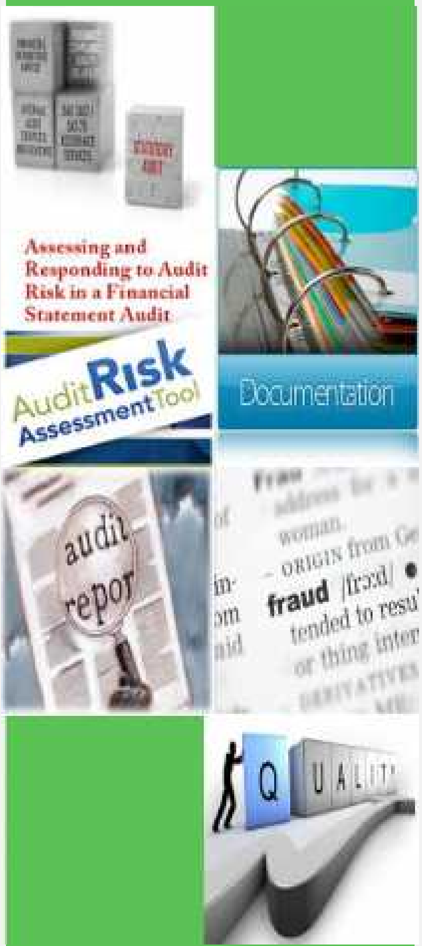
2014 Edition



"STANDARD ON AUDITING"

A Practical Approach

For CA FINAL

Prepared By

CA VINIT RATHI

"Please do not copy, respect the effort behind these notes."

Index of Standards on Auditing

Important Points to be discussed before you start this subject –

1. **I have divided Standards on Auditing in 5 Sections**
2. **It will be recommended to students that please have Practice Manual while going through this material.**
3. **All the efforts have been made to clarify each and every aspect on SA's but still one can have a problem so feel free to communicate.**
4. *This material covers last 25 attempts questions and Answers also.*
5. *This material also covers many Illustrative formats of Engagement Letters, Reports, etc. and amendment/changes made by ICAI till February – 2014*
6. **It must also be noted that there is no requirement to make reference PARA No. in your answers but still I have mentioned. (see note below)**
7. **It would always be suggested by me that to secure good marks in this particular subject please solve the complier and RTP for last FIVE attempts.**
8. **Remember one thing that this subject seems like theoretical but I must warn you all that this subject is fully practical and one of substantial/core part of our profession.**

Note → When you will go for questions which are given at the end of each SA you will find in Answer column that I have given reference of PARA No. from SA – 200 to SA – 550 but in remaining SA's I have made reference of Point No.. So don't get confused go by that PARA No. or POINT No. given in Answer column.

Section - I

Auditing and Assurance Standards

1. What are Auditing Standards?

In the simplest terms, auditing standards represent a codification of the best practices in the field of auditing. Auditing Standards are therefore, the performance benchmarks for the auditor. Auditing Standards for the professionals on how they should carry out their professional engagement, enshrined as the basic principles and essential procedures to apply those basic principles that relates to judgment or behaviour. The objective of the auditing standards is to a large extent serving the public interest.

2. Need for Auditing Standards

Formulation of Auditing Standards worldwide, including India, entails consideration of important factor's such as existing and accepted auditing practices in auditing, existing laws and regulations, usage and customs of trade and commerce, fundamental financial reporting principles, expectation of society from the auditor, Auditing standards therefore play critical role in –

1. Ensuring application of accepted financial reporting standards thereby lending credibility and wider acceptability to the financial statements.
2. Providing benchmarks against which the performance of the members can be measured and evaluated at global level also.
3. Ensuring compliance with the applicable legislative and regulatory framework.
4. Ensuring right approach of the professionals in complex/emerging areas of audit.
5. Ensuring consistency and quality in the work performed by the professionals.

Note → The Auditing Standards therefore are an important instrument for bring the expectation gap between the society and the Auditor.

3. Features of an Effective Auditing Standards

4. Auditing Standard – setting in India

The auditing standards in India are formulated by the Auditng and Assurance Board (AASB) of the ICAI. This Standards formulated by the AASB are issued under the authority of the Council of the Institute and are mandatory in nature. This implies that while carrying out their attest functions, it will be the duty of the members of the Institute to comply with these Standards. If for any reason a member has not been able to perform an audit in accordance with the applicable Standards, his report should draw attention to the material departures therefrom.

5. The Revised Preface

The Auditng profession in Indi too, which is looking forward to be reckoned among the best in the world and be accepted globally, this necessity comes as a necessary unavoidable. The AASB, as a top priority, has taken on the ambitious project of convergence with the International Standards issued by the International Auditng and Assurance Standards Board. As a first step towards convergence, it has, after going through its rigorous due process, in July 2007 published the Revised Preface of SQC, Auditing, Review, Other Assurance and Related Services, corresponding to its namesake issued by the IAASB in 2006. The Revised Preface, applicable from the April 1, 2008, has changed the face of the auditing literature, introducing some more fundamental concepts to the existing ones. The following paragraphs give a gist of the significant provisions of the Revised Preface.

5. Engagement Standards

Hitherto all the Auditing Standards issued by the AASB were known as the Auditing and Assurance Standards. The Revised Preface categorized and christens the Standards based on the nature of services being provided by a member. It therefore, introduces an umbrella concept of Engagement Standards. The terms "Engagement Standards"comprise the following Standards –

(a) Standards on Auditing (SAs), to be applied in the audit of historical financial information.

(b) Standards on Review Engagements (SREs), to be applied in the review of historical financial information.

(c) Standards on Assurance Engagements (SAEs), to be applied in assurance engagements, other than historical financial information.

(d) Standards on Related Services (SRSs), to be 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.

Note → The Revised Preface therefore, does away with the nomenclature "Auditng and Assurance Standards". It contains provisions for Standards, to be known as the Standards on Quality Control (SQCs), which would be fundamental to all the services covered by the Engagement Standards.

8. Standards on Auditing

The Standards on Auditng (SAs) referred to in the point no. 5 above are formulated in the context of an audit of Financial Statements by an Independent Auditor. They are to be adapted as necessary in the circumstances when applied to audits of other historical Financial Information

7. New Format of Presenting the Standards on Auditing

In line with the format adopted by the IAASB under its Clarity Project, the Revised Preface provided that instead of a running text, the Standards on Auditing would now contain TWO distinct sections, ONE the Requirements Section and, Other one , The Application Guidance Section.

8. Requirements Section

The Fundamental Principles of the Standard are contained in the Requirements section and represented by use of "SHALL". Hitherto the word, "SHOULD" was used in the Standards, for this purpose. Further, this format also does away with the need to present the principles laid down by the Standards in bold text.

9. Application Material

The application and other explanatory material contained in an SA are an integral part of the SA as they provide further explanation of, and guidance for carrying out, the requirements of an SA, along with the background information on the matters addressed in the SA. These may include examples of procedures, some of which the auditor may judge to be appropriate in the circumstances. Such guidance is, however, not intended to impose a requirement.

The Revised Preface also contains the principles as to when a SA would be inapplicable as also the reporting responsibilities of the members in case of non compliance with any of the Standards.

10. Authority Attached

The Revised Preface also contains the authority attached to various documents issued by the Council or the AASB under the authority of the Council of the Institute, viz., Standards, Statements, Guidance Notes, General Clarifications, Studies, etc.

11. Renumbering of Standards

The provisions of the Revised Preface, coupled with the difficulties otherwise being faced by the Board in writing Standards on the conventions followed by the IAASB, necessitated the need to adopt a new numbering pattern for the auditing standards. Whereas hitherto the auditing standards have categorized on the basis of the specific aspect of audit that they deal with and accordingly allotted the numbers from that category. These categories are as follows –

S.N.	*Category*	*Number Series*
1	**Standards on Quality Control**	**01 – 99**
2	**Introductory Matters**	**100 – 199**
3	**General Principles and Responsibilities**	**200 – 299**
4	**Risk Assessment and Responses to Assessed Risks**	**300 – 499**
5	**Audit Evidence**	**500 – 599**
6	**Using Works of Others**	**600 – 699**
7	**Audit Conclusions and Reporting**	**700 – 799**
8	**Specialised Areas**	**800 – 899**
9	**Standards on Review Engagements**	**2000 – 2699**
10	**Standards on Assurance Engagement**	**3000 – 3399**
11	**Subject Specific Standards**	**3400 – 3699**
12	**Standards on Related Services**	**4000 – 4699**

Some Additional Points

Comprehensive List of Revised/New Standards on Auditng (SAs) issued by AASB under Clarity Project

Note → Effective date means that the SA is effective for audits of the Financial Statements for periods beginning on or after the specified date.

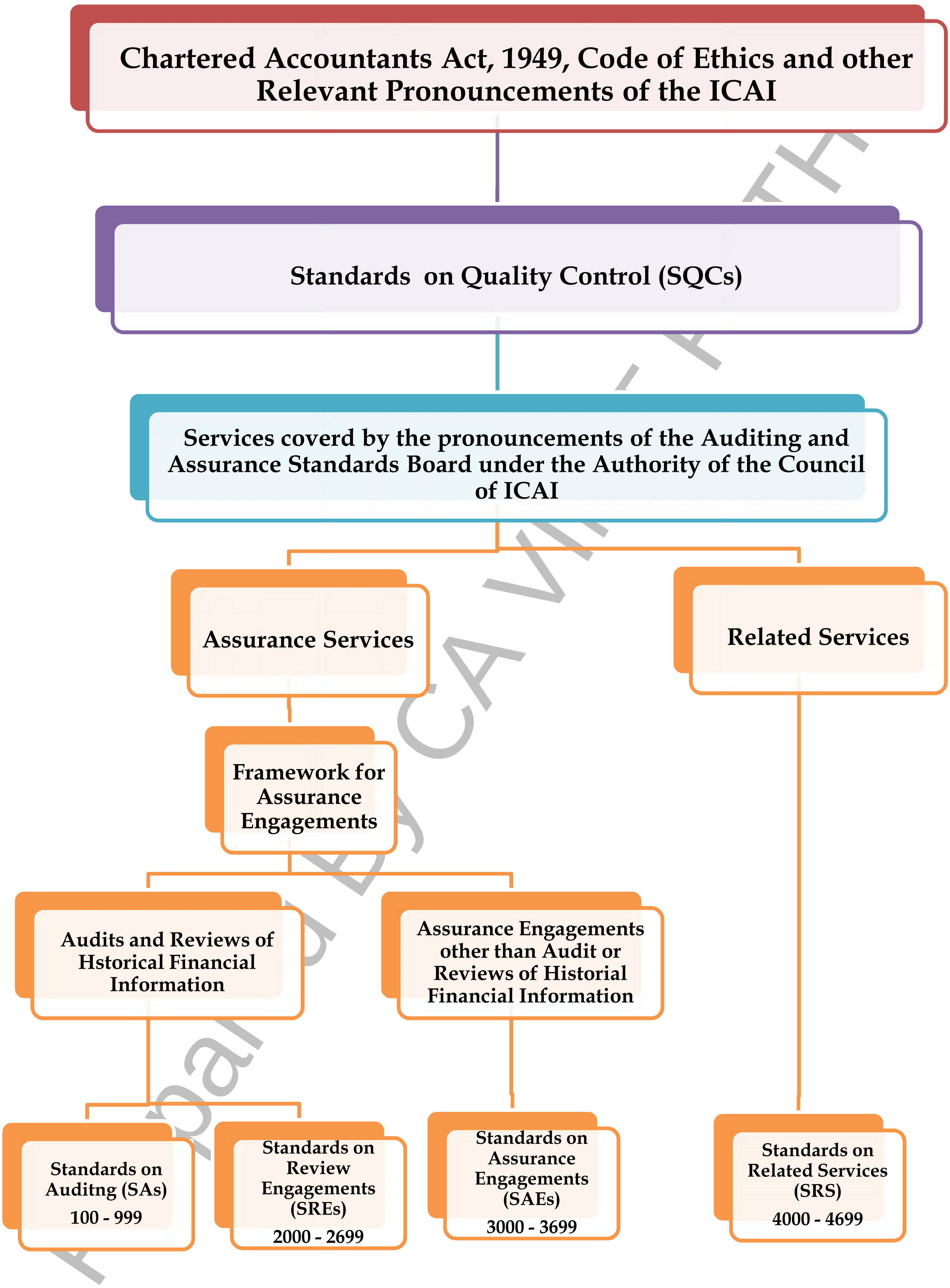
Quality Control						
Std. No. (SQC) (1 – 99)	**Title of Standard on Auditing**	**Published in Journal**	**Date from which effective**			
			April 1, 2008	**April 1, 2009**	**April 1, 2010**	**April 1, 2011**
SQC 1	Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements	October, 2007		✓		
Audits and Reviews of Historical Financial Information						
Std No. (SA) (100-999)	**Standards on Auditing (SAs)**					
200-299	**General Principles and Responsibilities**					
200 (R)	Overall Objective of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditng	March, 2010			✓	
210 (R)	Agreeing the Terms of Engagements	September, 2009			✓	
220 (R)	Quality Control for an Audit of Financial Statements	March, 2010			✓	
230 (R)	Audit Documentation	January, 2009		✓		
240 (R)	The Auditor's Responsibilities relating to Fraud in an Audit of Financial Statements	December, 2007		✓		
250 (R)	Consideration of Laws and Regulations in an Audit of Financial Statements	December, 2008		✓		
260 (R)	Communication with Those Charged with Governance	December, 2008		✓		
265	Communicating Deficiencies in Internal Control to those Charged with Governance and Management	September, 2009			✓	
299	Responsibility of Joint auditors		Effective for all audits related to accounting periods beginning on or after April 1, 1996			
300 – 499	**Risk Assessment and Response to Assessed Risks**					
300 (R)	Planning an Audit of financial Statements	December, 2008	✓			
315	Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and its Environment	February, 2008	✓			
320 (R)	Materiality in planning and Performing the Audit	August, 2009			✓	

330	The Auditor's Responses to Assessed Risks	February, 2008	✓			
402 (R)	Audit Considerations Relating to Entities using Service Organisations	August, 2009			✓	
450	Evaluation of Misstatements Identified During the Audit	August, 2009			✓	
500 – 599	**Audit Evidence**					
500 (R)	Audit Evidence	April, 2009		✓		
501 (R)	Audit Evidence—Specific Considerations for Selected Items	March, 2010			✓	
505 (R)	External Confirmations	March, 2010			✓	
510 (R)	Initial Audit Engagements—Opening Balances	March, 2009			✓	
520 (R)	Analytical Procedures	March, 2010			✓	
530 (R)	Audit Sampling	February, 2009		✓		
540 (R)	Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures	February, 2009		✓		
550 (R)	Related Parties	March, 2009			✓	
560 (R)	Subsequent Events	January, 2009		✓		
570 (R)	Going Concern	December, 2008		✓		
580 (R)	Written Representations	October, 2008		✓		
600 – 699	**Using Work of Others**					
600	Using the Work of Another Auditor		Effective for all audits related to accounting periods beginning on or after April 1, 2002			
610 (R)	Using the Work of Internal Auditors	August, 2009			✓	
620 (R)	Using the work of an Auditor's Expert	March, 2010			✓	
700 – 799	**Audit Conclusion and Reporting**					
700* (R)	Forming an Opinion and Reporting on Financial Statements	February, 2009				✓
705*	Modifications to the Opinion in the Independent Auditor's Report	February, 2010				✓
706*	Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report	February, 2010				✓
710 (R)	Comparative Information—Corresponding Figures and Comparative Financial Statements	April, 2010				✓
720	The Auditor's Responsibility in relation to Other Information in Documents containing Audited Financial Statements	April, 2010			✓	

* The Council of the ICAI, in partial modification of the decision taken by its at its 291st meeting held in December 2009, has decided that the effective date/applicability of three standards viz. SA 700 (Revised), SA 705 and SA 706 be postponed by one year and consequently the said Standards shall now be effective/applicable for audits of Financial Statements for periods beginning on or after 1st April, 2012 (instead of audits of Financial Statements for periods beginning on or after 1s April, 2011 as was earlier decided.

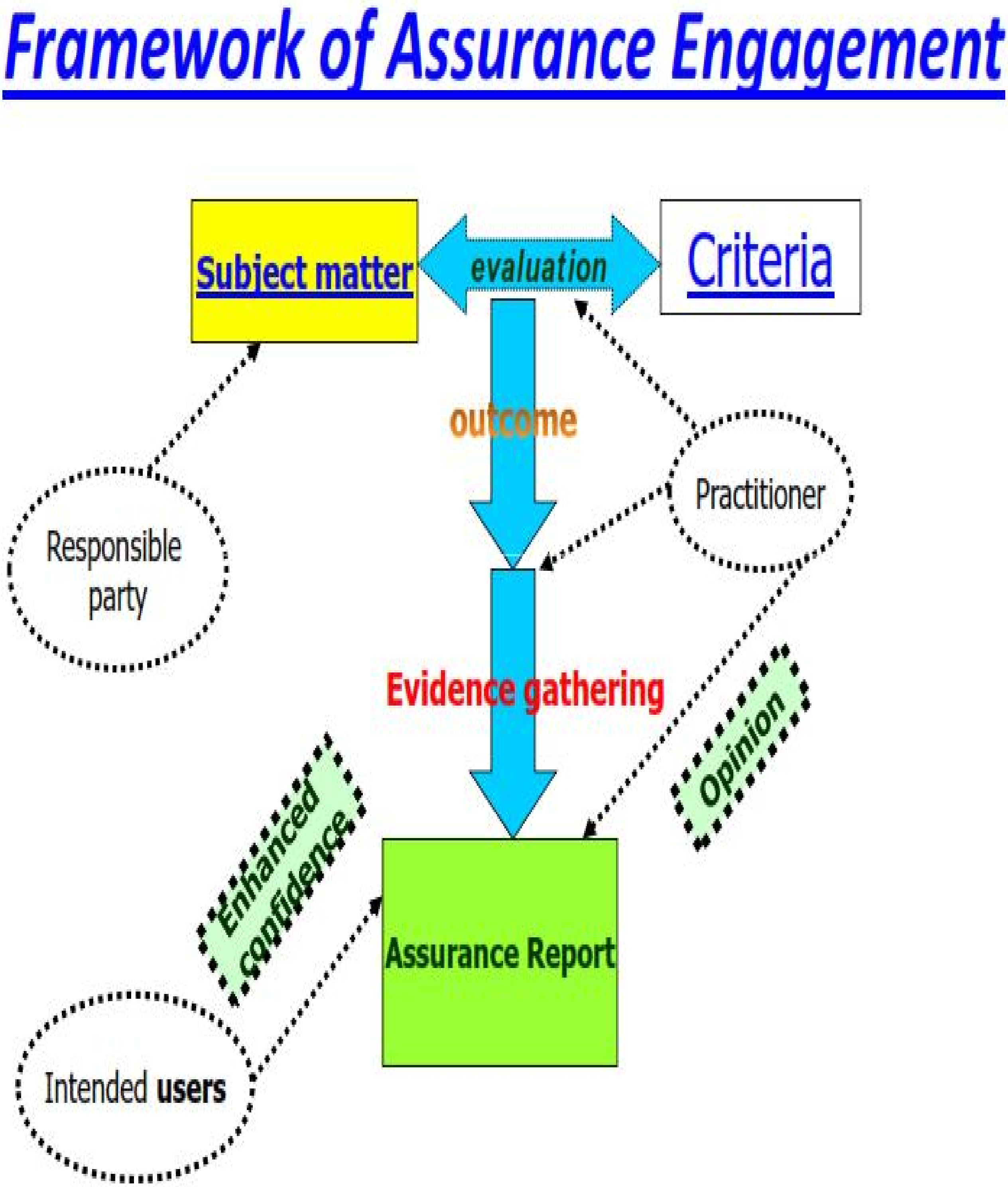
800 – 899	**Specialized Areas**					
800	Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks	April, 2010				✓
805	Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement	April, 2010				✓
810	Engagements to Report on Summary Financial Statements	April, 2010				✓
Std. No. (SRE) (2000-2699)	**Standards on Review Engagements (SREs)**					
2400 (R)	Engagements to Review Financial Statements	May, 2010			✓	
2410	Review of Interim Financial Information Performed by the Independent Auditor of the Entity	May, 2010			✓	
	Assurance Engagements Other Than Audits or Reviews of Historical Financial Information					
Std. No. (SRE) (3400-3699)	**Standards on Assurance Engagements (SAEs)**					
3000-3399	**Applicable to all Assurance Engagements**					
3400-3699	**Subject Specific Standards**					
3400	The Examination of Prospective Financial Information		Effective in relation to reports on projections/forecasts, issued on or after April 1, 2007			
3402	Assurance Reports On Controls at a Service Organisation	April, 2011				✓
	Related Services					
Std. No. (SRS) (4000-4699)	**Standards on Related Services (SRSs)**					
4400	Engagements to perform Agreed upon Procedures Regarding Financial Information		Applicable to all agreed upon procedures engagements beginning on or after April 1, 2004			
4410	Engagements to Compile Financial Information		Applicable to all agreed upon procedures engagements beginning on or after April 1, 2004			

Structure of Standards Issued By Auditing and Assurance Board Under the Authority of the Council.



Assurance Engagement

Definition → Assurance Engagement means an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the Intended User's other than the Responsible Parties about the outcome of the evaluation or measurement of a Subject Matter against Criteria



Standard on Quality Control (SQC 1)

Quality Control for Firms that performs Audits, Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements

1. Effective Date [Para –110]

This Standard on Quality Control is recommendatory for all engagements relating to accounting periods beginning on or after April 1, 2008 and is mandatory for all engagements relating to accounting periods beginning on or after April 1, 2009.

2. Introduction [Para – 3]

The firm should establish a system of quality control designed to provide it with reasonable assurance that the firm and its personnel comply with professional standards and regulatory and legal requirements, and that reports issued by the firm or engagement partner(s) are appropriate in the circumstances.

3. Definitions [Para – 6]

S. No.	*Terms*	*Description*
(a)	**Engagement Documentation**	The record of work performed, results obtained, and conclusions the practitioner reached (terms such as "working papers" or "workpapers" are also sometimes used). The documentation for a specific engagement is assembled in an engagement file.
(b)	**Engagement Partner**	The partner or other person in the Firm who is a member of ICAI and is in full time practice and is responsible for the engagement and its performance, and for the report that is issued on behalf of the Firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.
(c)	**Engagement quality control review**	A process designed to provide an objective evaluation, before the report is issued, of the significant judgments the engagement team made and the conclusions they reached in formulating the report.
(d)	**Engagement quality control reviewer**	A partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, with sufficient and appropriate experience and authority to objectively evaluate, before the report is issued, the significant judgments the engagement team made and the conclusions they reached in formulating the report. However, in case the review is done by a team of individuals, such team should be headed by a member of the Institute.
(e)	**Engagement team**	All personnel performing an engagement, including any experts contracted by the firm in connection with that engagement.
(f)	**Firm**	A sole practitioner/proprietor, partnership, or any such entity of professional accountants, as may be permitted by law.
(g)	**Inspection**	In relation to completed engagements, procedures designed to provide evidence of compliance by engagement teams with the firm's quality control policies and procedures.
(h)	**Listed Entity**	An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are traded under the regulations of a recognized stock exchange or other equivalent body.
(i)	**Monitoring**	A process comprising an ongoing consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements, designed to enable the firm to obtain reasonable assurance that its system of quality control is operating effectively.
(j)	**Network Firm**	An entity under common control, ownership or management with the firm or

		any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as being part of the firm nationally or internationally.
(k)	**Partner**	Any individual with authority to bind the firm with respect to the performance of a professional services engagement.
(l)	**Personnel**	Partner and Staff.
(m)	**Professional standards**	Engagement standards, as defined in the AASB's "Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services," and relevant ethical requirements as contained in the Code.
(n)	**Reasonable assurance**	In the context of this SQC, a high, but not absolute, level of assurance.
(o)	**Staff**	Professionals, other than partners, including any experts which the firm employs.
(p)	**Suitably qualified external person**	An individual outside the firm with the capabilities and competence to act as an engagement partner, for example a partner or an employee (with appropriate experience) of another firm.

