.

Company A has been looking for opportunities to comply with the recently launched and evolving guidelines for ESG in India

while Company B on the other hand is just focused to increase revenue and profits.

In December 2022, Company A made a decision to eliminate red-labeled products from its portfolio and to increase its research and development (R&D) spending to safeguard itself from the market shift due to the new regulatory norms; in 2022, it also discontinued yellow-labeled products. Company A is also planning to incur a small expenditure to improve their backend systems and provide for all its products a unique labeling system that is user friendly and interactive.

At the other end of the spectrum, 14% of Company B's top-selling products are derived from red- and yellow labeled

Company A will be cushioned for regulatory changes and thus, would not face potential future downsides. Company B has recently witnessed a 9% year on year growth in revenue from the last financial year and is planning to increase the production of its bestselling product, an insecticide DDT, categorized as red labelled by the Central Insecticide Board. Company B has recently been approached by the regulatory authority for an investigation for its products which include performing additional tests and studies to testify that its products have no adverse effects.

1. What would be the reporting requirements for each of the two companies?
2. Which Company has absorbed the impacts of possible future regulatory changes? What are the steps taken by that Company for complying with the regulatory standards?
3. What would be consideration by the auditors of Company A and B in the audit of FS? (SM)

Answer:

1. Both Companies A and B are among part of top 1000 listed companies. Hence, these companies have to mandatorily provide **BRSR reporting** (Business responsibility and Sustainability reporting) in accordance with **9 principles** of **NGBRC** as mandated by SEBI.
2. **Company A** has absorbed impact of **regulatory changes**. It has decided to **eliminate redlabelled and yellow-labelled products** from its portfolio which are toxic in nature. Besides, it has **increased its expenditure on R & D to meet with new regulatory norms**. It has also incurred expenditure for improving its **labelling system** which would help end users to know about the nature of the product. **All these steps have been taken by**

Company A for complying with regulatory standards.

- **Principal 2:** Company A is trying to meet with requirements of Principle 2 by making R & D expenditure. Further, it has also eliminated red-labelled/yellow-labelled products from its portfolio. "Principle 2 relates to the requirement that businesses should provide goods and services in a manner that is sustainable and safe".
 - **Principal 9:** Besides, by adopting a friendly bar-coded packaging labelling system, company is adhering to requirements of Principle 9 which states that businesses should engage with and provide value to their consumers in a responsible manner. Steps taken by a company to inform its consumers about safe and responsible usage of products fall in its domain.
 - **Principal 3:** Since toxic agrochemicals are also harmful to workers engaged in their manufacturing process, their discontinuation bodes well for workers in the company A in line with Principle 3 which states that businesses should respect and promote the well-being of all employees including those in their value chains. By discontinuing products which are harmful to soil, company A is meeting requirements of Principle 6 which states that businesses should respect and make efforts to protect and restore the environment.
3. **Company A is complying with regulatory norms** whereas 14% of company B's revenue are derived from red and yellow labelled products. In fact, **company B is planning to increase production of its red labelled product** i.e., insecticide DDT which has been categorized as such by Central Insecticide Board.
- The auditor of Company B would have to keep in **mind requirements of SA 250** in this regard. Non-compliance with laws and regulations may **result in fines, litigation or other consequences** for the entity that may have a **material effect on the FS**. It can result in material misstatements. Central Insecticide Board has already **launched its investigation** into products of company. All these factors would be taken into consideration by auditor of Company B.
- Auditors of Company A and Company B need to **obtain audit evidence regarding compliance with laws and regulations and audit procedures** have to be designed accordingly. Auditor of Company A can obtain assurance from regulatory compliance by the company. Fall of revenue by 8% in one year is not a matter of concern to them as it is a transitory phase.
- However, auditors of Company B would also have to take into consideration **requirements of SA 570 as non-compliance** with regulatory requirements could result into claims from such proceedings which the company may not be able to satisfy.

CHAPTER 19: Professional Ethics (CA Act, 1949)

➤ Introduction:

Ethics:	Moral principles which govern a person's behavior or the conducting of an activity. It is the branch of knowledge that deals with moral principles
Professional Ethics:	Consist of personal, organizational and corporate standards of behavior expected for professionals
ICAI Motto:	"Ya Esha Supteshu Jagrati" is adopted from Kathopanishad and it denotes 'eternal vigilance' - awakening when the world is asleep. A distinguishing feature of the accountancy profession is its acceptance of the responsibility to act in the public interest

➤ Overview of Code of Ethics: (MCQ Purpose Only)

Revised Code of Ethics contains the following material:	
Part 1: For All professional Accountants	Complying with the Code, Fundamental Principles and Conceptual Framework, which includes the fundamental principles and the conceptual framework
Part 2: For Professional Accountants in Service & Also applicable to CA in practice when providing service to firm as an Employee	Professional accountants in service include professional accountants employed, engaged or contracted in an executive or non-executive capacity in, <u>for example</u> : • Commerce, industry or service • The public sector • The public sector • The not-for-profit sector. • Regulatory or professional bodies
Part 3: Public Practice	Professional Accountants in Public Practice, which sets out additional material that applies to professional accountants in public practice when providing professional services
Part 4: Public Practice of Assurance services	Independence Standards , which sets out additional material that applies to professional accountants in public practice when providing assurance services, as follows: • Part 4A - Independence for Audit and Review Engagements, which applies when performing audit or review engagements. • Part 4B - Independence for Assurance Engagements Other than Audit and Review Engagements, which applies when performing assurance engagements that are not audit or review engagements

Note: A professional accountant **shall comply with the Code**. There might be circumstances where laws or regulations preclude an accountant from complying with certain parts of the Code. **In such circumstances**, those **laws and regulations prevail**, and the accountant shall comply with all other parts of the Code.

➤ Fundamental Principles to be followed by an accountant:

(1) Integrity (2) Professional Behavior (3) Confidentiality (4) Professional Competence & Due Care (5) Objectivity	
1) Integrity:	a) A professional accountant shall comply with the principle of integrity, which requires an accountant to be straightforward & honest in all professional and business relationships b) Shall not knowingly be associated with reports , returns, communications or other information where the accountant believes that the information Contains a materially false or misleading statement/ provided negligently/ Omits info



	(However, a professional accountant will not be considered to be in breach if he provides a modified report in respect of such above mentioned matter) c) When a professional accountant becomes aware of having been associated with information described in paragraph 2, the accountant shall take steps to be disassociated from that information.
2) Objectivity:	It requires an accountant not to compromise professional or business judgment because of Bias, conflict of Interest or undue Influence of others (BII) .
3) Professional Competence & Due Care: (Nov'24)	Q1. Code of ethics → Professional Competence and Due Care ? (Nov'24) a) Requires an accountant to Attain and maintain professional knowledge and skill which required to ensure that client or employing organization receives competent professional service, based on current technical and professional standards and relevant legislation; & b) Serving clients and employing organizations with professional competence requires the exercise of sound judgment in applying professional knowledge and skill when undertaking professional activities. c) Maintaining professional competence requires a continuing awareness and an understanding of relevant technical, professional and business developments. d) Take reasonable steps to ensure that those working in a professional capacity under the accountant's authority have appropriate training and supervision. e) Where appropriate, a professional accountant shall make clients, the employing organization, or other users of the accountant's professional services or activities, aware of the limitations inherent in the services or activities.
4) Confidentiality : (Special Trick :-)	Requires an accountant to respect the confidentiality of information acquired as a result of professional and employment relationships. An accountant shall: a) be alert to the possibility of inadvertent disclosure, including in a social environment, and particularly to a close business associate or an immediate or a close family member; b) maintain confidentiality of information within the firm or employing organization; c) maintain confidentiality of information disclosed by a prospective client or employing organization; d) not disclose confidential information acquired as a result of professional and employment relationships outside the firm or employing organization without proper and specific authority, unless there is a legal or professional duty or right to disclose; e) not use confidential information acquired as a result of professional and employment relationships for personal advantage of accountant or for advantage of a 3rd party; Q2. circumstances where professional accountants required to disclose confidential information, what are the points & consideration that should be kept in the mind ? <u>Circumstances where disclosure is appropriate:</u> a) Disclosure is required by law, for example: (i) Production of documents or other provision of evidence in the course of legal proceedings; or (ii) Disclosure to the appropriate public authorities of infringements of the law that come to light; b) Disclosure is permitted by law and is authorized by the client or the employing organization; and c) There is a professional duty or right to disclose, when not prohibited by law: (i) To comply with the requirements of peer review or quality review of the Institute (ii) To respond to an inquiry or investigation by a professional or regulatory body; (iii) To protect the professional interests of a professional accountant in legal proceedings; or



	(iv) To <u>comply with technical and professional standards</u>, including ethics requirements. Considerations before disclosing information: In deciding whether to disclose confidential information, factors to consider, depending on the circumstances, include: (i) Whether the interests of any parties, including third parties whose interests might be affected, <u>could be harmed</u> if the client or employing organization consents to the disclosure of information by the professional accountant. (ii) Whether all the relevant information is known and substantiated, to the extent practicable. (iii) The proposed type of communication, and to whom it is addressed. (iv) Whether the parties to whom the communication is addressed are appropriate recipients. Note: A professional accountant shall <u>continue to comply</u> with the principle of confidentiality <u>even after the end of the relationship</u> between the accountant and a client or employing organization	
5) Professional Behaviour: (L&R se update rhna is Professional competent, but unhe Comply bhi karna is Professional Behavior)	a) It requires an accountant to <u>comply with relevant laws and regulations</u> and avoid any conduct that the accountant <u>knows or should know might discredit the profession</u>. b) A professional accountant shall <u>not knowingly engage in any employment, occupation or activity that impairs or might impair the integrity, objectivity or good reputation</u> of the profession, and as a result would be incompatible with the fundamental principles. c) <u>When promoting himself</u> and his work, a professional accountant shall not bring the profession into disrepute. A professional accountant <u>shall be honest and truthful</u> and shall not make: - Exaggerated claims for the services they are able to offer, the <u>qualifications, Experience</u> - Disparaging references or unsubstantiated <u>comparisons to the work of others</u> d) The professional accountant should ensure that the contents of an <u>advertisement are true to the best of his knowledge and belief</u>, and are in <u>conformity with the Advertisement Guidelines</u>	
A professional accountant shall comply with EACH of the fundamental principles A professional accountant might face a situation in which <u>complying with one fundamental principle Conflicts with complying with one or more other fundamental principles</u>. In such a situation, the accountant might <u>consider consulting, with:</u> <u>(Example, I want to be Honest as per Integrity Vs. Confidentiality)</u> - Others within the firm or employing organization - Those charged with governance (TCWG) - The Institute - Legal counsel However, such consultation does <u>not relieve</u> the accountant from the <u>responsibility to exercise professional judgment to resolve the conflict</u> or, if necessary, and unless prohibited by law or regulation, disassociate from the matter creating the conflict		
Q3. What are the fundamental principles as per code of ethics ICAI & the threats involved while complying? <u>Hint: Explain above 5 fundamental principles (explain 1st point of each fundamental principle) & Explain all 5 threat to independence, given below (Explain meaning only, not examples)</u>		



Q4. Auditor is conducting audit of 2023, However Fees of 2022 is still not received, SO auditor is tempted to issue a Favourable report, so that company can take a Loan to repay auditor's fees. Explain the types of threats that may hinder Auditor's Independence while issuing Audit Report.

Hint: Explain all Below threats along with example

➤ Threats to Independence

Identify the threat (in compliance of Fundamental principles) → Evaluate them → eliminate/reduce to acceptable level

1) Self Interest Threats:	➤ Meaning: the threat that a financial or other interest will inappropriately influence a professional accountant's judgment or behaviour; ➤ Circumstances that may create self-interest threats: • Having a direct financial interest in a client • professional accountant quoting a low fee to obtain a new engagement (Fees is so low it might be difficult to perform engmnt as per professional standards) • professional accountant having access to confidential information that might be used for personal gain. • Having a close business relationship with a client • A professional accountant discovering a significant error when evaluating the results of a previous professional service performed by a member of the accountant's firm						
2) Self-review threat: <u>(Important)</u> <u>(Special Trick :-)</u>	➤ Meaning: the threat that a professional accountant will not appropriately evaluate the results of a previous judgment made; or an activity performed by the accountant, or by another individual within the accountant's firm or employing organization, on which the accountant will rely when forming a judgment as part of performing a current activity <u>[Note: In New ICAI SM, Only 2nd & 3rd points are given]</u> ➤ Example of Circumstances that may create Self-Review threats: <table border="1"> <tr> <td data-bbox="365 1123 495 1186">Original Data:</td><td data-bbox="495 1123 1524 1344"> 1) The discovery of a significant error during a re-evaluation of the work of the professional accountant in public practice 2) Reporting/Issuing Assurance report on the operation of financial systems after being involved in their design or implementation 3) Having prepared the original data used to generate records that are the subject matter of the engagement </td></tr> <tr> <td data-bbox="365 1344 495 1407">Job:</td><td data-bbox="495 1344 1524 1533"> 4) A member of the assurance team being, or having recently been, a director or officer of that client 5) A member of the assurance team being, or having recently been, employed by the client in a position to exert direct and significant influence over the subject matter of the engagement </td></tr> <tr> <td data-bbox="365 1533 495 1606">Service:</td><td data-bbox="495 1533 1524 1606"> 6) Performing a service for a client that directly affects the subject matter of the assurance engagement </td></tr> </table>	Original Data:	1) The discovery of a significant error during a re-evaluation of the work of the professional accountant in public practice 2) Reporting/Issuing Assurance report on the operation of financial systems after being involved in their design or implementation 3) Having prepared the original data used to generate records that are the subject matter of the engagement	Job:	4) A member of the assurance team being, or having recently been, a director or officer of that client 5) A member of the assurance team being, or having recently been, employed by the client in a position to exert direct and significant influence over the subject matter of the engagement	Service:	6) Performing a service for a client that directly affects the subject matter of the assurance engagement
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Service:	6) Performing a service for a client that directly affects the subject matter of the assurance engagement						
3) Familiarity threat:	➤ Meaning: the threat that due to a long or close relationship with a client, or employing organization, a professional accountant will be too sympathetic to their interests or too accepting of their work ➤ Examples of circumstances that may create familiarity threats: 1) A member of the engagement team having a close or immediate family relationship with a director or officer of the client 2) A director or officer of the client, or an employee in a position to exert significant influence over the subject matter of the engagement, having recently						



	served as the engagement partner. 3) Long association of an audit team member with the audit client
4) Advocacy Threat:	➤ Meaning: the threat that a professional accountant will promote a client's or employing organization's position to the point that the accountant's objectivity is compromised ➤ Examples of circumstances that may create advocacy threats: • Promoting shares in an entity when that entity is a financial statement audit client • Acting as an advocate on behalf of an assurance client in litigation or disputes with third parties • Lobbying in favor of legislation on behalf of a client.
5) Intimidation threat:	➤ Meaning: the threat that a professional accountant will be deterred from acting objectively because of actual or perceived pressures, including attempts to exercise undue influence over the accountant. ➤ Examples of circumstances that may create Intimidation threats: • Being threatened with dismissal or replacement in relation to a client engagement because of a disagreement about a professional matter • Being feeling pressured to agree with the judgment of a client because the client has more expertise on the matter in question • accountant being informed that a planned promotion will not occur unless the accountant agrees with an inappropriate accounting treatment • A professional accountant having accepted a significant gift from a client and being threatened that acceptance of this gift will be made public."

Q5. Distinguish: Self- interest threat from self - review threat in an assurance engagement

Hint: Explain both the threats with example

Q6. What is self-review threat? List the circumstances that may create self-review threats.

➤ **Evaluation of Threat**

Evaluation of Threat:	In case any threat is identified, evaluate whether threat to compliance with the fundamental principles is at an acceptable level.
Reasonable & Informed 3rd party:	It's a Kind of Test → Which professional accountant perform → about whether the same conclusions would likely be reached by another party. The reasonable and informed third party does not need to be an accountant but would possess the relevant knowledge and experience to understand and evaluate the appropriateness of the accountant's conclusions in an impartial manner

➤ **Addressing Threat & Safeguarding's to above threats:**

Addressing Threats:	If the professional accountant determines that the identified threats to compliance with the fundamental principles are not at an acceptable level, the accountant shall address the threats by eliminating them or reducing them to an acceptable level. <u>The accountant shall do so by:</u> - Eliminating the circumstances, including interests or relationships, that are creating the threats; - Applying safeguards, where available and capable of being applied, to reduce the threats to an acceptable level; or - Declining or ending the specific professional activity
Safeguards:	Safeguards are actions individually or in combination that the accountant takes that



effectively reduce threats to an acceptable level. Safeguards vary depending on the facts and circumstances. **Examples of actions that in certain circumstances might be safeguards to address threats include:**

Self-interest threat:	Assigning additional time and qualified personnel to required tasks when an engagement has been accepted might address a self-interest threat.
Self-interest threat:	Separating teams when dealing with matters of a confidential nature might address a self-interest threat
Self-review threat:	Having an appropriate reviewer, who was not a member of the team, review the work performed or advise as necessary might address a self-review threat.
Self-review, advocacy or familiarity threats:	Using different partners and engagement teams with separate reporting lines for the provision of non-assurance services to an assurance client might address self-review, advocacy or familiarity threats.
Self-interest, self-review, advocacy, familiarity, intimidation threats:	Involving another firm to perform or re-perform part of the engagement might address self-interest, self-review, advocacy, familiarity or intimidation threats.

Q7. A professional accountant is worried about engagement specific threat in complying fundamental principal. Enumerate some engagement specific safeguards to ward off such threats.

Hint: Refer above Safeguards

➤ **Non-Compliance with Laws and Regulations (NOCLAR) –Applicable Hai Boss !!**

Applicability:	International (IESBA) Code of Ethics	- In case of members in practice → Applicable to ALL assignments - In case of members in service → Applicable to ALL employers	
	As per ICAI Code of Ethics:	In case of Professional Accountant in practice:	Applicable to Audit of Listed Entities assignments, Below all conditions must fulfill: ✓ Shares of which are listed on recognized stock exchanges(s) in India and ✓ Net worth >= INR 250 crores
		In case of members in service:	Applicable to "Senior Professional Accountants" in service, being employees of listed entities
	➤ Senior professional accountants Means KMP [Directors, officers or senior employees able to exert significant influence over, and make decisions regarding, the acquisition, deployment and control of the employing organization's human, financial, technological, physical and intangible resources] ➤ "Audit engagement" means reasonable assurance engagement in which a professional accountant in public practice expresses an opinion on whether financial statements give a true fair view by an applicable financial reporting framework		
Meaning:	Where a professional accountant in public practice <u>or</u> senior professional accountant identifies any non-compliance with laws and regulations to comply with the principles of integrity and professional behavior it may have to report such non-compliance by alerting management / TCWG and take further actions as appropriate like reporting to regulatory bodies or withdrawing from engagement.		



In the course of providing a professional service to a client or carrying out professional activities for an employer, a Senior Professional accountant may come across an **instance of non-compliance with laws and regulations (NOCLAR)** or suspected NOCLAR committed or about to be committed by:

- The **client** /professional accountant's employing organisation (**Employer**)
- **TCWG** of client or Employing organisation
- **management** of a client/ employing organisation
- **other individuals** working for or under the direction of a client/ employing organisation

NOCLAR under Revised Code of Ethics does **NOT** address the **personal misconduct unrelated to the business** activities of the client/ employing organisation and non-compliance by parties other than listed out in the definition of NOCLAR

Examples:

As per IESBA, following examples would be covered in NOCLAR:

Fraud,
corruption &
bribery

Money laundering,
terrorist financing &
proceeds of crime

Securities
markets & trading

Banking and other
financial products
and services

Data protection

Environmental
protection

Public health and
safety

Tax and pension
liabilities &
payments

Points to Note:

During Course of Providing a Service:

NOCLAR will be **applicable** if a professional accountant encounters, or is made aware of, non-compliance/Suspected also, he is not required to investigate, nor responsible for ensuring complete compliance.

Expertise of Laws NOT Required:

A professional accountant is **expected to apply knowledge** and expertise, and exercise professional judgment. However, he is **not expected to have** a level of **knowledge of laws** and regulations **greater than which is required to undertake the engagement**

Out of Scope:

Matters that are clearly inconsequential, or relating to **personal misconduct** pertaining to business activities of the client not covered

Disclosure contrary to Law:

Disclosure, which is Contrary to Law **not Required**: As per IESBA Code, disclosure of the matter to an appropriate authority would be precluded if doing so would be contrary to law or regulation

NOCLAR vs. SA-250:

MAY'24 Qns

Q8. Explain difference between SA-250 L&R responsibility Vs. NOCLAR ?

	SA-250	NOCLAR
1	Applicable only on Audit , and not on other Assurance engagements	Applicable on professional accountants in service , and in practice , it applies to Auditors, as well as professional services other than Audit
2	Talks of auditor's responsibilities for laws having direct effect on the determination of material amounts and disclosures in the financial statements (such as tax and labour laws); and 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	NOCLAR, while being alike to SA 250 till this point, is further ahead of it in that it takes into account non-compliance that causes substantial harm resulting in serious consequences in financial or non-financial terms



		may be fundamental to the operating aspects of the business	
	3	Not defined stakeholders	NOCLAR is <u>related to</u> <u>affect of non-compliance</u> on <u>investors, creditors, employees</u> as <u>also the general public</u>
	4	Imminent breach → Not existent in SA 250	in exceptional circumstances → "imminent breach" of a L&R that would cause <u>substantial harm to investors, creditors, employees or the general public</u> → Consider: • <u>whether to discuss with mngt/tcwg &</u> • Apply <u>Professional judgement</u> → <u>whether to disclose the matter immediately to an appropriate authority</u> (Could be SEBI for fraudulent FR) in order to prevent or mitigate the consequences of such <u>imminent breach</u>
Respond to NOCLAR:	In case of Employment →	• Responsibility of <u>Senior Professional Accountant</u> in Service	
	In case of Audit Engagement →	• Responsibilities of <u>Professional Accountant</u>	
Documentation	follow the additional documents requirements as under: 1) How mngt / TCWG have responded to the matter. 2) The course of action the accountant considered , the judgments made <u>and the decisions that were taken, having regard to the reasonable and informed third party test.</u> 3) <u>How the accountant is satisfied that the responsibility of public interest has been fulfilled.</u> This documentation is in addition to complying with the documentation requirements under applicable auditing standards. SAs , for example, require a professional accountant performing an audit of financial statements to: 1) Prepare documentation sufficient to enable an understanding of significant matters arising during the audit , the conclusions reached, and significant professional judgments made in reaching those conclusions 2) Document discussions of significant matters with management , those charged with governance, and others, including the <u>nature of the significant matters</u> discussed and when and with whom the discussions took place; and 3) Document identified or suspected non-compliance , and the results of discussion with management and, where applicable, TCWG and other parties outside the entity.		
Confidentiality Provision:	1) C-1, P-1, S-II : A CA in practice shall be deemed to be guilty of professional misconduct, if he discloses information acquired in the course of his professional engagement to any person other than his client so engaging him, without the consent of his client or otherwise than as required by any law for the time being in force; 2) C-2, P-2, S-II : A member of the Institute, whether in practice or not , shall be deemed to be guilty of professional misconduct, if he being an employee of company, firm or person, discloses confidential information acquired in the course of his employment except as and when required by any law or except as permitted by the employer;		

Q9. SAM Yarns Ltd - a listed Company → The Company managed to get pollution clearance certificate by unfair means, while still there continues to be breach of pollution laws. the Director-Finance who is a CA came to

19.8 | Page

Professional Ethics

know of these matters. Comment the action expected of Director as per NOCLAR.

Hint: → In the given situation, SAM Yarns Limited, a **listed company**, (Explain the exact scenario of Qn)

- NOCLAR is **applicable** on professional accountants in **service**, and in practice.
- Applicable to **Senior Professional Accountants** in service, being employees of listed entities. (includes directors)
- NOCLAR takes into account non-compliance → resulting serious consequences in financial or non-financial term
- Refer above Notes: "Imminent Breach" i.e., 4th Point of "NOCLAR vs SA 250 Difference"

CA Rahul, Director-Finance is expected of taking the following action/responses:

- **Obtaining an Understanding** of the Matter
- **Addressing** the **Matter**.
- Determining **Whether Further Action Is Needed**.
- **Seeking Advice**.
- Determining Whether to **Disclose the Matter** to an **Appropriate Authority**.
- **Imminent Breach**.
- **Documentation**.