4. Elements of a System of Quality Control – [Para – 7]

S. N.	*Elements*
1.	***Leadership responsibilities for quality within the firm.***
2.	***Ethical requirements***
3.	***Acceptance and continuance of client relationships and specific engagements.***
4.	***Human resources.***
5.	***Engagement performance.***
6.	***Monitoring***

5. The quality control policies and procedures should be documented and communication to the Firm's personnel – [Para – 8]

Such communication describes the quality control policies and procedures and the objectives they are designed to achieve, and includes the message that each individual has a personal responsibility for quality and is expected to comply with these policies and procedures. In addition, the firm recognizes the importance of obtaining feedback on its quality control system from its personnel. Therefore, the firm encourages its personnel to communicate their views or concerns on quality control matters.

6. Leadership Responsibilities for Quality within the Firm –

Para No.	*Description*
9	The firm should establish policies and procedures designed to promote an internal culture based on the recognition that quality is essential in performing engagements. Such policies and procedures should require the firm's chief executive officer (or equivalent) or, if appropriate, the firm's managing partners (or equivalent), to assume ultimate responsibility for the firm's system of quality control.
12	Any person or persons assigned operational responsibility for the firm's quality control system by the firm's chief executive officer or managing board of partners should have sufficient and appropriate experience and ability, and the necessary authority, to assume that responsibility.

7. Ethical Requirement

14	The firm should establish policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements.

15	Ethical requirements relating to audits and reviews of historical financial information, and other assurance and related services engagements are contained in the Code. The Code establishes the fundamental principles of professional ethics, which include – (a) Integrity, (b) Objectivity, (c) Professional competence and due care, (d) Confidentiality, and (e) Professional behavior.
17	The firm's policies and procedures should emphasize the fundamental principles, which are reinforced in particular by (a) The leadership of the firm, (b) E ducation and training, (c) Monitoring, and (d) A process for dealing with non-compliance.

8. Independence

18	The firm should establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, others subject to independence requirements (including experts contracted by the firm and network firm personnel), maintain independence where required by the Code. Such policies and procedures should enable the firm to – (a) Communicate its independence requirements to its personnel and, where applicable, to others subject to them, and (b) Identify and evaluate circumstances and relationships that create threats to independence, and to take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement.
19	Such policies and procedures should require – (a) Engagement partners to provide the firm with relevant information about client engagements, including the scope of services, to enable the firm to evaluate the overall impact, if any, on independence requirements, (b) Personnel to promptly notify the firm of circumstances and relationships that create a threat to independence so that appropriate action can be taken, and (c) The accumulation and communication of relevant information to appropriate personnel so that – 1. The firm and its personnel can readily determine whether they satisfy independence requirements, 2. The firm can maintain and update its records relating to independence, and 3. The firm can take appropriate action regarding identified threats to independence.
20	The firm should establish policies and procedures designed to provide it with reasonable assurance that it is notified of breaches of independence requirements, and to enable it to take appropriate actions to resolve such situations. The policies and procedures should include requirements for – (a) All who are subject to independence requirements to promptly notify the firm of independence breaches of which they become aware, (b) The firm to promptly communicate identified breaches of these policies and procedures to – (i) The engagement partner who, with the firm, needs to address the breach, and (ii) Other relevant personnel in the firm and those subject to the independence requirements who need to take appropriate action, and (c) Prompt communication to the firm, if necessary, by the engagement partner and the other individuals referred to in subparagraph (b)(ii) of the actions taken to resolve the matter, so that the firm can determine whether it should take further action.
23	At least annually, the firm should obtain written confirmation of compliance with its policies and procedures on independence from all firm personnel required to be independent in terms of the requirements of the Code.
25	The Code discusses the familiarity threat that may be created by using the same senior personnel on an

	assurance engagement over a long period of time and the safeguards that might be appropriate to address such a threat. Accordingly, the firm should establish policies and procedures – (a) Setting out criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time, and (b) For all audits of financial statements of listed entities, requiring the rotation of the engagement partner after a specified period in compliance with the Code.
26	Using the same senior personnel on assurance engagements over a prolonged period may create a familiarity threat or otherwise impair the quality of performance of the engagement. Therefore, the firm should establish criteria for determining the need for safeguards to address this threat. In determining appropriate criteria, the firm considers such matters as (a) the nature of the engagement, including the extent to which it involves a matter of public interest, and (b) the length of service of the senior personnel on the engagement. Examples of safeguards include rotating the senior personnel or requiring an engagement quality control review.
27	The familiarity threat is particularly relevant in the context of financial statement audits of listed entities. **For these audits, the engagement partner should be rotated after a pre-defined period, normally not more than seven year**

8. Acceptance and Continuance of Client Relationships and Specific Engagements –

28	☞ The firm should establish policies and procedures for the acceptance and continuance of client relationships and specific engagements, designed to provide it with reasonable assurance that it will undertake or continue relationships and engagements only where it – (a) Has considered the **integrity of the client** and does not have information that would lead it to conclude that the client lacks integrity, (b) Is competent to perform the engagement and has the **capabilities, time and resources** to do so, and (c) Can comply with the **ethical requirements.** ☞ The firm should obtain such information as it considers necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. When issues have been identified, and the firm decides to accept or continue the client relationship or a specific engagement, it should **document how the issues were resolved.**

Significant matters to consider (examples) –

Client Integrity	Firm Capabilities	Ethical Issues
✓ The identity and business reputation of the client's principal owners, key management, related parties and those charged with its governance. ✓ The nature of the client's operations, including its business practices. ✓ Information concerning the attitude of the client's principal owners, key management and those charged with its governance towards such matters as aggressive interpretation of accounting standards and the internal control environment. ✓ Whether the client is aggressively concerned with maintaining the firm's fees as low as possible. ✓ Indications of an inappropriate	✓ Firm personnel have knowledge of relevant industries or subject matters, ✓ Firm personnel have experience with relevant regulatory or reporting requirements, or the ability to gain the necessary skills and knowledge effectively, ✓ The firm has sufficient personnel with the necessary capabilities and competence, Experts are available, if needed, ✓ Individuals meeting the criteria and eligibility requirements to perform engagement quality control review are available, where applicable, and	✓ The professional and legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities, and ✓ The possibility of withdrawing from the engagement or from both the engagement and the client relationship.

limitation in the scope of work. ✓ Indications that the client might be involved in money laundering or other criminal activities. ✓ The reasons for the proposed appointment of the firm and non-reappointment of the previous firm.	✓ The firm would be able to complete the engagement within the reporting deadline.	

9. Human Resources –

36	The firm should establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the capabilities, competence, and commitment to ethical principles necessary to perform its engagements in accordance with professional standards and regulatory and legal requirements, and to enable the firm or engagement partners to issue reports that are appropriate in the circumstances.
37	☞ Such policies and procedures address the following personnel issues – (a) Recruitment, (b) Performance evaluation, (c) Capabilities, (d) Competence, (e) Career development, (f) Promotion, (g) Compensation, and (h) Estimation of personnel needs. ☞ Addressing these issues enables the firm to ascertain the number and characteristics of the individuals required for the firm's engagements. The firm's recruitment processes include procedures that help the firm select individuals of integrity as well as the capacity to develop the capabilities and competence necessary to perform the firm's work.

10. Assignment of Engagement Teams –

42	The firm should assign responsibility for each engagement to an engagement partner. The firm should establish policies and procedures requiring that – (a) The identity and role of the engagement partner are communicated to key members of the client's management and those charged with governance, (b) The engagement partner has the appropriate capabilities, competence, authority and time to perform the role, and (c) The responsibilities of the engagement partner are clearly defined and communicated to that partner.
44	The firm should also assign appropriate staff with the necessary capabilities, competence and time to perform engagements in accordance with professional standards and regulatory and legal requirements, and to enable the firm or engagement partners to issue reports that are appropriate in the circumstances.

11. Engagement Performance –

46	The firm should establish policies and procedures designed to provide it with reasonable assurance that engagements are performed in accordance with professional standards and regulatory and legal requirements, and that the firm or the engagement partner issues reports that are appropriate in the circumstances.

12. Consultation –

51	The firm should establish policies and procedures designed to provide it with reasonable assurance that –

	(a) Appropriate consultation takes place on difficult or contentious matters, (b) Sufficient resources are available to enable appropriate consultation to take place, (c) The nature and scope of such consultations are documented, and (d) Conclusions resulting from consultations are documented and implemented.
52	Consultation includes discussion, at the appropriate professional level, with individuals within or outside the firm who have specialized expertise, to resolve a difficult or contentious matter

13. Differences of Opinion –

57	The firm should establish policies and procedures for dealing with and resolving differences of opinion within the engagement team, with those consulted and, where applicable, between the engagement partner and the engagement quality control reviewer. Conclusions reached should be documented and implemented.
58	Such procedures encourage identification of differences of opinion at an early stage, provide clear guidelines as to the successive steps to be taken thereafter, and require documentation regarding the resolution of the differences and the implementation of the conclusions reached. **The report should not be issued until the matter is resolved.**

14. Engagement Quality Control Review –

60	The firm should establish policies and procedures requiring, for appropriate engagements, an engagement quality control review that provides an objective evaluation of the significant judgments made by the engagement team and the conclusions reached in formulating the report. Such policies and procedures should – (a) Require an engagement quality control review for all audits of financial statements of listed entities, (b) Set out criteria against which all other audits and reviews of historical financial information, and other assurance and related services engagements should be evaluated to determine whether an engagement quality control review should be performed, and (c) Require an engagement quality control review for all engagements meeting the criteria established in compliance with subparagraph (b).
61	The firm's policies and procedures should require the completion of the engagement quality control review before the report is issued.
63	The firm should establish policies and procedures setting out – (a) The nature, timing and extent of an engagement quality control review, (b) Criteria for the eligibility of engagement quality control reviewers, and (c) Documentation requirements for an engagement quality control review.

15. Criteria for the eligibility of Engagement Quality Control Reviewers –

68	The firm's policies and procedures should address the appointment of engagement quality control reviewers and establish their eligibility through – (a) The technical qualifications required to perform the role, including the necessary experience and authority, and (b) The degree to which an engagement quality control reviewer can be consulted on the engagement without compromising the reviewer's objectivity.

16. Documentation of the Engagement Quality Control Review –

73	Policies and procedures on documentation of the engagement quality control review should require documentation that – (a) The procedures required by the firm's policies on engagement quality control review have been performed, (b) The engagement quality control review has been completed before the report is issued, and (c) The reviewer is not aware of any unresolved matters that would cause the reviewer to believe

	that the significant judgments the engagement team made and the conclusions they reached were not appropriate.

17. Engagement Documentation –

74	The firm should establish policies and procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized.

18. Confidentially, Safe Custody, Integrity, Accessibility and retrievability of Engagement –

77	The firm should establish policies and procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation.

19. Retention of Engagement Documentation –

82	The firm should establish policies and procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm or as required by law or regulation.

20. Monitoring –

86	The firm should establish policies and procedures designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, operating effectively and complied with in practice. Such policies and procedures should include an ongoing consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements.
93	The firm should evaluate the effect of deficiencies noted as a result of the monitoring process and should determine whether they are either – (a) Instances that do not necessarily indicate that the firm's system of quality control is insufficient to provide it with reasonable assurance that it complies with professional standards and regulatory and legal requirements, and that the reports issued by the firm or engagement partners are appropriate in the circumstances, or (b) Systemic, repetitive or other significant deficiencies that require prompt corrective action.
94	The firm should communicate to relevant engagement partners and other appropriate personnel deficiencies noted as a result of the monitoring process and recommendations for appropriate remedial action.
95	The firm's evaluation of each type of deficiency should result in recommendations for one or more of the following – (a) Taking appropriate remedial action in relation to an individual engagement or member of personnel, (b) The communication of the findings to those responsible for training and professional development, (c) Changes to the quality control policies and procedures, and (d) Disciplinary action against those who fail to comply with the policies and procedures of the firm, especially those who do so repeatedly.
96	Where the results of the monitoring procedures indicate that a report may be inappropriate or that procedures were omitted during the performance of the engagement, the firm should determine what further action is appropriate to comply with relevant professional standards and regulatory and legal requirements. It should also consider obtaining legal advice.
97	At least annually, the firm should communicate the results of the monitoring of its quality control system to engagement partners and other appropriate individuals within the firm, including the firm's chief executive officer or, if appropriate, it's managing partner(s). Such communication should enable the firm and these individuals to take prompt and appropriate action where necessary in accordance with their defined roles and responsibilities. Information communicated should include the following – (a) A description of the monitoring procedures performed.

	(b) The conclusions drawn from the monitoring procedures. (c) Where relevant, a description of systemic, repetitive or other significant deficiencies and of the actions taken to resolve or amend those deficiencies.

21. Complaints and Allegations –

101	The firm should establish policies and procedures designed to provide it with reasonable assurance that it deals appropriately with – (a) Complaints and allegations that the work performed by the firm fails to comply with professional standards and regulatory and legal requirements, and (b) Allegations of non-compliance with the firm's system of quality control.

22. Documentation –

106	The firm should establish policies and procedures requiring appropriate documentation to provide evidence of the operation of each element of its system of quality control.
107	How such matters are documented is the firm's decision. For example, large firms may use **electronic databases** to document matters such as independence confirmations, performance evaluations and the results of monitoring inspections. Smaller firms may use more simpler and informal methods such as manual notes, checklists and forms
108	Factors to consider when determining the **form and content** of documentation evidencing the operation of each of the elements of the system of quality control include the following – ✓ The size of the firm and the number of offices. ✓ The degree of authority both personnel and offices have. ✓ The nature and complexity of the firm's practice and organization.
108	The firm **retains** this documentation for a period of time sufficient to permit those performing monitoring procedures to evaluate the firm's compliance with its system of quality control, or for a longer period if required by law or regulation.

Standard on Auditing (SA) 200 (Revised)

Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing

1. Effective Date [Para – 10]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

This Standard on Auditing (SA) establishes the:

1. Independent Auditor's **Overall responsibilities** when conducting an audit of financial statements in accordance with SAs,
2. It sets out the **Overall objectives** of the Independent Auditor,
3. Explains the **nature and scope of an audit designed** to enable the Independent Auditor to meet those objective,
4. It Explains the **Scope, authority and structure of the SAs,**
5. **General responsibilities** of the independent auditor applicable in all audits, and
6. **Obligation to comply with the SAs.**

Note → SAs are written in the context of an audit of financial statements by an auditor. They are to be adapted as necessary in the circumstances when applied to audits of other historical financial information. **[Para – 2]**

3. Overall Objectives of the Auditor

Para No.	Aspect	Description
11 & 12	**Auditor's Objective**	In conducting an audit of financial statements, the overall objectives of the auditor are: (a) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and (b) To report on the financial statements, and communicate as required by the SAs, in accordance with the auditor's findings. Note → When – (a) Reasonable assurance cannot be obtained and (b) A qualified opinion in the auditor's report is insufficient in the circumstances for purposes of reporting to the intended users of the financial statements, the SAs require that the auditor disclaim an opinion or withdraw from the engagement, where withdrawal is legally permitted. ***[Para – 12]***

4. Definitions [Para – 13]

S. N.	Terms	Description
(a)	**Applicable financial reporting framework**	The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation and presentation of the financial statements, - (a) That is acceptable in view of the nature of the entity and the objective of the

		financial statements, **or** (b) That is required by law or regulation.
(b)	**Fair Presentation Framework**	A financial reporting framework that requires **compliance** with the requirements of the framework and – (a) Acknowledges explicitly or implicitly that, to achieve **Fair Presentation** of the financial statements, it may be necessary for management to provide **disclosures** beyond those specifically required by the framework, or (b) Acknowledges explicitly that it may be necessary for management to **depart** from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in **extremely rare circumstances.**
(c)	**Compliance Framework**	A financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (a) or (b) above.
(d)	**Audit Evidence**	**Information** used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both - information contained in the accounting records underlying the financial statements and other information. For purposes of the SAs: (a) **Sufficiency** of audit evidence is the measure of the **quantity** of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement and also by the quality of such audit evidence. (b) **Appropriateness** of audit evidence is the measure of the **quality** of audit evidence, ✓ That is, its relevance and its reliability in providing support for the conclusions on which the auditor's opinion is based.
(e)	**Audit Risk**	The risk that the auditor expresses an **inappropriate audit opinion** when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.
(f)	**Auditor**	☞ "Auditor" is used to refer to the **person or persons conducting the audit**, usually the engagement partner or other members of the engagement team, or, as applicable, the firm. ☞ Where an SA expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term "engagement partner" rather than "auditor" is used. "Engagement partner" and "firm" are to be read as referring to their public sector equivalents where relevant.
(g)	**Detection Risk**	The risk that the **procedures performed** by the auditor to reduce audit risk to an acceptably low level **will not detect a misstatement** that exists and that could be material, either individually or when aggregated with other misstatements.
(h)	**Financial Statement**	☞ A **structured representation of historical financial information**, including related notes, intended to communicate an entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information. ☞ The term "financial statements" ordinarily refers to a **complete set of financial statements** as determined by the requirements of the **applicable financial reporting framework,** but can also refer to a single financial statement.
(i)	**Historical Financial Information**	**Information expressed in financial terms** in relation to a particular entity, derived primarily from that entity's accounting system, about economic **events occurring in past time periods** or about economic **conditions or circumstances at points in time**

		in the past.
(j)	**Management**	The person(s) with executive responsibility for the conduct of the entity's operations. For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.
(k)	**Mis – Statement**	☞ A difference between the amounts, classification, presentation, or disclosure of a **reported** financial statement item and the amount, classification, presentation, or disclosure that is **required for the item to be** in accordance with the applicable financial reporting framework. Misstatements can arise from error or fraud. ☞ When the auditor expresses an opinion on whether the financial statements are presented fairly, in all material respects, or give a true and fair view, misstatements also include those **adjustments** of amounts, classifications, presentation, or disclosures that, in the auditor's judgment, are necessary for the financial statements to be presented fairly, in all material respects, or to give a true and fair view.
(l)	**Premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted** ***[This is also referred to as the "Premise"]***	Management and, where appropriate, those charged with governance have the following responsibilities that are fundamental to the conduct of an audit in accordance with SAs. That is, responsibility: (i) For the **preparation and presentation of the financial statements** in accordance with the applicable financial reporting framework. This includes the design, implementation and maintenance **of Internal Control** relevant to the preparation of Financial Statements that are free from material mis – statement, whether due to fraud and error; and (ii) To provide the auditor with: a. **All information**, such as records and documentation, and other matters that are relevant to the preparation and presentation of the financial statements; b. Any **additional information** that the auditor may request from management and, where appropriate, those charged with governance; and c. **Unrestricted access** to those within the entity from whom the auditor determines it necessary to obtain audit evidence. Note → In the case of a fair presentation framework, the responsibility is for – (a) The preparation and ***fair*** presentation of the financial statements in accordance with the financial reporting framework; or (b) The preparation of financial statements that give a ***true and fair view*** in accordance with the financial reporting framework. This applies to all references to "preparation and presentation of the financial statements" in the SAs.
(m)	**Professional Judgment**	The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in **making informed decisions** about the courses of action that are **appropriate** in the circumstances of the audit engagement.
(n)	**Professional Skepticism**	An attitude that includes – ✓ **A questioning mind,** ✓ B**eing alert** to conditions which may indicate possible misstatement due to error or fraud, and ✓ A **critical assessment** of audit evidence.
(o)	**Reasonable Assurance**	In the context of an audit of financial statements, a **high, but not absolute,** level of assurance.

(p)	**Risk of Material Mis – Statement**	The risk that the financial statements are **materially misstated prior to audit.** This consists of two components, at the assertion level, viz. (a) Inherent Risk, and (b) Control Risk. [See separate points below]
(q)	**Inherent Risk**	The **susceptibility** of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other mis-statements, **before consideration of any related controls.`**
(r)	**Control Risk**	The risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, **will not be prevented, or detected and corrected,** on a timely basis by the entity's internal control.
(s)	**Those Charge with governance**	The person(s) or organisation(s) (e.g., a corporate trustee) with **responsibility for overseeing the strategic direction** of the entity and obligations related to the **accountability of the entity.**

5. Requirements of SA – 200(R)

Para No.	*Aspects*	*Description/Auditors' Duties*
14	*Ethical Requirements*	☞ The auditor shall comply with relevant **ethical requirements,** including those pertaining to independence, relating to financial statement audit engagements. ☞ Relevant ethical requirements ordinarily comprise the Code of Ethics issued by the Institute of Chartered Accountants of India. The Code establishes the following as the fundamental principles of professional ethics: [Para A.15] (a) Integrity; (b) Objectivity; (c) Professional competence and due care; (d) Confidentiality; and (e) Professional behaviour Note → (a) The Code describes independence as comprising both **independence of mind and independence in appearance.** (b) The auditor's independence from the entity safeguards the auditor's ability to form an audit opinion without being affected by influences that might compromise that opinion ***[Para A. 16]***
15	*Professional Skepticism*	☞ The auditor shall plan and perform an audit with **professional skepticism** recognising that circumstances may exist that cause the financial statements to be materially misstated. **[Para – 15]** ☞ Professional skepticism includes **being alert** to, for example: ✓ Audit evidence that **contradicts** other audit evidence obtained. ✓ Information that brings into question the **reliability of documents** and responses to inquiries to be used as audit evidence. ✓ Conditions that may indicate possible **fraud.** ✓ Circumstances that suggest the need for **audit procedures in addition to those required by the SAs.** ☞ Maintaining professional skepticism throughout the audit is necessary if the auditor is, for example, to reduce the risks of: ✓ Overlooking unusual circumstances. ✓ Over generalising when drawing conclusions from audit observations.