➤ **Membership of the Institute:**

Membership:	On acceptance of application by the Council, the applicant's name shall be entered in the Register and a certificate of membership in the appropriate Form shall be issued to the applicant. <u>Gyaan:</u> Even If person cleared CA Final examination, He <u>can't use prefix "CA" or designation "Chartered Accountant"</u> until and <u>unless he receive membership number from ICAI</u>
Disabilities: (Section 8)	<u>Section 8 of the Chartered Accountants Act, 1949 enumerates the circumstances under which a person is debarred from having his name entered in the Register of Members, as follows:</u> i) If he has not attained the age of 21 years at the time of his application for the entry of his name in the Register; or ii) If he is of unsound mind and stands so adjudged by a competent court; or iii) If he is an undischarged insolvent ; or iv) If he, being a discharged insolvent , has not obtained from the court a certificate stating that his insolvency was caused by misfortune without any misconduct on his part; or v) If he has been convicted by a competent Court whether within or without India, of an offence involving moral turpitude and punishable with transportation or imprisonment or of an offence, not of a technical nature, committed by him in his professional capacity unless in respect of the offence committed he has either been granted a pardon or, on an application made by him in this behalf, the Central Government has, by an order in writing, removed the disability; or vi) If he has been removed from membership of the Institute on being found on inquiry to have been guilty of professional or other misconduct;
Types of Members:	1) Associate Member (ACA) → Any person, whose name has been entered in the Register, shall be deemed to have become an Associate of the Institute and shall also be entitled to use the letters A.C.A. after his name to indicate 2) Fellow Member (FCA) → An associate member who has been in continuous practice in India for at least 5 years shall be entered into the Register as a Fellow of the Institute, on payment of such fees along with the application made and granted in the prescribed manner.
Removal of Name:	As per section 20 of the Act, the Council may remove, from the Register, the name of any member of the Institute in the following cases- (i) Who is dead ; or (ii) From whom a request has been received to that effect; or (iii) Who has not paid fee required to be paid by him; or (iv) Who is found to have been subject at the time when his name was entered in the Register,



	or who at any time thereafter has become subject, to any of the disabilities mentioned in Section 8						
Restoration of Membership:	If the name of any member has been removed from the Register for non-payment of prescribed fee as required to be paid by him, then, on receipt of an application, his name may be entered again in the Register on payment of the arrears of annual fee and entrance fee along with such additional fee, as may be determined by the Council, However, the effective date in case of restoration of cancelled membership, in different situations, shall be in the following manner: <table border="1"> <tr> <td>Application for restoration and requisite fees are made within the same year of removal →</td><td>Restoration shall be with effect from the date on which it was removed from the Register</td></tr> <tr> <td>Removal of name under the orders of the Board of Discipline or the Disciplinary Committee or the Appellate Authority or the High Court →</td><td>Restoration shall be in accordance with such orders</td></tr> <tr> <td>In other cases →</td><td>Restoration shall be with effect from the date on which the application and fee are received</td></tr> </table>	Application for restoration and requisite fees are made within the same year of removal →	Restoration shall be with effect from the date on which it was removed from the Register	Removal of name under the orders of the Board of Discipline or the Disciplinary Committee or the Appellate Authority or the High Court →	Restoration shall be in accordance with such orders	In other cases →	Restoration shall be with effect from the date on which the application and fee are received
Application for restoration and requisite fees are made within the same year of removal →	Restoration shall be with effect from the date on which it was removed from the Register						
Removal of name under the orders of the Board of Discipline or the Disciplinary Committee or the Appellate Authority or the High Court →	Restoration shall be in accordance with such orders						
In other cases →	Restoration shall be with effect from the date on which the application and fee are received						
Penalty for Falsely Claiming to be member:	Section 24 of the Chartered Accountants Act, 1949 provides that any person who: Not being a member of the Institute; (a) represents that he is a member of the Institute; or (b) uses the designation Chartered Accountant - Being a member of the Institute, but not having a certificate of practice, represents that he is in practice or practices as a Chartered Accountant, Shall be punishable on: ➤ 1st conviction with fine Upto Rs.1000, and ➤ On any subsequent conviction with imprisonment which upto 6 months <u>or</u> with fine upto 5,000, <u>or</u> with both.						

Q10. Mr. Sheetal is a practicing CA. Due to **natural calamities** and misfortune in 2021 he became **undischarged insolvent**. After a few **court hearings**, finally, in the year 2023, he was declared **discharged insolvent and obtained a certificate from the court stating that his insolvency was caused by misfortune without any misconduct**.
comment w.r.t CA Act, 1949 and Schedules thereto, (especially Sec 8: Entry of name in Register of Members).

Hint:

Disabilities for the Purpose of Membership: **Sec 8** of CA Act, 1949 → If he, being a discharged insolvent, has not obtained from court a certificate stating that his insolvency was caused by misfortune without misconduct on his part.

In given case, it is **clearly stated** that **Mr. Sheetal was discharged insolvent**, and has also obtained from the court a certificate stating that his insolvency was caused by misfortune without any misconduct on his part, **Mr. Sheetal has not violated the provisions of Sec 8**, and he is **not debarred** from having his name entered in Register of Members.

➤ **Chartered Accountants In Practice:**

Practicing Chartered accountant:	A practicing CA is a person who is a member of the Institute and is holding Certificate of Practice ; and includes such members of the Institute who are deemed to be in Practice in accordance with the provisions of the CA Act, 1949.
Deemed Practice: 2(2)(iv)	"A member of the Institute shall be deemed "to be in practice" when individually or in partnership with Chartered Accountants in practice, or in partnership with members of such other recognised professions as may be prescribed, he, in consideration of remuneration received or to be received: (i) Engages himself in the practice of accountancy (ii) Offers to perform or performs service involving the auditing or verification of financial



	transactions, books, accounts or records, or the preparation, verification or certification of financial accounting and related statements or holds himself out to the public as an accountant (iii) Renders professional services or assistance in or about matters of principle or detail relating to accounting procedure or the recording, presentation or certification of financial facts or data; or (iv) Renders such other services as, in the opinion of the Council, are or may be rendered by a Chartered Accountant in practice • member shall be deemed to be in practice if he, in his professional capacity and neither in his personal capacity nor in his capacity as an employee, acts as a liquidator, trustee, executor, administrator, arbitrator, receiver, adviser or representative for costing, financial or taxation matters • Deemed to be in practice not only when he is actually engaged in the practice of accountancy but also when he offers to render accounting services whether or not he in fact does so Note: An associate or a fellow of the Institute who is a <u>salaried employee</u> of a Chartered Accountant in practice or a firm <u>shall be deemed to be in practice for</u> the <u>limited purpose of the training of Articled Assistants</u>
Significance of the COP- Sec 6:	No member of the Institute shall be entitled to practise whether in India or elsewhere unless he has obtained from the Council a certificate of practice Council of the institute is of view that: (i) Once the person concerned becomes a member of the Institute, he is bound by the provisions of the Chartered Accountants Act and its Regulations. (ii) If and when he appears before the Income-tax Tribunal as an Income-tax representative after having become a member of the Institute, he could so appear only in his capacity as a Chartered Accountant and a member of the Institute. (iii) A member of the Institute can have no other capacity in which he can take up such practice, separable from his capacity to practice as a member of the Institute." (iv) Chartered Accountant whose name has been removed from the membership for professional and/or other misconduct, during such period of removal, will not appear before the various tax authorities or other bodies before whom he could have appeared in his capacity as a member of this Institute. (v) Therefore, if a CA has surrendered his certificate of practice due to misconduct, he cannot in any other capacity take up any practice separable from his capacity to practice as a member of the institute
Cancellation of COP:	<u>Certificate of Practice (COP) shall be liable for cancellation, if:</u> (i) The name of the holder of the certificate is removed from the Register; or (ii) The Council is satisfied, after giving an opportunity of being heard to the person concerned, that such certificate was issued on the basis of incorrect, misleading or false information, or by mistake or inadvertence; or (iii) A member has ceased to practise; or (iv) A member has not paid annual fee for COP till 30th day of September of relevant year. Where a COP is cancelled, the holder shall surrender the same to the Secretary
Restoration of COP cancelled due to Non-Payment:	The Council may restore the COP, on an application made in the approved Form and on payment of prescribed fee, w.e.f. the date on which it was cancelled, to a member whose certificate has been cancelled due to non-payment of the annual fee for the COP and whose application, complete in all respects, together with the fee, is received by the Secretary before the expiry of the relevant year



Companies not to Engage in Accountancy:	• No company, whether incorporated in India or elsewhere, shall practice as chartered accountants. • LLP not having any company as its partner, can be engaged into practicing and thus take audit assignments. • If any company contravenes this provision, then, without prejudice to any other proceedings which may be taken against the company, every director, manager, secretary and any other officer thereof who is knowingly a party to such contravention shall be punishable with fine which may extend on first conviction to ₹1,000 and on any subsequent conviction to ₹ 5,000

Q11. A Chartered Accountant in practice has been **suspended from practice for a period of 6 months** and he had surrendered his Certificate of Practice for the said period. During the said period of suspension, though the member did not undertake any audit assignments, he undertook **representation assignments for income tax** whereby he would **appear before the tax authorities in his capacity as a Chartered Accountant**.

Answer:

Undertaking Tax Representation Work: A CA not holding certificate of practice cannot take up any other work because it would be violation of the relevant provisions of the CA Act, 1949. In case a member is suspended and is not holding Certificate of Practice, **he cannot in any other capacity take up any practice separable from his capacity to practice as a member of the Institute**. This is because once a person becomes a member of the Institute; **he is bound by the provisions of the CA Act, 1949 and its Regulations**. If he appears before the income tax authorities, he is only doing so in his capacity as a CA and a member of the Institute. Having bound himself by the said Act and its Regulations made there under, he cannot then set the Regulations at naught by contending that even though he continues to be a member and has been punished by suspension, he would be entitled to practice in some other capacity.

Conclusion: Thus, in the instant case, a CA would **not be allowed to represent** before the income tax authorities for the period he remains suspended. Accordingly, in the present case he is **guilty of professional misconduct**.

Q12. Same Qn as Above, Just after Suspending COP, during that period he designated himself as **Data Privacy consultant** (did work of Filing data privacy related return & Appeared before various authorities in Other Capacity that CA in Practice) → Guide Him, when he is under period of Suspension in Light of Sec 6 of CA.

Hint: Same answer as above: Guilty of professional misconduct

Also Mention Section 6 of CA Act i.e., :

- 1) **No member** of the Institute shall be entitled to practise whether in India or elsewhere **unless** obtained **COP**;
- 2) Every such member shall **pay such annual fee for his certificate** as may be determined,
- 3) COP obtained under sub-section (1) **may be cancelled by Council** under such circumstances as may be prescribed

Ambiguous Question: It's Old Qn of ICAI (Oct'23) → **when ICAI released the answer** → it mentioned the Exact same answer as Above Qn → But in Conclusion they Mention that → **HE IS NOT GUILTY**.

But Later on → They **Re-released the Answer** and Mention that He is **GUILTY**. (But that PDF was also deleted by ICAI)

Author's Suggestion → **Mention Both the Alternative** in Exams to be on a **Safer Side**

➤ Management Consultancy

Pursuant to Section 2(2)(iv) above, the Council has passed a resolution **permitting a Chartered Accountant in practice (CAip)** to render entire range of "**Management Consultancy and other Services**".

Exclude:	Management consultancy not include (Below services are also allowed to be render by CAip): 1. Audit 2. tax (both direct taxes and indirect taxes) representation or advice 3. Liquidator 4. Trustee 5. Arbitrator
Include:	Management consultancy includes following services:



1. Financial management planning and financial policy determination.
2. Capital structure planning and **advice regarding raising finance**.
3. Working capital management.
4. **Preparing project reports and feasibility studies**.
5. Preparing cash budget, cash flow statements, profitability statements, statements of sources and application of funds etc.
6. Budgeting including capital budgets and revenue budgets.
7. **Inventory management, material handling and storage**.
8. **Market research and demand studies**.
9. Price-fixation and other management decision making.
10. Management accounting systems, cost control and value analysis.
11. Control methods and management information and reporting.
12. **Personnel recruitment and selection**.
13. **Setting up executive incentive plans, wage incentive plans etc.**
14. Management and operational audits.
15. **Valuation of shares and business** and advice regarding amalgamation, merger and acquisition; **Acting as Registered Valuer** under the **Companies Act, 2013** read with The Companies (Registered Valuers and Valuation) Rules, 2017. (**Not P&M Valuation**)
16. Business Policy, corporate planning, etc.
17. Organisation structure and behavior.
18. **Systems analysis and services relating to EDP**.
19. Acting as **advisor or consultant** to an issue, including such matters as:
 - (a) **Drafting of prospectus** and listing agreement and completing formalities with Stock Exchanges, ROC and SEBI.
 - (b) Preparation of publicity budget.
 - (c) Advice regarding selection of various agencies connected with issue.
 - (d) Advice on the post issue activities.

Following activities are **not permitted** → (PUB Nii jaana...):

- 1) **Portfolio management**
- 2) **Underwriting**
- 3) **Broking**
- 4) **Financial advisor, and receive commission/fees from mutual fund company**

Explanation - For removal of doubts, it is hereby clarified that the activities of broking, underwriting and portfolio management are not permitted.

20. **Investment counseling** in respect of securities.
21. Acting as registrar to an issue and for transfer of shares/other securities.
22. Quality Audit.
23. Environment Audit.
24. Energy Audit.
25. Acting as **Recovery Consultant** in the Banking Sector.
26. **Insurance Financial Advisory Services** including Insurance Brokerage.
27. Acting as **Insolvency Professional** in terms of Insolvency and Bankruptcy Code, 2016.
28. **Administrative Services**

Administrative services involve assisting clients with their routine or mechanical tasks i.e

Examples of administrative services include:

- Word processing services.
- Preparing administrative or statutory forms for client approval.
- Submitting such forms as instructed by the client.
- Monitoring statutory filing dates, and advising an audit client of those dates.



For example, the functions of a GST practitioner as specified under Rule 83(8) of Central Goods and Services Tax Rules, 2017:

- (a) furnish the details of outward and inward supplies;
- (b) furnish monthly, quarterly, annual or final return;
- (c) make deposit for credit into the electronic cash ledger;
- (d) file a claim for refund;
- (e) file an application for amendment or cancellation of registration;
- (f) furnish information for generation of e-way bill;
- (g) furnish details of challan in form GST ITC-04;
- (h) file an application for amendment or cancellation of enrolment under rule 58;
- (i) file an intimation to pay tax under the composition scheme or withdraw from the said scheme.

Section 144 of Co. Act : Certain Services not Permitted by Auditor :

Can be rendered:

- As approved by the BOD or Audit Committee
- i.e., Tax audit, Certifications etc.

Services that can NOT be rendered directly or indirectly to Co, Holding or Subsidiary:

- Accounting & **B**ook Keeping
- **A**ctuarial Services
- **D**esign & Implementation of Financial Information System

- **M**anagement Services
- Investment **A**dvisory
- Rendered Outsourced **F**inancial services
- **I**nvestment Banking
- **I**nternal Audit
- **A**ny Other Prescribed

➤ Section 2(2)(iv) → Answer Starting Language (for Mngt Consultancy Qns)

Providing Management Consultancy and Other Services: Under **Sec 2(2)(iv)** of CA Act, 1949, a member of Institute shall be deemed "to be in practice" when → he, in consideration of remuneration received or to be received renders such other services as, in the opinion of the Council, are or may be rendered by a CA in practice. Pursuant to Section 2(2)(iv) above, the Council has passed a resolution permitting a Chartered Accountant in practice to render entire range of "Management Consultancy and other Services".

Q13. Mr. A, a practicing CA agreed to select and **recruit personnel**, **train** for and on behalf of a client. Is misconduct?

Hint: → Refer above → Section 2(2)(iv) → Answer Starting Language

The definition of the expression "Management Consultancy and other Services" includes Personnel recruitment and selection. Personnel Recruitment and selection includes, development of human resources including designing and conduct of training programmes, work study, job description, job evaluation and evaluations of workloads.

Conclusion: Therefore, Mr. A is **not guilty of professional misconduct**.

Q14. P, a CA in practice provides **management consultancy** to his clients. he also advised them on **Portfolio Management Services** whereby he **managed portfolios of some of his clients**. Is P guilty of professional misconduct?

Hint: Refer above → Section 2(2)(iv) → Answer Starting Language

- It allows to **act as advisor or consultant to issue of securities** including drafting of prospectus, filing with SEBI, etc.
- **however**, → **not permitted to undertake the activities of broking, underwriting and portfolio management services**
- In view of this, P would be **guilty of misconduct** under the Chartered Accountants Act, 1949.

Q15. CAip → Assignment of Advisor & Consultant to public issue → Ok, But, **Underwrote Public Issue** → **Guilty**

Q16. CAip want to pursue registered valuer course & want to Value plant & machinery under Co.Act 2013. (NEW)

Hint: → Refer above → Section 2(2)(iv) → Answer Starting Language

Council **permits** a CA in practice to render of "mngt Consultancy and other Services" → includes valuation of shares & business and advice regarding amalgamation, merger & acquisition, acting as Registered Valuer under Co. Act, 2013.

- Such rules qualify CA for valuation of securities or financial Assets only and **NOT** for the Plant & Machinery.
- Further Regulation 190A → generally permitted for attending classes & appearing for any examination. (Allowed)

➤ **Member in Practice Prohibited from using a Designation Other Than Chartered Accountant:** *(Link this with Clause 7, P-1, S-1)*

Sr.		Member in Service	Member in Practice
1	Prefix " CA ":	Yes Permitted	Yes Permitted
2	Use another recognised institute Prefix, Along with CA prefix " CA/CS/CMA "	Yes Permitted	Yes Permitted
3	Initial " CPA "	Not Permitted	Not Permitted
4	Use of Designation " Chartered Accountant ":	Yes Permitted	Yes Permitted
5	Use of Description or Designation other than "Chartered Accountant" : i.e., Director-RIL, Partner-KPRG, Cost Accountant, Company Secretary, Income-tax Consultant	- Yes Permitted if he is NOT using "Chartered accountant as designation" - Not Permitted if he is using "Chartered Accountant" as designation	Not Permitted (nor he can use any other description)
6	Use of description indicating membership & degrees recognised in this behalf by the Council: (B.com, M.com, LLB etc.)	Yes Permitted	Yes Permitted
7	Membership of a foreign Institute of Accountancy which has been recognized by the Council through a Memorandum of Understanding (MoU): Example South African Institute of Chartered Accountants (SAICA), Institute of Certified Public Accountants (CPA Ireland) and Institute of Chartered Accountants in England and Wales (ICAEW)	Yes Permitted	Yes Permitted

Note:

Merchant Banker / Advisor to an issue: ALLOW - Members may apply for and obtain registration as category IV Merchant Banker under the SEBI's rules and regulations and act as Advisor or Consultant to an issue. **In client Companies' offer documents and advertisements** regarding capital issue, **name** and **address** of the Chartered Accountant or firm of Chartered Accountants acting as Advisor or Consultant to the Issue could be indicated under the **caption "Advisor/Consultant to the Issue"**. **However**, the name and address of such Chartered Accountant/firm of Chartered Accountants should **not appear prominently**

*Hence, though a member cannot designate himself as a Cost Accountant, he can use the letters **A.C.M.A.** (Associate) or **F.C.M.A.** (fellow) after his name, when he is a member of that Institute*

➤ **Maintenance of Branch office - Sec. 27:**

Office:	A Place where a name board is fixed <u>or</u> where such place is mentioned in the letterhead <u>or</u> any other documents as a place of business.
Use of Name Board	Name board can be put in place of residence of member provided it is a name board of individual member and NOT of firm.



at residence:					
Requirement of Separate In- charge:	- If a CA in practice or a firm of CA has more than one office in India, each one of such offices should be in the separate charge of a member of the institute, who may be either partner/employee. - The requirement of Sec. 27 in regard as to a member being in-charge of an office of a CA or a firm of such CAs shall be satisfied only if the member is actively associated with such office. - Such association shall be deemed to exist if the member resides in the place where the office is situated for a period of not less than 182 days in a year or if he attends the said office for a period of not less than 182 days in a year.				
Exemption of Separate In- charge:	<table border="1"> <tr> <td>Members practicing in Hilly area:</td><td> Members practicing in hilly areas may open a temporary office in plains subject to following conditions: - Temporary office in plains may be opened for period not exceeding 3 Months. Name board of firm to be displayed at temporary office only during these 3 months. - Temporary office should not be mentioned as place of Business on office documents, Regular office need NOT be closed and all correspondence may continue at permanent office, Before commencement of every winter and at the close of such temporary office, it shall be obligatory on member to inform ICAI </td></tr> <tr> <td>Second office: <u>(not 3rd Office)</u></td><td> If it is situated in: Same premises in which first office is situated, or - In the same city, or Within 50 kms. from the municipal limits of CITY in which first office is situated Effective distance from 1st Office = 35 km + 10 km = 45 km </td></tr> </table>	Members practicing in Hilly area:	Members practicing in hilly areas may open a temporary office in plains subject to following conditions: - Temporary office in plains may be opened for period not exceeding 3 Months. Name board of firm to be displayed at temporary office only during these 3 months. - Temporary office should not be mentioned as place of Business on office documents, Regular office need NOT be closed and all correspondence may continue at permanent office, Before commencement of every winter and at the close of such temporary office, it shall be obligatory on member to inform ICAI	Second office: <u>(not 3rd Office)</u>	If it is situated in: Same premises in which first office is situated, or - In the same city, or Within 50 kms. from the municipal limits of CITY in which first office is situated Effective distance from 1st Office = 35 km + 10 km = 45 km
Members practicing in Hilly area:	Members practicing in hilly areas may open a temporary office in plains subject to following conditions: - Temporary office in plains may be opened for period not exceeding 3 Months. Name board of firm to be displayed at temporary office only during these 3 months. - Temporary office should not be mentioned as place of Business on office documents, Regular office need NOT be closed and all correspondence may continue at permanent office, Before commencement of every winter and at the close of such temporary office, it shall be obligatory on member to inform ICAI				
Second office: <u>(not 3rd Office)</u>	If it is situated in: Same premises in which first office is situated, or - In the same city, or Within 50 kms. from the municipal limits of CITY in which first office is situated Effective distance from 1st Office = 35 km + 10 km = 45 km				
Intimate to ICAI:	In all the cases of opening & closing of Branch office, CA in practice or a firm of such CAs shall inform the Council within 1 month of the opening or closing of a branch office.				

Q17. Write a short note on - Maintenance of branch offices by Chartered Accountants in practice → Refer above Topic

Q18. → CAip → Can put name-board in the place of residence of a member with the designation of CA,

⇒ **Can Not Put the Name Board of firm Name at Residence,**

Q19. Mr. K, CA practicing as a sole proprietor has an office in the suburbs of Chennai., he opens another office, which is within the city and at a distance of 30 km. from his office in the suburb. For running the new office, he has employed a retired Income Tax Commissioner who is not a Chartered Accountant

Hint:

As per Sec 27 of the CA Act, 1949 if a CAip has more than one office in India, each one of these offices **should be in the separate charge** of a member of the Institute. However, a member **can be in charge of two offices** if the **second office is located in the same premises or in the same city**, in which the first office is located; or the second office is located within a distance of 50 km. from the municipal limits of a city, in which the first office is located.

(Now Explain the Given Case, exactly same copy paste of Question).

Conclusion: In view of above provisions, there will be **no misconduct** if Mr. K will be incharge of both the offices. However, he is bound to declare which of the two offices is the main office.

Q20. opens another office in a suburb of Mumbai (80 kilometers away from municipal limits) → **professional misconduct.**

Q21. CAip opened another office (**at distance of 26 kms**). → Same Proprietor is Allowed to manage, However, **intimation is needed made to the ICAI** within a month. (**otherwise Misconduct**)

Q22. Mr. Z, a CAip, started his practice by setting up **office in hill Station (Kodaikanal)** → decided to **set up a temporary office** in the **nearby city Marudai**, situated at about 100 kms from the main office. For the months of **April, May & June only**. During these months, his **regular office was not closed** and Mr. Z was in-charge for both the offices. Discipline of ICAI, you are requested to analyse this complaint.

Hint: Explain all conditions & exemption of branch office, area of Kodaikanal is hill station, Therefore, in, no penal action needs to be taken, as Mr. Z is not guilty of professional misconduct.