		✓ Using inappropriate assumptions in determining the nature, timing, and extent of the audit procedures and evaluating the results thereof.
16	***Professional Judgment***	☞ The auditor shall exercise **professional judgment** in planning and performing an audit of financial statements. **[Para – 16]** ☞ Professional judgment is essential to the proper conduct of an audit. Professional judgment is necessary in particular regarding decisions about**: [Para A.23]** ✓ Materiality and audit risk. ✓ The nature, timing, and extent of audit procedures used to meet the requirements of the SAs and gather audit evidence. ✓ Evaluating whether sufficient appropriate audit evidence has been obtained, and whether more needs to be done to achieve the objectives of the SAs and thereby, the overall objectives of the auditor. ✓ The evaluation of management's judgments in applying the entity's applicable financial reporting framework. ✓ The drawing of conclusions based on the audit evidence obtained, for example, assessing the reasonableness of the estimates made by management in preparing the financial statements. ***Features of Professional Judgement*** ☞ The exercise of professional judgment in any particular case is based on the facts and circumstances that are known by the auditor.**[Para A.25]** ☞ Professional judgment can be evaluated based on whether the judgment reached reflects a competent **application of auditing and accounting principles** and is **appropriate** in the light of, and consistent with, the facts and circumstances that were known to the auditor up to the date of the auditor's report.**[Para A.26]** ☞ Professional judgment needs to be **exercised throughout the audit**.**[Para A.27]** ☞ Professional judgment also needs to be appropriately documented.**[Para A.27]** ☞ Professional judgement is **not to be used as the justification** for decisions that are not otherwise supported by the facts & circumstances of the engagement or sufficient appropriate audit evidence.
17	***Audit Evidence and Audit Risk***	☞ To obtain reasonable assurance, the auditor shall obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor's opinion. **[Para – 17]** ☞ Audit evidence is necessary to support the auditor's opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. Audit evidence might be the information obtained from sources inside or outside the entity such as previous audits, entity's accounting records, expert's report etc.**[Para A.28]** ☞ Audit risk is a function of the risks of material misstatement and detection risk. The assessment of risks is a matter of professional judgment, rather than a matter capable of precise measurement.**[Para A.32]** ☞ The risks of material misstatement may exist at two levels: **[Para A.34]** ✓ The overall financial statement level - relates pervasively to the financial statements as a whole and potentially affect many assertions.**[Para A.35]** ✓ The assertion level for classes of transactions, account balances, and disclosures – such risks are assessed in order to determine the nature, timing, and extent of further audit procedures necessary to obtain sufficient

		appropriate audit evidence. This evidence enables the auditor to express an opinion on the financial statements at an acceptably low level of audit risk.**[Para A.36]** ➢ The risks of material misstatement at the assertion level consist of two components: inherent risk and control risk.**[Para A.37]**
Conduct of an audit in accordance with SAs has the following aspects/components –		
18 To 20	*Complying with SAs relevant to the4 Audit*	☞ The auditor shall comply with **all SAs relevant** to the audit. An SA is relevant to the audit when the SA is **in effect** and the **circumstances** addressed by the SA exist.**[Para – 18]** ☞ The Auditor shall have an **understanding of the entire text** of an SA's, including its application and other Explanatory Material, to understand its objectives and to apply its requirements **properly.[Para – 19]** ☞ The auditor shall **not** represent compliance with SAs in the auditor's report unless the auditor has **complied** with the requirements of this SA and all other SAs relevant to the audit.**[Para – 20]**
21	*Objectives stated in individual SAs*	☞ To achieve the **overall objectives** of the auditor, the auditor shall use the objectives stated in relevant SAs in planning and performing the audit, having regard to the interrelationships among the SAs, to: **[Para – 21]** (a) Determine whether any audit procedures in addition to those required by the SAs are necessary in pursuance of the objectives stated in the SAs; and (b) Evaluate whether sufficient appropriate audit evidence has been obtained. ☞ Each SA contains one or more objectives which provide a link between the requirements and the overall objectives of the auditor. The objectives in individual SAs serve to focus the auditor on the desired outcome of the SA, while being specific enough to assist the auditor in: **[Para A.66]** ✓ **Understanding** what needs to be accomplished and, where necessary, the appropriate means of doing so; and ✓ Deciding whether **more needs to be done to achieve** them in the particular circumstances of the audit.
22 to 23	*Complying with Relevant Requirements*	☞ ***Normal Situations:*** The auditor shall comply with each requirement of an SA unless, in the circumstances of the audit: ***[Para – 22]*** (a) The entire SA is not relevant; or (b) The requirement is not relevant because it is conditional and the condition does not exist. ☞ ***Exceptional Situations: [Para – 23]*** ✓ In exceptional situations the auditor may judge it necessary to depart from a relevant requirement in an SA. In such circumstances, the auditor shall perform alternative audit procedures to achieve the aim of that requirement. ✓ The need for the auditor to depart from a relevant requirement is expected to arise only where the requirement is for a specific procedure to be performed and, in the specific circumstances of the audit, that procedure would be ineffective in achieving the aim of the requirement.
24	*Failure to Achieve an Objective*	☞ If an objective in a relevant SA cannot be achieved, the auditor shall evaluate whether this prevents the auditor from achieving the overall objectives of the auditor and thereby requires the auditor, in accordance with the SAs, to **modify the auditor's opinion or withdraw from the engagement.[Para – 24]** ✓ Whether an objective has been achieved is a matter for the auditor's professional judgment. That judgment takes account of the results of audit

		procedures performed in complying with the requirements of the SAs, and the auditor's evaluation of whether sufficient appropriate audit evidence has been obtained and whether more needs to be done in the particular circumstances of the audit to achieve the objectives stated in the SAs.**[Para A.74]** ☞ Failure to achieve an objective represents a **significant matter requiring documentation** as per SA – 230(R). **[Para – 24]**

6. An Audit of Financial Statements

Para No.	*Aspect*	*Description/Auditors' Duties*
3	**Purpose of an audit of Financial Statement**	The purpose of an audit is to ***enhance the degree of confidence of intended users*** in the financial statements by the ***expression of an opinion by the auditor*** on: (a) Whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework and (b) In case of most General Purpose Frameworks, whether the financial statements are presented ***fairly***, in all material respects, or give a ***true and fair view*** in accordance with the framework. (c) An audit conducted in accordance with SAs and relevant Ethical Requirements enables the Auditor to form that opinion. (d) Where the applicable laws and regulations may require auditors to provide opinions on other specific matters, for (e.g. The effectiveness of internal control, or the consistency of a separate management report with the financial statements, etc.). **[Para A.1]** (e) While the SAs include requirements and guidance in relation to such matters to the extent that they are relevant to forming an opinion on the financial statements, the auditor would be required to undertake further work if the auditor had additional responsibilities to provide such opinions.**[ParaA.1]** Note → The auditor's opinion therefore does not assure, for example, the future viability of the entity nor the efficiency or effectiveness with which management has conducted the affairs of the entity. **[Para A.1]**
4	**Management's Responsibilities are absolute**	(a) The financial statements subject to audit are those of the entity, prepared and presented by management of the entity with oversight from those charged with governance. (b) SAs do not – (i) Impose responsibilities on management or those charged with governance and (ii) Do not override laws and regulations that govern their responsibilities. (c) An audit in accordance with SAs is conducted on the premise that management and, where appropriate, those charged with governance have responsibilities that are fundamental to the conduct of the audit. (d) As part of Management responsibility for the preparation and presentation of the financial statements, management and, where appropriate, those charged with governance are responsible for. **[Para A.3]** (i) The identification of the applicable financial reporting framework, in the context of any relevant laws or regulations. (ii) The preparation and presentation of the financial statements in

		accordance with that framework. (iii) An adequate description of that framework in the financial statements. Note → The audit of the financial statements does not relieve management or those charged with governance of those responsibilities. **[Para – 4]**
5.	**Reasonable Assurance e**	(a) As the basis for the auditor's opinion, SAs require the auditor to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. (b) Reasonable assurance is a high level of assurance. (c) Reasonable Assurance is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (i.e., the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level. Note → Reasonable Assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive.
6.	**Materiality Concept**	(a) The concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements. (b) In general, misstatements, including omissions, are considered to be material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. (c) Judgments about materiality are made in the light of surrounding circumstances, and are affected by the auditor's perception of the financial information needs of users of the financial statements, and by the size or nature of a misstatement, or a combination of both. (d) The auditor's opinion deals with the financial statements as a whole and therefore the auditor is not responsible for the detection of misstatements that are not material to the financial statements as a whole.
7.	**Auditor's Duties under SAs**	The SAs require that the auditor exercise professional judgment and maintain professional skepticism throughout the planning and performance of the audit and, among other things: (a) Identify and assess risks of material misstatement, by obtaining an understanding of the entity, its environment and internal control. (b) Obtain sufficient appropriate audit evidence about whether material misstatements exist, through designing and implementing appropriate responses to the assessed risks. (c) Form an opinion on the financial statements based on conclusion drawn from the audit evidence obtained.
8 & 9	**Form of Opinion**	(a) The form of opinion expressed by the auditor will depend upon the applicable financial reporting framework and any applicable laws or regulations. (b) The auditor may also have certain other communication and reporting responsibilities to users, management, those charged with governance, or parties outside the entity, in relation to matters arising from the audit. These may be established by the SAs or by applicable laws or regulations.

A.4 & A.8	**Financial Statement**	(a) ***General/Special Purpose:*** The financial statements may be prepared in accordance with a financial reporting framework designed to meet – (i) The common financial information needs of a wide range of users (i.e., "general purpose financial statements"), or (ii) The financial information needs of specific users (i.e., "special purpose financial statements"). (b) ***Complete Set of Financial Statements:*** Generally, Financial Statements are intended to provide information about the state of affairs, results of operations and cash flows of an entity. For such frameworks, a complete set of financial statements would include – 1. A Balance Sheet, 2. Statement of Profit and Loss, 3. A Cash Flow Statement, and 4. Related Notes. (c) ***Single Financial Statement:*** In certain Financial Reporting Frameworks, a single financial statement and the related notes might constitute a complete set of financial statements normally, for e.g. In Government Departments and local bodies, the primary financial statement is a statement of cash receipts and payments.
A.45	**Inherent Limitations of Audit**	The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit, which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive. The inherent limitations of an audit arise from – ✓ The **nature of financial reporting,** ✓ The **nature of audit procedures,** and ✓ The need for the audit to be conducted within a **reasonable period of time and at a reasonable cost.**

Standard on Auditing (SA) 210 (Revised)

Agreeing the terms of Audit Engagements

1. Effective Date [Para – 2]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

1. This Standard on Auditing (SA) deals with the **auditor's responsibilities** in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance.
2. This SA also establishes that there are certain **preconditions** to the audit, the responsibility of which rests with the management and, where appropriate, those charged with governance.

3. Overall Objectives of the Auditor

Para No.	*Aspect*	*Description*
3	**Auditor's Objective**	The objective of the auditor is to accept or continue an audit engagement only when the basis upon which it is to be performed has been agreed, through – (a) Establishing whether the **preconditions for an audit** are present, and (b) Confirming that there is a **common understanding** between the auditor and management (and where appropriate, Those Charged with Governance) of the terms of the audit engagement.

4. Definition

Para No.	*Aspect*	*Description*
4	**Per – conditions for an audit**	(a) The use by Management of an acceptable Financial Reporting Framework in the preparation of the Financial Statements, and (b) The **agreement** of Management and Those Charge with Governance, to the premises on which an audit is conducted.
5	**Management**	For the purpose of this SA, references to "Management" should be read hereafter as "Management and, where appropriate, Those Charged with Governance".

5. Requirement of SA – 210 (R)

1. *Pre – Conditions for Audit* [Para – 6]

To establish whether the per – condition for pan audit are present, the Auditor shall:

Para No.	*Aspect*	*Auditor's Duties*
6a.	**Reporting Framework**	Determine whether the financial reporting framework to be applied in the preparation of the financial statements is **acceptable** with reference to the following– (a) The **nature of the entity** (for example, whether it is a business enterprise, or a not for profit organization), **[Para A.4]**

		(b) The **purpose** of the financial statements (for example, whether they are prepared to meet the common financial information needs of a wide range of users or the financial information needs of specific users), **[Para A.4]** (c) **Nature of the financial statements** (for example, whether the financial statements are a complete set of financial statements or a single financial statement), and **[Para A.4]** (d) **Whether law or regulation prescribes** the applicable Financial Reporting Framework. **[Para A.4]**
A. 4 and A.9 read with Appendix 2	**Determining the Acceptability of General Purpose Frameworks**	**Acceptable financial reporting frameworks** normally exhibit the following **attributes** that result in information provided in financial statements that is useful to the intended users: (a) ***<u>Relevance</u>*** – The information provided in the financial statements is relevant to the nature of the entity and the purpose of the financial statements. (b) ***<u>Completeness</u>*** – Transactions and events, account balances and disclosures that could affect conclusions based on the financial statements are not omitted. (c) ***<u>Reliability</u>*** – The information provided in the financial statements – (i) Where applicable, reflects the economic substance of events and transactions and not merely their legal form; and (ii) Results in reasonably consistent evaluation, measurement, presentation and disclosure, when used in similar circumstances. (d) ***<u>Neutrality</u>*** – It contributes to information in the financial statements that is free from bias. (e) ***<u>Understandability</u>*** – The information in the financial statements is clear and comprehensive and not subject to significantly different interpretation.
6b	**Management Responsibility**	Obtain, the **agreement of management** that **it acknowledges and understands its responsibility** (a) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation. (b) For such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and (c) To provide the auditor with: ✓ Access to all information of which management is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters, ✓ Additional information that the auditor may request from management for the purpose of the audit, and ✓ Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.
2. *<u>Limitation on Scope prior to Acceptance</u>*		
7	**Limitation on Scope prior to Acceptance**	If management or those charged with governance impose a limitation on the scope of the auditor's work in the terms of a proposed audit engagement such that the **auditor believes the limitation will result in the auditor disclaiming an opinion** on the financial statements, the **auditor shall not accept** such a limited engagement as an **audit engagement**, unless required by law or regulation to do so.

	3. Other Factors affecting Acceptance	
8	**Other factors affecting Acceptance**	If the preconditions for an audit are not present, the auditor shall discuss the matter with management. Unless required by law or regulation to do so, **the auditor shall not accept the proposed audit engagement**: (a) If the auditor has determined that the **Financial Reporting Framework** to be applied in the preparation of the financial statements is **unacceptable**, **(except as provided in paragraph 19)**, or (b) If the agreement **(i.e. Management's Representation on its Responsibilities)** referred to in paragraph 6(b) has not been obtained. **Note → Students are requested to also refer Para 19 & 20 of SA – 210**
	4. Agreement on Audit Engagement Terms	
9	**Agreement on Audit Engagement Terms**	The auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate.
	5. Engagement Letter ***Principles relating to recording of Agreed Terms as above in Audit Engagement Letter, etc***	
10	**Audit Terms not Prescribed by Law or Regulation**	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 – a) **The objective and scope of the audit of the financial statements,** b) **The responsibilities of the auditor,** c) **The responsibilities of management,** d) **Identification of the applicable financial reporting framework for the preparation of the financial statements, and** e) **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.** f) The form of any other communication of results of the audit engagement. g) The fact that because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with SAs. h) Arrangements regarding the planning and performance of the audit, including the composition of the audit team. i) The expectation that management will provide written representations. j) The agreement of management to make available to the auditor draft financial statements and any accompanying other information in time to allow the auditor to complete the audit in accordance with the proposed timetable. k) The agreement of management to inform the auditor of facts that may affect the financial statements, of which management may become aware during the period from the date of the auditor's report to the date the financial statements are issued. l) The basis on which fees are computed and any billing arrangements. m) A request for management to acknowledge receipt of the audit engagement letter and to agree to the terms of the engagement outlined therein.

		n) The fact that the audit process may be subjected to a peer review under the Chartered Accountants Act, 1949. o) Arrangements concerning the involvement of other auditors and experts in some aspects of the audit. p) Arrangements concerning the involvement of internal auditors and other staff of the entity. q) Arrangements to be made with the predecessor auditor, if any, in the case of an initial audit. r) Any restriction of the auditor's liability when such possibility exists. s) A reference to any further agreements between the auditor and the entity. t) Any obligations to provide audit working papers to other parties. **Note →** **Points (a) to (e) are mandatory. Other items may be included in Audit Engagement Letter wherever relevant.** **Points (f) to (n) are covered by Para A.22 and Points (o) to (t) are covered by Para A.23.** **Note →** It is in the interests of both the entity and the auditor that the ***auditor sends an audit engagement letter before the commencement*** of the audit to help avoid misunderstandings with respect to the engagement.
11	**Audit Terms prescribed by Law or Regulation**	If law or regulation prescribes in sufficient detail the terms of the audit engagement referred to in paragraph 10, 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 as set out in paragraph 6(b).
12	**Management Responsibility to be documented**	☞ **If law or regulation prescribes responsibilities of management similar to those described in paragraph 6(b),** the auditor may determine that the law or regulation includes responsibilities that, in the auditor's judgment, are equivalent in effect to those set out in that paragraph. ☞ For such responsibilities that are equivalent, the auditor may use the wording of the law or regulation to describe them in the written agreement. ☞ For those responsibilities that are not prescribed by law or regulation such that their effect is equivalent, the written agreement shall use the description in paragraph 6(b).
	6. *Recurring Audits*	
13	**Assessment by Auditor**	On recurring audits, the auditor shall assess – ☞ Whether circumstances require the terms of the audit engagement to be revised and ☞ Whether there is a need to remind the entity of the existing terms of the audit engagement.
A.27	**Factors**	The following factors may make it appropriate to revise the terms of the audit engagement or to remind the entity of existing terms – ✓ Any indication that the **entity misunderstands the objective and scope** of the audit. ✓ Any **revised or special terms** of the audit engagement. ✓ A recent change of **senior management**. ✓ A significant change in **ownership.** ✓ A significant change in **nature or size of the entity's business.** ✓ A change in **legal or regulatory requirements.**

<table>
<tr><td></td><td></td><td>✓ A change in the Financial Reporting Framework adopted in the preparation of the financial statements.
✓ A change in other reporting requirements.</td></tr>
<tr><td colspan="3">7. <u>Change in Terms in Engagement</u></td></tr>
<tr><td>A.28</td><td>Request for Change</td><td>A request from the entity for the auditor to change the terms of the audit engagement may result from –
☞ A change in circumstances affecting the need for the service,
☞ A misunderstanding as to the nature of an audit as originally requested or
☞ A restriction on the scope of the audit engagement, whether imposed by management or caused by other circumstances.</td></tr>
<tr><td>A.29 & A.30</td><td>Evaluation by Auditor</td><td>a) A change in circumstances that affects the entity's requirements or a misunderstanding concerning the nature of the service originally requested may be considered a reasonable basis for requesting a change in the audit engagement. [Para A.29]
b) In contrast, a change may not be considered reasonable if it appears that the change relates to information that is incorrect, incomplete or otherwise unsatisfactory (For example might be where the auditor is unable to obtain sufficient appropriate audit evidence regarding receivables and the entity asks for the audit engagement to be changed to a review engagement to avoid a qualified opinion or a disclaimer of opinion). [Para A.30]</td></tr>
<tr><td>14, 15, 16 & 17</td><td>Auditor's Duties in Specific Situation</td><td>Where there is a change in terms of engagement, any of the following situations shall arise:
<table>
<tr><th>Para No.</th><th>Situation</th><th>The Auditor Shall –</th></tr>
<tr><td>14</td><td>There is no reasonable justification for change in terms of audit engagement</td><td>Not agree to a change in the terms of the Audit Engagement.</td></tr>
<tr><td>15</td><td>Prior to completing the audit engagement, the auditor is requested to change the audit engagement to an engagement that conveys a lower level of assurance (for e.g. a Review or a Related Services)</td><td>Determine whether there is reasonable justification for doing so.
Note → In case of a reasonable justification the report on the related service would not include reference to:
(a) The original audit engagement, or
(b) Any procedures that may have been performed in the original audit engagement. [Para A.32]</td></tr>
<tr><td>16</td><td>If the terms of the audit engagement are changed.</td><td>With Management agree on and record the new terms of the engagement in an engagement letter or other suitable form of written agreement.</td></tr>
<tr><td>17</td><td>If the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted by management to continue the original audit engagement</td><td>☞ Withdraw from the audit engagement where possible under applicable law or regulation, and
☞ Determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators</td></tr>
</table></td></tr>
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<table>
<tr><td colspan="3">8. Additional Considerations in Engagement Acceptance</td></tr>
<tr>
<td>18</td>
<td>Financial Reporting Standards supplemented by Law or Regulation</td>
<td>
<table>
<tr><th>S. N.</th><th>Situation</th><th>Auditor Shall –</th></tr>
<tr><td>1.</td><td>If financial reporting standards established by an authorised or recognised standards setting organization are supplemented by law or regulation</td><td>Determine whether there are any conflicts between the financial reporting standards and the additional requirements.</td></tr>
<tr><td>2.</td><td>If such conflicts exist</td><td>Discuss with management the nature of the additional requirements and shall agree whether:
✓ The additional requirements can be met through additional disclosures in the financial statements, or
✓ The description of the applicable financial reporting framework in the financial statements can be amended accordingly.</td></tr>
<tr><td>3.</td><td>If neither of the above actions is possible</td><td>Determine whether it will be necessary to modify the auditor's opinion in accordance with SA 705 (Revised)</td></tr>
</table>
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</tr>
<tr>
<td>19 & 20</td>
<td>Financial Reporting Framework prescribed by Law or Regulation</td>
<td>
<table>
<tr><th>Situation</th><th>Auditor's Shall –</th></tr>
<tr><td>If the auditor has determined that the financial reporting framework prescribed by law or regulation would be unacceptable but for the fact that it is prescribed by law or regulation. [Para – 19]</td><td>Accept the audit engagement only if the following conditions are present:
a) Management agrees to provide additional disclosures in the financial statements required to avoid the financial statements being misleading, and
b) It is recognised in the terms of the audit engagement that:
✓ The auditor's report on the financial statements will incorporate an Emphasis of Matter paragraph, drawing users' attention to the additional disclosures, in accordance with SA 706 (Revised), and
✓ Unless the auditor is required by law or regulation to express the auditor's opinion on the financial statements by using the phrases "present fairly, in all material respects", or "give a true and fair view" in accordance with the applicable financial reporting framework, the auditor's opinion on the financial statements will not include such phrases.</td></tr>
<tr><td>If the conditions outlined in Para 19 are not present and the auditor is required by law or</td><td>a) Evaluate the effect of the misleading nature of the financial statements on the auditor's</td></tr>
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<tr>
<td>regulation to undertake the audit engagement. [Para – 20]</td>
<td>report, and
b) Include appropriate reference to this matter in the terms of the audit engagement.</td>
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<tr>
<td>21</td>
<td>Auditor's Report Prescribed by Law or Regulation</td>
<td>
<table>
<tr>
<th>S.N.</th>
<th>Situation</th>
<th>Auditor Shall –</th>
</tr>
<tr>
<td>1.</td>
<td>Where the law or regulation applicable to the entity prescribes the layout or wording of the auditor's report in a form or in terms that are significantly different from the requirements of SAs.</td>
<td>In such circumstance evaluate:
a) Whether users might misunderstand the assurance obtained from the audit of the financial statements and, if so,
b) Whether additional explanation in the auditor's report can mitigate possible misunderstanding.</td>
</tr>
<tr>
<td>2.</td>
<td>If the auditor concludes that additional explanation in the auditor's report cannot mitigate possible misunderstanding</td>
<td>Not accept the audit engagement, unless required by law or regulation to do so.</td>
</tr>
<tr>
<td>3.</td>
<td>An audit conducted in accordance with such law or regulation does not comply with SAs</td>
<td>Not include any reference within the auditor's report to the audit having been conducted in accordance with SAs</td>
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Standard on Auditing (SA) 220 (Revised)
Quality Control for an Audit of Financial Statements

1. Effective Date [Para – 5]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

1. This Standard on Auditing (SA) deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements.
2. It also addresses, where applicable, the responsibilities of the engagement quality control reviewer.
3. This SA is to be read in conjunction with relevant ethical requirements.