➤ **KYC Norms for CA in Practice**

Council of ICAI issued such norms to be observed by the members of the profession **who are in practice**, ICAI approved the following KYC Norms which are **mandatory** in nature and shall apply in **all assignments** pertaining to attestation functions

1. Where Client is an Individual/ Proprietor	2. Where Client is an Corporate Entity	3. Where Client is a Non- Corporate Entity
A) General Information: - Name of the Individual - PAN No. or Aadhar Card No. of the Individual - Business Description - Copy of last Audited FS B) Engagement Information: - Type of engagement	A) General Information: - Name & Address of entity - Business Description - Name of the Parent Company in case of Subsidiary - Copy of last Audited FS B) Engagement Information: - Type of engagement C) Regulatory Information: - Company PAN No. - Company Identification No. - Directors names & addresses - Directors' Identification No	A) General Information: - Name & Address of entity - Copy of PAN No. - Business Description - Partners name & Addresses (with their PAN/Aadhar card/DIN No.) - Copy of last Audited FS B) Engagement Information: - Type of engagement

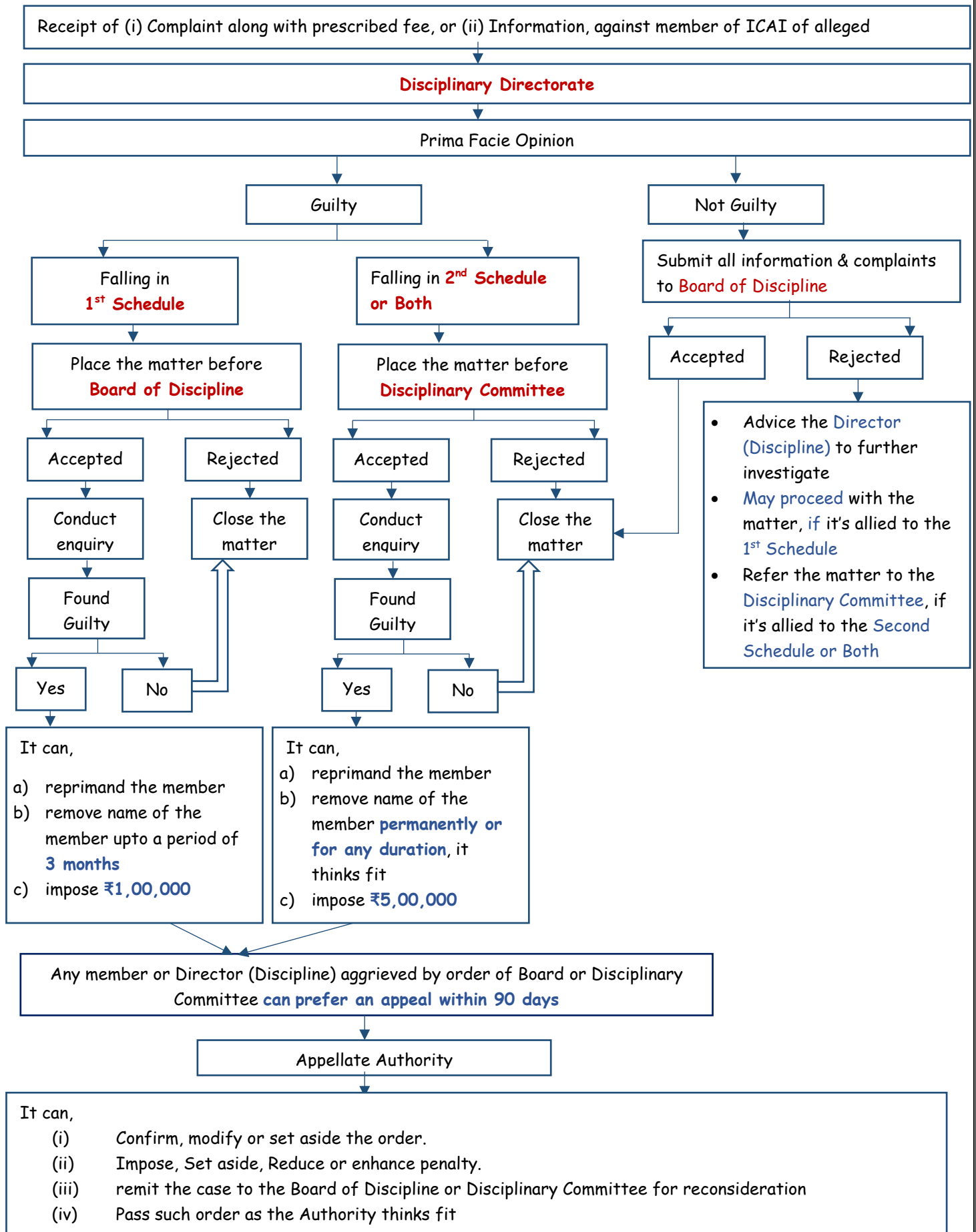
Q23. Mr. F, a CA, gave advisory services to PQR Pvt. Ltd. Further, he gave them **GST consultancy, compilation engagement for historical financial information** → F refused is saying that he **gave only consultancy services to the company and wasn't supposed to keep any information about the company**. Is Mr. F right?

Hint: → Contention of Mr. F is not valid as Mr. F should have kept following information in compliance with KYC Norms which are **mandatory in nature** and shall apply in all assignments pertaining to attestation functions (also for Consultancy assignments),

Explain KYC requirement "Where Client is an Corporate Entity" (As explained above)



➤ Disciplinary Procedure:



➤ Overview of schedules of CA Act, 1949

Schedule	Part	Title	No. of clauses
First	I	Professional Misconduct in relation to members in Practice	12
	II	Professional Misconduct in relation to members in Service	2
	III	Professional Misconduct in relation to members generally	3
	IV	Other Misconduct in relation to members generally	2
Second	I	Professional Misconduct in relation to members in Practice	10
	II	Professional Misconduct in relation to members generally	4
	III	Other Misconduct in relation to members generally	1

How to present professional ethics clauses Answers:

Present Answer in 3 to 4 Paras:

- 1) Explain **relevant clauses applicable** in Questions
- 2) Explain Given case (Do Copy paste of scenario given in question, then link it with clause)
- 3) Explain some other relevant information (Like analysis, If any Guidance Issued by ICAI etc..)
- 4) Conclusion : i.e., Guilty or not guilty (And under which clause & Schedule)

➤ First Schedule : PART-1 of schedules of CA Act, 1949 : Member in Practice

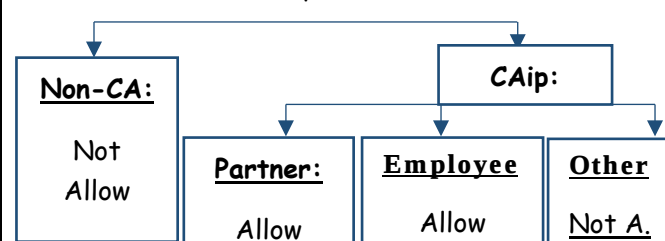
Clause 1 : Practice in my Name:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- **allows any person to practice in his name** as a CA,
- unless such person is also a CA in practice, and
- is in partnership with, or
- employed by himself

Points to Remember:

Who is allowed to practice in CA Name ? -:



- ✓ For above mentioned person who are not eligible to practice in CA name, They are **not even allowed to represent to income tax authority on behalf of firm**

Q24. CA Sant, a newly qualified professional with certificate of practice, approached CA Pant, (a know of CA Sant) , to allow him to have some practical and professional knowledge and experience in his firm before he can set up his own professional practice. CA Pant allowed him to sit in his office for 6 month and allotted a small chamber with other office infrastructure facility, he used to provide tax consultancy independent to the client of the firm and also filed few and GST return, although no documents were signed by him. During his association in CA Pant's office he did not get any share of profit, but only re-imbursement of usual expenses like conveyance, telephone etc. was made to him. After the end of agreed period, he was given a lump sum amount of 3 Lacs by CA Pant out of gratitude.

Hint:

- Explain **Clause (1) of Part I of the First Schedule** to the Chartered Accountants Act, 1949
- In **Given Case:** CA Pant allowed CA Sant (who is a newly qualified CA professional with COP) to sit in his office for 6 months, and allowed him to provide tax consultancy independently to his firm's clients, filing of some IT and GST Returns. He also allowed him to appear before various tax authorities on behalf of his firm. CA Sant was only reimbursed with his usual expenses and was not paid any salary or share of profit for the same. However, after the end of agreed period he was given a lump-sums of rupees 3,00,000 for his association out of gratitude



- **Conclusion:** Thus, in the present case **CA. Pant will be held guilty of professional misconduct** as per Clause (1) of Part I of First Schedule to the Chartered Accountants Act, 1949

Q25. Mr. C a CAip, Allow Following person to Practice his Name:

- 1) allowed his brother-in-law Mr. P who is not a CA, → **Guilty** (Can't allow as he is not CA).
- 2) allowed Mr. T who is employee in his firm → **Ok**, Yes he can allow

Clause 2 : Share Fees/Commission

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- **Pays or allows or agrees to pay or allow**, Directly or indirectly,
 - any **share, commission** or brokerage in **fees** or profits of his professional business to any person other than:
 - ✓ a **member** of the Institute (*i.e., Even Non Practice*), or
 - ✓ **partner**, or **retired partner**, or
 - ✓ **legal representative** of deceased partner, or
 - ✓ member of any other professional bodies, or with **such other persons having prescribed qualifications**.
- for the purpose of rendering such professional services from time to time in or outside India.

Points to remember (Regulation 53A of CA Regulation 1988):

Other Professional Bodies:	ICSI, ICWAI, Bar council of India (LLB), Indian institute of Architects , Institute of Actuaries of India
Person with prescribed qualification:	• CS, Cost accountant, Actuary, • B.E (engineer)., Bachelor of technology, Bachelor of architect, bachelor in law, MBA [for all above Degree → It should be from → University established by Law, Or, Institution recognised by Law (For MBA, also include, Technical institute recognised by All India Council for technical education) • Allow to accept assignments, wherein % of fees is deducted by govt. to meet administrative & other expense

Sharing of Goodwill in case of deceased:

In case of partnership:	If case of death of any partner, legal representative is allow to receive % of share if <u>partnership deed allow to do so</u> .
In case of sole proprietor:	Legal representative is allowed to transfer/sale goodwill within 1 year of death of partner, but can receive only LUMP-SUM consideration, <u>can-not receive % of share</u> [Payment <u>can be made in installments</u>, If agreement to sale contains such provision] However in case ownership is disputed between relatives (i.e., Wife/Child etc.), Then 1 year will be counted after resolution of dispute. [Name of Firm will not be removed by ICAI on receipt of information about death, only Upto 1 yr from death]

Q26. CA in Practice has offered her Article trainee 1% of Profit of Firm, Over & Above the normal stipend.

Answer:

Sharing Fees with an Articled Clerk: As per **Clause (2) of Part I of First Schedule** to the CA Act 1949, a CA in practice shall be deemed to be guilty of professional misconduct if he pays or allows or agrees to pay or allow, directly or indirectly, any share, commission or brokerage in the fees or profits of his professional business, to any person other than a member of the Institute or a partner or a retired partner or the legal representative of a deceased partner, or a member of any other professional body or with such other persons having such qualification as may be prescribed, for the purpose of rendering such professional services from time to time in or outside India.

In view of the above, the objections of the ICAI, as given in the case, are correct and reply of Mr. X, stating that he is paying 1 % profits of his firm over and above the stipend is not tenable.

Hence, Mr. X is guilty of professional misconduct in terms of Clause (2) of Part I of S-I to CA Act 1949.

Q27. Mr. Qureshi, CA, in practice died in a road accident. His widow proposes to sell the practice of her husband to



Mr. Pardeshi, CA, for ₹5 lakhs. The price also includes right to use the firm name - Qureshi and Associates.

Hint → **Sale of Goodwill**: w.r.t C-1, P-1, S-1 → sale is permitted subject to certain conditions discussed in above notes
→ the **legal heir of the deceased member has to obtain the permission** of Council **within a year** of the death.

Conclusion: The act of Mrs. Qureshi is **permissible** & Mr. Pardeshi can continue to practice in that name.

Q28. CA Ravi, a practicing CA, was **proprietor**. → CA Ravi died on 15th Sept, **2020**. CA Ravi is Roohi. On 30th Sept, **2021**, Roohi sold the practice of her husband to CA Balwan for ₹ 25 Lacs **along with right to use the firm name i.e.,**

(i) Whether Roohi can sell the practice to CA Balwan?

(ii) Can CA Balwan continue to practice as proprietor in name of M/s Ravi & Associates?

Hint: → **Explain C-2, P-1, S-1**: → **legal heir of deceased member has to obtain permission of the Council within a year**

(i) Mrs. Roohi **cannot sell the practice** of CA. Balwan **with right to use the firm name**. (as 1 yr passed)

(ii) CA Balwan **cannot continue to practice** in the name of the firm M/s. Ravi & Associates as a proprietor because the **name of the firm M/s. Ravi & Associates would be kept in abeyance only up to a period of 1 year** from the death.

Q29. Mr. K, a practicing CA gave 50% of the audit fees received by him to a non-CA, Mr. L, In Name of office allowance.

Hint: Explain C-2, P-I, S-1 → Mr. K will be held guilty of professional misconduct.

Q30. Mr. X is a practicing CA. Mr. Y is a practicing advocate. X & Y decided to **help each other & share profits**.

Hint: Explain C-2 & C-3 of P-1, S-1 → Regulation 53A → "Bar Council of India" (Advocate) is included. → **So not guilty**.

Clause 3: Accept Fees/Commission

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- **Accepts or agrees to accept** any part of the profits of the professional work
- of a person who is **not a member of the Institute**.

However, such a restriction does **not apply** in respect of following:

- member of any **other professional bodies (as specified in Clause 2)**, or
- with such other persons having prescribed qualifications (as specified in Clause 2).

Points to remember:

Referral Fees not prohibited:

It is not prohibited for a member in practice to charge Referral Fees, being the fees obtained by a **member in practice from another member in practice** in relation to referring a client to him.

Q31. CAip received Profit sharing from "Registered Valuer" → **Guilty** under C-3,P-1,S-1 (As not recognized in 53A/53B)

Clause 4 : Partnership:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

Enters into partnership in or outside India with any person **other than the following**:

1. **C.A. in practice**, or
2. Member of any **other professional body having prescribed** qualifications, or
3. person, who but for his residence abroad would be entitled to registered as member under Clause (v) of sec. 4(1), or
4. a person whose qualifications are recognized by CG or Council for the purpose of permitting such partnerships

Points to remember (Sec 53B):

Person qualified for partnership:

Company Secretary, Cost Accountant, Actuary, B.E., B. Tech, B. Arch, LLB, Architect (from recognised Universities or Institutes).
NOT ALLOWED with CFA/CPA/ACCA/New Your Certified Public Accountant Etc.

Author's Clarification Regarding Partnership with **MBA**

- **MBA is Not Included in Sec 53B** → So Some Author's suggest Partnership with MBA is not Allowed (Old ICAI FAQ Also, Deleted Not)
- However, ICAI Code of Ethics Says → **Partnership with Person** Mentioned in Sec



53A(3) (Refer Clause 2) is **Also Allowed** → **MBA is included** in It.

(Hence It's **Ambiguous Point** → 2 Different section says 2 different Things, Students are advised to **Mention both the Alternative in Exams**:

- **Alternative 1**: Since Section **53B** **Exclude MBA** → So Partnership **Not Allowed**
- **Alternative 2**: As per ICAI Clarification in Clause 4: Partnership with **Sec 53A(3)** Members are allowed → So MBA is included in it → hence **Partnership Allowed**)

NOTE: Member **can-not form** Multi-Disciplinary **partnerships** **till** such time that **Regulators of such other professionals also permit** partnership with CA

Q32. Can CAip enter into **Partnership with Advocate** → Regulation 53B include Advocate → **Not Guilty** (C-4,P-1,S1)
[Ambiguous Question]: In one attempt ICAI said, "Mr.P" is **Guilty** as per C-4,P1,S1, Because Member can-not form Multi Disciplinary partnerships **till such time that Regulators of such other professionals also permit partnership with CA**, And Till now relevant act governing Advocate do not allow Advocate to do partnership with CA" - **So ITS BETTER TO MENTION BOTH THE ANSWER's IN EXAM AS ALTERNATIVE]**

Clause 5 : Secure Business:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

Secures any professional **business** through the services of a person

- **Who is NOT** an **employee** or not his **partner** or
- by means which are not open to a CA.

Clause 6 : Solicits clients/Advertise:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- **Solicits clients** or professional work either directly or indirectly,
- by **circular**, **advertisement**, **interview**, **personal communication** or or by any other means (**CAip**).

However, solicitation is relaxed in following cases:

- **Securing professional work from another CA in practice.**
- **Responding to tenders** or enquiries issued by various users of professional services or organizations.

Points to remember: (Some are Special Tadka :-)

Respond to tender:	CA in practice can respond to tender only in 2 cases: • If Minimum fees is already mentioned in tender, Or • Tender is not exclusively reserved for CA's (i.e., open for other professionals also) <i>(Note: EMD & Security deposit is allow)</i>				
Advertisement & note in press:	<u>As a general rule a member can't advertise.</u> • However, a member may advertise change in partnership, address of practice and telephone numbers provided it contains a bare statement of facts and <u>area of distribution and number of insertions in newspaper should be limited.</u> • A Member is permitted to give classified advertisements in journal / news letter of institute for sharing professional work or seeking partnership or salaried employment of accountancy nature provided it contains only CA's name, address, tel. no., fax or e-mail address and address of social Networking sites of members (not firm Name). Mere factual position of experience and area of specialization, relevant to seek response to the advertisement, are permissible.				
Empanelment for allotment of work:	Govt companies/Dept, bank, court, co-operative societies & other similar institution prepare panel for allotment of Audit/other such work. <table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 20%;">Allow:</td><td>Only when member is aware that such panel exist</td></tr> <tr> <td>Not Allow:</td><td>Roving enquiries for existence of such panel</td></tr> </table>	Allow:	Only when member is aware that such panel exist	Not Allow:	Roving enquiries for existence of such panel
Allow:	Only when member is aware that such panel exist				
Not Allow:	Roving enquiries for existence of such panel				



Vision & values on visiting card	Not allowed to print such things on visiting cards	
Publication of books/articles by CA:	Allow to writes	Not allow
	- Designation "CA" - Name of Firm	Any professional attainment (i.e., Professional experience)
Issue of greeting cards or invitation:	Permitted to use designation "Chartered Accountant" as well as name of firm in - Greeting cards, invitations for marriages and religious ceremonies and any invitation for opening or inauguration of office, or - letters regarding change in office premises or telephone numbers - provided these are sent <u>only to clients, relatives and friends of the members concerned</u>	
Advt. for silver/golden Jubilee:	Allow : advertisement for Silver, Golden, Diamond, Platinum or Centenary celebrations of the Chartered Accountants Firms may be published in newspaper or newsletter.	
Sponsoring activities:	CA in practice not allow to sponsor an event, Except : - Programme Organizing Unit (PoU) of the ICAI, provided such event has the prior approval of Continuing Professional Education (CPE) Directorate of the ICAI. - activities relating to Corporate Social Responsibility : May mention their individual name with the prefix "CA". However, the mention of Firm name or CA Logo is not permitted.	
Advertisement of Teaching / Coaching activities by members:	Not Allow:	Allow:
	- Advertisement of Coaching /teaching activities by a member in practice - abstain from <u>advertising their association with Coaching</u> /teaching activities through hoardings, posters, banners	members may put, outside their Coaching /teaching premises, sign board mentioning the name of Coaching /teaching Institute, contact details and subjects taught therein only.
Television or Movie Credits:	Allow, however While sharing name of the <u>member or Firm of CAs</u> for inclusion in Television or Movie Credits, it must be taken care of that exhibition of name is not made differently as compared to other entries in the credits	
Making roving enquiries	Not allow : "Do you need this service" ?	
Seeking from Professional Colleagues:	Allow : But do <u>not try to show that you are superior than others</u>	
Scope of representation u/s 140(4):	Scope of representation u/s 140(4) of Companies Act, 2013: Allow: Auditor can provide letter by indicating → his <u>independent working as a professional throughout the term</u> of office & his <u>willingness to continue</u> as auditor, <u>if shareholder decided to do so</u> Not Allow: Letter which is solicitating in nature, Derogatory remarks for management, highlighting contribution made by CA in company	
Acceptance of original work:	✓ Not allow : <u>Acceptance of original work</u> emanating from a client introduced by another member, Or Even Another Work → it should be his duty to ask the client that he should come through the other member	
Public Interview:	✓ Allow to use Member & Firm name ✓ But , it should not result in publicity or highlighting professional attainment	



Advertisement in newspaper	✓ Prohibited , to advertise in newspaper boxes
Education videos:	✓ Allow ✓ Not allow : To made reference of Firm name, contact details or website address
Guidelines for Website:	✓ Allow: Any color, Any Format, Pull Model, Website address in stationery, Passport size photo, Link of its page on social networking site (however members should not solicit people to visit or like their respective page(s) on such social Networking site) ✓ Not Allow: Push model, Office photograph ✓ No standard format of the Website is being given to provide independence to the Members ✓ The following information may be displayed on the Firms/Members' Websites: - Member/Trade/Firm name. - Year of establishment. - Member/Firm's address (both Head Office and Branches), tel. no(s), fax no(s) and email ID(s). - Nature of services rendered (to be displayable only on specific "pull" request) - Partners details like name, year of qualification, other qualification(s), tel. no.(s), e-mail address, area of Experience (to be displayable only on specific "pull" request). - Details of employees like name, designation, area of experience (to be displayable only on specific "pull" request) - Job vacancies for the CA/firm of Chartered Accountants (including articleship). - No. of articled assistants. (to be displayable only on specific "pull" request). - Nature of assignments handled (to be displayable only on specific "pull" request). - Name of clients and fee charged NOT be given Note: Disclosure of names of clients and/or fees charged, on the website is permissible only where it is required by a regulator, In that case it is mentioned on the website [in italics], below such disclosure itself, that "<i>This disclosure is in terms of the requirement of [name of the regulator] having jurisdiction in [name of the country/ area where such regulator has jurisdiction] vide [Rule/ Directive etc. under which the disclosure is required by the Regulator]</i>" • Not necessary to intimate ICAI the address of website (MCQ) • Listing on search engine is permitted: by Only name CA, Chartered accountant, Indian CA, Indian CPA • Website may provide a link to the Website of ICAI, its Regional Councils and Branches and also the Website of Govt./Govt. Departments/Regulatory authorities/other Professional Bodies. (Not C.S., CMA, NSE, BSE)

Q33. Mr. S, a CA published a book & gave his personal details as author. & also mentioned his professional **experience**.

Hint: → Explain C-6, P-1, S-1 of CA act 1949

Therefore, members **should not adopt any indirect methods to advertise their professional practice** with a view to gain **publicity** and thereby solicit clients or professional work. → the Council has specified that a member is **not permitted to indicate in a book or an article, published by him, his association with any firm of CA's**. In this case, Mr. S, a CA published the book and mentioned his **professional experience** in detail in the same.

Conclusion: Mr. S has **committed the professional misconduct** by mentioning his professional experience.

[Author's Note: This Question is also is in New SM of ICAI, But ICAI mistakenly forgot to update the description of **Answer**. **Writing Firm Name is allowed, But writing experience Is not allowed : So It's a Misconduct]**

Q34. CA created a website → contains bio-data of partners also contains the **passport size photographs** of partners.

Hint:→ C-6, P-I of S-I → Can create its own website using any format subject, designed that it does not solicit clients
→ The guidelines of the ICAI to allow Firm Details, bio-data of partners and display of a passport size → **no violation**

Q35. CA firm responded to tender of State Govt for computerization of records & paid ₹50,000 as **earnest deposit**.



Hint: → C-6, P-1, S-1 → Explain Topic "**Respond to tender**" as explained above

Conclusion: computerization of land revenue records does not fall within exclusive areas → so **Not Guilty**.

Q36. Mr. X, a CA in practice, wrote two letters to a firm of CAs; → requesting to allot him some professional work.

Hint: → C-6, P-1, S-1 → securing professional work from another CA is Permitted. → thus **not Guilty**.

Q37. A CA Firm Website color was Very Bright & on "Push" Technology → where Clients name were displayed

Hint: C-6, P-1, S-1 → Council has issued relevant guidelines for Website:

(1) **No restriction on Color** of Website (2) **Need PULL** Technology (3) **Names of Clients & fees charged not to be given**

However, disclosure of names of clients and/or fees charged, on the website is **permissible only where it is required by a regulator**, → provided that such disclosure is only to the extent of requirement of the regulator. Where such disclosure of names of clients and/ fees charged is made on the website, the member/ firm shall ensure that it is mentioned on the website [in italics], below such disclosure itself, that "This disclosure is in terms of the requirement of [name of the regulator] having jurisdiction in [name of the country/area where such regulator has jurisdiction] vide [Rule/ Directive etc. under which the disclosure is required by the Regulator]."

In view of the above, M/s XYZ would have no restriction on the colours used in the website but failed to satisfy the other two guidelines. Thus, the firm would be **liable for professional misconduct** since it would amount to soliciting.

Q38. A CA firm, contained a link to "All India Chartered Accountants Association", a voluntary association.

Hint: it is permitted that

- Website may provide a link to the website of ICAI, its Regional Councils, Branches and Government Departments and
- Other professional Bodies like AICPA, ICAEW, and CICA.

link to "All India Chartered Accountants Association" which is **not permitted**, liable for misconduct under C-6, P-1, S-1

Q39. CA. Intelligent, a CAip, provides **part -time tutorship under the coaching** of the Institute. → he was awarded 'Best Faculty of the year' as gratitude from Institute → He posted his framed photograph on his website.

Hint: on website, No photographs are permitted, Only display of passport size photograph is permitted, → **guilty**

Q40. CAip, created his own website → also circulated the info contained in website through E-mail.

Hint: → No standard format or restriction on colors is there, However None of the information contained in the website be circulated on their own or through E-mail or by any other mode (except "Pull" request) → **Guilty** (C-6, P1, S1)

Q41. A partner of a firm of CA during a T.V. interview handed over a bio-data of his firm. also detailed achievements of partner & his recognition as an expert in the field of taxation.

Hint: C-6, P-1, S-1 → Such an act would definitely lead to the promotion of firms' name & publicity → **guilty**.

Q42. An advertisement was published in a Newspaper containing the photograph of Mr. X, a member of the institute wherein he was congratulated on the occasion of the opening ceremony of his office.

Hint: C-6, P-1, S-1 → **Guilty**

Q43. Mr. X, a CA → wrote several letters to the Assistant Registrar of Co-operative Societies stating that though his firm was on the panel of auditors, no audit work was allotted to the firm.

Hint: liable for professional misconduct C-6, P-1, S-1.

Q44. CA "A" seeking clients through family and friends, Further "CA A" build colorful website → and shared website address on his all-social media & stories, with caption "Easy online stock certification services" → also entered in agreement with Digital marketer, to share 5% commission.

Hint: C-6, P-1, S-1 → Mr. A is wrong in seeking clients through family/friends. → Can create website but comply with Guidelines → Thus, CA, A would be **held guilty of professional misconduct** under C-6, P-1, S-1 of CA Act 1949..

Q45. A special notice has been issued for a resolution → that CA. Smart shall **not be re-appointed as an auditor**. Consequently, CA. Smart submitted a representation in writing u/s 140(4)(iii) of Co. Act, 2013. He indicated his willingness to continue as an auditor if reappointed by the shareholders of the Company.

Hint: Explain Clause:- (6) of Part I of First Schedule,

- As per Provision:- **Section 140(4)(iii)** of the Companies Act, 2013:
 - Provides a right, to the retiring auditor, to make representation in writing to the company.



- Retiring auditor has a right for his representation to be circulated among the members & and to be read out at the meeting.
- However, the content of letter should be set out in a dignified manner how he has been acting independently and
- May, in addition, indicate, his willingness to continue as auditor, if re- appointed by shareholders.
- CA. Smart will not be held guilty for professional misconduct

Note:

Q46. Above same Qn was asked in MTP, just one change was there in Qn → "In the representation, CA. included the contributions made by him in strengthening the control procedures of the company".

So, Above answer format will be same → however, in this case → he will be **GUILTY**

Q47. Mr. Sodhi, a CAip, is proposed to be removed as the auditor of a company makes unsubstantiated and derogatory remarks against the management of the company in his representation u/s 140 of the Companies Act.

Hint: Mr. Sodhi is guilty of professional misconduct as per Clause:- (6) of Part I of First Schedule.

Q48. Z, a CA wrote several letters to Govt Dept, pointing out seniority of his firm, with a view to get the audit work.

Hint: Council Guidelines:- Advt for the CAip is not permitted to claim any superiority → he is guilty: C-6,P-1, S-1

Q49. A letter is sent by a CAip to Ministry, inquiring whether a panel of auditors Exist, If yes, Include him in panel

Hint: → where the existence of such a panel is within the knowledge of the member, he is free to write to the concerned organization with a request to place his name on the panel.

However, it would not be proper for the member to make roving inquiries for having his name included in any such panel, So member is guilty of misconduct as per Clause (6) of Part I of S-I

Q50. CA. Srishti and CA. Mishti are 2 partners of the CA firm → CA. Srishti organised a religious ceremony at her home → in Invitation card she added her designation "Chartered Accountant" with her name. Later on, the invitations were distributed to all the relatives, close friends and clients of both the partners.

Hint: Using the designation "Chartered Accountant" in invitation cards is permitted under Guidelines issued in C-6, P-1, S-1 → provided cards are distributed to relatives, close friends and clients of the concerned member. In present case, invitations are also given to relatives, close friends & clients of partner also; hence it's misconduct.

Q51. a firm of CA responded to a tender issued exclusively for CA's However no minimum fee was prescribed.

Hint: Shall be held guilty of professional conduct for responding to such tender

Q52. During the ceremony of a new branch office of CA. Young, his friend CA. Old introduced to CA. Young, his friend and client Mr. Rich, the owner of an Export House whose accounts had been audited by CA. Old. After few days, Mr. Rich approached CA. Young and offered a certification work which hither to have been done by CA. Old.

Hint: → The Council has prohibited include that a member should not accept the original professional work emanating from a client introduced to him by another member.

- If any professional work of such client comes to him directly, it should be his duty to ask the client that he should come through the other member dealing generally with his original work. → So CA Young is Guilty (C-6, P-1,S-1)

Q53. for audit proposal of Bank → Bank mailed the audit firms maximum fee per branch & asked to submit quotations.

Hint: CA firm will be is guilty of Professional misconduct, Because CA can't reply until & unless MINIMUM FEES quoted.

Q54. A CAip → provide coaching to CA students online → he advertises his classes on various social media platforms.

Hint:

- Regulation 190A of CA Regulations, 1988 provides that a CA in practice shall not engage in any business or occupation other than the profession of accountancy except with the permission granted by resolution of Council.
- The Council has passed a resolution, granting general permission for private tutorship and part time tutorship under coaching organization of the Institute. Such general permission is subject to condition that direct teaching hours devoted should not exceed 25 hours a week in order to be able to perform attest functions.
- Explain Clause 6,P-1,S-1
- Further, an advertisement of online coaching activities through social media platforms amounts to indirect



solicitation as well as solicitation by another means → violative of C-6 of P-I of the S-I to CA Act, 1949.

- member in practice can engage in **PRIVATE TUTORSHIP** subject to Council Guidelines but he cannot advertise
- Guilty of professional misconduct under Clause (6) of Part I of First Schedule

Clause 7: Advertise professional attainment:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- **Advertises his professional attainments** or services, Or,
- **uses any designation or expressions other than the Chartered Accountant** on professional documents, visiting cards, letter heads or sign boards.

However, **recognized degree of university** or title indicating membership of ICAI or other recognized institution may be used.

Points to remember: (Some are Special Tadka :-)

Advt. through write-up:	• Allowed, Subject to guidelines (Discussed later)	
Other Designation:	Not Allow:	Words Like Income tax consultant, corporate lawyer, Cost consultant, MP
	Allow:	Insolvency professional, registered valuer
Date of setting up practice:	Not allowed: On letter head or other professional documents	
Practice as Advocate, CS, CMA:	Subject to permission may practice as Advocate, CS, CMA, but can't use designation "Chartered Accountant" simultaneously to above designations It is clarified that in the event of the permission being granted to a member in practice to also hold COP of sister Institute(s)/Bar Council, such a member be treated as a member in full-time practice.	
Press Notice: Success of examination	Allow: i.e., Success of article/employee's in examination (should not contain any element of undesirable publicity)	
Appearance of CA : Electronic media i.e. TV, Films, internet etc.,	Allow, even firm name also : Members may appear electronic media or give lectures at forums and may give their names and describe themselves as CA. Special qualifications or specialised knowledge directly relevant to the subject matter of the programme may also be given. however, any exaggerated claim or any kind of comparison is not permissible	
Appointments Public Importance:	i.e, MP, MLA etc. Allow: To use "CA" Not allow: Firm Name	
Size of sign board:	For his office, Own discretion, Good taste, However not allowed to use: Glow signs & Large size boards	
Name Plate @ Home:	• "CA Member" - Allow • "Firm Name" - Not Allow	
Public announcement with Director's details:	Example : Prospectus (CA Acting as director of company) • Allow: Name of CA, No. of year • Not Allow: Firm Name, descriptions regarding his expertise, specialisation and knowledge in any particular field • He should request mngt that before any such prospectus or public announcements or public communication mentioning the name of the member concerned, is issued, the material pertaining to the member concerned should, as far as practicable be got approved by him.	
Use of Logo:	Can use only Common logo as prescribed by ICAI (Not permit to use any custom logo)	
Photograph in Magazine:	Allow: Only if Free	



Visiting Card rules:

- **Not allow:** Vision & values, Photograph
 - **Allow:** QR Code
- (However, QR should not contain any information which is not otherwise permissible to show in Visiting cards)

Q55. A practising CA uses a visiting card in which he designates himself, as Chartered Accountant & a Tax Consultant

Hint:

- **Sec 7** of CA Act, 1949 read with **C-7, P-I** of S-I → prohibits advertising of professional attainments or services of a member. It also restrains a member from using any designation or expression other than that of a CA.
- It would amount to misconduct unless it be a degree of a university/professional body recognised by CG or Council.
- Conclusion: Thus, it is **improper** to use designation "Tax Consultant" since neither it is a degree of a University established by law in India or recognised by the Central Government nor it is a recognised professional membership by the Central Government or the Council.

Q56. A practising CA visiting card → designates himself, besides as Chartered Accountant, Cost Accountant.

Hint: Council resolved → members are permitted to use letters indicating membership of the ICMAI but not designation

Q57. Mr. SP, a CA, He designates himself under the caption "Merchant Banker" in client offer documents and 'Advisor to issue' in his own letterheads, visiting cards and professional documents

Hint: → Guilty of professional misconduct as per Clause (7) of Part I of First Schedule, Because:

- in Client Companies' offer documents and advertisements regarding capital issue, name and address of the CA acting as Advisor or Consultant to the Issue could be indicated under the caption "Advisor/ Consultant to the Issue".
- But, members **Can't** use designation of 'Merchant Banker' or 'Advisor/Consultant to Issue' in their own letter etc.

Q58. A CA in practice, is IP (Insolvency Professional) has mentioned the same on his visiting cards, letter heads

Hint: A CA empanelled as IP (Insolvency Professional) can mention 'Insolvency Professional' (Not Guilty)

Q59. The visiting card as well the QR code contains (printed on visiting card) his name, office and residential address,

Hint: under C-7, printing photograph on the visiting cards is not permissible. However Quick Response Code may be printed on visiting card provided that the Code does not contain information that is not otherwise permissible to be printed in their visiting card. **No misconduct**, information contained in QR Code are permissible.

Q60. a CA in practice is a partner in 3 firms. While printing his personal letter heads, B gave the names of all the firms in which he is a partner.

Hint: Explain C-7 of P-I of S-1, → there is no prohibition for printing names of all 3 firms, **Not guilty**

Q61. The offer document of a listed company in which Mr. D, a practising Chartered Accountant is a director mentions the name of Mr. D as a director along with his various professional attainments and spheres of specialisation.

Hint: Explain Clause 6, Clause 7, & "Public announcement with Director's details" topic, → If company gives any announcement that gives descriptions about CA expertise, specialisation & knowledge in any particular field, in such cases the member concerned has to take necessary steps to ensure that such prospectus or public announcements or public communications do not advertise his professional attainments, it shall constitute a **misconduct** in Clauses 6 & 7

Q62. a CAip, delivered a speech in the national conference he told to the audience that he is a management expert and his firm provides services of taxation at reasonable rates., also distributed his business cards.

Hint: → Explain Clause 6, Clause 7 of Part I of the First Schedule, He is **guilty of professional misconduct**:

- Member may appear on TV/films/Radio/give lectures at forums and may give their names and describe themselves as CA. Special qualifications or specialized knowledge directly relevant to the subject matter of the programme may also be given but no reference should be made, in the case of practicing member to the name and address or services of his firm. What he may say or write must not be promotional of his or his firm but must be an objective professional view of the topic under consideration.
- Thus, it is improper to use designation "Management Expert" since neither it is a degree of a University established by law in India or recognised by the C.G nor it is a recognised professional membership by the C.G or Council

Q63. X & Co., CAs informed selected multinational organizations, who are not their clients, that "Mr. Y", the former Partner - in - charge of taxation of one of the largest accounting firms of the world, had joined them as a partner.



Hint: They are guilty of misconduct under clause 6 & 7 of P-1 of 1st Schedule

Q64. A CA Ramesh Mehta in practice appearing on TV on budget proposals, on the basis of the bio- data furnished by him, as the **Senior most partner** of M/S Mehta & Verma a leading firm established in Indore in 1988.

Hint: Explain Clause 6 & 7 both,

→ but no reference should be made, to the name and address or services of his firm, Use of adjective expressions such as "a leading firm of CA's and Senior Most Partner, date of establishment of firm, Hence Guilty

Clause 8: Communicate to previous CA

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- accept a position as **Auditor previously held by another chartered accountant** or certified auditor auditor who has been issued certificate under the Restricted Certificate Rules, 1932
- without first communicating with him in **writing**.

Points to remember: (Some are Special Tadka :-)

Shall not accept audit:	• Non-compliance of provisions of Sec. 139 and 140 of Companies Act, 2013. • Non-payment of undisputed audit fee (except sick unit). • Issuance of a qualified Report by earlier auditor However in case of issuance of qualified report, member may accept audit if he thinks that attitude of retiring auditor wasn't proper and justified. But if the report was qualified for good and valid reasons, non-acceptance of audit would be a healthy practice.
Non availability of Previous Auditor:	Fees pending due to non-availability of previous auditor, may advise the client to purchase Demand Draft of the amount equivalent to undisputed Audit Fees of retiring auditor
Duty of Retiring Auditor:	To respond back On the request of the Incoming Auditor for providing known information regarding any facts or other information needs to be aware before deciding whether to accept the engagement
Positive Evidence of Delivery required:	Members should communicate with a retiring auditor in such a manner as to retain in their hands positive evidence of the delivery of the communication to the addressee. In the opinion of the Council, the following would in the normal course provide such evidence: • Communication by a letter sent through "Registered Acknowledgement due", or • By hand against a written acknowledgement, or • Acknowledgement of the communication from retiring auditor's vide email address registered with the Institute or his last known official email address, or • Unique Identification Number (UDIN) generated on UDIN portal (subject to separate guidelines to be issued by the Council in this regard)
Certificate of posting:	Not allow: Its not conclusive proof of communication
Premise found lock:	<u>received back by the Incoming Auditor</u> with " Office found Locked " <u>written</u> on the Acknowledgement Due shall be deemed as having been delivered to the retiring auditor.
Firm not found:	Received back with remarks " No such office exists at this address ", and the address of communication is the same as registered with the Institute on the date of dispatch, the letter will be deemed to be delivered
Tax audit:	Its healthy practice to communicate to statutory auditor by tax auditor
All kind of Audits:	The requirement for communicating with the previous auditor being a Chartered Accountant in practice would apply to all types of Audit viz., Statutory Audit, Tax Audit, GST Audit, Internal Audit, Concurrent Audit or any other kind of audit
Assignment done by other professionals:	In case of assignments done by other professionals not being Chartered Accountants, it would also be a healthy practice to communicate (Not mandatory)



Audit of Govt co., bank or branches:	in the case of audit of government Companies/ banks or their branches, in case the time schedule given for the assignment is such that there is no time to wait for the reply from the outgoing auditor, incoming auditor may give a conditional acceptance of the appointment and commence the work which needs to be attended to immediately after he has sent the communication to the previous auditor in accordance with this clause. In his acceptance letter, he should make clear to the client that his acceptance of appointment is subject to professional objections, if any, from the previous auditors and that he will decide about his final acceptance after taking into account the information received from the previous auditor. He Must hold report till reply not receive
Other points:	• If auditor started assignment before received NOC : Its professional misconduct • If previous auditor doesn't gave reply within reasonable time: Then can accept audit • Low fees quoted to take audit: Allow • If internal auditor appointed then its not necessary to communicate to statutory auditor, as this clause is applicable in situation of replacing another auditor, But Internal & Statutory auditor are parallel in position : Not replacement

Q65. Mr. X, a CA accepted his appointment as tax auditor of the Income-tax Act, and commenced the tax audit within 2 days of his appointment → After commencing he realised his mistake of accepting this tax audit without sending any communication to the previous tax auditor. To rectify his mistake, before signing the tax audit report, he sent a registered post to the previous auditor and obtained the postal acknowledgement?

Hint: Explain Clause (8) of Part I of First Schedule to the Chartered Accountants Act, 1949 → **Guilty**

- The object of the incoming auditor communicating in writing with the retiring auditor is to ascertain whether there are any circumstances which warrant him not to accept the appointment, for example, whether the previous auditor has been changed on account of having qualified the report or he had expressed a wish not to continue on account of something inherently wrong with the administration of the business

Q66. W, a CA had sent letters under certificate of posting to the previous auditor informing him his appointment

Hint: Explain Clause (8) of Part I of First Schedule → **GUILTY**

- mere posting letter "under certificate of posting" is not sufficient evidence of communication, → communication by a letter sent "Registered Acknowledgement Due" or by hand against a written acknowledgement is positive evidence

Q67. CAip was appointed to carry out internal audit. However, failed to intimate appointment to statutory auditors.

Hint: → This clause is applicable in situation of replacing of one auditor by another auditor. Internal auditor and statutory audition are parallel positions and not replacement positions. → **No violation of C-8 of P-1, S-1**

Q68. Central Government holds 65% of the share capital in this company → Due to lack of time → Auditor accepted position by giving conditional acceptance after communicating with Previous auditor.

Hint: C-8, P1, S1 → **Not guilty** → as no time to wait for reply → it's a Govt Company

Q69. V&A have been offered Statutory Audit of TLP Ltd., CA V, partner of the firm, communicated with the previous auditor enquiring as to whether any professional reason exists for which he should not accept the audit assignment. Previous auditor informed that he issued a qualified report, so management is changing the auditor.

Hint: Explain **Clause 8, P-I, S-I**

The professional reasons for **not accepting an audit** would be:

- (a) Non-compliance of Sec 139 & 140 of Co. Act, 2013 as mentioned in C-9, P-I, S-1 to CA Act, 1949; and
- (b) Non-payment of undisputed Audit Fees by auditees other than in case of Sick Units; and
- (c) **Issuance of a qualified report.**

There is no rule, written or unwritten, which would prevent an auditor from accepting the appointment offered to him under the circumstance of Issuance of qualified report. However, before accepting the audit, he should ascertain the full facts of the case.

So, it can be concluded that V&A may accept the audit of TLP Ltd if CA V is satisfied that the attitude of the

retiring auditor was not proper and justified. If, on the other hand, CA V feels that the retiring auditor had qualified the report for good and valid reasons, he should refuse to accept the audit of TLP Ltd.

Clause 9 : Not comply Sec 139, 140 & 141:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- **Accepts an appointment as AUDITOR** of a company,
- Without ascertaining whether requirements of Sec. 225 of Companies Act, 1956 (**Sec. 139 appointment & 140 removal** of Companies Act 2013 read with **Sec. 141 disqualification**) in respect of such appointment have been duly complied with

Points to remember: (Some are Special Tadka :-)

Auditor willing to appoint, not reappointed:	• Where auditor is willing to re-appoint, but not get reappointed by company, Then "representation received by auditor" (which was circulated to shareholders), also send that representation to ICAI • Incoming auditor is require to check whether above requirement complied • This apply in case of "Removal of auditor of Govt co" or "other statutory body" also
Some examples of misconduct:	• i.e, Accepted assignment where director is relative of auditor • 1st time auditor is appointed by Directors, instead of BOD
Guideline by Board for Removal of Auditor	• If Auditor RESIGN / Or He Not Gave company offer to Reappoint → Send <u>communication to BOD (Reason)</u>, <u>If he consider it's professional Reason, then Also send Communication to ICAI</u> [Incoming Auditor will check that Communication has been Made] • If Auditor was Willing for Reappointment → But Not reappointed By company → <u>Send copy of the statement which he may have sent to the management to INSTITUTE</u> • The above procedure is also followed in the case of removal of auditors by the government and other statutory authorities.

[Refer "Additional PDF Booklet", Relevant section of Companies act are explain there]

Q70. CA Raja was appointed as Auditor of Castle Ltd. for the year 2019-20. Since he declined to accept the appointment, Board of Directors appointed CA Rani as the auditor in place of CA Raja, & also accepted by CA Rani.

Answer:

Board can appoint the auditor in the case of **casual vacancy** under **section 139(8)** of the Companies Act, 2013. The **non-acceptance of appointment by CA. Raja does not constitute a casual vacancy** to be filled by the Board. In this case, it will be deemed that no auditor was appointed in the AGM.

Further, as per Sec 139(10) of Co.Act, 2013 when at any AGM, no auditor is appointed or re-appointed, the **existing auditor shall continue** to be the auditor of the company. The appointment of auditor by the Board is defective in law.

(Explain C-9,P1, of 1st Schedule As given in above notes)

CA. Rani is guilty of professional misconduct (she accepted appointment without verifying statutory requirements.)

Q71. Mr. X is a CA accepted the appointment as Statutory Auditor → without communicating with the previous auditor & He also failed to ascertain the compliance of requirement of Section 139 and 140 of Companies Act, 2013.

Hint: Guilty of Clause 8 & 9 of Part I of the First Schedule to the Chartered Accountants Act, 1949

Q72. You observe that previous auditors resigned. &, Balance Sheet shows an audit fee payable of ₹25,000.

Hint: Explain Clause 8 & 9 of P-1, S-1

Q73. Mrs. Fair is a Director of XYZ Pvt Ltd, having 15 % share-holdings in the company. the company appointed C.A. Mr. Lovely, Mrs. Fair's spouse, as its statutory auditor.

Hint: Explain C-9,P-1,S-1 & Sec 143(3)(f) of Co.Act 2013, → Mr. Lovely should not accept the appointment as statutory auditor of the company, where his wife Mrs. Fair is director. This is contravention of section 141 (3)(f) of Co. Act, 2013.

Q74. X & Co. CA were informed by True & Co. Ltd. that they have been appointed as auditor of the company in place of ABC & Co. who have been removed, However Shareholder approval is still pending, and auditor commenced the work.

Hint: Commencing work without appointed as auditor in AGM is a non- compliance of Sec. 139, (guilty → C-9, P-1, S-1)



Q75. CA Mehta was appointed as the Auditor of CS Ltd. after obtaining a certificate from the management that the provisions of the Sec 139 & 140 of the Companies Act, 2013 have been complied with. Comment w.r.t CA Act, 1949

Hint: Explain Clause (9) of Part I of the First Schedule. → Guilty

the incoming auditor has to ascertain whether the Company has complied with the provisions of the above sections. The word "ascertain" means "to find out for certain". This would mean that the incoming auditor should find out for certain as to whether the Company has complied with the provisions of Sections 139 and, 140 of the Companies Act, 2013. In this respect, it would not be sufficient for the incoming auditor to accept a certificate from the management of the Company that the provisions of the above sections have been complied with. It is necessary for the incoming auditor to **verify the relevant records** of the Company and ascertain as to whether the Company has, in fact, complied with the provisions of the above sections.

Q76. Mr. Ram resigned as Statutory Auditor on 31/07/22 (for FY 22-23) → Mr. Sunil accepted the position (appointment letter was duly signed by BOD), Appointment letter date was 31/07/22, Which he accepted on 01/08/22. On 15/08/22 → He communicated Mr. Ram for reason of his resignation. Board filed ADT-1 with registrar on 31/08/22.

Hint: Explain C-9, P-1, S-1.