3. Objectives of the Auditor [Para – 6]

Para No.	Aspect	Description
6	**Objective**	The objective of the auditor is to implement quality control procedures at the engagement level that provide the auditor with reasonable assurance that: (i) The audit complies with professional standards and regulatory and legal requirements, and (ii) The Auditor's Report issued is appropriate in the circumstances.

4. Definition [Para – 7]

S.N.	Aspect	Description
(a)	**Engagement Partner**	The partner or other person in the firm who is a member of the Institute of Chartered Accountants of India and is in full time practice and is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.
(b)	**Engagement Quality Control Review**	A process designed to provide an objective evaluation, before the report is issued, of the significant judgments the engagement team made and the conclusions they reached in formulating the report.
(c)	**Engagement Quality Control Reviewer**	A partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, with sufficient and appropriate experience and authority to objectively evaluate, before the report is issued, the significant judgments the engagement team made and the conclusions they reached in formulating the report. However, in case the review is done by a team of individuals, such team should be headed by a member of the Institute.
(d)	**Engagement team**	All personnel performing an engagement, including any experts contracted by the firm in connection with that engagement
(e)	**Firm**	A sole practitioner/proprietor, partnership, or any such entity of professional accountants, as may be permitted by law.
(f)	**Inspection**	In relation to completed engagements, procedures designed to provide evidence of compliance by engagement teams with the firm's quality control policies and procedures.

(g)	**Listed Entity**	An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are traded under the regulations of a recognized stock exchange or other equivalent body.
(h)	**Monitoring**	A process comprising an ongoing consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements, designed to enable the firm to obtain reasonable assurance that its system of quality control is operating effectively.
(i)	**Network firm**	A firm or entity that belongs to a network.
(j)	**Network**	A larger structure: (i) That is aimed at cooperation, and (ii) 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.
(k)	**Partner**	Any individual with authority to bind the firm with respect to the performance of a professional services engagement.
(l)	**Personnel**	Partners and Staff.
(m)	**Professional Standards**	Engagement Standards, as defined in the "Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services", issued by the Institute of Chartered Accountants of India and relevant ethical requirements as contained in the Code of Ethics issued by the Institute.
(n)	**Relevant Ethical Requirements**	Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise the Code of Ethics of the Institute of Chartered Accountants of India related to an audit of financial statements.
(o)	**Staff**	Professionals, other than partners, including any experts which the firm employs.
(p)	**Suitably qualified external person**	An individual outside the firm with the capabilities and competence to act as an engagement partner, for example a partner or an employee (with appropriate experience) of another firm.

5. Requirements of SA – 220

Para No.	**Aspects**	**Description**
8	**Leadership Responsibility**	The engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned.
9 & 10	**Relevant Ethical Requirements**	a) Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. b) If the Engagement Partner comes to know that the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action.
11	**Independence**	The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall – a) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate circumstances and relationships that create threats to independence, b) 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 the audit engagement, and c) 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 engagement, where withdrawal is permitted by law or regulation. d) The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action.
12 & 13	**Acceptance and Continuance of Client Relationships and Audit Engagements**	a) The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed, and shall determine that conclusions reached in this regard are appropriate. b) If the engagement partner obtains information that would have caused the firm to decline the audit engagement had that information been available earlier, the engagement partner shall communicate that information promptly to the firm, so that the firm and the engagement partner can take the necessary action
14	**Assignment of Engagement Teams**	The engagement partner shall be satisfied that the engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to: a) Perform the audit engagement in accordance with professional standards and regulatory and legal requirements, and b) Enable an auditor's report that is appropriate in the circumstances to be issued.
Engagement Performance		
15	**Direction, Supervision & Performance**	The engagement partner shall take responsibility – a) The direction, supervision and performance of the audit engagement in compliance with professional standards and regulatory and legal requirements, and b) The auditor's report being appropriate in the circumstances.
16 & 17	**Reviews**	a) The engagement partner shall take responsibility for reviews being performed in accordance with the firm's review policies and procedures. b) On or before the date of the auditor's report, the engagement partner shall, through a review of the audit documentation and discussion with the engagement team, be satisfied that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor's report to be issued.
18	**Consultation**	The engagement partner shall – a) Take responsibility for the engagement team undertaking appropriate consultation on difficult or contentious matters, b) Be satisfied that members of the engagement team have undertaken appropriate consultation during the course of the engagement, both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm, c) Be satisfied that the nature and scope of, and conclusions resulting from, such consultations are agreed with the party consulted, and d) Determine that conclusions resulting from such consultations have been implemented.
Engagement Quality Control Review		

<table>
<tr><td>19</td><td>Concept of Review</td><td>For audits of financial statements of listed entities, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required, the engagement partner shall –
a) Determine that an engagement quality control reviewer has been appointed,
b) Discuss significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer, and
c) Not date the auditor's report until the completion of the engagement quality control review.</td></tr>
<tr><td>20</td><td>Duties of QC Reviewer</td><td>The engagement quality control reviewer shall perform an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor's report. This evaluation shall involve –
a) Discussion of significant matters with the engagement partner,
b) Review of the financial statements and the proposed auditor's report,
c) Review of selected audit documentation relating to the significant judgments the engagement team made and the conclusions it reached, and
d) Evaluation of the conclusions reached in formulating the auditor's report and consideration of whether the proposed auditor's report is appropriate.</td></tr>
<tr><td>21</td><td>Special Matters – Listed Entities</td><td>For audits of financial statements of listed entities, the engagement quality control reviewer, on performing an engagement quality control review, shall also consider the following –
a) The engagement team's evaluation of the firm's independence in relation to the audit engagement,
b) 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, and
c) Whether audit documentation selected for review reflects the work performed in relation to the significant judgments made and supports the conclusions reached.</td></tr>
<tr><td>22</td><td>Difference of Opinion</td><td>If differences of opinion arise –
a) Within the Engagement Team,
b) With those Consulted or,
c) Where applicable, between the Engagement Partner and the Engagement Quality Control Reviewer.
The engagement team shall follow the firm's policies and procedures for dealing with and resolving differences of opinion.</td></tr>
<tr><td>23</td><td>Monitoring</td><td>☞ An effective system of quality control includes a monitoring process designed to provide the firm with reasonable assurance that its policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively.
☞ The engagement partner shall consider the results of the firm's monitoring process as evidenced in the latest information circulated by the firm and, if applicable, other network firms and whether deficiencies noted in that information may affect the audit engagement.</td></tr>
<tr><td colspan="3">Documentation</td></tr>
<tr><td colspan="2">The Auditor shall document [Para – 24]</td><td>The QC Reviewer shall document [Para – 25]</td></tr>
</table>

The auditor shall document – a) Issues identified with respect to compliance with relevant ethical requirements and how they were resolved. b) Conclusions on compliance with independence requirements that apply to the audit engagement, and any relevant discussions with the firm that support these conclusions. c) Conclusions reached regarding the acceptance and continuance of client relationships and audit engagements. d) The nature and scope of, and conclusions resulting from, consultations undertaken during the course of the audit engagement.	The engagement quality control reviewer shall document, for the audit engagement reviewed, that – a) The procedures required by the firm's policies on engagement quality control review have been performed, b) The engagement quality control review has been completed on or before the date of the auditor's report, and c) The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made and the conclusions they reached were not appropriate.

Standard on Auditing (SA) 230 (Revised)

Audit Documentation

1. Effective Date [Para – 4]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2009.**

2. Scope of this SA [Para – 1]

- ✓ This Standard on Auditing (SA) deals with the auditor's responsibility to prepare audit documentation for an audit of financial statements. It is to be adapted as necessary in the circumstances when applied to audits of other historical financial information.
- ✓ The application of this SA – 230 is not limited to specific requirement, additional documentation requirements may be established by –
  - ☞ Laws or Regulations, and
  - ☞ Other SAs

3. Auditor's Objective [Para – 5]

The objective of the auditor is to prepare documentation that provides –

(a) A sufficient and appropriate record of the basis for the auditor's report, and

(b) Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.

4. Definitions [Para – 6]

S.N.	Aspect	Definitions
(a)	**Audit Documentation**	1. The record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached (terms such as "working papers" or "work papers" are also sometimes used). 2. Audit documentation may be recorded on paper or on electronic or other media. Examples of audit documentation include – [Para A.3] ✓ Audit programmes ✓ Analyses ✓ Issues memoranda ✓ Summaries of significant matters ✓ Letters of confirmation and representation ✓ Checklists ✓ Correspondence (including e-mail) concerning significant matters. 3. The documentation is not limited to records prepared by the auditor but may include other appropriate records such as minutes of meetings prepared by the entity's personnel and agreed by the auditor. Others with whom the auditor may discuss significant matters may include other personnel within the entity, and external parties, such as persons providing professional advice to the entity. [Para A.3] 4. The auditor need not include in audit documentation superseded drafts of working papers and financial statements, notes that reflect incomplete or preliminary thinking, previous copies of documents corrected for

		typographical or other errors, and duplicates of documents. [Para A.4] 5. The documentation is not limited to records prepared by the auditor but may include other appropriate records such as minutes of meetings prepared by the entity's personnel and agreed by the auditor. Others with whom the auditor may discuss significant matters may include other personnel within the entity, and external parties, such as persons providing professional advice to the entity. [Para A.14]
(b)	**Audit File**	One or more folders or other storage media, in physical or electronic form, containing the records that comprise the audit documentation for a specific engagement.
(c)	**Experienced Auditor**	An individual (whether internal or external to the firm) who has practical audit experience, and a reasonable understanding of – 1. Audit processes, 2. SAs and applicable legal and regulatory requirements, 3. The business environment in which the entity operates, and 4. Auditing and financial reporting issues relevant to the entity's industry.

5. Purpose of Documentation [Para – 2 & 3]

Nature of Audit Documentation	Basic Purpose of Audit Documentation
Audit documentation that meets the requirements of this SA and the specific documentation requirements of other relevant SAs provides – (a) Evidence of the auditor's basis for a conclusion about the achievement of the overall objective of the auditor, and (b) Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.	1. Assisting the engagement team to plan and perform the audit. 2. Assisting members of the engagement team responsible for supervision to direct and supervise the audit work, and to discharge their review responsibilities in accordance with Proposed SA 220 (Revised). 3. Enabling the engagement team to be accountable for its work. 4. Retaining a record of matters of continuing significance to future audits. 5. Enabling the conduct of quality control reviews and inspections in accordance with SQC 1. 6. Enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements.
Additional Requirement	

6. Requirements of SA – 230

<table>
<tr><th>Para No.</th><th>Aspect</th><th>Description/Auditor's Duties</th></tr>
<tr><td>7</td><td>Timeliness</td><td>The auditor shall prepare audit documentation on a timely basis.</td></tr>
<tr><td colspan="3"><u>Documentation of Audit Procedures and Audit Evidence</u></td></tr>
<tr><td>8</td><td>Basic Requirements</td><td>The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand –
(a) The nature, timing, and extent of the audit procedures performed to comply with the SAs and applicable legal and regulatory requirements,
(b) The results of the audit procedures performed, and the audit evidence obtained, and
(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.
☞ Judging the significance of a matter requires an objective analysis of the facts and circumstances. Examples of significant matters include – [Para A.8]
1. Matters that give rise to significant risks (as defined in SA 315).Results of audit procedures indicating –
(a) That the financial statements could be materially misstated, or
(b) A need to revise the auditor's previous assessment of the risks of material misstatement and the auditor's responses to those risks.
2. Circumstances that cause the auditor significant difficulty in applying necessary audit procedures.
3. Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis on Matter Paragraph in the Auditor's Report</td></tr>
<tr><td>A.2</td><td>Factors Governing Form & Content of Working Papers</td><td>The form, content and extent of audit documentation depend on factors such as –
1. The size and complexity of the entity.
2. The nature of the audit procedures to be performed.
3. The identified risks of material misstatement.
4. The significance of the audit evidence obtained.
5. The nature and extent of exceptions identified.
6. 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.
7. The audit methodology and tools used.</td></tr>
<tr><td>9</td><td>Audit Procedures</td><td>In documenting the nature, timing and extent of audit procedures performed, the auditor shall record –
(a) The identifying characteristics of the specific items or matters tested,
(b) Who performed the audit work and the date such work was completed, and
(c) Who reviewed the audit work performed and the date and extent of such review.</td></tr>
<tr><td>10</td><td>Discussions</td><td>The auditor shall document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place.</td></tr>
<tr><td>11</td><td>Inconsistencies</td><td>If the auditor identified information that is inconsistent with the auditor's final conclusion regarding a significant matter, the auditor shall document how the auditor addressed the inconsistency.</td></tr>
<tr><td>12</td><td>Departure from SA</td><td>If, in exceptional circumstances, the auditor judges it necessary to depart from a relevant requirement in a SA, the auditor shall document how the alternative</td></tr>
</table>

	Requirement	audit procedures performed achieve the aim of that requirement, and the reasons for the departure. A requirement is not relevant only in the cases where – [Para A.19] (a) The SA is not relevant [for example, if an entity does not have an internal audit function, nothing in SA – 610 (R) is relevant], or (b) The requirement is conditional and the condition does not exist (for example, the requirement to modify the auditor's opinion where there is an inability to obtain sufficient appropriate audit evidence, and there is no such inability).
13	**Matters arising after the Date of Auditor's Report**	If, in exceptional circumstances, the auditor performs new or additional audit procedures or draws new conclusions after the date of the auditor's report, the auditor shall document – (a) The circumstances encountered, (b) The new or additional audit procedures performed, audit evidence obtained, and conclusions reached, and their effect on the auditor's report, and (c) When and by whom the resulting changes to audit documentation were made and reviewed.
	Assembly of Final Audit File	
14,15 & 16	1. The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report. [Para – 14] 2. After the assembly of the final audit file has been completed, the auditor shall not delete or discard audit documentation of any nature before the end of its retention period. [Para – 15] 3. SQC 1 requires firms to establish policies and procedures for the timely completion of the assembly of audit files. An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than ***60 days*** after the date of the auditor's report. [Para A.21] 4. The completion of the assembly of the final audit file after the date of the auditor's report is an administrative process that does not involve the performance of new audit procedures or the drawing of new conclusions. Changes may, however, be made to the audit documentation during the final assembly process if they are administrative in nature. Examples of such changes include – [Para A.22] ✓ Deleting or discarding superseded documentation. ✓ Sorting, collating and cross referencing working papers. ✓ Signing off on completion checklists relating to the file assembly process. ✓ Documenting audit evidence that the auditor has obtained, discussed and agreed with the relevant members of the engagement team before the date of the auditor's report. 5. SQC 1 requires firms to establish policies and procedures for the retention of engagement documentation. The retention period for audit engagements ordinarily is no shorter than ***seven years*** from the date of the auditor's report, or, if later, the date of the group auditor's report. [Para A.23] 6. In circumstances other than those envisaged in paragraph 13 where the auditor finds it necessary to modify existing audit documentation or add new audit documentation after the assembly of the final audit file has been completed, the auditor shall, regardless of the nature of the modifications or additions, document – [Para – 16] (a) The specific reasons for making them, and (b) When and by whom they were made and reviewed.	
A.25	**Ownership of Audit**	☞ Standard on Quality Control (SQC) 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance

	Documentation	and Related Services Engagements", issued by the Institute, provides that, unless otherwise specified by law or regulation, 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, or, in the case of assurance engagements, the independence of the auditor or of his personnel.

Standard on Auditing (SA) 240 (Revised)

The Auditor's Responsibilities Relating to Fraud, in an Audit of Financial Statements

1. Effective Date [Para – 9]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2009.**

2. Scope of this SA [Para – 1]

This Standard on Auditing (SA) deals with the auditor's responsibilities relating to fraud in an audit of financial statements. Specifically, it expands on how SA 315, "Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment," and SA 330, "The Auditor's Responses to Assessed Risks," are to be applied in relation to risks of material misstatement due to fraud.

3. Auditor's Objective [Para – 10]

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

4. Definitions [Para – 11]

S.N.	Aspect	Definition
(a)	**Fraud**	An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.
(b)	**Fraud Risk Factors**	Events or conditions that indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud.

5. Characteristic s [Para – 2 & 3]

Para No.	Description
2	☞ Misstatements in the financial statements can arise from either fraud or error. ☞ The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional.
3	☞ Although fraud is a broad legal concept, for the purposes of the SAs, the auditor is concerned with fraud that causes a material misstatement in the financial statements. ☞ Two types of intentional misstatements are relevant to the auditor – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets. 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.
6	☞ Fraud may involve sophisticated and carefully organized schemes designed to conceal it, such as forgery, deliberate failure to record transactions, or intentional misrepresentations being made to the auditor. ☞ Attempts at concealment may be even more difficult to detect when accompanied by collusion. Collusion may cause the auditor to believe that audit evidence is persuasive when it is, in fact, false.

	☞ While the auditor may be able to identify potential opportunities for fraud to be perpetrated, it is difficult for the auditor to determine whether misstatements in judgment areas such as accounting estimates are caused by fraud or error.
7	The risk of the auditor not detecting a material misstatement resulting from management fraud is greater than for employee fraud, because management is frequently in a position to directly or indirectly manipulate accounting records, present fraudulent financial information or override control procedures designed to prevent similar frauds by other employees.

6. Responsibility for Fraud Prevention and Detection [Para – 4]

- ☞ The primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.
- ☞ It is important that management, with the oversight of those charged with governance, place a strong emphasis on fraud prevention, which may reduce opportunities for fraud to take place, and fraud deterrence, which could persuade individuals not to commit fraud because of the likelihood of detection and punishment.
- ☞ This involves a commitment to creating a culture of honesty and ethical behavior which can be reinforced by an active oversight by those charged with governance.
- ☞ In exercising oversight responsibility, those charged with governance consider the potential for override of controls or other inappropriate influence over the financial reporting process, such as efforts by management to manage earnings in order to influence the perceptions of analysts as to the entity's performance and profitability.

6. Responsibility of Auditor [Para 5 – 8]

S.N.	Aspect	Auditor Responsibility
(a)	**Reasonable Assurance**	☞ An auditor conducting an audit in accordance with SAs is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. [Para – 5] ☞ Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements will not be detected, even though the audit is properly planned and performed in accordance with the SAs. [Para – 5] ☞ The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error.[Para – 6]
(b)	**Professional Skepticism**	☞ When obtaining reasonable assurance, the auditor is responsible for maintaining an attitude of professional skepticism throughout the audit, considering the potential for management override of controls and recognizing the fact that audit procedures that are effective for detecting error may not be effective in detecting fraud. ☞ The requirements in this SA are designed to assist the auditor in identifying and assessing the risks of material misstatement due to fraud and in designing procedures to detect such misstatement.

7. Requirements

1. Professional Skepticism –		
Para No.	**Aspect**	**Description/Auditor's Duties**

<table>
<tr><td>12</td><td>Attitude of Skepticism</td><td>The auditor shall maintain an attitude of professional skepticism throughout the audit, recognizing the possibility that a material misstatement due to fraud could exist, notwithstanding the auditor's past experience of the honesty and integrity of the entity's management and those charged with governance.

Note → Audit of Financial Statements is aimed at expression of opinion and not on the meticulous detection of each fraud and error. The Auditor uses his judgement in obtaining reasonable assurance on the Financial Statements. He would not investigate each and every transaction in depth to identify frauds and errors, unless circumstances arouse his suspicion.</td></tr>
<tr><td>13</td><td>Authenticity of Records</td><td>☞ Unless the auditor has reason to believe the contrary, the auditor may accept records and documents as genuine.
☞ If conditions identified during the audit, cause the auditor to believe that a document may not be authentic or that terms in a document have been modified but not disclosed to the auditor, the auditor shall investigate further.</td></tr>
<tr><td>14</td><td>Inconsistencies</td><td>Where responses to inquiries of management or those charged with governance are inconsistent, the auditor shall investigate the inconsistencies.</td></tr>
<tr><td colspan="3">2. <u>Discussion among the Engagement Team –</u></td></tr>
<tr><td>15</td><td>Discussion</td><td>☞ SA 315 requires a discussion among the engagement team members and a determination by the engagement partner of matters which are to be communicated to those team members not involved in the discussion. This discussion shall place particular emphasis on how and where the entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud might occur.
☞ The discussion shall occur notwithstanding the engagement team members' beliefs that management and those charged with governance are honest and have integrity.</td></tr>
<tr><td colspan="3">3. <u>Risk Assessment Procedures and Related Activities</u> → When performing risk assessment procedures and related activities to obtain an understanding of the entity and its environment, including the entity's internal control, required by SA 315, the auditor shall perform the following procedures to obtain information for use in identifying the risks of material misstatement due to fraud [Para – 16]. –</td></tr>
<tr><td>17</td><td>Inquiry of Management</td><td>The auditor shall make inquiries of management regarding –
(a) Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments,
(b) Management's process for identifying and responding to the risks of fraud in the entity, including any specific risks of fraud that management has identified or that have been brought to its attention, or classes of transactions, account balances, or disclosures for which a risk of fraud is likely to exist,

Note → In the case of entities with multiple locations management's processes may include different levels of monitoring of operating locations, or business segments.
Management may also have identified particular operating locations or business segments for which a risk of fraud may be more likely to exist. [Para A.14]</td></tr>
</table>

		(c) Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity, and (d) Management's communication, if any, to employees regarding its views on business practices and ethical behavior.
18 & 19	**Inquiry of Others within the Entity**	☞ The auditor shall make inquiries of management, and others within the entity as appropriate, to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity. [Para – 18] ☞ For those entities that have an internal audit function, the auditor shall make inquiries of internal audit to determine whether it has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain its views about the risks of fraud. [Para – 19]
20 & 21	**With Respect to Those Charged With Governance**	☞ Unless all of those charged with governance are involved in managing the entity, the auditor shall obtain an understanding of how those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks. [Para – 20] ☞ The auditor shall make inquiries of those charged with governance to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity. These inquiries are made in part to corroborate the responses to the inquiries of management. [Para – 21]
22	**Unusual or Unexpected Relationships**	The auditor shall evaluate whether unusual or unexpected relationships that have been identified in performing analytical procedures, including those related to revenue accounts, may indicate risks of material misstatement due to fraud.
23	**Other Information**	The auditor shall consider whether other information obtained by the auditor indicates risks of material misstatement due to fraud. ***For example –*** ☞ Engagements to review interim financial information may be relevant in the identification of the risks of material misstatement due to fraud. ☞ The discussion among team members may provide information that is helpful in identifying such risks.
24	**Evaluation of Fraud Risk Factors**	☞ The auditor shall evaluate whether the information obtained from the other risk assessment procedures and related activities performed indicates that one or more fraud risk factors are present. ☞ While fraud risk factors may not necessarily indicate the existence of fraud, they have often been present in circumstances where frauds have occurred and therefore may indicate risks of material misstatement due to fraud.
	4. Identification and Assessment of Risks due to Fraud –	
25	**I & A the risk at FS Level and at Assertion Level**	In accordance with SA 315, the auditor shall identify and assess the risks of material misstatement due to fraud – ✓ At the financial statement level, and ✓ At the assertion level for classes of transactions, account balances and disclosures.
26	**I & A the risk based on presumption**	☞ When identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions or assertions give rise to such risks.