- **Sec 139(8)** → Casual vacancy filled by Board within 30 days of resignation, However if it's auditor **Resignation** → approval in **General meeting (GM)** require within **3 months** of Board's recommendation.
- Before appointment, take Written consent from auditor & Certificate from him reg. Sec 141 compliance
- After appointment → **company shall Inform the registrar within 15 days in ADT-1**
- **Explain C-8, P-1, S-1**
- Given Case, Appointment Made by BOD (not approved in GM), **Accepted appointment on 01-08-2022, but communicated to Mr. Ram on 15-08-2022**, Further M. **Company filed ADT-1 with registrar on 31-08-2022.**
- Therefore, he has **not ascertained from company whether requirements of Sec 139 and 140 of Co.Act, 2013**
- Mr. Sunil is **guilty of professional misconduct both under clause 8 and 9 of S-1.**

Clause 10 : Fees charged % of profit or Contingent upon finding:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- Charges or offers to charge, **accepts** or offers to accept in respect of any professional employment,
- fee which is based on a **%age of profits or**
- which are **contingent upon findings**, or results of such employment,
- except as permitted under regulations.

Points to remember:

Fees fixed by court or public authority:	• Permitted : Not be considered as contingent
Permitted: (VR-CCD-FC & insolvency professional & non-audit)	In respect of below mentioned cases fees may be fixed as specified below: • In the case of Valuer for purposes of direct taxes and duties: on the basis of %age of value of property valued. • Receiver or liquidator: on the basis of %age of realisation or disbursement of assets. • Co-operative society: on the basis of %age of paid up capital or working capital or gross/net income or profits. • management Consultancy services: on the basis of %age which may be contingent upon the findings, or results of such work; • Debt recovery services: on the basis of %age of the debt recovered • certain Fund-raising services: on the basis of a %age of the fund raised (Institute has not yet notified any fund raising services on which CA is eligible to charge fees on basis of % of fund raised)



- services related to **Cost optimization**: on the basis of %age of benefit derived
- Any other service or audit: as may be decided by the Council. Following activities have been decided by the Council for this clause: (i) Acting as **Insolvency Professional** (ii) **"Non-Assurance" Services to "Non-Audit" Clients**

Q77. Mr. V a practicing CA acting as liquidator, charged his professional fees on % of the realization of assets.

Hint: Refer Clause 10, P-1, S-1 & also mention all permitted activities → Mr. P shall not be held guilty.

Q78. Mr. X, CAip, valued goodwill of a business for purpose of taxation laws & he would get 5% of value of goodwill

Hint: Refer Clause 10, P-1, S-1 & also mention all permitted activities, Mr. X is not guilty of any misconduct.

Q79. Mr. X has charged a fee for representing his client in an income tax appeal based on the expected relief as a result of the appeal. The fees will be higher of : (i) Rs. 5,00,000 Or, (ii) 10% of Tax Demand Reduced.

Hint: Refer Clause 10, P-1, S-1 & also mention permitted activities → "provides non-assurance services to Non-Audit Clients", → Mr. Kumar will not be held guilty

(Note: Above is amended answer as per May'24 Paper, and this is correct answer)

Q80. Mr. Clever, a CA, prepared a project report for one of his client, Mr. King, to obtain long term loan of ₹100 lakhs from a scheduled bank and decided to charge fees @10% of the loan approved.

Hint: he decided to raise the invoice of his service @10% of the loan to be sanctioned in future, which is basically contingent upon the findings, Hence Mr. Clever will be held guilty for professional misconduct

Q81. E Ltd to optimize resource utilization & cost reduction, Appointed CA & offered 5% of benefit derived.

Hint: not Guilty of professional misconduct

Clause 11 : Other business & profession:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- **Engages in any Business or occupation** other than the profession of chartered accountant **unless permitted by Council** so to engage.

Note: However, a member **may become director** (NOT being M.D. or Whole-time director) in a company provided he or any of his **partner is not interested in such company as an auditor.**

Points to remember:

General permission:

Occupations for which permission has been granted generally:

1. **Employment under C.A. in practice** or firms of such CAs.
2. **Private tutorship.**
3. **Authorship** (create) of Books/Articles. (**Any type of book**)
4. **Editorship** (edit/polish) of professional journal (**not magazine**).
5. Holding of **Life Insurance Agency** license for limited purpose of Renewal Commission.
6. Attending class and appearing for any exams.
7. Holding of public elective offices such as **MP or MLA**.
8. **Honorary office** of charitable - educational or other non-commercial institute.
9. **Notary public, Justice of peace, Special Executive Magistrate** and like.
10. **Part time tutorship under coaching** organization of institute.
11. Valuation of paper, acting as paper setter, head-examiner or moderator for any exam.
12. Acting as **Surveyor/Loss Assessor** under Insurance Act.
13. Acting as **Recovery Consultant** in the Banking Sector.
14. **Owning** agricultural land and carrying out **agricultural activity**.
15. Chartered Accountant in practice may act as a **liquidator, trustee, executor, administrator, arbitrator, receiver, adviser or representative for costing, financial or taxation matter**, or may take up an appointment that may be made by the Central Government or a State Government or a court of law or any other legal authority or may act as a **Secretary** in his professional capacity, provided his employment is not on



	a salary-cum-full-time basis" (May'2024 Qn)			
Special permission:	Occupations for which specific and Prior approval is required: 1. Full time/Part time employment in Business concerns provided he/his relative do not hold substantial interest in such concerns. The Term relative means Husband, wife, brother or sister or any lineal ascendant or descendent. 2. Full time/Part time employment in non-business concern. 3. Office of Managing Director/Whole-time Director of a body corporate provided that the member &/or any of his relatives do not hold substantial interest in such concern. 4. Interest in family business concerns. 5. Interest in any educational institute. 6. Part time/Full time lectureship for courses other than ICAI Examinations. 7. Part time/Full time tutorship under any educational institution other than coaching organisation of institute. 8. Editorship of journals other than professional journals. 9. Any other Business/Occupation for which Executive Committee considers that permission may be granted			
Acquiring interest in family business: (Require special approval)	A member of the Institute can acquire interest in family business in any of the following manner: (i) as a proprietary firm (ii) as a partnership firm (iii) in the name and style of Hindu Undivided Family as its Karta or a member. It would be necessary for the members to provide evidence <u>that</u> interest in the family business concern devolved on him as a result of inheritance/succession/partition of the family business. It is also necessary for the member to show that he was NOT actively engaged in carrying on the said business and that the family business concern in question was not created by himself. • Sleeping partner in family business → Require permission • Director in any company → Allow (not require permission)			
Teaching & Education:	1) Honorary office hold in educational inst.		General permission	
	2) Private tutorship (not coaching center)			
	3) Interest in any educational institution		Special permission	
	4) Employment for teaching:	ICAI →	Part-Time →	General permission
		ICAI →	Full-Time →	Not allow
		Other coaching	Part-time →	Special permission
	Full-time →			
	• For GENERAL Permission w.r.t Education: is subject to the condition that direct teaching hours devoted to such activities taken together should not exceed 25 hours a week in order to be able to perform attest functions.			
Director Simplicitor:	Yes Allowed to become a Director Simplicitor [i.e., means an ordinary / simple Director who is not a MD or WTD and is required only in the Board Meetings of the company and not paid any remuneration except for attending such meetings]			
Subsidiary Co. auditor:	Subsidiary Company Auditor → CAN-NOT be a Director of its Holding Company (Decided by Ethical Standard Board (ESB))			
Trading in Derivative:	Q82. Summary of Qn in MAY 2024 MTP Ethical Standards Board of ICAI has announced that it is permissible for a CAip to engage in derivative transactions in his personal capacity			



but **not in professional capacity** i.e. for clients i.e.,:

- **Derivative Trading on behalf of Client** (i.e., Professional capacity) → **Not Allowed**
- Derivative trading on **personal capacity (Equity & Currency Derivative)** → **Allowed**
- **Commodity Derivative trading** → **NOT ALLOWED**

Q83. CAip, started a full-time lecturer in a college. Also, becomes a partner with his brother in business.

Hint: Explain Clause (11) & Clause (4) of Part I of 1st Schedule CA Act 1949 → **liable for professional misconduct**

- As both the Above mentioned activities require Prior & Specific permission from Council

Q84. CA Sumati is CAip. CA Sumati is owner of domain cap.net. → to generate additional revenue CA Sumati sold this domain name to XYZ Limited for earning royalty of Rs. 2,25,000. does it requires approval of Institute ?

Hint: As per Regulation 190A, activity of selling domain name for earning Royalty is → "other business/occupation"

Hence, CA Sumati is **guilty of professional misconduct under Clause 11 of Part I of Schedule I.**

Q85. A CAip, took over as executive chairman of Company on 1.4.19. On 10.4.19 he applied to the Council for permission

Hint: Explain Clause (11) of Part I of 1st Schedule CA Act 1949, → Mr. A is **guilty of professional misconduct**

Q86. C.A. Prabhu is a leading tax practitioner. He does **trading in commodity derivatives**. Is professional misconduct?

Hint: C-11, P-1, S-1 → trading in commodity derivatives which is not covered under general permission → **Guilty**

Q87. A CA in practice **entered into partnership with his uncle in Textile business**, which, however, did not take off.

Hint: CA will be guilty under **clause 4 & 11 of Part I** of First Schedule

Q88. M, a CA in practice, is the **Statutory Auditor of S Ltd.** for the year ended 31st March 2015. In January 2015, he was appointed as a **Director in H Ltd.**, which is the *holding Company of S Ltd.*

Hint: C-11, P-1, S-1, he can be a director of a company wherein he or any of his partners is not interested in such company as auditor, Hence it is **allowed for auditor under Clause 11** to become Director of Holding, **However:**

- Public conscience is expected to be ahead of law, so requirement of **independence should be interpreted much more strictly.**
- Members should thus not place themselves in position which would either compromise their independence.

Conclusion: auditor of a subsidiary cannot be a director of a holding company as it will affect his independence

Q89. CA Raghu is practicing CA, Sam, a student of CA Course approached CA Raghu to take guidance on some topics of Income-Tax related to his course. CA Raghu, on request started providing Private Tutorship to Sam.

Hint: CA. Ram would **not be held guilty** of professional misconduct

Q90. A CA in practice takes up the appointment as **managing director of a public limited company**

Hint: It does not prohibit a CA from being a director of a company, except MD or a whole-time director, Hence Guilty.

Q91. Mr. B a practicing CA holding a valid COP. He **accepted the appointment as Director** of the Green World Co. Ltd. Mr. C, a partner of Mr. B is statutory auditor of the said company.

Hint: Explain **Clause 11 of Part I of the First Schedule & Clause 4 of Part I of the Second Schedule**

- As well as explain **Section 141(3)(c) of Co. Act 2013** i.e., Disqualifies a person to be appointed as an auditor if he is a partner of an officer of the company
- Further Sec 141 (4), Requires the appointed auditor to **vacate his office if he incurs any of the disqualifications**
- Conclusion:
 - **Mr. B will be held for Professional Misconduct under Clause 11 of Part 1** of 1st Schedule to CA Act, 1949.
 - Mr. C, a partner of Mr. B, **should vacate office as per Sec. 141(4)** of Co. act, being disqualified u/s 141(3)(c)

Q92. Mr. Kartik a CAip has been appointed **editor of a monthly journal which analyses performance of Stock Market.**

Hint: → C-11 permits editorship of professional journals, But performance analysis of stock market & mutual fund schemes cannot be treated as professional journal → hence, Mr. Kartik held guilty of professional misconduct

Q93. CA. Moni a CAip. → was offered editorship of a 'Company Audit' Journal which she accepted.

Hint: Clause 11 **permits editorship of professional journals**, hence no misconduct arises on part of Manav.

Q94. CA. Mansi is a CAip. Due to this passion of her, she also wrote a cookery book "Delight your tummy".

Hint: Clause 11 **permits authorship of any book**, hence no misconduct arises on part of CA. Mansi.



Q95. CA. AB, a practicing CA, is a **promoter director** of ABG Pvt. Ltd. and moreover he is also a **sleeping partner** in his family business of garments manufacturing firm. Is CA. AB liable for professional misconduct ?

Hint: Explain Clause 11, P1, S1 → **To accept the position of MD** → **to obtain prior permission**. Furthermore **he can't take part in his family business even as a sleeping partner** without taking prior approval.

Promoter/Promoter Director - There is no bar for a member to be a promoter / signatory to the MOA / AOA of any company. There is also no bar for such a promoter / signatory to be a Director Simplicitor of that company (not required to obtain specific permission of the Council in such cases).

- **As Promoter Director**- **Not guilty** of professional misconduct under Chartered Accountants Act, 1949
- **As Sleeping Partner**- **guilty** → **as she did not obtain prior approval of the Council**. C-11, P-I of 1st Schedule

Q96. Holding Company (HH Ltd) offered Mr. D (Auditor of Subsidiary) to take up the position of Director (not MD/ WTD) of HH limited. At the same time, Mr. D's friend approaches him with an assignment to act as a Recovery Consultant for a bank.

Hint:

Ethical Standards Board (ESB) noted that public conscience is expected to be ahead of law. Members, therefore, are expected to **interpret the requirement as regards independence much more strictly** than what the law requires and should not place themselves in positions which would either compromise or jeopardise their independence. In the view of the above, the Board, via a clarification, **decided that the auditor of a Subsidiary company cannot be a Director of its Holding company**, as it will affect the independence of the auditor.

Mr. D should not accept as director of HH Limited. However, **can act as a recovery consultant for a bank**.

Q97. Sanyam, a CA in practice is **owner** of **3 agriculture lands**. he **started carrying out agricultural activities**.

Hint: agricultural activities which is covered under the general permission. **not guilty** under C-11 of P-I of S-I

Q98. CA. Bahubali a CAip. Is **Special Executive Magistrate**. → He also took over as the **executive chairman** of Software Company on 1.4.2022. Does **trading in commodity derivatives**. However, he has **got special permission of Council of ICAI for becoming executive chairman and for trading in commodity derivatives**.

Hint: Clause (11) of Part I of First Schedule:

- **Not guilty** for acting as **Special Executive Magistrate** as it is covered under the **general permission**.
- **Not guilty**, for **Executive Chairman & trading in commodity derivatives** as it took **Special permission** for the same

Clause 12 : Sign by other than CA partner:

A CA in Practice is deemed to be guilty of professional Misconduct if he:

- a person **not being a member** of the institute in practice, or
- a member not being his **partner (So only CAip + Partner: Not employee)**
- to sign on his behalf or on behalf of his firm,
- any **Balance Sheet, P&L A/c, Report** or Financial Statements

Points to remember:

Permitted:	Council has clarified that power to sign routine documents on which a professional opinion or authentication is not required to be expressed may be delegated and such delegation will not attract provisions of this clause. Examples of such instances are - Issue of audit queries during the course of audit. - Asking for information or issue of questionnaire. - Letter forwarding draft observations/financial statements. - Initiating and stamping of vouchers and of schedules prepared for the purpose of audit. - Acknowledging and carrying on routine correspondence with clients. - Issue of memorandum of cash verification and other physical verification or recording the results thereof in the books of the clients. - Issuing acknowledgements for records produced. Raising of bills and issuing acknowledgements for money receipts. Attending to routine matters in tax practice, subject to provisions of Section 288 of Income Tax Act.



- (x) Any other matter incidental to the **office administration and routine work** involved in practice of accountancy.

Q99. a practicing CA gives power of attorney to an employee CA to sign reports and FS on his behalf.

Hint:

- **Clause (12) of Part I of First Schedule** to the Chartered Accountants Act, 1949
- The term 'Financial Statement' for this purpose would cover an examination of the accounts or financial statements given under a statutory enactment or otherwise.
- Further, **Clause (1) of Part II of the 2nd Schedule** to the CA Act, 1949 states that a member of the Institute, whether in practice or not, shall be deemed to be guilty of professional misconduct, if he contravenes any of the provisions of this Act or the regulations made there under or any guidelines issued by the Council
- Conclusion: Accordingly, S is **guilty of professional misconduct** under C-12, P1, S-1 & also under C-1, P-II, S-II

Q100. Mr. A a CAip → delegated authority to Mr. Y a CA his **employee for taking care of routine matters of his office.**

- (i) He **issued the audit queries** to client which were raised during the course of audit. → **Allowed (it's a Routine work)**
 (ii) He issued **production certificate to a client under the GST Act.** → **It's Not a Routine Work, He is Guilty**
 (iii) He **attended the Income Tax proceedings for a client as authorized representative** → **Allowed**

Please comment on eligibility of Mr. Y for conducting such jobs in name of M/s A & Co. and liability of Mr. A.

Hint: Explain **Clause (12) of Part I of First Schedule** to the Chartered Accountants Act, 1949

Q101. Mr. S, the auditor of ABC Pvt. Ltd. has **delegated following works to his articles and staff:**

- (1) Issue of audit queries during course of audit. → **Allowed** (2) Issue of memorandum of cash verification → **Allowed**
 (3) Letter forwarding draft observations on FS → **Allowed** (4) Signing FS of company → **Not Allowed**

Hint: → Explain → C-12, P-1, S-1

Q102. CA. Smart, a practicing CA was on Europe tour between → Meanwhile one of his **clients requesting for a stock certificate** to be produced to the bank urgently, CA. **Smart directed his assistant**, who is also a CA to sign.

Hint: → CA. Smart is guilty of **professional misconduct**, C-12, P-1, S-1 to the Chartered Accountants Act, 1949.

Q103. During absence of Mr. 'Y', His assistant has conducted the under mentioned jobs in the name of M/s K & Co.

- a) He issued **Net worth certificate** to a client for furnishing to a Bank. → **Not Allowed**
 b) He **attended the GST proceedings** for a client as authorized representative before GST Authorities. → **Allowed**

➤ **First Schedule : PART-2 of schedules of CA Act, 1949 : Member in Service-**

Clause-1 A CA in service is guilty of professional misconduct if he:

- **pays** or allows or agrees to pay directly or indirectly to any person
- **any share in the emoluments** of the **employment** undertaken by him (*Not even to another CA*).

Clause-2 A CA in service is guilty of professional misconduct if he:

- accepts or **agrees to accept** any part of fees, profits or gains **from**
- a **lawyer**, a **CA or broker engaged by such company**, firm or person or **agent or customer** of such company, firm or person
- by way of **commission or gratification**

Q104. Mr. 'C', a CAip while in employment also, **recommends a particular lawyer to his employer.** The lawyer, out of professional fee received from employer paid a particular sum as **referral fee** to Mr. 'C'.

Hint: Explain **Clause (2) of Part II of First Schedule** of the Chartered Accountant Act, 1949 → **Mr. C is guilty.**

➤ **First Schedule : PART-3 of schedules of CA Act, 1949 : Member's Generally-**

Clause-1 A CA is deemed to be guilty of professional misconduct if he **Not being a fellow** of the Institute **but acts** as a **fellow** of the Institute.

Clause-2 A CA is deemed to be guilty of professional misconduct if he

- does **not supply the information** called for, or
- does **not comply** with the requirements asked for by
- the **Institute, Council or any of its committees, Director** (Discipline), Board of Discipline, Disciplinary Committee, **Quality Review Board** or the appellate authority.

Clause-3 A CA is deemed to be guilty of professional misconduct if he

- **while inviting professional work from another chartered accountant** or
- while **responding to tenders** or enquiries or
- while **advertising through a write up** or anything as provided for in clauses (6) and (7) of Part I of this schedule,
- **gives information knowing it to be false.**

Q105. Mr. 'G', while applying for a **certificate of practice (COP)**, did not fill in the columns which solicit information about his engagement in other occupation or business, while he was indeed engaged in a business.

Hint: Explain **Clause (2) of Part III of First Schedule** to the Chartered Accountants Act, 1949 → **Guilty**

- while applying for a COP, did not fill in the columns which solicit information about his engagement in other occupation or business, while he was indeed engaged in a business Details of engagement in business need to be disclosed.

Q106. Mr. X, a CA, employed as a paid Assistant with a CA firm, leaves the services of the firm on 31st Dec, 2019. Despite many reminders from ICAI he fails to reply regarding the date of leaving the services of the firm.

Hint: held **guilty** of professional misconduct as per Clause (2) of Part III of the First Schedule to the CA Act, 1949.

Q107. The ICAI required that all firms having networking relationship with any other entity **need to furnish information online**. XYZ Associates **failed to respond**. Comment on this with reference to Professional misconduct.

Hint: held **guilty** of professional misconduct as per Clause (2) of Part III of the First Schedule to the CA Act, 1949.

➤ **First Schedule : PART-4 – Other Misconduct : Member's Generally-**

- A member of the Institute, whether in practice or not, shall be deemed to be **guilty of other misconduct**, if he
1. is held **guilty of any civil or criminal court** for an offence which is punishable with **imprisonment for a term not exceeding 6 months**.
 2. In the opinion of the Council brings **disrepute to the profession** or the Institute as a result of his action **whether or not related to his professional work**.

Some illustrative examples, where a member may be found guilty of "**Other Misconduct**", under the aforesaid provisions rendering, himself unfit to be member are:

- (i) Where a CA had adopted **coercive methods on a bank for having a loan sanctioned** to him.
- (ii) Where a chartered accountant **retains the books of account** and documents of the client and **fails to return these to the client on request without a reasonable cause**.
- (iii) Where a chartered accountant makes a **material misrepresentation**.
- (iv) **Misappropriation by office-bearer of a Regional Council** of the Institute, of a large amount and **utilisation thereof for his personal use**.
- (v) **Non-replying within a reasonable time** and **without a good cause** to the letter of the **public authorities**
- (vi) Where a chartered accountant **uses the services of his articled** or audit clerk for purposes **other than professional practice**.

Q108. Write a short note on Other Misconduct.

Hint: Explain Part 4 of 1st schedule (along with above given examples) as well as part 3 of 2nd Schedule

Q109. ICAI Illustration: YKS & Co., a proprietary firm of Chartered Accountants was **appointed as a concurrent auditor** of a bank. YKS, the proprietor, **used his influence to get a loan** and thereafter **failed to repay** the loan.

Hint: ➔ "other misconduct" of CA Act, 1949 → Explain C-2, P-4, S-1. ➔ Here the CA is expected to maintain the highest standards of integrity even in his personal affairs and any deviation from these standards calls for disciplinary action ➔ Explain the present Case ➔ This brings disrepute to the profession of a CA. ➔ **Guilty**

Q110. Mr. Chintamani, a CAip has been **elected as the treasurer the Regional Council** of the ICAI. ➔ it was found that



Mr. Chintamani had received a personal benefit of ₹40,000 from the tour organized by ICAI Committee.

Hint: → Explain C-2, P-4, S-1 → guilty of other misconduct

Q111. CA K is contesting Central Council Elections of Institute, engages his Article Assistant for election campaigning.

Hint: Explain Clause (2) of Part IV of First Schedule, He would be guilty of professional misconduct,

• A member may be found guilty of "Other Misconduct", if he uses the services of articles for personal work.

Q112. Mr. R, a CAip approached Manager of a Bank for a loan of Rs. 25 lakhs. He also informed the Manager that if the loan is sanctioned, the I.T return of the Manager will be filed without any fees, as quid Pro quo for the loan

Hint: Mr. R will be held guilty of other misconduct under Clause (2) of Part IV of S-1 CA Act, 1949.

Q113. A CA has forged the Will of his Late uncle (MTP'25)

Hint: Guilty C-1, P4, S1 → CA is expected to maintain the highest standards of integrity even in personal affairs

Q114. Ms. Preeto, a CA, had an account with a bank. The normal balance in this account remained at a level below ₹ 5,000. The bank inadvertently credited this account with a cheque of ₹2,70,000 belonging to another account holder. When CA. Preeto came to know about this she withdrew the amount of ₹2,75,000 and closed the bank account. Can the bank approach the ICAI for disciplinary action against CA. Preeto? Or

CA has issued a cheque for repayment of Loan, which was bounced back. Comment w.r.t the CA Act, 1949

Hint: Explain Clause (2) of Part IV of First Schedule

- liable to disciplinary action U/S 21 of the CA Act, if he is found guilty of professional or "Other Misconduct".
- cheques were dishonored due to insufficiency of funds, the drawer will be held guilty of offence under Negotiable Instruments act, 1881 and consequently he would be held guilty of "Other Misconduct".

➤ **Second Schedule : PART-1 – Professional Misconduct i.r.t. Members in Practice:**

Clause 1: Confidentiality in All engagement:

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- **discloses the information** acquired in the course of his professional engagement
- to any person other than his client so engaging him **without the consent of his client** or
- **otherwise than as required by any law** for the time being in force.