		☞ Paragraph 47 specifies the documentation required when the auditor concludes that the presumption is not applicable in the circumstances of the engagement and, accordingly, has not identified revenue recognition as a risk of material misstatement due to fraud.
27	**Assessed risk as Significant Risk**	The auditor shall treat those assessed risks of material misstatement 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.
5. Responses to Assessed Risk of Material Mis – Statement due to Fraud –		
28 & 29	**At Financial Statement Level**	In accordance with SA 330, the auditor shall determine overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level. [Para – 28] In determining overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level, the auditor shall – (a) Assign and supervise personnel taking account of the knowledge, skill and ability of the individuals to be given significant engagement responsibilities and the auditor's assessment of the risks of material misstatement due to fraud for the engagement, (b) Evaluate whether the selection and application of accounting policies by the entity, particularly those related to subjective measurements and complex transactions, may be indicative of fraudulent financial reporting resulting from management's effort to manage earning, and (c) Incorporate an element of unpredictability in the selection of the nature, timing and extent of audit procedures.
30	**At Assertion Level**	The Auditor shall design and perform further audit procedures whose nature, timing and extent are responsive to the assessed risk of material mis – statement due to fraud at the assertion level.
31, 32 & 33	**Risk related to Management override of Controls**	☞ Management is in a unique position to perpetrate (commit) fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities. Due to the unpredictable way in which such override could occur, it is a risk of material misstatement due to fraud and thus a significant risk. [Para – 31] ☞ ***Audit Procedure*** – The Auditor shall design and perform audit procedures in the areas relating to – (i) Journal Entries, (ii) Accounting Estimates, and (iii) Unusual Transaction. [Refer table below] [Para – 32] ☞ ***Additional Procedure*** – The auditor shall determine whether, in order to respond to the identified risks of management override of controls, the auditor needs to perform other audit procedures in addition to those specifically referred to above. [Para – 33]

6. Audit Procedures towards Management Override of Controls

Aspect	Description/Auditor's Duties
Journal Entries	✓ Test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements. ✓ Make inquiries of individuals involved in the financial reporting

		process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments, ✓ Select journal entries and other adjustments made at the end of a reporting period, and ✓ Consider the need to test journal entries and other adjustments throughout the period
	Accounting Estimates	✓ Review accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud. ✓ Evaluate whether the judgments and decisions made by management in making the accounting estimates included in the financial statements, even if they are individually reasonable, indicate a possible bias on the part of the entity's management that may represent a risk of material misstatement due to fraud. If so, the auditor shall re - evaluate the accounting estimates taken as a whole, and ✓ Perform a retrospective review of management judgments and assumptions related to significant accounting estimates reflected in the financial statements of the prior year.
	Unusual Transaction	For significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual given the auditor's understanding of the entity and its environment and other information obtained during the audit, the auditor shall evaluate whether the business rationale (or the lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets.
		7. Evaluation of Audit Evidence
34	**Analytical Procedures**	The auditor shall evaluate whether analytical procedures that are performed when forming an overall conclusion as to whether the financial statements as a whole are consistent with the auditor's understanding of the entity and its environment indicate a previously unrecognized risk of material misstatement due to fraud.
35	**Indentifies a Misstatement**	When the auditor identifies a misstatement, the auditor shall evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the auditor shall evaluate the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management representations, recognizing that an instance of fraud is unlikely to be an isolated occurrence.
36	**Assessment of the Risks of Material Misstatement**	☞ If the auditor identifies a misstatement, whether material or not, and the auditor has reason to believe that it is or may be the result of fraud and that management (in particular, senior management) is involved, the auditor shall re-evaluate the assessment of the risks of material misstatement due to fraud and its resulting impact on the nature, timing and extent of audit procedures to respond to the assessed risks. ☞ The auditor shall also consider whether circumstances or conditions indicate possible collusion involving employees, management or third parties when reconsidering the reliability of evidence previously obtained.
37	**Implications**	When the auditor confirms that, or is unable to conclude whether, the financial statements are materially misstated as a result of fraud the auditor shall evaluate the implications for the audit.
		8. Auditor Unable to Continue the Engagement –

38	**Auditor Unable to Continue the Engagement**	If, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit, the auditor shall – (a) Determine the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities, (b) Consider whether it is appropriate to withdraw from the engagement, where withdrawal from the engagement is legally permitted, and (c) If the auditor withdraws – 1. Discuss with the appropriate level of management and those charged with governance, the auditor's withdrawal from the engagement and the reasons for the withdrawal, and 2. 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.
9. Management Representation –		
39	**Management Representation**	The auditor shall obtain written representations from management and, where applicable, those charged with governance that – (a) They acknowledges their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud, (b) They have disclosed to the auditor the results of management's assessment of the risk that the financial statements may be materially misstated as a result of fraud, (c) They have disclosed to the auditor their knowledge of fraud or suspected fraud affecting the entity involving – 1. Management, 2. Employees who have significant roles in internal control, or 3. Others where the fraud could have a material effect on the financial statements, and (d) They have disclosed to the auditor their knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.
10. Communication to Management and with Those Charged with Governance –		
40	**To Management**	If the auditor has identified a fraud or has obtained information that indicates that a fraud may exist, the auditor shall communicate these matters on a timely basis to the appropriate level of management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities.
41 & 42	**To Those Charge with Governance**	☞ Unless all of those charged with governance are involved in managing the entity, if the auditor has identified or suspects fraud involving – [Para – 41] 1. Management, 2. Employees who have significant roles in internal control, or 3. Others where the fraud results in a material misstatement in the financial

		statements. ☞ The auditor shall communicate these matters to those charged with governance on a timely basis. If the auditor suspects fraud involving management, the auditor shall communicate these suspicions to those charged with governance and discuss with them the nature, timing and extent of audit procedures necessary to complete the audit. [Para – 42]
43	**To Regulatory and Enforcement Authorities**	☞ If the auditor has identified or suspects a fraud, the auditor shall determine whether there is a responsibility to report the occurrence or suspicion to a party outside the entity. ☞ Although the auditor's professional duty to maintain the confidentiality of client information may preclude such reporting, the auditor's legal responsibilities may override the duty of confidentiality in some circumstances.
		11. Documentation –
44	**Matter covered by SA – 315(R)**	☞ The significant decisions reached during the discussion among the engagement team regarding the susceptibility of the entity's financial statements to material misstatement due to fraud, and ☞ The identified and assessed risks of material misstatement due to fraud at the financial statement level and at the assertion level.
45	**Matters Covered by SA – 330(R)**	☞ The overall responses to the assessed risks of material misstatement due to fraud at the financial statement level and the nature, timing and extent of audit procedures, and the linkage of those procedures with the assessed risks of material misstatement due to fraud at the assertion level, and ☞ The results of the audit procedures, including those designed to address the risk of management override of controls.
46	**Communication**	The auditor shall document communications about fraud made to management, those charged with governance, regulators and others.
47	**Revenue Recognition**	When the auditor has concluded that the presumption that there is a risk of material misstatement 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.

I. Examples of Fraud Risk Factors – Fraudulent Financial Reporting

A. Incentives / Pressures –

1. **Financial Stability or Profitability is threatened by economic, industry, or entity operating condition, e.g.**
   (a) High degree of competition or market saturation, accompanied by declining margins.
   (b) High vulnerability to rapid changes, such as changes in technology, product obsolescence, or interest rates.
   (c) Significant declines in customer demand and increasing business failures in either the industry or overall economy.
   (d) Operating losses making the threat of bankruptcy, foreclosure, or hostile takeover imminent.
   (e) Recurring negative cash flows from operations or an inability to generate cash flows from operations while reporting earnings and earnings growth.
   (f) Rapid growth or unusual profitability especially compared to that of other companies in the same industry.
   (g) New accounting, statutory, or regulatory requirements.

2.	**Excessive pressure exists for management to meet the requirements or expectations of third parties due to the following –** (a) Profitability or trend level expectations of investment analysts, institutional investors, significant creditors, or other external parties (particularly expectations that are unduly aggressive or unrealistic), including expectations created by management in, for example, overly optimistic press releases or annual report messages. (b) Need to obtain additional debt or equity financing to stay competitive—including financing of major research and development or capital expenditures. (c) Marginal ability to meet exchange listing requirements or debt repayment or other debt covenant requirements. (d) Perceived or real adverse effects of reporting poor financial results on significant pending transactions, such as business combinations or contract awards.
3.	**Information available indicates that the personal financial situation of management or those charged with governance is threatened by the entity's financial performance arising from the following** (a) Significant financial interests in the entity. (b) 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. (c) Personal guarantees of debts of the entity. (d) There is excessive pressure on management or operating personnel to meet financial targets established by those charged with governance, including sales or profitability incentive goals.

	B. Opportunities
1.	**The nature of the industry or the entity's operations provides opportunities to engage in fraudulent financial reporting that can arise from the following** (a) Significant related-party transactions not in the ordinary course of business or with related entities not audited or audited by another firm. (b) 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. (c) Assets, liabilities, revenues, or expenses based on significant estimates that involve subjective judgments or uncertainties that are difficult to corroborate. (d) Significant, unusual, or highly complex transactions, especially those close to period end that pose difficult "substance over form" questions. (e) Significant operations located or conducted across international borders in jurisdictions where differing business environments and cultures exist. (f) Use of business intermediaries for which there appears to be no clear business justification. (g) Significant bank accounts or subsidiary or branch operations in tax-haven jurisdictions for which there appears to be no clear business justification.
2.	**The monitoring of management is not effective as a result of the following** (a) Domination of management by a single person or small group (in a non owner-managed business) without compensating controls. (b) Oversight by those charged with governance over the financial reporting process and internal control is not effective.
3.	**There is a complex or unstable organizational structure, as evidenced by the following** (a) Difficulty in determining the organization or individuals that have controlling interest in the entity. (b) Overly complex organizational structure involving unusual legal entities or managerial lines of authority. (c) High turnover of senior management, legal counsel, or those charged with governance.

4. Internal control components are deficient as a result of the following

(a) Inadequate monitoring of controls, including automated controls and controls over interim financial reporting (where external reporting is required).

(b) High turnover rates or employment of accounting, internal audit, or information technology staff those are not effective.

(c) Accounting and information systems that are not effective, including situations involving significant deficiencies in internal control

C. Attitudes/Rationalisations

1. Communication, implementation, support, or enforcement of the entity's values or ethical standards by management, or the communication of inappropriate values or ethical standards, that are not effective.
2. Non-financial management's excessive participation in or preoccupation with the selection of accounting policies or the determination of significant estimates.
3. Known history of violations of securities laws or other laws and regulations, or claims against the entity, its senior management, or those charged with governance alleging fraud or violations of laws and regulations.
4. Excessive interest by management in maintaining or increasing the entity's stock price or earnings trend.
5. The practice by management of committing to analysts, creditors, and other third parties to achieve aggressive or unrealistic forecasts.
6. Management failing to remedy known significant deficiencies in internal control on a timely basis.
7. An interest by management in employing inappropriate means to minimize reported earnings for tax-motivated reasons.
8. Low morale among senior management.
9. The owner-manager makes no distinction between personal and business transactions.
10. Dispute between shareholders in a closely held entity.
11. Recurring attempts by management to justify marginal or inappropriate accounting on the basis of materiality.
12. The relationship between management and the current or predecessor auditor is strained, as exhibited by the following –
    (a) Frequent disputes with the current or predecessor auditor on accounting, auditing, or reporting matters.
    (b) Unreasonable demands on the auditor, such as unrealistic time constraints regarding the completion of the audit or the issuance of the auditor's report.
    (c) Restrictions on the auditor that inappropriately limit access to people or information or the ability to communicate effectively with those charged with governance.
    (d) Domineering management behavior 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 to or consulted on the audit engagement.

II. Examples of Fraud Risk Factors – Misappropriation of Assets

A. Incentives/Pressures –

1. Personal financial obligations may create pressure on management or employees with access to cash or other assets susceptible to theft to misappropriate those assets.
2. 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 –
    (a) Known or anticipated future employee layoffs.
    (b) Recent or anticipated changes to employee compensation or benefit plans.
    (c) Promotions, compensation, or other rewards inconsistent with expectations.

B. Opportunities –

1. **Certain characteristics or circumstances may increase the susceptibility of assets to misappropriation. For example, opportunities to misappropriate assets increase when there are the following**
   (a) Large amounts of cash on hand or processed.
   (b) Inventory items that are small in size, of high value, or in high demand.
   (c) Easily convertible assets, such as bearer bonds, diamonds, or computer chips.
   (d) Fixed assets which are small in size, marketable, or lacking observable identification of ownership.
2. **Inadequate internal control over assets may increase the susceptibility of misappropriation of those assets. For example, misappropriation of assets may occur because there is the following:**
   (a) Inadequate segregation of duties or independent checks.
   (b) Inadequate oversight of senior management expenditures, such as travel and other reimbursements. Inadequate management oversight of employees responsible for assets, for example, inadequate supervision or monitoring of remote locations.
   (c) Inadequate job applicant screening of employees with access to assets.
   (d) Inadequate record keeping with respect to assets.
   (e) Inadequate system of authorization and approval of transactions (for example, in purchasing).Inadequate physical safeguards over cash, investments, inventory, or fixed assets.
   (f) Lack of complete and timely reconciliations of assets.
   (g) Lack of timely and appropriate documentation of transactions, for example, credits for merchandise returns.
   (h) Lack of mandatory vacations for employees performing key control functions.
   (i) Inadequate management understanding of information technology, which enables information technology employees to perpetrate a misappropriation.
   (j) Inadequate access controls over automated records, including controls over and review of computer systems event logs.

C. Attitudes/Rationalisations –

1. Disregard for the need for monitoring or reducing risks related to misappropriations of assets.
2. Disregard for internal control over misappropriation of assets by overriding existing controls or by failing to take appropriate remedial action on known deficiencies in internal control.
3. Behavior indicating displeasure or dissatisfaction with the entity or its treatment of the employee.
4. Changes in behavior or lifestyle that may indicate assets have been misappropriated.Tolerance of petty theft.

Standard on Auditing (SA) 250 (Revised)

Consideration of Laws & Regulations in an Audit of Financial Statements

1. Effective Date [Para – 9]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2009.**

2. Scope of this SA [Para – 1]

1. This Standard on Auditing (SA) deals with the auditor's responsibility to consider laws and regulations when performing an audit of financial statements.
2. This SA does not apply to other assurance engagements in which the auditor is specifically engaged to test and report separately on compliance with specific laws or regulations.

3. Effect of Laws and Regulation [Para – 2]

1. The effect on the financial statements of laws and regulations varies considerably.
   - Those laws and regulations to which an entity is subject constitute the legal and regulatory framework.
   - The provisions of some laws or regulations have a direct effect on the financial statements in that they determine the reported amounts and disclosures in an entity's financial statements.
   - Other laws or regulations are to be complied with by management or set the provisions under which the entity is allowed to conduct its business but do not have a direct effect on an entity's financial statements.
   - Some entities operate in heavily regulated industries (such as banks and chemical companies). Others are subject only to the many laws and regulations that relate generally to the operating aspects of the business (such as those related to occupational safety and health).
2. 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 financial statements.

3. Definition [Para – 11]

1.	**Non – Compliance**	✓ Acts of omission or commission by the entity, ✓ Either intentional or unintentional, ✓ Which are contrary to the prevailing laws or regulations. • Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees. ✓ Non-compliance does not include personal misconduct (unrelated to the business activities of the entity) by those charged with governance, management or employees of the entity.

4. Type of Laws & Regulations [Para – 6]

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

1.	**Direct Effect**	Laws and Regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements such as tax and labour laws, and
2.	**Do not have direct effect**	Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental – • To the operating aspects of the business, • To an entity's ability to continue its business, or • To avoid material penalties (for example, compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations etc.)
Note → Non – Compliance with such laws and regulations may therefore have a material effect on the financial statements (see paragraph 14).		

5. Responsibilities

Para No.	Aspect	Description
3	**Management Responsibility**	1. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial statements. [Para – 3] 2. Examples of the types of policies and procedures an entity may implement to assist in the prevention and detection of non-compliance with laws and regulations – [Para A.2] (a) Monitoring legal requirements and ensuring that operating procedures are designed to meet these requirements. (b) Instituting and operating appropriate systems of internal control. (c) Developing, publicising and following a code of conduct. (d) Ensuring employees are properly trained and understand the code of conduct. (e) Monitoring compliance with the code of conduct and acting appropriately to discipline employees who fail to comply with it. (f) Engaging legal advisors to assist in monitoring legal requirements. (g) Maintaining a register of significant laws and regulations with which the entity has to comply within its particular industry and a record of complaints. **Note →** In larger entities, these policies and procedures may be supplemented by assigning appropriate responsibilities to the following – [Para A.2] • An internal audit function. • An audit committee. • A compliance function.

4 & 5	**Auditor's Responsibility**	1. The auditor is not responsible for preventing non-compliance and cannot be expected to detect non- compliance with all laws and regulations. [Para – 4] 2. The auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether caused by fraud or error. [Para – 5] 3. Sometimes the auditor may be specifically required to report, as part of the audit of the financial statements, on whether the entity complies with certain provisions of laws or regulations. [Para A.5] 4. In some audit engagements, (e.g. audit of government ventures and undertakings, etc.) there may be additional audit responsibilities with respect to the consideration of laws and regulations which may relate to the audit of financial statements or may extend to other aspects of the entity's operations. [Para A.6] 5. In the context of laws and regulations, the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for such reasons as the following – [Para – 5] (a) There are many laws and regulations, relating principally to the operating aspects of an entity that typically do not affect the financial statements and are not captured by the entity's information systems relevant to financial reporting. (b) 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. (c) Whether an act constitutes non – compliance is ultimately a matter for legal determination by a court of law. 6. Ordinarily, the further removed non-compliance is from the events and transactions reflected in the financial statements, the less likely the auditor is to become aware of it or to recognise the non- compliance.

6. Requirements

A. Basic Duties of an Auditor – [Para – 7]		
1.	**Direct Effect**	To obtain sufficient appropriate audit evidence about compliance with the provisions of those laws and regulations.
2.	**Do not Direct Effect**	Undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial statements.
B. The Auditor's Consideration of Compliance with Laws and Regulations		
12	**Obtain a general understanding of –**	As part of obtaining an understanding of the entity and its environment in accordance with SA the auditor shall obtain a general understanding of – (a) The legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates, and (b) How the entity is complying with that framework.
13	**Obtain sufficient appropriate audit evidence**	The auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements.

14	**Perform Audit Procedures**	Audit procedures to help identify instances of non- compliance with other laws and regulations that may have a material effect on the financial statements – (a) Inquiring of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations, and (b) Inspecting correspondence, if any, with the relevant licensing or regulatory authorities (e.g., RBI License for NBFC Companies.)
8 & 15	**Remain Alert**	Remain alert to the possibility that other audit procedures applied may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. **For Examples – [Para A.11]** ✓ Reading minutes, ✓ Inquiring of the entity's management and in-house legal counsel or external legal counsel concerning litigation, ✓ Claims and assessments, ✓ Performing substantive tests of details of classes of transactions, ✓ Account balances or disclosures.
16	**Written Representation**	Request Management and, where appropriate, those charged with governance to provide Written Representations that all known instances of non-compliance or suspected non- compliance with laws and regulations whose effects should be considered when preparing financial statements have been disclosed to the auditor. **Note →** W R's do not provide Sufficient Appropriate Audit Evidence on their own and, accordingly, do not affect the nature and extent of other audit evidence that is to be obtained bv the Auditor.
17	**Note for above 12 to 16 Para's**	In the absence of identified or suspected non-compliance, the auditor is not required to perform audit procedures regarding the entity's compliance with laws and regulations, other than those set out in paragraphs
	C. Audit Procedure's when Non – Compliance is Identified or Suspected	
A.13	**Indicators of Non–Compliance**	When the auditor becomes aware of the existence of, or information about, the following matters, it may be an indication of non-compliance with laws and regulations – ✓ Investigations by regulatory organisations and government departments or payment of fines or penalties. ✓ 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 by the entity or in its industry or to the services actually received. ✓ Purchasing at prices significantly above or below market price. ✓ 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. ✓ Unusual transactions with companies registered in tax havens. ✓ Payments for goods or services made other than to the country from which the goods or services originated. ✓ Payments without proper exchange control documentation. ✓ 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.

Para No.	Situation	The Auditor shall –
18	The auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance	(a) Obtain an understanding of the nature of the act and the circumstances in which it has occurred, and (b) Further information to evaluate the possible effect on the financial statement
19	Auditor suspects there may be non-compliance	(a) Discuss the matter with management and, where appropriate, those charged with governance. (b) The auditor shall consider the need to obtain legal advice. ✓ Management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, ✓ In the auditor's judgment, the effect of the suspected non-compliance may be material to the financial statements.
20	If sufficient information about suspected non-compliance cannot be obtained	Evaluate the effect of the lack of sufficient appropriate audit evidence on the auditor's opinion.

Note → **1.** The auditor shall evaluate the implications of non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations, and take appropriate action. [Para – 21 and A.17]

2. In exceptional cases, the auditor may consider whether, unless prohibited by law or regulation, withdrawal from the engagement is necessary when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances, even when the non-compliance is not material to the financial statements. When deciding whether withdrawal from the engagement is necessary, the auditor may consider seeking legal advice. [Para A.18]

3. If withdrawal from the engagement is prohibited, the auditor may consider alternative actions, including describing the non- compliance in an Other Matter(s) paragraph in the auditor's report. [Para A.18]

D. Reporting of Identified or Suspected Non – Compliance :

1. Reporting to Those Charge with Governance

Para No.	Situation	The Auditor shall –
22	**Management is not aware of non-compliance**	Communicate with those charged with governance matters involving non-compliance with laws and regulations that come to the auditor's attention during the course of the audit. **Note →** **Exceptions** – Reporting is not required: (a) When all the matters are clearly inconsequential, or (b) All TCWG are involved in the Management of the Entity, and therefore aware of matters communicated already by the Auditor.
23	**Non-Compliance is believed to be intentional and material**	Communicate the matter to those charged with governance as soon as practicable.

24	**Management/TC WG with Governance are involved in non – compliance**	☞ Communicate the matter to the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board. ☞ Where no higher authority exists, or if the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report, the auditor shall consider the need to obtain legal advice.

2. Reporting in Auditor's Report on Financial Statements

Para No.	Situation	The Auditor Shall –
25	The Auditor Non – Compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements	In accordance with SA – 705, express a Qualified or Adverse Opinion on the Financial Statements
26	The Auditor is precluded by management or those charged with governance from obtaining sufficient appropriate audit evidence to evaluate whether non-compliance that may be material to the financial statements has, or is likely to have, occurred	Express a Qualified Opinion or Disclaim an Opinion on the Financial Statements on the basis of a Limitation on the scope of the audit in accordance with SA 705.
27	The Auditor is unable to determine whether non-compliance has occurred because of limitations imposed by the circumstances rather than by management or those charged with governance	Evaluate the effect on the Auditor's Opinion in accordance with SA 705.

3. Reporting to Regulatory and Enforcement Authorities

28	**Identified or Suspects Non – Compliance with Laws and Regulations**	The Auditor Responsibility – 1. Determine whether the auditor has a responsibility to report the Identified or Suspected Non – Compliance to parties outside the entity. [Para – 28] 2. The auditor's professional duty to maintain the confidentiality of client information may preclude reporting identified or suspected non-compliance with laws and regulations to a party outside the entity. [Para A.19] 3. However, the auditor's legal responsibilities vary under different laws and regulations and, in certain circumstances. [Para A.19] 4. The duty of confidentiality may be overridden by statute, the law or courts of law. [Para A.19] 5. Under the present legal and regulatory framework for Financial Institutions in India, their auditor has a statutory duty to report the occurrence, or suspected occurrence, of Non – Compliance with Laws and Regulations to supervisory authorities. [Para A.19] **Note →** For example, the auditor is required to report certain matters of non-compliance to RBI as per the requirements of NBFC's Auditor's Report (Reserve Bank) Directions, 1988, issued by the Reserve Bank of India. Also, some laws or Regulations require the Auditor to report Mis – Statements to authorities in those cases where Management and TCWG, fail to take corrective action. [Para A.19] 6. In case of certain entities, such as national governments, regional (for example, state, provincial, territorial) governments, local (for example, city, town) governments and related governmental entities (for example, agencies, boards, commissions and enterprises), the auditor may be obliged to report on instances of non-compliance to governing authorities or to report them in the

		auditor's report. [Para A.20]
E. Documentation –		
29	**Documentation**	☞ The auditor shall document identified or suspected non-compliance with laws and regulations and the results of discussion with management and, where applicable, those charged with governance and other parties outside the entity ☞ The auditor's documentation of findings regarding identified or suspected non-compliance with laws and regulations may include, for example: ✓ Copies of records or documents. ✓ Minutes of discussions held with management, those charged with governance or parties outside the entity.

Space for Notes

Standard on Auditing (SA) 260 (Revised)

Communication with Those Charged with Governance

1. Effective Date [Para – 4]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2009.**

2. Scope of this SA [Para – 1]

1. Deals with the auditor's responsibility to communicate with those charged with governance in relation to an audit of financial statements.
2. Although this SA applies irrespective of an entity's governance structure or size, particular considerations apply where all of those charged with governance are involved in managing an entity, and for listed entities.
3. This SA does not establish requirements regarding the auditor's communication with an entity's management or owners unless they are also charged with a governance role.

3. Auditor's Objective w.r.t. TCWG [Para – 5]

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

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

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

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

4. Definitions [Para – 6]

S.N.	Terms	Definitions
(a)	**TCWG**	☞ The person(s) or organisation(s) (e.g., a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. ☞ For some entities those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector undertakings or an owner-manager. ☞ In some cases, those charged with governance are responsible for approving the entity's financial statements (in other cases management has this responsibility).
Governance Structures may vary reflecting different size and ownership characteristics. For Example		
A.5	**Form of Governance Structures**	☞ **Based on Legal Structure** – In most of the entities, those charged with governance hold positions that are an integral part of the entity's legal structure, for example, company directors. In others, for example, some government undertakings a body that is not part of the entity is charged with governance. [Para A.5] ☞ **Based on Management** – In some cases, some or all of those charged with governance are involved in managing the entity. In others, those charged with governance and management comprises different persons. [Para A.5] ☞ **Based on Responsibility** –

		✓ In some cases, TCWG are responsible for approving the entity's Financial Statements (In other cases management has this responsibility). [Para A.5] ✓ In most entities, governance is the collective responsibility of a governing body, such as a board of directors, a supervisory board, partners, proprietors, a committee of management, a council of governors, trustees, or equivalent persons. [Para A.6] ✓ In some smaller entities, however, one person may be charged with governance, for example, the owner-manager where there are no other owners, or a sole trustee. When governance is a collective responsibility, a subgroup such as an audit committee or even an individual, may be charged with specific tasks to assist the governing body in meeting its responsibilities. Alternatively, a subgroup or individual may have specific, legally identified responsibilities that differ from those of the governing body. [Para A.6]
(b)	**Management**	☞ The person(s) with executive responsibility for the conduct of the entity's operations. ☞ For some entities, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner – manager. ☞ Management is responsible for the preparation of the financial statements, overseen by those charged with governance, and in some cases management is also responsible for approving the entity's financial statements (in other cases those charged with governance have this responsibility).

5. Requirements

A. Management and Auditor's Responsibility to Communicate		
Para No.	**Aspect**	**Description**
A.2 & A.3	**Responsibility**	(a) The auditor is responsible for communicating with TCWG, observations that arise from the audit that are significant. Management also has responsibility to communicate matters of governance interest to TCWG. [Para A.2] (b) Communication by the auditor does not relieve management of this responsibility, and vice – versa. Communication of these matters by management may, however, affect the form or timing of the auditor's communication with those charged with governance. [Para A.2] (c) Laws or regulations may restrict the auditor's communication of certain matters with those charged with governance. In following cases, the auditor may consider obtaining Legal Advice. [Para A.3] ✓ For example, laws or regulations may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act. ✓ In some circumstances, potential conflicts between the auditor's obligations of confidentiality and obligations to communicate may be complex.
B. Those Charged with Governance		
7	**Identification**	The auditor shall determine the appropriate person(s) within the entity's governance structure with whom to communicate
8	**Sub Group**	When the auditor communicates with a subgroup of those charged with governance, for example, an audit committee, or an individual, the auditor shall

		determine whether the auditor also needs to communicate with the governing body.
9	**Governance = Management**	In some cases, all of those charged with governance are involved in managing the entity, for example, a small business where a single owner manages the entity and no one else has a governance role. In these cases, if matters required by this SA are communicated with person(s) with management responsibilities, and those person(s) with those Management responsibilities.

Note → If appropriate person(s) with whom to communicate may not be clearly identifiable from the applicable legal framework or other engagement circumstances, (for e.g. family-owned entities, some not-for-profit organisations, and some government entities). In such cases, the auditor may need to discuss and agree with the engaging party the relevant person(s) with whom to communicate. [Para A.7]

C. Matters to be Communicated

Para No.	Matters	Description
10	**Auditor's Responsibilities**	(a) The auditor is responsible for forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance, and [Para – 10] (b) The audit of the financial statements does not relieve management or those charged with governance of their responsibilities. [Para – 10] (c) The auditor's responsibility for performing the audit in accordance with SAs, The matters that SAs require to be communicated with TCWG. [Para A.13] (d) SAs do not require the auditor to design procedures for the purpose of identifying supplementary matters to communicate with those charged with governance. [Para A.13] (e) When applicable, the auditor's responsibility for communicating particular matters required by laws or regulations, by agreement with the entity or by additional requirements applicable to the engagement. [Para A.13]

Note → The above information is often included in the Engagement Letter or other suitable form of written agreement that records the agreed terms of engagement. Providing the Governance Team with a copy of such letter may be an appropriate way to communication with them.

11	**Audit Scope**	The auditor shall communicate with those charged with governance – 1. An overview of the planned scope and timing of the audit. [Para – 11] 2. How the auditor proposes to address the significant risks of material misstatement, whether due to fraud or error. [Para A.17] 3. The auditor's approach to internal control relevant to the audit. [Para A.17] 4. The application of the concept of materiality in the context of an audit. 5. Where the entity has an internal audit function, the extent to which the auditor will use the work of internal audit. [Para A.18]
12	**Significant Audit Finding**	The auditor shall communicate with those charged with governance – 1. The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures. 2. Significant difficulties, if any, encountered during the audit, such as – ✓ Significant delays in management providing required information. ✓ An unnecessarily brief time within which to complete the audit. ✓ Extensive unexpected effort required to obtain sufficient appropriate audit

		evidence. ✓ The unavailability of expected information. ✓ Restrictions imposed on the auditor by management. ✓ Management's unwillingness to make or extend its assessment of the entity's ability to continue as a going concern when requested **Note →** In some circumstances, such difficulties may constitute a scope limitation that leads to modification of the Auditor's Opinion 3. Unless all of those charged with governance are involved in managing the entity– (a) Significant matters, if any, arising from the audit that were discussed, or subject to correspondence with management, and (b) Written representations the auditor is requesting, and 4. Other matters, if any, arising from the audit that, in the auditor's professional judgment, is significant to the oversight of the financial reporting process.
13	**Auditor's Independence, In case of Listed Entities only**	(a) A statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence, and (b) (i) All relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgment, may reasonably be thought to bear on independence. (ii) This shall include total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity. (iii) These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor, and (c) The related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level.

Exception → In the case of listed entities may also be relevant in the case of some other entities, particularly those that may be of significant public interest because, as a result of their business, their size or their corporate status, they have a wide range of stakeholders. (E.g. public sector entities, credit institutions, insurance companies and retirement benefit funds.) [Para A.27]

On the other hand, there may be situations where communications regarding independence may not be relevant, (for example, where all of those charged with governance have been informed of relevant facts through their management activities.) [Para A.27]

D. Communication Process –

14	**Preliminary**	☞ The auditor shall communicate with those charged with governance the form, timing and expected general content of communications, covering aspects like – [Para – 14 & A.33] ✓ Purpose of Communications, ✓ The form in which communications will be made, ✓ The person(s) in the audit team and amongst those charged with governance who will communicate regarding particular matters, ✓ The auditor's expectation that communication will be two-way, and that those charged with governance will communicate with the auditor, matters

		they consider relevant to the audit, (for example, strategic decisions that may significantly affect the nature, timing and extent of audit procedures, the suspicion or the detection of fraud, and concerns with the integrity or competence of senior management). ✓ The process for taking action and reporting back on matters communicated by the auditor. ✓ The process for taking action and reporting back on matters communicated by those charged with governance. ☞ Before communicating matters with those charged with governance, [Para A.37] ✓ The auditor may discuss them with management, unless that is inappropriate. For example, it may not be appropriate to discuss questions of management's competence or integrity with management. ✓ When the entity has an internal audit function, the auditor may discuss matters with the internal auditor before communicating with those charged with governance. ☞ In addition to recognising management's executive responsibility, these initial discussions may clarify facts and issues, and give management an opportunity to provide further information and explanations.
15 & 16	**Forrms of Communications**	(a) The auditor shall communicate in writing with those charged with governance regarding significant findings from the audit when, in the auditor's professional judgment, oral communication would not be adequate. Written communications need not include all matters that arose during the course of the audit. [Para – 15] (b) The auditor shall communicate in writing with those charged with governance regarding auditor independence. [Para – 16] (c) In addition to the significance of a particular matter, the form of communication (e.g., whether to communicate orally or in writing, the extent of detail or summarisation in the communication, and whether to communicate in a structured or unstructured manner) may be affected by such factors as – [Para A.42] ✓ Whether the matter has been satisfactorily resolved. ✓ Whether management has previously communicated the matter. ✓ The size, operating structure, control environment, and legal structure of the entity. ✓ In the case of an audit of special purpose financial statements, whether the auditor also audits the entity's general purpose financial statements. ✓ Legal requirements. In some jurisdictions, a written communication with those charged with governance is required in a prescribed form by local law. ✓ The expectations of those charged with governance, including arrangements made for periodic meetings or communications with the auditor. ✓ The amount of ongoing contact and dialogue the auditor has with those charged with governance. ✓ Whether there have been significant changes in the membership of a governing body.
17	**Timing**	The auditor shall communicate with those charged with governance on a timely basis.
18	**Adequacy**	(a) The auditor shall evaluate whether the two-way communication between the auditor and those charged with governance has been adequate for the purpose

		of the audit. (b) If it has not, the auditor shall evaluate the effect, if any, on the auditor's assessment of the risks of material misstatement and ability to obtain sufficient appropriate audit evidence, and shall take appropriate action such as. ✓ Modifying the auditor's opinion on the basis of a scope limitation. ✓ Obtaining legal advice about the consequences of different courses of action. ✓ Communicating with third parties (e.g., a regulator), or a higher authority in the governance structure that is outside the entity, such as the owners of a business (e.g., shareholders in a general meeting), or the responsible government minister or parliament in the public sector. ✓ Withdrawing from the engagement where permitted in the relevant jurisdiction.
E. Documentation –		
19	**Documentation**	Where matters required by this SA to be communicated are communicated orally, the auditor shall document them, and when and to whom they were communicated. Where matters have been communicated in writing, the auditor shall retain a copy of the communication as part of the audit documentation.
F. Communication with Third Parties –		
A.38 & A.39	**Communication with Third Parties**	1. In some cases, disclosure to third parties may be illegal or otherwise inappropriate. 2. Communication to Third Parties (e.g. Bankers or Regulatory Authorities), where Governance Team itself may wish to provide Third Parties, with copies of a written from the Auditor. 3. In such cases, the Third Parties be informed that the communication was not prepared with them in mind, for example, by stating in written communications with those charged with governance – ✓ That the communication has been prepared for the sole use of those charged with governance and, where applicable, the group management and the group auditor, should not be relied upon by third parties, ✓ That no responsibility is assumed by the auditor to third parties, and ✓ Any restrictions on disclosure or distribution to third parties. 4. The auditor may be required by laws or regulations to, for example – ✓ Notify a regulatory or enforcement body of certain matters communicated with those charged with governance. The auditor has a duty to report misstatements to authorities where management and those charged with governance fail to take corrective action. ✓ Submit copies of certain reports prepared for those charged with governance to relevant regulatory or funding bodies, or other bodies (such as Central Government in the case of some public sector undertakings) or 5. Make reports prepared for those charged with governance publicly available.

Standard on Auditing (SA) 265

Communication of Deficiencies in Internal Control to Those Charged with Governance and Management

1. Effective Date [Para – 4]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

1. This SA deals with the auditor's responsibility to communicate appropriately to those charged with governance and management deficiencies in internal control[1] that the auditor has identified in an audit of financial statements.
2. This SA does not –
   - ✓ Impose additional responsibilities on the auditor regarding obtaining an understanding of internal control and designing and performing tests of controls over and above the requirements of SA 315 and SA 330, SA 260 (Revised).
   - ✓ Prohibit the auditor from communicating to those charged with governance and management other internal control matters that the auditor has identified during the audit. [Para – 3]

3. Auditor's Objective [Para – 5]

The objective of the auditor is to communicate appropriately to those charged with governance and management deficiencies in internal control that the auditor has identified during the audit and that, in the auditor's professional judgment, are of sufficient importance to merit their respective attentions.

4. General Duties of Auditor [Para – 2]

1. The auditor is required to obtain an understanding of internal control relevant to the audit when identifying and assessing the risks of material mis – statement.
2. In making those risk assessments, the auditor considers internal control in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control.
3. The auditor may identify deficiencies in internal control not only during this risk assessment process but also at any other stage of the audit. This SA specifies which identified deficiencies the auditor is required to communicate to those charged with governance and management.

5. Definitions [Para –6]

Para No.	Terms	Definitions
(a)	Deficiency in Intenal Control	This exists when – (a) A control is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements on a timely basis, or (b) A control necessary to prevent, or detect and correct, misstatements in the financial statements on a timely basis is missing.
(b)	Significanct Deficiency in Internal Control	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 those charged with governance.

Note → The significance of a deficiency or a combination of deficiencies in internal control depends on –
- ✓ Whether a misstatement has actually occurred,
- ✓ The likelihood that a misstatement could occur and
- ✓ The potential magnitude of the misstatement.

Significant deficiencies may therefore exist even though the auditor has not identified misstatements during the audit.

6. Requirements

	A. Identify Deficiencies [Para – 7]	
S.N.	**Aspect**	**Description**
1.	**Identify Deficiency**	The auditor shall determine whether, on the basis of the audit work performed, the auditor has identified one or more deficiencies in internal control. [Para – 7]
2.	**Confim Deficiencies**	For this purpose auditor may discuss the relevant facts and circumstances of the auditor's findings with the appropriate level of management. [Para A.1]
3.	**Preliminary Response**	The Auditor may obtain other relevant information like – [Para A.2] (a) Management's understanding of the actual or suspected causes of the deficiencies. (b) Exceptions arising from the deficiencies that management may have noted, for example, misstatements that were not prevented by the relevant information technology (IT) controls. (c) A preliminary indication from management of its response to the findings.
	B. Recognise Significant Deficiencies	
8	**Recognisation of SD**	If the auditor has identified one or more deficiencies in internal control, the auditor shall determine, on the basis of the audit work performed, whether, individually or in combination, they constitute significant deficiencies.
A.6	**Matter to be Considered**	Examples of matters that the auditor may consider in determining whether a deficiency or combination of deficiencies in internal control constitutes a significant deficiency include – 1. The likelihood of the deficiencies leading to material misstatements in the financial statements in the future. 2. The susceptibility to loss or fraud of the related asset or liability. 3. The subjectivity and complexity of determining estimated amounts, such as fair value accounting estimates 4. The financial statement amounts exposed to the deficiencies. 5. The volume of activity that has occurred or could occur in the account balance or class of transactions exposed to the deficiency or deficiencies. 6. The importance of the controls to the financial reporting process; for example– ✓ General monitoring controls (such as oversight of management).Controls over the prevention and detection of fraud. ✓ Controls over the selection and application of significant accounting policies. ✓ Controls over significant transactions with related parties. ✓ Controls over significant transactions outside the entity's normal course of business. ✓ Controls over the period-end financial reporting process (such as controls

		over non-recurring journal entries). 7. The cause and frequency of the exceptions detected as a result of the deficiencies in the controls. 8. The interaction of the deficiency with other deficiencies in internal control.
A.7	**Indicators**	Indicators of significant deficiencies in internal control include, for example – 1. Evidence of ineffective aspects of the control environment, such as – ✓ Indications that significant transactions in which management is financially interested are not being appropriately scrutinized by those charged with governance. ✓ Identification of management fraud, whether or not material, that was not prevented by the entity's internal control. ✓ Management's failure to implement appropriate remedial action on significant deficiencies previously communicated. 2. Absence of a risk assessment process within the entity or evidence of an ineffective entity risk assessment process, such as management's failure to identify a risk of material misstatement that the auditor would expect the entity's risk assessment process to have identified. 3. Evidence of an ineffective response to identified significant risks (e.g., absence of controls over such a risk).Misstatements detected by the auditor's procedures that were not prevented, or detected and corrected, by the entity's internal control. 4. Disclosure of a material misstatement due to error or fraud as prior period items in the current year's Statement of Profit and Loss. 5. Evidence of management's inability to oversee the preparation of the financial statements.

C. Communicate Significant Deficiencies

9	**To Government**	The auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis
10	**To Management**	The auditor shall also communicate to management at an appropriate level of responsibility on a timely basis –

Matters to be Communicate	**Appropriate Level of Management**
In writing, significant deficiencies in internal control that the auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances. [Para – 10]	**CEO/CFO/Equivalent [Para A.19]**
Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties and that, in the auditor's professional judgment, are of sufficient importance to merit management's attention. [Para – 10]	**Operational Management [Para A.19]**

A.30	**To Regulatory**	Law or regulation may require the auditor or management to furnish a copy of the auditor's written communication on significant deficiencies to appropriate regulatory authorities. Where this is the case, the auditor's written communication may identify such regulatory authorities.

Level of details at which to communicate depends on – [Para A.15]

(a) The nature of the entity. For instance, the communication required for a public interest entity may be different from that for a non-public interest entity.

(b) The size and complexity of the entity. For instance, the communication required for a complex entity may be different from that for an entity operating a simple business.

(c) The nature of significant deficiencies that the auditor has identified.

(d) The entity's governance composition. For instance, more detail may be needed if those charged with governance include members who do not have significant experience in the entity's industry or in the affected areas.

(e) Legal or regulatory requirements regarding the communication of specific types of deficiency in internal control.

D. Matters to be included in Written Communication

11	**Matters to be included**	The auditor shall include in the written communication of significant deficiencies in internal control – 1. A description of the deficiencies and an explanation of their potential effects, and 2. Sufficient information to enable those charged with governance and management to understand the context of the communication. In particular, the auditor shall explain that – (a) The purpose of the audit was for the auditor to express an opinion on the financial statements, (b) The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control, and (c) The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance.

<table>
<tr><td colspan="2"><u>E. Pervious Communication/Continuous Deficiencies</u></td></tr>
<tr><td colspan="2">Management and Those charged with Governance may already be aware of significant deficiencies that the auditor has identified during the audit and may have chosen not to remedy them because of cost or other considerations.[Para A.16]
In such Cases, the Auditor has the following responsibilities –</td></tr>
<tr><td>In case of Know n Significant Deficiencies[Para A.17]</td><td>In Case of Known Other Deficiencies [Para A.24]</td></tr>
<tr><td>The auditor shall repeat the communication, if remedial action has not yet been taken, by –
(a) May repeat the description from the previous communication, or
(b) Simply reference the previous communication.</td><td>In case of known Other than Significant Deficiencies to management in a prior period, the Auditor need not repeat the communication in the current period, except in case of –
(a) A change of Management, or
(b) If new information has come to the Auditor's attention that alters the prior understanding of the Auditor and Management regarding the deficiencies.</td></tr>
<tr><td colspan="2">The Failure of management to remedy Significant and Other Deficiencies in Internal Control that were previously communicated may become a Significant Deficiency by itself, requiring communication with TCWG.</td></tr>
</table>

Standard on Auditing (SA) 299

Responsibility of Joint Auditors

1. Effective Date [Para – 13]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 1996.**

2. Scope of this SA [Para – 1]

- **Applicability** – This Standard deals with the professional responsibilities which the auditors undertake in accepting such appointments as joint auditors.
- **Exception** – The Standard does not deal with the relationship between a principal auditor who is appointed to report on the financial statements of an entity and another auditor who is appointed to report on the financial statements of one or more divisions or branches included in the financial statements of the entity, e.g., the relationship between a company auditor appointed under section 224 of the Companies Act, 1956 and a branch auditor appointed under section 228 of the said Act

3. Definitions [Para – 1]

The practice of appointing more than one auditor to conduct the audit of large entities is in vogue these days. Such auditors, known as joint auditors, conduct the audit jointly and report on the financial statements of the entity.

4. Requirements

Para No.	Aspects	Description
2 & 3	**Divisoin of Work among the Joint Auditors**	1. **Manner of Division** – Where joint auditors are appointed, they should, by mutual discussion, divide the audit work among themselves. The division of work would usually be in following manner – [Para – 2] (a) In terms of audit of identifiable units, or (b) Specified areas. (c) Items of assets or liabilities or income or expenditure , (d) With reference to periods of time. 2. **Common Coverage Areas** – Certain areas of work, owing to their importance or owing to the nature of the work involved, would often not be divided and would be covered by all the joint auditors. [Para – 2] 3. **Documentation** – The division of work among joint auditors as well as the areas of work to be covered by all of them should be adequately documented and preferably communicated to the entity. [Para – 3]
4 & 5	**Co – ordination among the Joint Auditors**	1. **Communication** – A joint auditor should communicate in writing the following to all other Joint Auditors – (a) Matter which are relevant to the areas of responsibility of other joint auditors, (b) Matter which deserve their attention, and (c) Matte that disclosure or require discussion with, or application of judgement by, other joint auditors, he should communicate the same to all the other joint auditors. 2. **Pre – Audit Report** – This should be done by the submission of a report or note prior to the finalisation of the audit.