Points to remember:

- **Not apply** when information is **available publicly** (i.e., Listed company published financials)
- Principal Auditor do **not have right of access** to the audit **working papers of the branch** auditors
- In case fraud is identified in Listed company, Report to CG u/s 143(12), Not to ROC
- There is a difference between sharing of working papers and sharing of information. So far as the information is concerned, member can provide the same to the client or to a Regulatory body after obtaining the consent of the client.

Q115. Mr. Parekh,. During the course of his presentation he shared some of the vital information of his client's.

Hint: Explain Clause (1) of Part I of the Second Schedule to the CA Act, 1949 → Guilty

Q116. Due to some disputes, Company removed the auditor → so auditor made the complaint to the ROC → including non-existence of fixed assets, bogus creditors etc. (MTP'25)

Hint: An accountant, in public practice, has access to a great deal of information of his client which is of a highly confidential character. → So maintain the dignity and status of the profession → should treat such info as having been provided to him, only to facilitate the performance of his professional duties.

- The Code of Ethics further clarifies that such a duty continues even after completion of the assignment.
- In Given case, Auditor made a Voluntary disclosure → without consent of Client, or Without Law requirement
- **So, Guilty** under Clause (1) of Part I of the Second Schedule of CA Act 1949

Q117. XYZ Co. Ltd. has applied to a bank for loan facilities. The bank on studying the FS of the company notices that you are the auditor and the banker called you to asks for your opinion regarding the company and also asks for detailed information regarding a few items in the financial



Hint: Explain **Clause (1) of Part I of the Second Schedule** of the Chartered Accountants Act, 1949

- **SA 200** → the auditor should respect the confidentiality of information acquired in the course of his work and should **not disclose any such information to a 3rd party without specific authority or unless there is a legal or professional duty to disclose**"
- Thus, there is no requirement compelling the auditor to divulge information obtained in the course of audit and included in the working papers to any outside agency except as and when required by any law

Q118. A CAip was engaged by a **businessman** to represent him before the tax authorities on current matters. he came across certain documents pointing of **tax frauds in preceding years for which the client was not represented by him**. Is the member liable to disclose the existence and contents of the documents to tax authorities?

Hint: Explain **Clause (1) of Part I of the Second Schedule** to the Chartered Accountants Act, 1949

- **Code of Conduct:-** In respect of taxation matters, the code of conduct recommends that **"If the fraud discovered by the member, relates to the accounts or tax matters of the client for past year(s) for which the client was not represented by the member the client should be advised to make a disclosure. The member may however, continue to act for the client in respect of current matter, but is under no obligation so to continue"**
- Member is **not liable to disclose** the existence and contents of the documents to tax authorities.

Q119. in the course of the audit of a listed company discovered serious violations of the provisions of the companies Act, 2013, Non Existence of fixed assets, bogus creditors → **informed the registrar of companies (ROC).**

Hint: **Clause (1) of Part I of the Second Schedule,**

Section 143(12) of Co. Act 2013 if an auditor has **reason to believe that an offence involving fraud** is being or has been committed against the company by employees of company, → he shall **immediately report to Central Govt.**

An accountant, in public practice, has access to a great deal of information of his client which is of a highly **confidential** character. So for maintaining **dignity & status** of profession.

He made voluntary disclosure of the information acquired during the professional engagement without the consent of the client and without there being any requirement in law → **Mr. C will be guilty.**

Clause 2 : Certify F.S without Examination: (Along with Clause 7 & 8 of S-II, P-1)

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- **certifies** or submits in his name or in the name of his firm a report of an examination of **financial statements**
- **unless the examination** of such statements and the related records has been made by:
 - ✓ him or
 - ✓ by a **partner** or
 - ✓ an **employee** in his firm or
 - ✓ by **another CA in practice.**

Q120. Mr. A, a CA was auditor of 'A Ltd. During the FY 2019-20, the **investment appeared in the Balance Sheet of company of ₹10 lakhs & was same amount as in the last Yr.** Later on, it was found that the company's investments were only ₹25,000, but the **value of investments was inflated** for purpose of obtaining higher loan.

Hint: Explain **Clause 2, 7, 8 of Part I of Second Schedule**

Auditor's responsibility:-

- The **primary duty of physical verification** and valuation of investments **is of the management.**
- However, the auditor's duty is also to **verify the physical existence** and valuation of investments placed, at least **on the last day of the accounting year.**
- The auditor should **verify the documentary evidence for the cost/value** and physical existence of the investments at the end of the year.
- He should **not blindly rely upon the Management's representation**

In the instant case:- Such non-verification happened for two years. It also appears that auditors failed to confirm the value of investments from any proper source. In case auditor has **simply relied on the management's representation, the auditor has failed to perform his duty.**

Mr. A, will be held liable for **professional misconduct under Clauses (2), (7) and (8) of Part I of S-II**



Clause 3: Certify Estimates & Contingent Earnings:

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- **permits his name** or the name of his firm to be **used in connection with an estimate of earnings contingent upon future transactions** in manner which may lead to the belief that he vouches for the accuracy of the forecast.

Points to remember:

Participation in preparation of forecasts & their review: SAE 3400 "The Examination of Prospective Financial Information" **allows to a member to review the prospective financial information** subject to following conditions: **(SAB- Not vouch)**

- (a) He indicates the **Source** of information.
- (b) He gives in his report the major **Assumptions** made in arriving at the forecasts.
- (c) He indicates the **Basis of forecasts.**
- (d) He does **not vouch for the accuracy** of the forecasts.

Q121. Mr. 'E', a practicing CA, was **requested by one of his client to prepare a projection for next 5 years** and also a report on the same. Mr. 'E' after prepared the same **stated in his report 'The sources of information, the basis of forecasts and also the major assumptions** made in arriving at the forecasts. also stated that he does **not vouch for the accuracy** of the forecasts.

Hint: Explain C-3, P-1, S-2 → SAE 3400 "The Examination of Prospective Financial Information", Provides that the management is responsible for the preparation and presentation of the prospective financial information, including the identification and disclosure of the sources of information, the basis of forecasts and the underlying assumptions.

There is no violation of the Chartered Accountants

Q122. a CA prepares and **certifies projected FS** of his client & Client **forwarded the same to banks to secure loans.**

Hint: Explain Clause (3) Part I of Second Schedule, & Explain SAE 3400 as explained in above qn,

Auditor's Responsibility:-

- The auditor may be asked to **examine and report on the prospective financial information to enhance its credibility**, whether it is intended for use by third parties or for internal purposes.
- Thus, while making report on projection, the auditor **need to mention that his responsibility is to examine the evidence supporting the assumptions** and
- Other information in the prospective financial information, his responsibility does not include verification of the accuracy of the projections; therefore, he does **not vouch for the accuracy of the same.**

Conclusion: - Thus, Mr. L will be held **guilty of misconduct** in view of above

Clause 4 : Express opinion- When Substantial interest : (Along with Clause 9 of S-I, P-1)

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- **expresses his opinion on financial statements** of any business or enterprise
- in which he, his firm or a partner in his firm has a **substantial interest.**

Points to remember:

- **Can-not** even do **bookkeeping** (Write) client books
- **Allow** to do **cost evaluation** of client which he is auditing (**Not allowed** to do **cost audit**)
- **Not to permit a CA in employment** to **certify the financial statements** of the company **in which he is employed**
- The Council has also decided that a Chartered Accountant should **not by himself** or in his firm name:
 - ✓ **accept the Auditorship of a college**, if he is working as a **part-time lecturer** in the college.
 - ✓ accept the **Auditorship of a Trust** where his partner is either an employee or a **trustee** of the Trust.
- **A member of the Institute cannot express the opinion in the following cases:**
 - ✓ Where the member himself is owner/partner of concerned business.
 - ✓ Where the partner/relative of the member has substantial interest in concerned business.
 - ✓ Where the member himself or his partner or relative is a director or in the employment of an officer or an employee of the company.



- A **statutory auditor cannot** be the **internal auditor** of the same entity.
- An **internal auditor cannot** be the **tax auditor/GST Auditor** of the same entity.
- A member shall **not accept the assignment of audit** of a Company for a **period of 2 years from the date of completion of his tenure as Director**, or resignation as Director of the said Company.

Q123. Mr. D, a practicing CA, is appointed as a Director Simplicitor in XYZ Pvt. Ltd. After one year of appointment, Mr. D resigned as the Director and accepted the Statutory Auditor position of the company. Is Mr. D right?

Hint: Explain Clause (4) of Part I of the Second Schedule → GUILTY

- Sec 141 of Co. Act, 2013 specifically prohibits a member from auditing the accounts of a company in which he is an officer or employee, underlying principle of independence of mind is equally applicable tax audits also.
- not accept assignment of audit of a Company for a period of 2 Yr from date of completion of his tenure as Director

Q124. A firm of CA was appointed by a company to evaluate the costs of the various products manufactured by it for its information system. One of the partners of the firm was a Non-Executive Director of the company

Hint: Not constitute any misconduct in Clause (4) of Part I of the Second Schedule

Q125. Mr. Shah, a CA certified the FS of a company in which his wife is a Director holding substantial interest

Hint: Explain C-4, P-I, S-II, & Sec 141(3)(f) of Co. Act, 2013 → Mr. Shah shall have to vacate the office accordingly

Q126. CA Dev is practicing. He issued 'Turnover Certificate' for M/s. ASAUS Traders to be forwarded to the Bank for the purpose of availing Loan facility. Brother of CA Dev was proprietor of M/s. ASAUS Traders.

Hint: Explain Clause (4) of Part I of Second Schedule → CA Dev is guilty

Further, it is not permissible for a member to undertake the assignment of certification, wherein the client is relative of the member. "relative" refer definition mentioned in Accounting Standard (AS)-18 (Brother is included)

Clause 5 : Not disclose material fact in FS: (Along with Clause 6 of S-II, P-1)

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- fails to **disclose a material fact**
- **known to him** which is not disclosed in a financial statement, but disclosure of which is necessary in making such FS not misleading where he is concerned with that financial statement in a professional capacity.

Points to remember:

- **Financial statements** would cover both reports and certificate
- CA had been held **guilty** for his **failure to report to shareholders** about the **non-creation of a sinking fund** in accordance with the Debenture Trust Deed.
- CA had been held **guilty** of professional misconduct by Supreme Court for having **Not disclosed the fact to the beneficiaries** that **large amount of loan have been given out of the funds of an Employees Provident Fund** to the Employer Company in contravention of the Rules of the Provident Fund

Q127. Auditor came to know that the company has taken a loan of ₹10L from Employee Provident Fund (contravention of the applicable rules). The said loan was not reflected in books. Auditor ignored this info in his report.

Hint: Explain Clause (5) of Part I of Second Schedule to the Chartered Accountants Act, 1949 → Guilty

Q128. ENI Ltd; has created a separate Trust "ENI Employees Gratuity Fund Trust". Both the Company and Trust are under the same management. Mr. A is the auditor of both the entities. Mr. A has observed that some part of the expenditure was not applied towards the objects of the Trust. He informed the matter to the Board of Trustees through a separate report but did not qualify the Audit Report of the Trust.

Hint: Aware of the contraventions, However, he had issued the annual accounts without any qualification, Chartered Accountant is guilty of professional misconduct

Q129. CA. Dice had signed the Balance sheet of QR Ltd. for the year ended 31/03/19 which failed to give disclosure of the charge created for Rs.4.35 Crores against the Corporate Guarantee given in favour of a Group Company. Group size of balance sheet is 26.11 Crore

Hint: → this clause refers to failure to disclose a "material fact", which is known to him, in a financial statement reported on by the auditor. It is obvious, that before a member could be held guilty of misconduct, materiality has to



be established. The determination of materiality has been provided in SA 320,

FRF often discuss the concept of materiality in the context of the preparation and presentation of FS.

In Given Case → 4.45 Crore seems material (group B/S of 26.11 Crore) → So Misconduct → C-5, P-1, S-2

Clause 6: Fail to report material misstatement: (Along with Clause 5 of S-II, P-1)

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- fails to **report** a material misstatement known to him to appear in a financial statement with which he is concerned in a professional capacity

Points to remember:

Company did **not provide for depreciation** & **auditors fails to report**

Q130. A practicing CA was appointed to represent a company before the tax authorities. He submitted certain information and explanations to the authorities on behalf of his clients, which found to be false and misleading.

Hint: Explain Clause (5) & Clause (6) of Part I of Second Schedule to the CA Act, 1949 → Not Guilty

- In given case, the CA had submitted the statements before the taxation authorities. These statements are based on the data provided by company. Although the statements prepared were based on incorrect facts and misleading, the CA had only submitted them acting on the instructions of his client as his authorized representative

Q131. Mr. X partner of X & co. CA, has compiled and signed the balance sheet of False Limited., for submission to the bankers of the said company. Mr. X has also compiled and signed at the request of the company another balance Sheet inflating the value of assets by 20%, for submission to a term lending institution. Both the Balance Sheets were not in conformity with the books of accounts maintained by the company.

Hint: Mr. X would be held guilty under clauses 5 and 6 of Part I of Second Schedule

Clause 7: Grossly Negligent : (Along with Clause 8 of S-II, P-1)

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- Does **not** exercise due diligence, or is grossly negligent in the conduct of his professional duties

Points to remember:

- Example of Gross negligence:
 - ✓ Failure to check the bank balances with the pass books of the banks and to obtain certificates of balances from the bankers in respect of those balances.
 - ✓ Not completing his work relating to the audit and non- submission of audit report in due time to enable the company to comply with the statutory requirement in this regard.
 - ✓ Issuing wrong consumption certificate in respect of raw material and components without examination of stock register and other relevant matters
 - ✓ Accepting arbitrary valuation of closing stock without any verification.
 - ✓ Certified figures to be circulated in newspaper based on MIS report, without any verification.
- However:
 - ✓ Auditor appointed for audit of FS of HO, NOT liable for branch
 - ✓ Assessee maintain 2 types of BOA → Auditor is not liable

Q132. CA Chiranjiv who conducted ABC audit of a Haryana daily 'New Era' certified the circulation figures based on Management Information System Report (M.I.S Report) without examining the books of Account.

Hint: → Explain Clause (7) of Part I of Second Schedule of Chartered Accountants Act, 1949

In the instant case, CA Chiranjiv did not exercise due diligence and is grossly negligent in the conduct of his professional duties since he certified the circulation figures without examining the books of accounts.

To ascertain the number of paid copies verification of remittances from the agents, credit allowed to the agents for unsold copies returned, examination of books of account is essential. Further certification of circulation figures based on statistical information without cross verification with financial records amounts to gross negligence and failure to exercise due diligence → guilty of professional misconduct as per Clause (7) of Part I, 2nd Schedule.

Q133. Mr. D, a CAip, did not complete his work relating to audit and had not submitted his audit report in due time



Hint: guilty, C-7, P-1, S-II

Q134. Mr. Yuvi, a CAip, is auditor of Prime Ltd. He **advised the Managing Director (MD)** of company to include 'orders under negotiation' in sales, to **reflect higher profit** and better financial position → Mr. Yuvi, thereafter, gave clean reports on balance sheet prepared accordingly without examining the accounts. Comment as per CA Act.

Hint: Mr. Yuvi, is **grossly negligence** in conduct of his professional duties. **Further, he has also brought disrepute to the profession by advising unethical practice** to the MD of company, → **guilty** → **C-7, P-1, S-II & C-2, P-4, S-I**

Q135. The Cashier of a company committed a fraud and absconded with the proceeds thereof. In the course of the audit, at the end of the year, the **auditor failed to discover the fraud**. After the audit was completed, however, the fraud was discovered by the Chief Accountant. Investigation made at that time indicates that the **auditor did not exercise proper skill and care** & performed his work in a desultory & haphazard manner → disciplinary proceedings.

Hint: Explain **Clause (7) of Part I of the Second Schedule**:

- Auditor did not exercise proper skill and care & that he performed his work in desultory & haphazard manner
- Cash is a very significant item in any situation and the fact that the cashier had left during the year without notice should have placed the auditor on alert as regards the cash book
- **As per SA 240** → it can be concluded that the auditor did not plan & perform the audit with attitude of professional skepticism. Thus, having regard to this and a fraud has actually taken place during the year, committed by the absconding cashier, it is reasonable to think that prima facie there is a case against the auditor for gross negligence.

Conclusion: - Such instances require **reference to Disciplinary Committee** of the Council of the Institute.

Q136. Mr. Fair a practicing CA was appointed to carry out a **Balance Sheet Audit** of a Non-Profit Organisation. The **Internal Auditors detected certain irregularities** in the Branch which Mr. Fair had failed to detect.

Hint: C-7, P1, S-II, Statutory auditor has been appointed to carry out the balance sheet audit, he is not required to check the matters relating to branch in depth. Hence there is **no professional misconduct on part of Mr. Fair**.

Q137. A search under Sec 132 of Income Tax Act in the premises of a leading merchant led to the discovery of 2 sets of account books - one set to record all the income correctly and second to record only limited income. A CA has issued audit report on the basis of **second set of books**. What would be your Answer if the first set of account books carried evidence of checking by the CA?

Hint: Explain Clause 7, It has been found that **client has maintained two sets of account books** - one set to record all the income correctly and second to **record only limited income**. CA has issued audit report on the basis of second set of books. In this case, there will not be any misconduct on part of CA if **the auditor is not aware of the first set of books**. However, if there exist evidences that auditor is aware of first set of books also, then he will be deemed to be guilty of professional misconduct being grossly negligent in performance of his duties.

Hence, **not be deemed to be guilty** of misconduct

Q138. Mr. B a CAip expressed his opinion on the FS → It was later found that the **closing stock was valued arbitrarily** by mgmt which was **accepted by him without verification & big amount of revenue expenditure was capitalized**.

Hint: Mr. B is **guilty of gross negligence** by virtue of clause 7 of Part I of second schedule

Q139. Mr. Mohan is a practicing CA → He **issued a certificate of consumption which did not reflect the correct factual position** of the consumption of raw material by the concerned entity. It is found that the **certificate is given on the basis of data appearing in the minutes of meeting** of the Board of Directors

Hint: He is **Guilty of Professional Misconduct** under **Clause (2), Clause (7) & Clause (8)** of Part I of 2nd Schedule

- He has **failed in his duty of examining the record**.
- He has **relied on the minutes of BOD meeting which is not proper evidence** to show the consumption of raw material.
- The relevant record of production and stock register should have been scrutinized thoroughly and properly.

Q140. Nam & Co, conducted **Stock Audit** of DEF Ltd. as per instructions issued by HEG Bank. However instead of visiting the site → the firm **relied on the Management Information Systems report** along with inspections reports and **photographs of Stock taken by the employees** of DEF Ltd.. Comment with reference to the CA Act, 1949.

Hint: Held **guilty of Professional Misconduct** under **Clause (2), (7) & (8) of Part I of Second Schedule**

- Explain Clause (7) of Part I of 2nd Schedule to CA Act, 1949,
- It is a vital clause which usually gets attracted whenever it is necessary to judge whether the accountant has



honestly and reasonably discharged his duties. The expression negligence covers a wide field and extends from the frontiers of fraud to collateral minor negligence.

- To conduct stock audit, ascertainment of existence and physical condition of stocks, cross tallying the stock with Stock statement submitted by bank borrower, correct classification of stocks for valuation purpose etc. is essential. Further submitting stock audit report without physically verifying the stock amounts to gross negligence.

Q141. Aagam Private Limited requested CA Sheetal, a practicing CA, to digitally sign the form related to resignation of Mr. Rohit, one of the Director of Aagam Private Limited, along with the copy of Resignation Letter to be uploaded on the website of Registrar of Companies. The **signature of Mr. Rohit was simply copied and pasted by another Director** of Aagam Private Limited. CA Sheetal, **without verifying the genuineness of the resignation letter**, digitally signed the form and the said form was uploaded on the website of Registrar of Companies.

Hint: Explain Clause (7) of Part I of Second Schedule → Guilty

Due to forged resignation letter, the resignation of Mr. Rohit from directorship of the Aagam Private Limited had been occurred. It was noted that CA Sheetal had not taken any step to verify forged signature on resignation letter which anyone would have taken in normal circumstances.

Clause 8 : Fail to obtain sufficient information : (Along with Clause 7 of S-II, P-1)

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- **Fails to obtain sufficient information**
- which is **necessary for expression of an opinion** or its exceptions are sufficiently material to negate the expression of an opinion

Q142. Z, a practicing CA issued a certificate of circulation of a periodical without going into the most elementary details of how the circulation of a periodical was being maintained i.e. by not looking into the financial records, bank statements or bank pass books.

Hint: Explain Clause (8) of Part I of Second Schedule to the CA Act, 1949 → Guilty

- The chartered accountant should not express his opinion before obtaining the required data and information. As an auditor, Mr. Z ought to have verified the basic records to ensure the correctness of circulation figures

Clause 9: Not follow Audit procedures (SA's): (Along with Clause 7 & 8 of S-II, P-1)

A CA in practice shall be deemed to be guilty of professional misconduct if he -

- **Fails to invite attention** to any **material departure**
- **from the generally accepted procedure of audit** applicable to the circumstances

Points to remember:

- i.e., Not followed SA's, Guidance note etc., & also not drawn attention in audit report regarding its departure.
- **For Audit of Listed Company:** **Peer Review Certificate** needed,
- Mention & **generate UDIN**

Q143. CA K is a Practicing CA (name M/s K & Associates). LST Ltd, a **listed entity**, appointed M/s K & Associates as **Statutory Auditor** for the year ended 31st March, 2022. CA K signed the balance sheet of LST Limited. M/s K & Associates **never subjected themselves to the Peer Review process** of the Institute. CA Act implications ?

Hint: **(Full Qn is Covered in Additional PDF Booklet)**

Alternate 1:

Explain Clause (9) of Part I of the Second Schedule:

- audit should be performed in accordance with "**generally accepted procedure of audit applicable to circumstances**".
→ Pronouncements of Institute is issued by way of **Engagement & Quality Control Standards, Statements**, etc..
- **SEBI → Statutory audit of listed companies** under the Co. Act, 2013 shall be **done by only those auditors who have subjected themselves to the Peer Review & hold a valid certificate** issued by the Peer Review Board of ICAI.
- **In the given case CA K would be held guilty under C-9, P-1, S-II, as CA K did not comply with SEBI Notification.**

Alternate 2:

- **C-1, P-II of S-II, → guilty → if he contravenes any provisions of this Act, or any guidelines issued by Council.**
- **The Statement on Peer Review shall be deemed to be a guideline of the Council.**



- As per the Statement every Practice Unit including its branches who has conducted Statutory Audit of Enterprises whose equity or debt securities are listed in India or abroad → subject to Peer Review
- Hence, CA K would be held **guilty** of professional misconduct under clause (1) of Part II of 2nd Schedule

Clause 10 : Client's money in different bank a/c:

A CA in Practice shall be deemed to be guilty of professional misconduct if he -

- **Fails to keep moneys of his client**
- **other than fees or remuneration** or money meant to be expended, **in a separate banking account** or to **use such moneys** for **purposes** for which they are **intended** within a reasonable time.

Points to remember:

In connection with compliance of Clause 10, Council has considered some practical difficulties of the members and the following suggestions have been made to remove these difficulties:

- Allow:** An **advance received by a CA** against services to be rendered does not fall under Clause (10) of Part I of the Second Schedule. (i.e, Branch visit expense paid to auditor in advance, before auditor gone for visit)
- Allow:** **Moneys received for expenses to be incurred**, for example, payment of prescribed statutory fees, purchase of stamp paper etc., which are intended to be spent within a **reasonably short time** need not be put in a separate bank account. For this purpose, the expression reasonably short time, would depend upon the circumstances of each case.
- Moneys received for expenses to be incurred which are not intended to be spent within a reasonably short time as aforesaid, should be put in a separate bank account immediately.
- Moneys received by a Chartered Accountant, in his capacity as trustee, executor, liquidator, etc. must be put in a separate bank account immediately.
- CA receive Rs.1 lacs on 01/09/2015 for advance tax installment to be paid on 15th Sep, 15th Dec, 15th Mar : So CA should keep balance money after remitting 1st installment in separate bank a/c. otherwise guilty**

Q144. A charitable institution entrusted ₹10L with its auditors M/s Ram a CA firm, to invest in a specified securities. The auditors **deposited it in their Savings bank A/c and no investment was made in the next 3 months.**

Hint: Explain Clause (10) of Part I of Second Schedule to the Chartered Accountants Act, 1949. → **GUILTY**

- If he should receive such funds, it would be his duty to deposit them in a separate banking account, and to utilise such funds only in accordance with the instructions of the client or for the purposes intended by the client.