<table>
<tr><td></td><td></td><td colspan="2">3. <u>Post – Audit Communication</u> – If any such matter is brought to the attention of the entity or other Joint Auditors by an Auditor after report has been submitted, the other Joint Auditors would not be responsible for those matters.</td></tr>
<tr><td>5
To
9</td><td>Nature of the Responsibility of Joint Auditors</td><td><u>Joint & Several Responsibility</u></td><td><u>Several Responsibility</u></td></tr>
<tr><td colspan="4"><u>Please refer Audit under Companies Act, 1956 page no. 88 and 89</u></td></tr>
<tr><td>10
&
11</td><td>Reliance on Other Joint Auditor's Work</td><td colspan="2">1. <u>Compliance with SA</u> –Each joint auditor is entitled to assume that the other joint auditors have carried out their part of the audit work in accordance with the generally accepted audit procedures (Standards on Auditing).
2. <u>No need for review</u> – It is not necessary for a joint auditor to review the work performed by other joint auditors or perform any tests in order to ascertain whether the work has actually been performed in such a manner.
3. <u>Reliance</u> – Each joint auditor is entitled to rely upon the other joint auditors for bringing to his notice any departure from generally accepted accounting principles or any material error noticed in the course of the audit.
4. <u>Branch Audit Situation</u> – Where separate financial statements of a division/branch are audited by one of the joint auditors, the other joint auditors are entitled to assume –
(a) A true and fair view of the state of affairs and of the working results of the division/branch concerned,
(b) Compliance with Legal and Professional Requirement, and
(c) Correctness of disclosure of such Financial Statements.
However, subject to such observations as may be communicated by the joint auditor concerned</td></tr>
<tr><td>12</td><td>Reporting Responsibility of JA's</td><td colspan="2"><u>Refer Audit Under Companies Act, 2013 page no. 89</u></td></tr>
<tr><td colspan="4">Some Extra Points</td></tr>
</table>

<table>
<tr><td colspan="4"><u>Question Bank for SA – 200 Series</u></td></tr>
<tr><th>S.N.</th><th>Question</th><th>Marks and Attempt</th><th>Answer</th></tr>
<tr><td>1.</td><td>Write short notes on the Frauds through supplier ledger.</td><td>[4 Marks]
[Nov. 2008 & May 2011]</td><td>See Below</td></tr>
<tr><td>Ans.</td><td colspan="3"><u>Frauds though suppliers ledger</u> –
Fraud through supplies ledger could be made in any of the following ways, which the auditor has to take case of –
1. Adjusting fictitious as duplicate invoices as purchases in the accounts of suppliers and subsequently misappropriating the money when payments are made in respect of these invoices.
2. Suppressing credit notes issued by suppliers and withdrawing the corresponding amount not claimed by them.
3. Withdrawing amounts which remain unclaimed for more than the normal time limit for one reason or other by showing the same have been paid to the parties.
4. Accepting invoices at prices considerably highest than the market price and collecting the excess claim from the suppliers directly.</td></tr>
<tr><td>2.</td><td>Explain briefly duties and responsibilities of an auditor in case of material misstatement resulting from Management Fraud.</td><td>[6 Marks]
[Nov. 2009]</td><td>See Below</td></tr>
<tr><td>Ans.</td><td colspan="3">As per SA 240 (Revised), "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements" misstatement in the financial statements can arise from fraud or error. The term fraud refers to an 'Intentional Act' by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage. The auditor is concerned with fraudulent acts that cause a material misstatement in the financial statements.

Fraud involving one or more members of management or those charged with the governance is referred to as "management fraud". The primary responsibility for the prevention and detection of fraud rests with those charged with the governance and the management of the entity.

SA 200, "Objective and General Principles Governing an Audit of Financial Statements," indicates that an audit conducted in accordance with the standards on auditing generally accepted in India, is designed to provide reasonable assurance that the financial statements taken as a whole are free from material misstatement whether caused by error or fraud. The fact that an audit is carried out may act as deterrent, but the auditor is not and cannot be held responsible for the prevention of fraud and error. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of financial statements will not be detected, even though the audit is properly planned and performed in accordance with the standards on auditing generally accepted in India. An audit does not guarantee that all material misstatement will be detected because of such factors, as the use of judgment, the use of testing, the inherent limitations of internal control and the fact that much of the evidence available to the auditor is persuasive rather than conclusive in nature.

Certain levels of management may be in a position to override control procedures designed to prevent similar frauds by other employees. Auditor's opinion on the financial statements is based on the concept of obtaining reasonable assurance, hence in an audit; the auditor does not guarantee that material misstatements will be detected.</td></tr>
</table>

3.	While conducting statutory Audit of ABC Ltd., you come across IOUs amounting to ₹ 2 Crores as against a cash balance shown in books of ₹ 2.10 Crores. You also observe that despite similar high balances throughout the year, small amounts of ₹ 50,000 are withdrawn from the bank to meet day-to-day expenses. Comment.	**[5 Marks] [June 2009]**	**See Below**
Ans.	**According to SA 240, "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements"** when the auditor comes across such circumstances indicating the possible misstatements resulting from the fraud then the auditor needs to consider the impact of fraud on financial statements and its disclosure in the audit report. In this case, the circumstances indicate that the possible misstatement in financial statements is due to fraud and error and the auditor must investigate further to consider effect on financial statements. **The Guidance Note on Audit of Cash and Bank balances** also mentions that if the entity is maintaining an unduly large balance of cash, he should carry out surprise verification of cash more frequently to ascertain whether it agrees. If cash in hand is not in agreement with the book balance, he should seek explanations and if the same are not satisfactory should state the said fact appropriately in his Audit Report.		
4.	In the course of audit of A Ltd you suspect the management has indulged in fraudulent financial reporting? State the **possible source of such fraudulent financial reporting.**	[6 Marks] [May 2012]	**Refer Para. No. 31, 32 & 33 of SA – 240 on Page no. 48 and also refer e.g. on FFR on Page no. 51**
5.	R & Co, a firm of Chartered Accountants have **not revised the terms of engagements** and obtained confirmation from the clients, **for last 5 years** despite **changes in business and professional environment.** Please elucidate the **circumstances** that may warrant the **revision in terms of engagement.**	[4 Marks] [May 2013]	**Refer Para. No. A.27 of SA – 210 on Pg no. 30**
6.	As a Statutory Auditor hoe would you deal with following? While auditing accounts of a public limited company for the year ended 31st March 2013, an auditor found out **an error in the valuation of inventory, which affects the financial statement materially** – Comment as per SA's	[5 Marks] [Nov. 2003]	**See Below**
Ans.	SA 240, "The Auditor's Responsibility to Consider Fraud and Error in an Audit of Financial Statements", requires that if circumstances indicate the possible existence of fraud or error, the auditor should consider the potential effect of the suspected fraud or error on the financial information. If the **auditor believes** the **suspected fraud or error** could have a **material effect** on the financial information, he should perform such **modified or additional procedures** as he determines to be appropriate. SA 240 also requires that the **auditor should consider the implications** of the misstatement in relation to other aspects of the audit, particularly, **the reliability of management representations.**		

	Further, SA 450 also requires that in such circumstances, the auditor should consider requesting the management to adjust the financial information or consider extending his audit procedures. If the management refuses to adjust the financial information and the results of extended audit procedures do not enable the auditor to conclude that the aggregate of uncorrected misstatements is not material, the auditor should express a qualified or adverse opinion, as appropriate. **In the instant case,** the auditor has detected the material errors affecting the financial statements; the auditor should communicate his findings to the management on a timely basis, consider the implications on true and fair view and also ensure that appropriate disclosures have been made.		
7.	Write a short note on **Responsibility of Joint Auditors?**	**[4 Marks]** **[Nov. 2004]**	**Refer SA – 299 on Page no. 73**
8.	As a Statutory Auditor how would you deal with the following? The Managing Director of the Company has committed a **"Teeming and Lading" Fraud. The amount involved has been however subsequently after the year end deposited in the company.**	**[4 Marks]** **[Nov. 2005]**	**See Below**
Ans.	**<u>Fraud Committed by Managing Director</u> –** The Managing Director of the company has committed a "Teeming and Lading" fraud. The fact that the amount involved has been subsequently deposited after the year end is not important because the auditor is required to perform his responsibilities as laid down in SA 240 , "The Auditor's Responsibility to Consider Fraud and Error in an Audit of Financial Statements". First of all, as per SA 240, the auditor need to perform procedures whether the financial statements are materially misstated. Because an instance of fraud cannot be considered as an isolated occurrence and it becomes important for the auditor to perform audit procedures and revise the audit risk assessment. Secondly, the auditor need to consider the impact of fraud on financial statements 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 management, it affects the reliability of audit evidence previously obtained since there is a genuine doubt about representations of management. **<u>Reporting</u>** – The auditor shall have to report under CARO, 2003 indicating the nature and amount involved in respect of fraud noticed during the year.		
9.	"The auditors should communicate audit matters of governance interest arising from the audit of financial statements with those charged with the governance of an entity". Briefly **state the matters to be included in such Communication.**	**[8 Marks]** **[Nov. 2006]**	**Refer Para. No. 10 to 13 of SA – 260 on Page no. 64 & 65**

10.	State the **reporting responsibility of an auditor** in the context of **non-compliance of Law and Regulation** in an audit of Financial Statement.	**[8 Marks] [Nov. 2006]**	**Refer Para. No. 22 to 28 of SA – 250 on Page no. 59 & 60**
11.	M/s PQR & Company, Chartered Accountants have been appointed Statutory Auditors of a listed Company for the year ended 31st March, 2013. **Draft an appropriate engagement letter to be sent to the Board of Directors for the same.**	**[12 Marks] [Nov. 2007]**	**See Below**
Ans.	**<u>Draft of an Engagement Letter</u>** **To the Board of Directors** You have requested that we audit the balance sheet of (Name of the Company) as at 31st March, 2013 and the related profit and loss account and the cash flow statement for the year ended on that date. We are pleased to confirm our acceptance and our understanding of this engagement by means of this letter. Our audit will be conducted with the objective of our expressing an opinion on the firm statements. We will conduct our audit in accordance with the auditing standards generally accepted in India and with the requirements of the Companies Act, 1956. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. However, having regard to the test nature of an audit, persuasive rather than conclusive nature of audit evidence together with inherent limitations of any accounting and internal control system, there is an unavoidable risk that even some material misstatements of financial statements, resulting from fraud, and to a lesser extent error, if either exists, may remain undetected. In addition to our report on the financial statements, we expect to provide you with a separate letter concerning any material weaknesses in accounting and internal control systems which might come to our notice. The responsibility for the preparation of financial statements on a going concern basis is that of the management. The management is also responsible for selection and consistent application of appropriate accounting policies, including implementation of applicable accounting standards along with proper explanation relating to any material departures from those accounting standards. The management is also responsible for making judgements and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the entity at the end of the financial year and of the profit or loss of the entity for that period. The responsibility of the management also includes the maintenance of adequate accounting records and		

	internal controls for safeguarding of the assets of the company and for the preventing and detecting fraud or other irregularities. As part of our audit process, we will request from management written confirmation concerning representations made to us in connection with the audit. We also wish to invite your attention to the fact that our audit process is subject to 'peer review' under the Chartered Accountants Act, 1949. The reviewer may examine our working papers during the course of the peer review. We look forward to full cooperation with your staff and we trust that they will make available to us whatever records; documentation and other information are requested in connection with our audit. Our fees will be billed as the work progresses. This letter will be effective for future years unless it is terminated, amended or superseded. Please sign and return the attached copy of this letter to indicate that it is in accordance with your understanding of the arrangements for our audit of the financial statements. **For XYZ and Co.** **Chartered Accountants** ____________________ **Signature** **(Name of the Member)** **(Designation)** **Membership** **Number** **Date –** **Address –** **Acknowledged on behalf of PQR Company by** **(Signed)** **Name and Designation** **Date –**

Section – II

Standard on Auditing (SA) 300 (Revised)

Planning an Audit of Financial Statements

1. Effective Date [Para – 2]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2008.**

2. Scope of this SA [Para – 1]

- SA – 300 deals with the Auditor's **responsibilities to plan** an audit of FS's, in the context of Recurring Audit.
- Additional considerations in initial audit engagements are separately identified

Note → Planning an audit involves establishing the overall Audit Strategy for the engagement and developing an Audit Plan. [Para A.1]

3. Overall Objectives of the Auditor [Para – 3]

To plan the audit so that it will be performed in an effective manner.

4. The Role and Timing of Audit Planning

Para No.	Aspect	Description
A.1	**Benefits of Planning**	As we know that planning is one very most powerful element and has many benefits in Audit. Some benefits are – 1. Helping the auditor to devote appropriate attention to important areas of the audit. 2. Helping the auditor identify and resolve potential problems on a timely basis. 3. Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner. 4. Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks, and the proper assignment of work to them. 5. Facilitating the direction and supervision of engagement team members and the review of their work. 6. Assisting, where applicable, in coordination of work done by auditors of component and experts
A.2	**Factors affecting Planning**	The nature and extent of planning activities will vary according to – 1. The size and complexity of the entity, 2. The key engagement team members' previous experience with the entity, and 3. Changes in circumstances that occur during the audit engagement.
A.3	**Timing of activities to be performed in Audit**	The timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures (for example, planning includes the need to consider, prior to the auditor's identification and assessment of the risks of material misstatement).
A.4	**Discussion of Elements Planning**	The auditor may decide to discuss elements of planning with the entity's management to facilitate the conduct and management of the audit engagement (for example, to coordinate some of the planned audit procedures with the work of the entity's personnel).

		Note → When discussing matters included in the overall audit strategy or audit plan, care is required in order not to compromise the effectiveness of the audit. For example, discussing the nature and timing of detailed audit procedures with management may compromise the effectiveness of the audit by making the audit procedures too predictable. [Para A.4]

4. Requirement

Para. No.	Terms	Description
4	**Involvement of Key Engagement Team Members**	☞ The engagement partner and other key members of the engagement team shall be involved in planning the audit, including planning and participating in the discussion among engagement team members. [Para – 4] ☞ Their involvement in planning the audit draws on their experience and insight, thereby enhancing the effectiveness and efficiency of the planning process. [Para A.5]
5	**Preliminary Engagement Activities**	The auditor shall undertake the following activities at the beginning of the current audit engagement – (a) Performing procedures required by SA 220 , "Quality Control for Audit Work" regarding the continuance of the client relationship and the specific audit engagement'. (b) Evaluating compliance with ethical requirements, including independence, as required by SA 220, and (c) Establishing an understanding of the terms of the engagement, as required by SA 210, "Terms of Audit Engagements".
		<u>Planning Activities</u>
6 & 7	**Development of Overall Audit Strategy**	☞ The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. [Para – 6] ☞ Establishing the Overall Audit Strategy, the Auditor shall – [Para – 7] (a) Identify the characteristics of the engagement that define its scope, (b) Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required, (c) Consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts, (d) Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant, and (e) Ascertain the nature, timing and extent of resources necessary to perform the engagement.
8	**Develop an Audit Plan**	The auditor shall develop an audit plan that shall include a description of – (a) The nature, timing and extent of planned risk assessment procedures, as determined under SA 315 "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment". (b) The nature, timing and extent of planned further audit procedures at the assertion level, as determined under SA 330 "The Auditor's Responses to Assessed Risks".

		(c) Other planned audit procedures that are required to be carried out so that the engagement complies with SAs.
9	**Updating and Changing Audit Strategy and Audit**	☞ The auditor shall update and change the overall audit strategy and the audit plan as necessary during the course of the audit. [Para 9] ☞ As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and thereby the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks. [Para A.14] ☞ This may be the case when information comes to the auditor's attention that differs significantly from the information available when the auditor planned the audit procedures. For example, audit evidence obtained through the performance of substantive procedures may contradict the audit evidence obtained through tests of controls. [Para A.14]
10	**Direction, Supervision and Review**	☞ The auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work. ☞ Factors affecting NTE of the DSR are – (a) The size and complexity of the entity. (b) The area of the audit. (c) The assessed risks of material misstatement (for example, an increase in the assessed risk of material misstatement for a given area of the audit ordinarily requires a corresponding increase in the extent and timeliness of direction and supervision of engagement team members, and a more detailed review of their work). (d) The capabilities and competence of the individual team members performing the audit work.
11	**Documentation**	The auditor shall document – (a) The overall audit strategy, (b) The audit plan, and (c) Any significant changes made during the audit engagement to the overall audit strategy or the audit plan, and the reasons for such changes.
12	**Additional Considerations in Initial Audit Engagement**	The auditor shall undertake the following activities prior to starting an initial audit– (a) Performing procedures required by SA 220 regarding the acceptance of the client relationship and the specific audit engagement, and (b) Communicating with the predecessor auditor, where there has been a change of auditors, in compliance with relevant ethical requirements, including review of the Predecessor Auditor's working papers, whenever permissible, (c) The audit procedures necessary to obtain sufficient appropriate audit evidence regarding opening balances as per SA – 510 (d) Other Procedures required by the Firm's system of Quality Control for Initial Audit Engagements.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	You have been appointed as the auditor of **a Multiplex Cinema House.** Draw an **audit programme** in respect of **its Revenue and Expenditure.**	[8 Marks] [Nov. 2008]	See Below

Ans.

Audit Programme of Multiplex –

1. Peruse the **Memorandum of Association and Articles of Association** of the entity.
2. Ensure the **object clause** permits the entity to engage in this type of business.
3. In the case of income from sale of tickets –
   (a) Verify the **control system** as to how it is ensured that the collections on sale of tickets of various shows are properly accounted.
   (b) Verify the **system of relating** to on line booking of various shows and the system of realization of money.
   (c) Check that there is **overall system of reconciliation of collections** with the number of seats available for different shows on a day.
4. Verify the **internal control system and its effectiveness** relating to the income from cafes shops, pubs etc., located within the multiplex.
5. Verify the **system of control** exercised relating to the income receivable from advertisements exhibited within the premises and inside the hall such as hoarding, banners, slides, short films etc.
6. Verify the **system of collection** from the parking areas in respect of the vehicles parked by the customers.
7. 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.**
8. Ensure at the **time of settlement any payment of advance** made to the distributor is also adjusted against the amount due.
9. Verify the **system of payment of salaries and other benefits to the employees** and ensure that statutory requirements are complied with.
10. Verify the **payments effected** in respect of the **maintenance of the building and ensure the same is in order.**

S.N.	Questions	Marks and Attempt	Answer
2.	A & Co. was appointed as auditor of **Great Airways Ltd.** As the audit partner what **factors shall be considered in the development of overall audit plan?**	[8 Marks] [May 2011]	**Refer Para No. 6 to 8 on Pg. no. 3 to 4 and Also See Below**

Ans.

Development of an overall plan – Overall plan is basically intended to provide direction for audit work programming and includes the determination of timing, manpower development and co-ordination of work with the client, other auditors and other experts. The auditor should consider the following matters in developing his overall plan for the expected scope and conduct of the audit.

	1. Terms of his engagement and any statutory responsibilities. 2. Nature and timing of reports or other communications. 3. Applicable Legal or Statutory requirements. 4. Accounting policies adopted by the clients and changes, if any, in those policies. 5. The effects of new accounting and auditing pronouncement on the audit. 6. Identification of significant audit areas. 7. Setting of materiality levels for the audit purpose. 8. Conditions requiring special attention such as the possibility of material error or fraud or involvement of parties in whom directors or persons who are substantial owners of the entity are interested and with whom transactions are likely. 9. Degree of reliance to be placed on the accounting system and internal control. 10. Possible rotation of emphasis on specific audit areas. 11. Nature and extent of audit evidence to be obtained. 12. Work of the internal auditors and the extent of reliance on their work, if any in the audit. 13. Involvement of other auditors in the audit of subsidiaries or branches of the client and involvement of experts. 14. Allocation of works to be undertaken between joint auditors and the procedures for its control and review. 15. Establishing and coordinating staffing requirements.		
3.	In the audit planning process of X Ltd., you would like to consider **audit risk at the financial statement level.** What are the **factors can influence** your decision?	**[3 Marks]** **[May 2010]**	**See Below**
Ans.	**<u>Audit risk at financial statement level</u>** The following factors will be considered for determination of audit risk at financial statement level. 1. Integrity of Management. 2. Management experience, knowledge and changes during the period. 3. Unusual pressures on the Management. 4. Nature of entity's business. 5. Factors affecting the Industry in which the entity operates.		

Standard on Auditing (SA) 315 (Revised)

Identifying and Assessing The Risk of Material Misstatement Through Understanding the Entity and Its Environment

1. Effective Date [Para – 2]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2008.**

2. Scope of this SA [Para – 1]

This Standard on Auditing (SA) deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements, through understanding the entity and its environment, including the entity's internal control.

3. Objective [Para – 1]

The objective of the auditor is to identify and assess the risks of material misstatement at the financial statement and assertion levels, through understanding the entity and its environment, including the entity's internal control, thereby providing a basis for designing and implementing responses to the assessed risks of material misstatement.

4. Definitions [Para – 4]

(a)	**Assertions**	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.
(b)	**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 and execute its strategies, or from the setting of inappropriate objectives and strategies.
(c)	**Internal Control**	The process designed, implemented and maintained by those charged with governance, management 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. The term "controls" refers to any aspects of one or more of the components of internal control.
(d)	**Risk Assessment Procedure**	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 risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.
(e)	**Significant Risk**	An identified and assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration.

Note → **<u>Materiality of an item may be judged using many factors, which include</u> –**

1. Value or Amount of transaction in the relative context.
2. Percentage Analysis.
3. Impact on the overall figure of Profit or Loss.
4. Comparison with previous year's figures.
5. Estimation Errors in determinable amounts.
6. Minor Deviations from Statutory Requirements.
7. Substantial effect of small inaccuracies.
8. Cumulative effect of small and insignificant items.