Q145. M/s. ABC, a firm of CA **received ₹2 lakhs in March, 2015 from a client to pay the Advance Tax. However, the firm has used that money for its own purpose** and later on adjusted the same with the O/s fee payable.

Hint: Guilty of Professional misconduct under Clause (10) of Part I of Second Schedule.

Q146. Mr. Ram CA in practice has received 5 lacs rs. From client, which is to be return back when client will again come back from America. He accepted money in his saving bank account, and **for temporary purpose he used some part of money for his son birthday party, which he again compensated** before coming of client from America.

Hint: amounts to professional misconduct under Clause (10) of Part I of Second Schedule.

Q147. CA N was appointed as an auditor of JAL Ltd. The company has branches all over the state of Haryana. CA N, in consultation with mngt, **decided to Visit 6 out of 10 branches. mngt decided to pay him advance of Rs.2.00 Lacs against the estimated expenses of 2.50 Lacs on visits to be conducted as a part of services rendered. As agreed, Rs.2.00 Lacs was transferred in his Saving bank account from which he met all the expenses.**

Hint: "An advance received by a Chartered Accountant against services to be rendered does not fall under Clause (10) of Part I of the Second Schedule" In the given case, CA N was given an advance of Rs. 2 Lakhs against the estimated expenses of ₹ 2.50 Lakhs on visits to be conducted as a part of services rendered.

Applying the above, it can be concluded that CA N is **not guilty of professional misconduct**

➤ **Second Schedule, Part II "Professional Misconduct In Relation To The Members Of The Institute Generally":**



Clause 1:

A member of the Institute shall be deemed to be guilty of professional misconduct if he **contravenes** any of:
the **provisions of this Act or the Regulations** made thereunder or the **Guidelines** issued by the Council.

Points to remember:

The Regulations under which cases of contravention have generally come to the notice of the Council are the following:

Regulation 47:	Premium from Articled Clerks - prohibited
Regulation 48 :	Stipend to Articled Clerks - stipend to be paid on monthly basis (cannot defer beyond month, even if firm paying interest on that amount to article for delay, then also misconduct)
Regulation 190A:	Chartered Accountants not to engage in any other business or occupation (Refer Clause 11, Part I of First Schedule)
Regulation 192:	Restriction on fees (Refer Clause 10 of Part I of First Schedule)
Other regulations:	- Can train max 10 articles together - Articles timing: Not beyond 11:00 AM & Not before 5 PM - Article should work minimum 35 hrs a week & Max 45 hrs a week

Relevant Judgments:

- Entering into an **agreement to pay the articles clerk on annual basis**, results into violation of Regulation 48.
- Accepting a loan from an article or his relative** in case of engagement of the article results into violation of Regulation 47 (However **can take loan from Partner's article relative**)

Clause 2:

(link: Clause 1, S-2, P-1)

A member of the Institute shall be deemed to be guilty of professional misconduct if he being an **employee of any company**, firm or person, **discloses confidential information** acquired in the course of his employment **except as and when required by any law or except as permitted by the employer**

Clause 3:

(link: Clause 2, S-1, P-3)

A member of the Institute shall be deemed to be guilty of professional misconduct if he **includes in any information, statement, return or form to be submitted to the Institute, Council or any of its Committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the Appellate Authority, any particulars knowing them to be false.**

Clause 4:

A member of the Institute shall be deemed to be guilty of professional misconduct if he **defalcates or embezzles money received in his professional capacity**

Q148. Mr. Witty, the principal, offered an Article trainee, **stipend** at the rate of Rs. 2,000 per month to be **paid every 6th month along with interest at the rate of 10% per annum** compounded monthly.

Hint: failed to make the payments of stipend every month in accordance with Regulation 48. → guilty (C-1, P-II, S-2)

Q149. M/s. ABC, a firm of Chartered Accountants has **taken a loan for acquiring computers, from a company whose Managing Directors' son is an Articled Trainee with A, a partner of M/s ABC.**

Hint: Explain **Clause (1) of Part II of the Second Schedule,**

As per Regulation: Regulation 47 of the Chartered Accountant's Regulations, 1988

- Prohibits a member from accepting any premiums or loans, in connection with his engagement as articled clerk.
- In any form from an articled clerk directly or indirectly.

In Present case **articled trainee has no direct interest** in that company and the **loan was not related to his engagement**. There will **no professional misconduct**

Q150. Normal working hour of CA office were 11 am to 6 PM, However a **Article clerk was attending college classes from 10 am to 1.55 PM.** But when ICAI asked the Principal about college classes timing of article, He replied the timing of **7am to 9.30 am.** Will the Chartered Accountant be held guilty of professional misconduct?



Hint: guilty under C-1, P-2, S-II & under Clause 3 of Part II of S-II for submission of false info to the ICAI.

Q151. The manager of ZedEx (P) Ltd. approached CA. Vineet in the need of a **certificate in respect of a consumption statement** of raw material. **Without having certificate of practice (COP)**

Hint: Section 6 of CA Act, 1949 provides that no member of the Institute shall be entitled to practice (whether in India or elsewhere) unless he obtained from the Council a certificate of practice, will be held **guilty** → C-1, P2, S2

Q152. Mr. P and Mr. Q are running a firm of CA in the name of M/s PQ & Co. On 23.05.2015, they **included the name of Mr. R, a practicing CA, without his knowledge, as a partner while submitting an application for empanelment as auditor for Public Sector Bank.** However, Later they added Mr. R as a partner on 25.05.2015.

Hint: Mr. P and Mr. Q, both, would be held **guilty of professional misconduct: Clause (3) of Part II of 2nd Schedule**

➤ **Second Schedule, Part III “Other Misconduct In Relation To The Members Of The Institute Generally”:**

A member of the Institute, whether in practice or not, shall be deemed to be guilty of **other misconduct**, if he is guilty by any **civil or criminal court** for an offence which is **punishable for a term exceeding 6 months**

➤ **Council General Guidelines: (If not follow this guideline, then misconduct: C-1, S-2, P-II)**

Conduct of a Member being an employee :	A member of the Institute who is an employee shall exercise due diligence and shall NOT be grossly negligent in the conduct of his duties.	
Maintenance of books of accounts:	Q153. L, a chartered accountant did <u>not maintain books of account</u> for his professional earnings on the ground that his income is <u>less than the limits prescribed u/s 44AA</u> of the Income Tax Act, 1961. Q. CA in Practice <u>maintains notes in his mobile</u> where he records the fees received from clients. Answer: Maintenance of Books of Account: As per the Council General Guidelines 2008, under Chapter 5 on maintenance of books of accounts, it is specified that if a CA in practice or the firm of CA of which he is a partner fails to maintain and keep in respect of his/its professional practice, proper books of account including the 1) Cash Book and 2) Ledger, He is deemed to be guilty of professional misconduct. Accordingly, it does not matter whether section 44AA of the Income Tax Act, 1961 applies or not. Hence, Mr. L is guilty of professional misconduct. [not maintain proper books of accounts and writes the fees received from various clients in notes on his mobile. Notes maintained by him in mobile cannot be treated as BOA] Also Mention Clause (1) of Part II of the Second Schedule while Answering the question	
Tax Audit assignments:	About:	A member of the Institute in practice shall not accept, in a FY, more than the “specified number of tax audit assignments” under Section 44AB of the Income-tax Act, 1961
	60 per Partner:	60 audit per partner calculation (Whether Corporate or Non-Corporate assessee) [i.e., If the firm have 4 partner, then Total no. of audits firm can do is $60 \times 4 = 240$ Audits, Even a single partner can also sign all 240 audit report]
	Exclude 44AD etc	Audit u/s 44AD / 44 ADA / 44 AE of IT Act 1961 → Shall not be taken into account for purpose of reckoning the “specified no. of tax audit assignment”
	Part time P. Partner:	Part time Practicing Partner of a firm → shall not be included to calculate tax audit assignment of the firm



	Partner practice in personal cap.	where any partner accepts one or more tax audit assignments in his individual capacity, → the total number of such assignments which may be accepted by him shall not exceed the "specified number of tax audit assignments" in the aggregate.
	Partner in different firm:	where any partner is also a partner of any other firm, → the number of tax audit assignments which may be taken for all the firms together in relation to such partner shall not exceed the "specified number of tax audit assignments" in the aggregate
	HO & Branch:	The audit of the head office and branch offices of a concern shall be regarded as 1 tax audit assignment
	Branches	One or more branch of the same concern → 1 tax audit
	Joint audit	Even accepted as Joint Audit with other firm → then also will be counted in Limit
	Each yr audit	In computing the "specified number of tax audit assignments" each year's audit would be taken as a separate assignment.
	Q154. Mr. Gaurav is a partner in M/s. XYZ & Co., a firm of CA with 6 partners. During year 2020-21, Mr. Gaurav alone signed 290 tax audit reports consisting corporate & non-corporate assesses Hint: - As per Council General Guidelines 2008, a member of the Institute in practice shall not accept, in a financial year, more than the "specified number of tax audit assignments" under Section 44AB of the Income-tax Act, 1961. "the specified number of tax audit assignments" means, 60 tax audit assignments per partner in the firm, in a FY, whether in respect of corporate or non-corporate assesses - one partner can individually sign all the tax audit reports subject to specified tax audit assignment limits on behalf of all the partners in the firm of Chartered Accountants - In the instant case, there are 6 partners in M/s XYZ & Co., a Chartered Accountants firm, accordingly specified ceiling limit for the firm will be (60 tax audit assignments per partner X 6 partners) = 360 - Conclusion: Hence, Mr. Gaurav shall not be deemed to guilty of professional misconduct provided total number of tax audit reports on behalf of firm do not exceeds 360.	
Appointment of an Auditor in case of non-payment of undisputed fees:	Q155. Mr. C accepted the statutory audit of M/s PSU Ltd., whose net worth is negative for year 2019-20. The audit was to be conducted for 2020-21. The audited accounts for year 2020-21 showed liability for payment of tax audit fees of ₹15,000 in favour of previous auditor. Answer: - As per Chapter 7 of Council General Guidelines 2008, A member of the Institute in practice shall not accept the appointment as auditor of an entity in case the undisputed audit fee (including out of pocket expenses) of another Chartered Accountant for carrying out the statutory audit under the Companies Act, 2013 or various other statutes has not been paid: - In the case of sick unit, the above prohibition of acceptance shall not apply. "Sick unit" shall mean a unit registered for not less than 5 years, which has at the end of any financial year accumulated losses ≥ its entire net worth. - Conclusion: In the instant case, though the undisputed fees are unpaid, Mr. C would still not be guilty of professional misconduct since the M/s PSU Ltd. is a sick unit having negative net worth for the year 2019-20	
Specified number of audit assignments:	- A member of the Institute in practice shall not hold at any time appointment of more than the "specified number of audit assignments" of Companies u/s 141 of the Companies Act, 2013. (For Companies: Mentioned in Sec 141 - 20 Audits) - But as per ICAI Guidelines, For this purpose, the "specified number of audit assignments" means - (a) in the case of a Chartered Accountant in practice or a proprietary firm of Chartered	



(co. act → 20 companies exclude OPC, Small, dormant, pvt PUSC < 100 cr)

Accountant, **30 audit assignments** whether in respect of **private Companies or other Companies**, with the exception of OPC and dormant companies.

(b) in the case of Chartered Accountants in practice, **30 audit assignments per partner** in the firm, whether in respect of private Companies or other Companies, with the exception of OPC and dormant companies.

- The number of partners of a firm on the date of acceptance of audit assignment shall be taken into account
- CA practice, whether in **full-time or part-time employment elsewhere**, shall **not** be counted for the purpose of determination of "specified number of audit of Companies" by firms of Chartered Accountants
- A CA in practice as well as firm of CA in practice shall **maintain a record** of the audit assignments accepted by him or by the firm of Chartered Accountants (Same record is required to be maintained for **tax audit assignments**):

Sr. No	Name of Company	Registration No.	Date of appointment	Date of Acceptance

Appointment as **Statutory auditor**:

(Other Fees > Stat Audit Fees)

Q156. A is the auditor of Z Ltd., which has a turnover of ₹200 crore. The audit fee for the year is fixed at ₹50 lakhs. During the year, company offers A an assignment of mngt consultancy within the meaning of Section 2(2)(iv) of the CA Act, 1949 for a remuneration of ₹1 crore.

Answer:

- A member of the Institute in practice shall **not accept the appointment** as statutory auditor of:
 - ✓ **PSU/Government Company/Listed Company** and
 - ✓ **Other Public Companies** having **turnover ≥ ₹ 50 crore** in a year

Where **remuneration of any other work or assignment or service** from same undertaking/company on a which in total **exceeds the fee payable for carrying out the statutory audit** of the same undertaking/company.

[The **above restrictions** shall **apply in respect of fees for other work(s) or service(s) or assignment(s) payable to the statutory auditors and their associate concern(s) put together**]

- For the above purpose, the term "**other work**" or "service" or "assignment" shall **include Management Consultancy and all other professional services** permitted by the Council pursuant to Section 2(2)(iv) of the Chartered Accountants Act, 1949 but shall **not include**:
 - (a) **audit under any other statute**;
 - (b) **certification** work required to be done by the statutory auditors; and
 - (c) any **representation** before an authority;
- **Clause 1 of Part II of Second Schedule**, a member of the Institute will be held guilty of professional misconduct if he Contravenes any of the provisions
- **Conclusion:** In view of the above position it would be a misconduct on A's part if he accepts the management consultancy assignment for a fee of ₹1 crore.

Guidelines Given in Network Firms: When there are Network Firms

For the Firm, which is Conducting Stat. Audit of Entity:	Same Provision as mentioned above is applicable
For The Remaining Firms in Network (Collectively)	<u>They can get fees from Other service upto 3 times of the fee payable for carrying out the statutory audit of the same undertaking</u>

Q157. Public Ltd. Company, T.O 200 Crore Rs., Audit fees Rs. 80L, also accepted one assignment



	from auditee reg. representation before I.T Appellate Tribunal, fees Rs. 1.75 Crore. Answer: Hint: Refer above whole Provision → "Not include" → "any representation before an authority" hence Not a misconduct.
Appointment of an auditor when he is indebted to a concern:	A member of the Institute in practice or a partner of a firm in practice or a firm or a relative of such member or partner shall not accept appointment as auditor of a concern while indebted to the concern or given any guarantee or provided any security in connection with the indebtedness of any third person to the concern, for limits fixed in the statute and in other cases for amount exceeding ₹ 1,00,000/- ✓ Even he can't receive advance fees ✓ However he can accept fees based on Progressive basis ✓ However for Companies, Rs.5 lacs limit will apply (As mentioned in Sec 141 of Co.Act) Q158. D, who conducts the tax audit u/s 44AB of M/s ABC, a partnership firm, has received the audit fees of ₹2,50,000 on progressive basis (for Yr End 31.3.2020). The A.report was, however, signed on 25.5.2020. Hint: Entire Audit Fees Received in Advance: not accept appointment as auditor of a concern while indebted to the concern or given any guarantee amount exceeding ₹1,00,000/- However, the Research Committee of the ICAI has expressed the opinion that where in accordance with the terms of engagement of auditor by a client, the auditor recovers his fees on a progressive basis as and when a part of the work is done without waiting for the completion of the whole job, he cannot be said to be indebted to the company at any stage Conclusion: Mr. D will not be held guilty for misconduct. Q159. Mr. E, proprietor of M/s. E & Co. is the statutory auditor of a Company which owns a store dealing in computer equipments. During the year 2014-15, E purchased a computer from the store costing Rs.25,000 for his son. He did not make any payment for the same, but asked the company to adjust the same against the audit fees payable of Rs.50,000. Hint: Mr. E is permitted to continue the office as his indebtedness does not exceed ₹ 5 Lacs
UDIN:	A member of the Institute in practice shall generate Unique Document Identification Number (UDIN) for all kinds of the certification, GST and Tax Audit Reports and other Audit, Assurance and Attestation functions undertaken/signed by him which made mandatory from the following dates through announcements published on the website of the ICAI www.icai.org at the relevant time: (i) For all Certificates w.e.f. 1st February, 2019. (ii) For all GST and Tax Audit Reports w.e.f. 1st April, 2019. (iii) For all other Audit, Assurance and Attestation functions w.e.f. 1st July, 2019. Q160. Mr. Kushal, a practicing CA has signed the GST Audit Reports, Tax Audit Reports u/s 44AB of the Income tax Act, 1961 for FY 2019-20 digitally signed & without generating UDIN on the ground that there is no field for mentioning UDIN on digitally signed online reports. Hint: Explain Above UDIN concept & Clause (1) of Part II of the Second Schedule. non-generating of UDIN amounts to professional misconduct under C-1, P-2, S-II
Logo Guideline: (Amendment)	• Can be used by Practicing as well as non-practicing CA • "CA" in Blue Color → With a Tri Color Tick Mark (Upside Down) → With White Background. • Blue Letter: The letters CA have been put in blue, the corporate colour which not only stands out on the background but also denotes creativity, innovativeness, knowledge, integrity, trust, truth, stability and depth. • Upside Down Tick Mark: Typically used by CA → included in Wisdom & Value • India: India word is also included to show institute connection with India



	• Green-color: in the tick mark signifies growth, prosperity, harmony and freshness. • Do not change the design and colors, including the white background. Refrain from rotating or tilting the logo.								
Guidelines for Corporate Form of Practice: (Management consultancy company)	• Council decided to allow members in practice to render Management Consultancy and Other Services in Corporate form, <u>subject to the guidelines</u> to be issued by the Institute in this regard. • The Council decided to allow members in practice to hold the office of <u>Managing Director, Whole-time Director or Manager</u> of a body corporate within the meaning of the Companies Act provided that the body corporate is engaged exclusively in rendering Management Consultancy and Other Services • Complies with the conditions(s) as specified by the Council from time to time in this regard. <u>Various conditions as stated in the guidelines are:</u> <table border="1"> <tr> <td>Name of MC company:</td><td>Shall have a distinct name which shall be approved by the Institute</td></tr> <tr> <td>Registration:</td><td>Required to be registered with the Institute in a prescribed Form.</td></tr> <tr> <td>Ethical Compliance:</td><td> 1) If the individual practitioner/sole-proprietorship firm/partnership firm is the statutory auditor of an entity then the Management Consultancy Company should not accept the internal audit or book-keeping or such other professional assignments, which are prohibited for the statutory auditor firm. 2) Ceiling on Non-audit fees is applicable in relation to a Management Consultancy Company (i.e., Max Fees Upto Audit Fees) 3) The Management Consultancy Company shall comply with clauses (6) & (7) of Part-I of the First Schedule to the Chartered Accountants Act, 1949 and such other directives as may be issued by the Institute from time to time </td></tr> <tr> <td>Object of MC company:</td><td>The Management Consultancy Company shall engage itself only in Management Consultancy & Other Services prescribed by the Council pursuant to powers u/s 2(2)(iv) of the CA Act, 1949.</td></tr> </table>	Name of MC company:	Shall have a distinct name which shall be approved by the Institute	Registration:	Required to be registered with the Institute in a prescribed Form.	Ethical Compliance:	1) If the individual practitioner /sole-proprietorship firm/partnership firm is the statutory auditor of an entity then the Management Consultancy Company should not accept the internal audit or book-keeping or such other professional assignments, which are prohibited for the statutory auditor firm. 2) Ceiling on Non-audit fees is applicable in relation to a Management Consultancy Company (i.e., Max Fees Upto Audit Fees) 3) The Management Consultancy Company shall comply with clauses (6) & (7) of Part-I of the First Schedule to the Chartered Accountants Act, 1949 and such other directives as may be issued by the Institute from time to time	Object of MC company:	The Management Consultancy Company shall engage itself only in Management Consultancy & Other Services prescribed by the Council pursuant to powers u/s 2(2)(iv) of the CA Act, 1949.
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Object of MC company:	The Management Consultancy Company shall engage itself only in Management Consultancy & Other Services prescribed by the Council pursuant to powers u/s 2(2)(iv) of the CA Act, 1949.								

Q161. CA R, a CAip is specializing Info Systems Audit. HKC Limited, a Company engaged in rendering **management consultancy** offered him to appoint as its **managing director**. He accepted the position **without obtaining prior permission** from the Institute. **One of his friends, CA S informed him that now he cannot retain full time certificate of practice**, thus cannot do attest function and train articled assistants. Comment w.r.t CA act

Hint: → Explain Clause 11, P-1, S-1 i.e., → guilty if he engages in any business or occupation other than CA.

- The Council decided to **allow members in practice to hold the office of MD, WTD or Manager** of a body corporate within the meaning of the Companies Act, 2013 provided that the body corporate is **engaged exclusively in rendering Management Consultancy** and Other Services permitted by the Council in pursuant to **Section 2(2)(iv) of the CA Act, 1949** and complies with the conditions(s) as specified by the Council from time to time in this regard. The **name of the Management Consultancy Company is required to be approved by the Institute** and such Company has to be registered with Institute.
- The **members can retain full time Certificate of Practice** besides being the Managing Director, WTD or Manager of such Management Consultancy Company. There will be **no restriction on the quantum of the equity holding of the members, either individually and/ or along with the relatives**, in such Company. Such members shall be regarded as being in full- time practice and therefore **can continue to do attest function** and wherein they are also entitled to train articled/audit assistants. → Thus, the action of CA R is valid.

Q162. J, a CAip has **not maintained the record** of audit assignments of the companies on the **ground** that he is **conducting lesser number of audits prescribed under Section 141 (3) (g) of Co.Act, 2013.**

Hint: deemed to be guilty of professional misconduct If he holds at any time appointment of more than the specified number of audit assignments of the companies U/s 141(3)(g) and 143 of Co. Act, 2013.



shall maintain a record of the audit assignments accepted as laid out in guidelines issued by the Council of the ICAI:

S. No.	Name of the Company	Registration Number	Date of appointment	Date of Acceptance	Date on which Prescribed Form filed with Registrar of Companies

Mr. J is guilty of professional misconduct under Part II of 2nd schedule of Chartered Accountants Act 1949

➤ Self Regulatory Measures (Only Recommended by ICAI, Not Mandatory):

Branch Audits:	The branch audits of a company should <u>not be conducted by its statutory auditors consisting of 10 or more members</u> , but should be <u>conducted by the local firms</u> of auditors consisting of <u>less than ten members</u>
Ratio Between Qualified and Unqualified Staff:	Chartered Accountants engaged in audit work should have at least 1 member for every 5 non-qualified members of the staff, <u>excluding articled and audit assistants, typists, peons and other persons not engaged directly in such professional work</u>
Minimum Fees:	Institute has issued revised Minimum scale of Fees for the professional assignments of the members of ICAI

Q163. M/s ASKS, a CA Firm, accepts an audit assignment of a private limited company for a fee of ₹4,000 only.

Hint: prescribed minimum audit fee is recommendatory, not yet mandatory in nature. not guilty of misconduct

Q164. Mr. Rahul, a locally based CA, accepted an audit assignment at a fee lower than that charged by the previous auditor, who was stationed in another town and had to spend a lot of money on travel for which he did not charge.

Hint: Since the previous auditor was stationed in another town and therefore, had to incur higher cost on account of conveyance, and the previously the fee was decided on a composite basis inclusive of travelling expenses of the auditor, it cannot be said that Mr. Rahul has accepted an audit assignment based on under cutting of fees.

Conclusion: - Mr. Rahul will not be held guilty for misconduct

➤ Guidelines for Networking :

Definitions: (Eg. KPMG & BSR & Co.)	Network: [All conditions to fulfill]	<u>A larger structure:</u> (a) That is aimed at co-operation; and (b) That is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy , the use of a common brand name , or a significant part of professional resources .
	Network Firm:	Means a firm or Entity that belongs to a Network
Reference in its stationery or promotional materials:	Even though a firm does not belong to a network and does <u>not use a common brand name</u> as part of its firm name, it may give the appearance that it belongs to a network if it makes reference in its stationery or promotional materials to being a member of an association of firms. Accordingly, if care is not taken in how a firm describes such memberships, a perception may be created that the firm belongs to a network	
Professional Resources: <i>Trick: CPT & AT me network bana lo</i>	Where the larger structure is aimed at co-operation and the entities within the structure share a significant part of professional resources , it is deemed to be a network. <u>Professional resources include:</u> Common systems that enable firms <u>to exchange information</u> such as client data, billing and time records; Partners and staff; Technical departments that consult on technical or industry specific issues, transactions or events for assurance engagements;	



	• Audit methodology or audit manuals; and • Training courses and facilities.																		
What is not Network:	1) Sharing of immaterial cost 2) Sharing is limited to immaterial professional resources 3) Association between firm of unrelated entities (Just for mutual benefit)																		
Forms of network:	The different forms of Network can be as under: <table><tr><th>Sr.no</th><th></th><th></th></tr><tr><td>1</td><td>Mutual entity:</td><td>A network can be constituted as a mutual entity which will act as a facilitator for the constituents of the Network</td></tr><tr><td>2</td><td>Partnership:</td><td>A network can be constituted as a partnership firm subject to the condition that the total number of partners does not exceed 20</td></tr><tr><td>3</td><td>LLP:</td><td>A network can be constituted as a Limited Liability Partnership subject to the provision of the Chartered Accountant Act</td></tr><tr><td>4</td><td>Company:</td><td>A network can be constituted as company <u>subject to the guidelines prescribed by Institute</u> for corporate form of practice and formation of management consultancy services company</td></tr><tr><td>5</td><td>Any Other entity:</td><td>Network Firms shall consist of sole <u>Practitioner/proprietor, partnership or any such entity</u> of professional accountants as may be permitted by the Act</td></tr></table> Note 1: A firm is allowed to join only 1 network Note 2: Firms having common partners shall join only one Network Note 3: Network Can't practice, Firms under network will practice	Sr.no			1	Mutual entity:	A network can be constituted as a mutual entity which will act as a facilitator for the constituents of the Network	2	Partnership:	A network can be constituted as a partnership firm subject to the condition that the total number of partners does not exceed 20	3	LLP:	A network can be constituted as a Limited Liability Partnership subject to the provision of the Chartered Accountant Act	4	Company:	A network can be constituted as company <u>subject to the guidelines prescribed by Institute</u> for corporate form of practice and formation of management consultancy services company	5	Any Other entity:	Network Firms shall consist of sole <u>Practitioner/proprietor, partnership or any such entity</u> of professional accountants as may be permitted by the Act
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5	Any Other entity:	Network Firms shall consist of sole <u>Practitioner/proprietor, partnership or any such entity</u> of professional accountants as may be permitted by the Act																	
Approval of name of network: (Form A)	• The Network may have distinct name which should be approved by the Institute. • To distinguish a "Network" from a "firm" of Chartered Accountants, the words "& Affiliates" shall be used after the name of the network and the words "& Co." / "& Associates" shall NOT be used. The prescribed format of application for approval of Name for Network is at Form 'A'. • The Institute shall approve or reject the name of the Network and intimate the same to the Network at its address mentioned in Form 'A' within a period which shall not be later than 30 days from the date of receipt of the said Form																		
Registration of network with entities in India: (Form B)	• After the name of a Network is approved as per provision under these Guidelines, the Institute shall reserve such name for period of 3 months from the date of approval • Network shall get itself registered with the Institute by applying in Form B within the period of 3 months • Registration of Network with Institute is mandatory																		
Network with outside India: (Form D)	• File declaration with institute: ✓ By Authorised representative of Indian Firm ✓ In Form-D, Within 30 days of arrangement																		
Change in constitution: (Form C)	In case of change in the constitution of registered Network on account of any entry into or exit from the Network , the network shall communicate the same to the Institute by filing Form 'C' within a period of 30 days from the date of change in the constitution.																		
Q165. AJ & Associates and PK & Co., CA firms have joined the Network firm A to Z & Affiliates registered with Institute. AJ & Associates was statutory auditor of B Ltd. for last 10 years. Due to rotation of auditor as per																			

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Professional Ethics



section 139 (2) of Companies Act, 2013, B Ltd. retires AJ & Associates and appoints PK & Co., as auditor for the year 2020-21. Comment as per Chartered Accountant Act, 1949 - Guidelines for Networking.

Hint: As per Council General Guidelines, 2008, Chapter XV, Guidelines for Networking, once the relationship of network arises, it will be necessary for such a network to comply with all applicable ethical requirements prescribed by the Institute from time to time in general and the following requirements in particular in those cases where rotation of firms is prescribed by any regulatory authority, no member firm of the network can accept appointment as an auditor in place of any member firm of the network which is retiring.

In the given situation, AJ & Associates was statutory auditor of B Ltd. For last 10 years and due to rotation of auditor as per section 139(2) of the Companies Act, 2013 B Ltd., retires AJ & Associates and appoints PK & Co. as auditor for the year 2020-21.

It may be considered that AJ & Associates and PK & Co., chartered accountant firms have joined the network firm namely A to Z & Affiliates registered with Institute. In view of above Guidelines for Networking PK & Co., is disqualified for appointment as an auditor of B Ltd.

➤ Council Guidelines for Advertisement, 2008

Meaning of Write-Up:	"Write up" means the writing of particulars according to the information given in the Guidelines setting out services rendered by the Members or firms and any writing or display of the particulars of the Member(s) in Practice or of firm(s) issued, circulated or published by way of print or electronic mode or otherwise including in newspapers, journals, magazines and websites, which include social Networking Websites (in Push as well as in Pull mode) in accordance with the Guidelines
Condition to be complied:	The write-up shall comply with the following conditions: - It shall be honest and truthful. - There shall be no exaggerated claims for the services offered by the member or the Firm, or the qualifications or experience of the member or any of the partners or any other person associated with the Firm. - It must not make any disparaging references or unsubstantiated comparisons to the work of others. - It should not be of a nature that may bring the profession into disrepute. - It should not contain testimonials or endorsements concerning Member(s) or names of clients (both the past and present) or the fees charged. - It should not contain any information about achievements /awards (except the awards given by the Central or State Governments or Regulatory bodies) or any other position held, or accreditation(s) granted by any organisation. - Monogram of any kind or use of any kind of catch words is not permissible. - The Membership No./FRN (as may be applicable) is mandatory to be mentioned in the write-up. - It should not be of font size exceeding 14. - It must not be violative of any provisions of Chartered Accountants Act, 1949, Chartered Accountants Regulations, 1988, Code of Ethics, 2020 or any Guideline of the Council
Information to be contained in Write-Up:	- CA Name - Name of Firm of CA - Firm Registration number - Membership No. with Institute - Age - Date of becoming ACA - Date of becoming FCA - Date from which COP held - Recognized qualifications - Languages known



- (xi) Telephone/Mobile/Fax No.
- (xii) Professional Address
- (xiii) Website
- (xiv) E-mail
- (xv) CA Logo
- (xvi) Passport style photograph
- (xvii) Details of Employees (Nos.):
- (xviii) Chartered Accountants -
- (xix) Other Professionals -
- (xx) Articles/Audit Assistants
- (xxi) Other Employees
- (xxii) Names of the employees and their particulars on the lines allowed for a member as stated above.
- (xxiii) Services provided
- (xxiv) (a)
- (xxv) (b)
- (xxvi) (c)
- (xxvii) Position held as Director or Managing Director in a Management Consultancy Company registered with the Institute.

➤ **FEES – Relative Size** (i.e., Fees from single client is Higher)

Intro & Threats	When the total fees generated from an Audit client [single client & its related parties] by the firm expressing the audit opinion represent a large proportion of the total fees of that firm , the dependence on the client and concern about losing the client create a self-interest or intimidation threat .						
What to Do?	If Limit mentioned in this Para exceeds (Threat), Then Audit firm needs to Disclose / report the fact to ICAI (Institute)						
Limit:	Disclosure is required where for 2 consecutive years, Below Limits are Crossed: <table border="1"> <thead> <tr> <th>When Auditee Is:</th><th>Limit:</th></tr> </thead> <tbody> <tr> <td>Non-Public Interest Entities (PIE):</td><td>The gross annual professional fees from an audit client represent more than 40% of the total fees of the firm</td></tr> <tr> <td>Public interest entities</td><td>The gross annual professional fees from an audit client represent more than 20% of the total fees of the firm</td></tr> </tbody> </table> [If the fees continue to exceed mentioned limits, the firm shall in each such year disclose this fact to the Institute]	When Auditee Is:	Limit:	Non-Public Interest Entities (PIE):	The gross annual professional fees from an audit client represent more than 40% of the total fees of the firm	Public interest entities	The gross annual professional fees from an audit client represent more than 20% of the total fees of the firm
When Auditee Is:	Limit:						
Non-Public Interest Entities (PIE):	The gross annual professional fees from an audit client represent more than 40% of the total fees of the firm						
Public interest entities	The gross annual professional fees from an audit client represent more than 20% of the total fees of the firm						
Exemption:	Above threshold is NOT APPLICABLE if: 1) Firms exempted - Firm total fees received by the firm does not exceed Rs. 20 Lakhs (Including fees for other services rendered) Including different firms in which such member or firm may be a partner to all audit clients 2) Audit Clients exempted: audit of government Companies, public undertakings, nationalized banks, and public financial institutions, or where appointments of auditors are made by Government or Regulators						
Public Int. Entity:	a) Listed Entity, Or, b) Defined by regulation or legislation as a public interest entity c) For which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities. d) Banks and Insurance Companies are to be considered as Public Interest Entities.						

.....Refer Additional PDF for some Numerical Examples given By Author . Special :-p



➤ Other Guidelines:

Online 3rd Party Platform:	- A number of non-Chartered Accountants' firms, corporates including banks, finance Companies and newspapers have set up their own Websites providing advisory services on taxation and other areas where CA's are rendering professional service. - Some of such Websites may request Chartered Accountants to provide consultation and advice through their Websites. No other service, besides consultancy & advice can be rendered through such websites. - On the Website, contact address of the CA concerned is not provided nor such Website will contain any material which advertises professional achievements or except making a statement that they are Chartered Accountants. - Don't mention Name of CA & Contact no. of CA
Publication of Name in the Telephone or other Directories:	Allow, Even can give on special request & made payment, But following conditions to fulfill: - The entry should NOT appear in any other category except that of 'Chartered Accountants'. - The member/firm should belong to the town/city in respect of which the directory is being published. - The order of the entries should not be in any manner other than alphabetical. - The entry should not be made in a differential or prominent manner giving the impression of publicity/advertisement. - The entries should NOT be restricted and should be open to all the CA's /firms of Chartered Accountants in the particular city/town in respect whereof the directory is published. - The members can also include their names in trade/ social directories
Application based Service provider Aggregators:	i.e., Urbabclap.com It is NOT permissible for members to list themselves with online Application based service provider Aggregators, wherein other categories like businessmen, technicians, maintenance workers, event organizers etc. are also listed
Advt. in Press (Exemption): Link with C-6 → 1) Allow: Change in partnership nwspr 2) Allow: sharing/seeking work partnership in institute journal classified (no firm name)	- A special exemption has been made as regards publication of the name and address of a member or that of his firm Name, with the description Chartered Accountant(s), in an advertisement appearing in the press in the following circumstances, Provided that the advertisement is not displayed more prominently than is usual for such advertisements or the name of the member or that of his firm with the designation Chartered Accountant(s) appears in type not bolder than the substance of advertisement: - Advertisement for recruiting staff in the member's own office. - Advertisement inserted on behalf of clients <u>requiring staff</u> or wishing to <u>acquire or dispose of business or property</u>. - Advertisement for the sale of a business or property by a member acting in a <u>professional capacity as trustee, liquidator or receiver</u>. When advertising for staff, it is desirable that members should avoid the expression such as "a well-known firm", since this would savour of advertisement. Similar considerations apply to advertisements for articled assistants.

Q166. Govt introduced one GEM Portal E-market to showcase their innovative products and services to → Govt As well to Public. Can CA Firm register in this portal for rendering professional services to Govt departments?

Hint:

- Council Advt Guidelines 2008 → not permissible** to list on online app based service provider **Aggregators**.
- Further, C-6, P-1, S-I → Govt Dept, Govt Companies/ corporations, courts, cooperative societies & banks & other similar institutions prepare panels of Chartered Accountants for allotment of audit and other professional work . Can register only if existence of such a panel is within knowledge of a member, No Roving enquiries.**



- Here It's allowed to register, because → Registering on GEM Portal is not like empanelment on aggregator, → as aggregator means 3rd party platform, by which we provide service to client, But here, Client (Govt) itself operating the GEM portal, and CA firm want to provide service to that Govt only.
- Allow to register, **no violation** of the ethical norms of the Institute, as registering on portal is pre-requirement to provide service to Govt dept (However, comply with tender guidelines issued by institute)

➤ Recent decision of Ethical standard Board:

A CA is ALLOW to carry following Activities:	A CA is NOT ALLOW to carry following Activity:
1) CAip can provide Advisory to <u>Audit client</u> related to BRSR	1) CAip can't prepare BRSR study of Audit Clients (Business Responsibility & Sustainability Reporting)
2) CAip Can provide Assurance on BRSR of FS Audit Client	2) Member in practice cannot act as Trademark or Patent Attorney (i.e., applying trademark/patent. Replying disputes etc.
3) advice in relation to Intellectual Property Rights (IPR) is a routine professional work	3) Can-not publish retail report as equity research advisor
4) CA in practice can be an equity research advisor	4) Take agencies of UTI, GIC or NSDL
5) Registration Authority (RA) for obtaining digital signatures	5) ~~Member of a Trust, cannot be the auditor of trust~~
6) Can hold the credit card of a bank when he is also the auditor provided the outstanding balance on the said card does not exceed Rs. 100,000	6) Can-not take audit of bank in case he has taken <u>loan against a Fixed Deposit</u>
7) Can act as Mediator or arbitrator	7) statutory audit of the society wherein immediate <u>family member i.e., spouse or dependent</u> , of member hold honorary position of one of the managing committee
8) CA who is Member of Trust can be Auditor of trust (Provided that No Law prohibits + No conflict of interest/Complying code of ethics)	8) Not permissible for a member who has been Director of a Company, upon resignation from the Company to be appointed as an auditor of the said Company, and the cooling period for the same may be 2 years .
9) To be a settlor of a trust	9) Cannot become Financial Advisors and <u>receive fees/commission from Financial Institutions</u> such as Mutual Funds, Insurance Companies, NBFCs
10) can act as the internal auditor of a company & statutory auditor of its employees PF Fund	10) cannot exercise lien over the client documents
11) Can Become a <u>member</u> of the ' Board of Management ' in Primary (Urban) Co-operative Banks, [Provided not involve day to day working, only sitting fees will rec]	11) not permissible for CA Firm to print its vision and values behind the visiting cards (However, can be printed on the firm profile and may be provided in response to a specific request)
12) Can Register his OWN CA Firm on MSME Portal (Udyog Aadhar)	12) Messaging Applications to send messages to make people aware about his practice, and mention the services
13) <u>Internal Auditor</u> Can Purchase/Deal with Shares of the company	13) CA being Director Simplicitor in a Company → cannot sign ROC Forms of the Company as (It's conflict of interest)
14) Can be Authorized Representative of foreign Company (Provided <u>he in not auditor</u> of that)	14) CAiP is NED Director of Company → can -not accept Stat audit of JV of Company
15) Two or more CA Firms → Can Conduct Joint Training Sessions for there Clients (i.e., GST) → can share Fees rec. from client	
16) can provide services through kiosk only <u>if the services provided, permitted under CA Act</u>	



17) <u>statutory auditor /tax auditor</u> can be the valuer of unquoted equity shares of same entity, ONLY IF LAW PERMITS (i.e., IT act) 18) CA in service is allowed to take e-return registration if it does not conflict with employment obligation. <u>However, he cannot certify the return</u> 19) CA in Service: can be a tax representative against authority of Employer (But NOT Employee of Employer) 20) CAip can do assessment/performance audit of <u>the centres of skill development council of Government</u> of India (As it's Mngt Consultancy) 21) CAip can accept assignment of Mystery Audit. 22) CAip can <u>mention his position</u> as promoter/Director on the <u>portal of a Company</u> → (don't mention professional attainments & name of firm with) → No Violation of C-6 & 7 23) CAip can become Professional Director in the <u>Board</u> of Management of a <u>Co-operative Bank</u> 24) CAip can setup office in IFSC/GIFT city. 25) Can render professional services to IFSC units from offices outside IFSC. 26) It is permitted for CAip → to charge fees on % of Grant utilized by Education institute for purpose. (i.e., Education institute received Grant → CA Appointed to verify that whether Education institute Utilised grant for same purpose) ... as its non-audit work 27) CAip can be appointed as NED/independent Director of <u>Co-operative Bank</u>. (don't involve in day-to-day activities)	15) Custom license broker 16) statutory auditor of a bank cannot for the same financial year accept stock audit of the same branch of the bank or any of the branches 17) A concurrent auditor of a bank 'X' cannot be appointed as statutory auditor of bank 'Y', which is sponsored by 'X'. 18) Statutory auditor can't engage in Compilation engmnt of that entity (SRS 4410) 19) Auditor of Bank → can't accept ASM assignment of Same bank customer simultaneously (he can accept either of one at same time) 20) CAip cannot be appointed as an Internal Auditor and Procurement officer simultaneously in an organization

**** Note: Criteria related to Indebtness / No. of Limit on Audit → Applicable only on Statutory auditor (not Concurrent/ Internal or Mngt Auditor)**

****** Due to the provision of Section 149(3) i.e., requirement for a Director u/s 149(3) of the Companies Act, 2013 to reside in India for a minimum period of 182 days in the previous calendar year → The Ethical Standards Board, decided that such a Director would be within the scope of Director Simplicitor (which is generally permitted as per ICAI norms) , if he is non -executive director, required in the Board Meetings only , and not paid any remuneration except for attending such Board Meetings**

➤ **Other Integrated Qns Hint (Covered in Detail in Additional PDF):**

Q167. Internal Auditor of Company can-not accept GST audit of Same company Simultaneously:

- Because there is Conflict in role of Statutory & internal auditor → so if accept → Guilty of Misconduct

Q168. CA Jayprakash did following things:

Audit of college accepted, for which he is working part-time as Lecturer (Not taken permission of ICAI)

Guilty (C-4,P-1,S-2 : Substantial interest) & Guilty for C-11, P-1, S-1 (Not taken permission)

CA Firm Sponsored the CSR event, and hoarding of CA Firm name was used in the event



Guilty C6, P-1 → Can mention the "CA" (but Firm Name & CA logo not permissible)

So due to above, Council reprimand it & fined 1 lacs Rs., **he preferred appeal** against this, but in appeal he **submitted some false documents**

Guilty C-3, P2, S-II (False Info to ICAI)

Based on Above, What maximum punishment could have been imposed on CA Jayprakash by the said authority **alleged of misconduct falling in 1st as well as 2nd Schedule, → placed before the Disciplinary Committee.**

The maximum punishment which could have been imposed on him by the said authority would be:

(i) reprimanding the member. (ii) removing name of the member permanently or for any duration, it thinks fit.
(iii) imposing fine upto ₹5,00,000.

Q169. CA in practice done Following

- **Equity research** to advice his friend → Allowed (but do not publish retail report)
- **Paper setter** for accountancy subject in School → Allowed (C-11, P-1, S-1)

So.....Now its Time to Summarise the INTERLINKING of the clauses ☺
It's Special :-)

Required Information not submitted or wrong info submitted:

S-1. Part 3

S-2, Part 2

Clause 2	Clause 3
does not supply the information called for, or does not comply with the requirements asked for by the Institute, Council or any of its committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the appellate authority.	while inviting professional work from another chartered accountant or while responding to tenders or enquiries or while advertising through a write up or anything as provided for in clauses (6) and (7) of Part I of this schedule, gives information knowing it to be false.

Clause 3

A member of the Institute shall be deemed to be guilty of professional misconduct if he includes in any **information, statement, return or form to be submitted to the Institute,** Council or any of its Committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the Appellate Authority, any particulars knowing them to be **false.**

DO PRACTICE/SIGN/EXAMINATION – USING OUR OWN NAME:

S-1, P-1, Clause 1

allows any person to **practice** in his name as a Chartered Accountant

Except:

MEMBER (CA)

+

Employee/Partner

S-1, P-1, Clause 12

a person not being a member of the institute in practice or a member not being his partner to **sign** on his behalf or on behalf of his firm, **any Balance Sheet, P&L A/c, Report or Financial Statements**

Except

Member (CA) + Partner

S-2, P-1, Clause 2

certifies or **submits** in his name or in the name of his firm a **report of an examination** of financial statements

Except:

SELF or
EMPLOYEE or
PARTNER or
ANOTHER CA IN PRACTICE



CA Didn't do Checking....Negligence etc etc.....
ALL CLAUSES SHOULD BE WRITE TOGETHER: S-2 : Part 1

Clause 2	Clause 7	Clause 8	Clause 9
certifies or submits in his name or in the name of his firm a report of an examination of <u>financial statements</u> (Without doing examination)	Does not exercise due diligence , or is grossly negligent in the conduct of his professional duties	fails to obtain sufficient information which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion	Fails to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances
NOTE: - Only for F.S. certification - ZERO Checking	NOTE: - All engagement - Low checking	NOTE: - Reporting & Certification - Issued wrong opinion due to not checking some important matters	NOTE: - Auditing - Didn't followed SA's etc.. + Not made disclosure of departure

Mistake in FS & Certification – Known to CA
ALL CLAUSES SHOULD BE WRITE TOGETHER: S-2 : Part 1

Clause 5

fails to disclose a material fact known to him which is **not disclosed in a financial statement**, but disclosure of which is necessary in making such financial statement not misleading

Example: Loan was given from PF Trust fund

Clause 6:

fails to report a **material misstatement** known to him to appear in a financial statement

Example S-III Depreciation rate not applies

AUDITOR & ITS RELATIVE:
ALL CLAUSES SHOULD BE WRITE TOGETHER

S-1, Part-1 : Clause 9

accepts an appointment as auditor of a company, **without ascertaining** whether **requirements** of Sec. 225 of Companies Act, 1956 (Sec. 139 & 140 of Companies Act 2013 read with **Sec. 141**), in respect of such appointment have been duly complied with.

(SECTION 141 : Auditor is disqualify where spouse is director)

S-2, Part-1 : Clause 4

expresses his opinion on financial statements of any **business** or enterprise in **which** he, **his firm** or a **partner in his firm** **has a substantial interest**

CONFIDENTIALITY

CA IN PRACTICE

S-2, P-1, C-1

A CA in practice shall be deemed to be guilty of professional misconduct if he – **discloses the information acquired in the course of his professional engagement** to any person other than his client so engaging him without the consent of his client or

EMPLOYED CA

S-2, P-2, C-2

A member of the Institute shall be deemed to be guilty of professional misconduct if he being an employee of any company, firm or person, **discloses confidential information acquired in the course of his employment.**

SOLICITATE CLIENT, ADVERTISE PROFESSIONAL ATTAINMENT

These both clauses have different meaning, But manytimes ICAI quotes both the clauses in 1 Answer, so its better to quote both of them

S-1, P-1, C-6

A CA in Practice is deemed to be guilty of professional Misconduct if he: Solicits clients or professional work either directly or indirectly, by circular, advertisement, personal communication or interview or by any other means.

S-1, P-1, C-7

A CA in Practice shall be deemed to be guilty of professional Misconduct if he: sAdvertises his professional attainments or services, or uses any designation or expressions other than the Chartered Accountant on professional documents, visiting cards, letter heads or sign boards.



Schedule 1, Part 1

Clause 3:

Accepts or agrees to accept **any part of the profits** of the professional work of a **person who is not a member** of the Institute



Clause 10

Charges or offers to charge, accepts or offers to accept in respect of any professional employment **fees** which are **based on a percentage of profits** or which are **contingent upon the findings**, or results of such employment

Clause 11

Engages in any business or occupation other than the profession of chartered accountant unless permitted by the Council so to engage

Example : CA in practice helped his brother in his FMCG business (in selling product) & his brother share him some profit %

USING FIRM NAME IS ALLOW or NOT

ALLOW (But subject to some conditions)	NOT ALLOW
Clause 6 : - Publication of book & Article - Greeting card - Television & movie - Public interview (TV/Radio etc...)	Clause 6: - Sponsoring activity (CSR) - Classified advt. in Journal/Newspaper/Press for seeking partner & employee - Educational video
	Clause 7 - Office of public importance (MP/MLA etc...)
Guideline: Newspaper advt. for Selling asset of client, recruiting staff for himself or client	Guideline: When giving classified advt of sharing work/need partnership in institute magazine