5. Requirements [Para – 4]

A. Perform "Risk Assessment Procedure"		
5	**Auditor's Duties**	The auditor shall perform risk assessment procedures to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. Risk assessment procedures by themselves, however, do not provide sufficient appropriate audit evidence on which to base the audit opinion.
6	**Procedures**	Inquiries of management and of others within the entity who in the auditor's judgment may have information that is likely to assist in identifying risks of material misstatement due to fraud or error. Analytical procedures. Observation and inspection.
7 & 8	**Relevance of Information Obtained**	The auditor shall consider whether information obtained from the auditor's client acceptance or continuance process is relevant to identifying risks of material misstatement. Where the engagement partner has performed other engagements for the entity, the engagement partner shall consider whether information obtained is relevant to identifying risks of material misstatement.
B. Using the Information obtained from previous audits		
9	**Experience from Previous Audits**	When the auditor intends to use information obtained from the auditor's previous experience with the entity and from audit procedures performed in previous audits, the auditor shall determine whether changes have occurred since the previous audit that may affect its relevance to the current audit.
C. Discussions by Engagement Partner & Team Members		
10	**Team Discussion**	☞ The engagement partner and other key engagement team members shall discuss the susceptibility of the entity's financial statements to material misstatement, and the application of the applicable financial reporting framework to the entity's facts and circumstances. ☞ The engagement partner shall determine which matters are to be communicated to engagement team members not involved in the discussion.
D. Obtain Understanding of Entity and its Environment [5 Aspects]		
11	**Aspects**	The auditor shall obtain an understanding of the following – (a) Relevant industry, regulatory, and other external. (b) The nature of the entity, including: 1. Its operations; 2. Its ownership and governance structures; 3. The types of investments that the entity is making and plans to make; and 4. The way that the entity is structured and how it is financed; (c) The entity's selection and application of accounting policies. (d) The entity's objectives and strategies, and those related business risks that may result in risks of material misstatement. (e) The measurement and review of the entity's financial performance.
E. Obtain an Understanding of Entity's Internal Control relevant to audit [4 Sections].		
12	**General Nature and Characteristics of Internal Control**	☞ **Duties –** The auditor shall obtain an understanding of internal control relevant to the audit. ☞ **Limitations of IC [Para A.42 – A.46]** (a) Control provides only Reasonable Assurance about achieving the Entity's Financial Reporting Objectives. (b) Human Judgment – Human Error

		(c) The operation of a control may not be effective, such as where information produced for the purposes of internal control (for example, an exception report) is not effectively used because the individual responsible for reviewing the information does not understand its purpose or fails to take appropriate action. (d) Controls can be circumvented by the collusion of two or more people or inappropriate management override of internal control. (e) In designing and implementing controls, management may make judgments on the nature and extent of the controls it chooses to implement, and the nature and extent of the risks it chooses to assume. (f) Smaller entities often have fewer employees which may limit the extent to which segregation of duties is practicable. ☞ **Manual &n Automated Elements of IC – SEE separate Table at the end of SA**
12	**Controls Relevant to the Audit**	☞ **Relevant Controls –** Although most controls relevant to the audit are likely to relate to financial reporting, but not all controls that relate to financial reporting are relevant to the audit. It is a matter of the **auditor's professional judgment** whether a control, individually or in combination with others, is relevant to the audit. ☞ **Examples –** Controls relating to – (a) Completeness and accuracy of Information, (b) Operations and Compliance of Objectives, and Statute/Regulation compliance, etc. are relevant to the audit. ☞ **Factors –** Factors relevant to the auditor's judgment about whether a control, individually or in combination with others, is relevant to the audit may include such matters as the following: ✓ Materiality. ✓ The significance of the related risk. ✓ The size of the entity. ✓ The nature of the entity's business, including its organisation and ownership characteristics. ✓ The diversity and complexity of the entity's operations. ✓ Applicable legal and regulatory requirements. ✓ The circumstances and the applicable component of internal control. ✓ The nature and complexity of the systems that are part of the entity's internal control, including the use of service organisations. ✓ Whether, and how, a specific control, individually or in combination with others, prevents, or detects and corrects, material misstatement.
13	**Nature, Extent of Understanding of Rel. Control**	When obtaining an understanding of controls that are relevant to the audit, the auditor shall evaluate the design of those controls and determine whether they have been implemented, by performing procedures in addition to inquiry of the entity's personnel.
F. Understanding the Components of Internal Control [5 Items]		
14	**Control Environment**	The auditor shall obtain an understanding of the control environment and shall evaluate whether – (a) Management, with the oversight of those charged with governance, has created and maintained a culture of honesty and ethical behaviour; and (b) The strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control, and (c) Whether those other components are not undermined by deficiencies in the control environment.

15 To 17	**Entity's Risk Assessment Process (RAP)**	1. **Existence of RAP –** The auditor shall obtain an understanding of the entity's process for: (a) Identifying business risks relevant to financial reporting objectives; (b) Estimating the significance of the risks; (c) Assessing the likelihood of their occurrence; and (d) Deciding about actions to address those risks. 2. **Auditor's Duties when there is RAP –** (a) Where the auditor identifies risks of material misstatement that management failed to identify, the auditor shall evaluate whether there was an underlying risk of a kind that the auditor expects would have been identified by the entity's risk assessment process. (b) If there is such a risk, the auditor shall obtain an understanding of why that process failed to identify it, and evaluate whether the process is appropriate to its circumstances or if there is a material weakness in the entity's risk assessment process. 3. **Auditor's Duties when there is no RAP –** (a) If the entity has no such processes as aforesaid, then the auditor shall discuss with management whether business risks relevant to financial reporting objectives have been identified and how they have been addressed. (b) Evaluate whether the absence of a documented RAP is appropriate in the circumstances or determine if there is a significant deficiency in the IC w.r.t. Entity's RAP.
18 & 19	**Information System, Including related business processes, relevant to Financial Reporting, and Communication**	☞ The auditor shall obtain an understanding of the information system by evaluating– (a) The significant classes of transactions; (b) The procedures, within both information technology (IT) and manual systems; (c) The related accounting records, supporting information and specific accounts in the financial statements; (d) How the information system captures events and conditions, other than transactions, that are significant to the financial statements; (e) The financial reporting process; (f) Controls surrounding journal entries. ☞ The auditor shall obtain an understanding of matters relating to financial reporting, including – (a) Communications between management and those charged with governance; and (b) External communications, such as those with regulatory authorities.
20 & 21	**Control activities relevant to the Audit**	☞ An audit requires an understanding of only those control activities related to significant class of transactions, account balance, and disclosure in the financial statements and the assertions which the auditor finds relevant in his risk assessment process. ☞ In understanding the entity's control activities, the auditor shall obtain an understanding of how the entity has responded to risks arising from IT.
22 To 24	**Monitoring Controls**	☞ The auditor shall obtain an understanding of the major activities that the entity uses to monitor internal control over financial reporting, including those related to those control activities relevant to the audit, and how the entity initiates corrective actions to its controls.

		☞ The auditor shall obtain an understanding of the sources of the information used in the entity's monitoring activities, and the basis upon which management considers the information to be sufficiently reliable for the purpose.
G. Identifying and Assessing the risks of Material Misstatements -		
25	**Levels of Risks**	The FS Level, and The Assertion Level
26	**Auditor's Procedures**	(a) Identify risks, (b) Assess the identified risks, (c) Relate the identified risks to what can go wrong at the assertion level, taking account of relevant controls that the auditor intends to test; and (d) Consider the likelihood of misstatement, including the possibility of multiple misstatements, and whether the potential misstatement is of a magnitude that could result in a material misstatement.
H. Identifying Significant Risks		
27	**Significant Risks**	As part of the risk assessment as described in paragraph 25, the auditor shall determine whether any of the risks identified are, in the auditor's judgment, a significant risk. In exercising this judgment, the auditor shall exclude the effects of identified controls related to the risk.
28	**Factors**	(a) Whether the risk is a risk of fraud; (b) Whether the risk is related to recent significant economic, accounting, or other developments; (c) The complexity of transactions; (d) Whether the risk involves significant transactions with related parties; (e) The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; and (f) Whether the risk involves significant transactions that are unusual.
29	**Controls**	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.
I. Identifying Risks for which Substantive Procedures alone do not provides SAAE		
30	**Identification of Risks**	In respect of some risks, the auditor may judge that it is not possible or practicable to obtain sufficient appropriate audit evidence only from substantive procedures. In such cases, the entity's controls over such risks are relevant to the audit and the auditor shall obtain an understanding of them.
J. Revision of Risk Assessment [Para 31]		
The auditor's assessment of the risks of material misstatement at the assertion level may change during the course of the audit as additional audit evidence or information is obtained. In such case, the auditor shall revise the assessment and modify the further planned audit procedures accordingly.		
K. Documentation [Para – 32]		
The auditor shall document – (a) The discussion among the engagement team and the significant decisions reached; (b) Key elements of the understanding obtained regarding each of the aspects of the entity and its environment, internal control components, the sources of information and the risk assessment procedures performed; (c) The identified and assessed risks of material misstatement at the financial statement level and at the assertion level; and (d) Significant risks identified, and related controls.		

Note – Classification of Assertions

A. Assertions about Classes of Transactions and Events for the period under audit.

1.	Occurrence	Transactions and events that have been recorded have occurred and pertain to the entity.
2.	Completeness	All transactions and events that should have been recorded have been recorded
3.	Accuracy	Amounts and other data relating to recorded transactions and events have been recorded appropriately.
4.	Cut – off	Transactions and events have been recorded in the correct accounting period.
5.	Classification	Transactions and events have been recorded in the proper accounts.

B. Assertions about Account Balances at the period – end.

1.	Existence	Assets, liabilities, and equity interests exist.
2.	Rights and Obligations	The entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
3.	Completeness	All assets, liabilities and equity interests that should have been recorded have been recorded.
4.	Valuation and Allocation	Assets, liabilities, and equity interests are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.

C. Assertions about Presentation and Disclosure.

1.	Occurrence and Rights & Obligations	Disclosed events, transactions, and other matters have occurred and pertain to the entity.
2.	Completeness	All disclosures that should have been included in the financial statements have been included.
3.	Classification and Under – Standability	Financial information is appropriately presented and described, and disclosures are clearly expressed.
4.	Accuracy and Valuation	Financial and other information are disclosed fairly and at appropriate amounts.

Examples of Assertions in particular instances.

1.	Cash in Hand	(a) That the Cash exists on the B/S date. (b) That there is no charge on the Cash Balance. (c) That the amount of Cash available is Rs ……… (d) That the Cash Balance is properly disclosed in the FS.\ (e) That there is no unrecorded Cash Balance.
2.	Secured Loans	(a) That the liability of Rs………. Lakhs exists on the date of B/S. (b) That the loans are the liability of the Company. (c) That the loans are secured to the extent of Rs……..] (d) That the loans are recorded at the appropriate carrying value. (e) That all transactions relating to loans are recorded & recognized at proper values & expenses is allocated to the proper period.

3.	**Machinery – Cost XXX (-) Dep. (XXX) XXX**	(a) That the Machinery physically exists on the B/S date. (b) That it is recorded at Historical Cost at Rs……… (c) That the M/c is free of charge/lien. (d) That P.Y. figures are properly B/F to the C.Y. (e) That Dep. Is charged at fair rated and on a consistent basis. (f) That the applicable Accounting Standards (AS 10, AS 6 and AS 16) are followed.
4.	**Investments**	1. That Investments are free of any charge/lien, etc. 2. That Investments are shown at lower of Cost or Market Price. 3. That Investments exists on the date of B/S. 4. The Investments are classified according to the purpose of the holding as per AS – 13. 5. That Investments are within the limits prescribed under the Companies Act, 1956 or Companies Act, 2013 6. That all Investments of the Company are disclosed. 7. That all the write – offs, purchase and sale transaction are recorded in the books of accounts, Profit and Loss is properly recognized in the FSs.

Manual & Automated Elements of Internal Controls [See Para 12 – 1]

A.57	**Suitability of Manual Elements in IC**	Manual elements in internal control may be more suitable where judgment and discretion are required such as for the following circumstances – ☞ Large, unusual or non-recurring transactions. ☞ Circumstances where errors are difficult to define, anticipate or predict. ☞ In changing circumstances that require a control response outside the scope of an existing automated control. ☞ In monitoring the effectiveness of automated controls.
A.58	**Disadvantage of Manual Elements in IC**	(a) They may be **less reliable** than automated elements because they can be more easily bypassed, ignored, or overridden and (b) They are also **more prone to simple errors and mistakes.** So, consistency of application of a manual control element cannot therefore be assumed. (c) They are **less suitable** for the following circumstances – ☞ **High volume** or recurring transactions, or in situations where errors that can be anticipated or predicted can be prevented, or detected and corrected, by control parameters that are automated. ☞ **Control activities** where the specific ways to perform the control can be adequately designed and automated.
A.55	**Benefits of IT in IC**	IT benefits an entity's internal control by enabling an entity to – ☞ Consistently apply predefined business rules and perform complex calculations in processing large volumes of transactions or data; ☞ Enhance the timeliness, availability, and accuracy of information; ☞ Facilitate the additional analysis of information; ☞ Enhance the ability to monitor the performance of the entity's activities and its policies and procedures; ☞ Reduce the risk that controls will be circumvented; and ☞ Enhance the ability to achieve effective segregation of duties by implementing security controls in applications, databases, and operating systems.
A.54	**Risks due to use of It in IC**	IT also poses specific risks to an entity's internal control, including, for example – ☞ Reliance on systems or programs that are inaccurately processing data, processing inaccurate data, or both. ☞ Unauthorised access to data that may result in destruction of data or improper changes to data, including the recording of unauthorised or non-existent

		transactions, or inaccurate recording of transactions. Particular risks may arise where multiple users access a common database. ☞ The possibility of IT personnel gaining access privileges beyond those necessary to perform their assigned duties thereby breaking down segregation of duties. ☞ Unauthorised changes to data in master files. ☞ Unauthorised changes to systems or programs. ☞ Failure to make necessary changes to systems or programs. ☞ Inappropriate manual intervention. ☞ Potential loss of data or inability to access data as required.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	**IT system**s also pose (cause/create/pretense) **specific risks** to an **entity's internal control?** What are those risks?	[4 Marks] [May 2010]	**Refer Para No. A.54 on Pg. no. 13**
2.	What are the points to be considered while **evaluating the "Knowledge of the Business" in the conduct of an audit?**	[8 Marks] [June 2009]	**Refer Para No. 11 on Page no. 8 also Refer Below**
Ans.	**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 accounting estimates and management representations**, and to make **judgement regarding the appropriateness of accounting policies and disclosures.**		
3.	As auditor of Z Ltd., you would like to limit your **examination of account balance tests.** What are the **control objectives** you would like the **accounting control system to achieve to suit your purpose?**	[4 Marks] [May 2010]	**Refer Note – Classification of Assertions on Page no. 12 also Refer Below**
Ans.	**Basic Accounting Control Objectives –** The basic accounting control objectives which are sought to be achieved by any accounting control system are – 1. Whether all transactions are recorded; 2. Whether recorded transactions are real; 3. Whether all recorded transactions are properly valued; 4. Whether all transactions are recorded timely; 5. Whether all transactions are properly posted; 6. Whether all transactions are properly classified and disclosed; 7. Whether all transactions are properly summarized.		

Standard on Auditing (SA) 320 (Revised)
Materiality in Planning and Performing Audit

1. Effective Date [Para – 7]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

This Standard on Auditing (SA) deals with the auditor's responsibility to apply the concept of materiality in planning and performing an audit of financial statements.

3. Objective [Para – 8]

The Objective of the auditor is to apply the concept of materiality appropriately in planning and performing the audit.

4. Definition [Para – 9]

Performance Materiality – The amount or amounts set by the auditor at less than materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. If applicable, performance materiality also refers to the amount or amounts set by the auditor at less than the materiality level or levels for particular classes of transactions, account balances or disclosures.

5. Materiality in the Context of an Audit

2	**Materiality Framework**	**Materiality generally explains that –** a) Misstatements, including omissions, could be material if it influences the decisions of the user; b) Judgments are affected by the size or/& nature of a misstatement or combination for both; and c) Judgments which are material to users are based on a consideration of the common financial information needs of users as a group, and not for individual whose needs may vary.
3	**FRF doesn't provide discussion on Materiality**	The applicable financial reporting framework does not include a discussion of the concept of materiality, the characteristics referred to in paragraph 2 provide the auditor with such a frame of reference.
4	**Auditor's Assumption's**	The auditor's determination of materiality is a matter of professional judgment, and it is reasonable for the auditor to assume that users – i. Have a reasonable knowledge of business economic activities and accounting; ii. Understand that financial statements are prepared, presented and audited to levels of materiality; iii. Recognize the uncertainties inherent in the judgments and estimation; iv. Make reasonable economic decision on the basis of the information in the financial statements.
5	**Recognition of Materiality**	The concept of materiality is applied by the auditor – (a) in **planning and performing** the audit, and (b) in **evaluating** the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements and (c) in **forming the opinion** in the auditor's report.

6	**Aspects to be considered in Materiality**	***Material judgments provide the provide the basis in;*** a) Determining the nature, timing and extent of risk assessments procedures; b) Identifying and assessing the risks of material misstatement; c) Determining the nature, timing and extent of further audit procedures. d) Considering not only the size but also the nature of the uncorrected misstatements and particular circumstances of their occurrence while evaluating the financial statements.
A.1	**Materiality and Audit Risk**	(a) Audit risk is the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. (b) Audit risk is a function of the risks of material misstatement and detection risk. (c) **Materiality – Risk Relationship** – Where the materiality level is to be set very high, even the largest number will have effect on the decision of users, so the risk that the Auditor will conclude with an inappropriate opinion is low. Where the materiality level is set to be low, individual balance and classes of the balance becomes more critical, and the Auditor's Risk corresponding rises. (d) Materiality and audit risk are considered throughout the audit, in particular, when – 1. Identifying and assessing the risks of material misstatement; 2. Determining the nature, timing and extent of further audit procedures; and 3. Evaluating the effect of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report

6. Requirements

10 & 11	**Determining Materiality when planning the Audit**	☞ The auditor shall determine the level of materiality for the FS and also for a particular class of transactions when this class of transaction affects the decision of the user. ☞ The auditor shall determine performance materiality for purposes of assessing the risks of material misstatement and determining the nature, timing and extent of further audit procedures.
A.2 & A.3	**Benchmarking**	☞ **Meaning** – Benchmarking is one recognised method through which an Auditor determining materiality level. A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole. ☞ **Factors** – Factors that may affect the identification of an appropriate benchmark include the following – (a) The elements of the financial statements (for example, assets, liabilities, equity, revenue, expenses); (b) Whether there are items on which the attention of the users of the particular entity's financial statements tends to be focused (for example, for the purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets); (c) The nature of the entity, where the entity is at in its life cycle, and the industry and economic environment in which the entity operates; (d) 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

		(e) The relative volatility of the benchmark. ☞ **Examples of benchmarks** that may be appropriate, depending on the circumstances of the entity, include categories of reported income such as profit before tax, total revenue, gross profit and total expenses, total equity or net asset value. Profit before tax from continuing operations is often used for profit-oriented entities. When profit before tax from continuing operations is volatile, other benchmarks may be more appropriate, such as gross profit or total revenues. **[Para A.3]**
12 & 13	**Revision as the Audit Progresses**	☞ The auditor shall revise materiality in the event of becoming aware of information during the audit that would have caused the auditor to determine a different amount initially. ☞ When materiality is revised then auditor should consider that whether performance materiality and further audit procedures are appropriate or not.

7. Documentation [Para – 14]

Auditor shall document –

1. Materiality for the financial statements as a whole.
2. If applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures.
3. Performance materiality and
4. Any revision of (i) – (iii), above as the audit progressed.

Some Past Attempts Question

S.N.	Question	Marks and Attempt	Answer
1.	Mr. X was appointed as the auditor of M/s Easygo Ltd. and intends to apply the concept of materiality for the financial statements as a whole. Please guide him as to the **factors that may affect the identification of an appropriate benchmark for this purpose.**	**[4 Marks]** **[Nov. 2013]**	**Refer Para No. A.2 on Page no. 16**

Standard on Auditing (SA) 330
The Auditor's Responses to Assessed Risks

1. Effective Date [Para – 2]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2008.**

2. Scope of this SA [Para – 1]

This Standard on Auditing (SA) deals with the auditor's responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor in accordance with SA 315, in a financial statement audit.

3. Objective [Para – 3]

The objective of the auditor is to obtain sufficient appropriate audit evidence about the assessed risks of material misstatement, through designing and implementing appropriate responses to those risks.

4. Definitions [Para – 4]

(a)	**Substance Procedure**	An audit procedure designed to detect material misstatements at the assertion level. Substantive procedures comprise – (i) Tests of details (of classes of transactions, account balances, and disclosures), and (ii) Substantive analytical procedures.
(b)	**Test of Controls**	An audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level.

5. Requirements

A. Overall Responses at Financial Statement Level		
5	**Requirement**	The auditor shall design and implement overall responses to address the assessed risks of material misstatement at the financial statement level.
A.1	**Overall Responses**	Overall responses to address the assessed risks of material misstatement at the financial statement level may include – (a) Emphasizing to the audit team the need to maintain professional skepticism. (b) Assigning more experienced staff or those with special skills or using experts. (c) Providing more supervision. (d) Incorporating additional elements of unpredictability in the selection of further audit procedures to be performed. (e) Making general changes to the nature, timing or extent of audit procedures, for example – (i) Performing substantive procedures at the period end instead of at an interim date; or (ii) Modifying the nature of audit procedures to obtain more persuasive audit evidence.
A.2	**Control Environment**	The assessment of the risks of material misstatement at the financial statement level, and thereby the auditor's overall responses, is affected by the auditor's understanding of the control environment. An effective control environment may allow the auditor to conduct some audit procedures at an interim date rather than at the period – end.

B. Audit Procedures at Assertion Level		
6	**Requirement**	The auditor shall design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level.
7	**Factors**	The auditor shall design and perform audit procedures that are responsive to the assessed risks of material misstatement at the assertion level and in designing such audit procedures, the auditor shall – (a) Consider the reasons for the assessment given to the risk of material misstatement at the assertion level for each class of transactions, account balance, and disclosure, including inherent risks and control risks. (b) Obtain more persuasive audit evidence when the auditor's assessment of risk is high.
C. Performing Tests of Controls, their Nature, Extent & Timing		
8	**Need for Tests of Control**	The auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls when – (a) The auditor intends to rely on the operating effectiveness of controls; or (b) Substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level.
9	**Persuasive Evidence**	In designing and performing tests of controls, more persuasive audit evidence should be obtained when greater reliance is placed on the effectiveness of a control.
10	**Nature and Extent of TOCs**	☞ Auditor should perform other audit procedures and inquiries to obtain audit evidence about the operating effectiveness of the controls. ☞ Further, he should determine whether the controls to be tested depends upon indirect controls, and if so, whether it is necessary to obtain audit evidence supporting the effective operation of those indirect controls
11	**Timing of TOCs**	The auditor shall test controls for the particular time, or throughout the period, for which the auditor intends to rely on those controls
D. Using Audit Evidence obtained during Interim Period		
12	**Requirement**	When the auditor obtains audit evidence about the operating effectiveness of controls during an interim period, the auditor shall: (a) Obtain audit evidence about significant changes to those controls subsequent to the interim period; and (b) Determine the additional audit evidence to be obtained for the remaining period.
E. Using Audit Evidence obtained in Previous Audits		
13	**Factors**	If the auditor decides to use audit evidence about the operating effectiveness of controls obtained in previous audits, the auditor shall consider the following – (a) The effectiveness of other elements of internal control; (b) The risks arising from the manual or automated controls; (c) The effectiveness of general IT-controls; (d) The effectiveness of the control and its application by the entity, including the nature and extent of deviations in the application of the control noted in previous audits, and whether there have been personnel changes that significantly affect the application of the control; (e) Whether the lack of a change in a particular control poses a risk due to changing circumstances; and (f) The risks of material misstatement and the extent of reliance on the control.

<table>
<tr><td>14</td><td>Establishing Continuing Relevance of Evidence</td><td>(a) If the auditor plans to use audit evidence from a previous audit about the operating effectiveness of specific controls, the auditor shall establish the continuing relevance of that evidence by obtaining audit evidence about whether significant changes in those controls have occurred subsequent to the previous audit.
(b) The auditor shall obtain this evidence by performing inquiry combined with observation or inspection, to confirm the understanding of those specific controls, and
<table><tr><td>In the case of any such change</td><td>The auditor should test the operating effectiveness of such controls in the current audit.</td></tr><tr><td>In the case of no such change</td><td>The auditor should test the operating effectiveness of such controls at least once in every third audit, and shall test some controls each audit.
This will avoid the possibility that auditor tests all controls on which he intends to rely in a single audit period with no testing of controls in subsequent Two Audit Periods.</td></tr></table></td></tr>
<tr><td colspan="3"><u>F.</u> <u>Control over Significant Risks</u> [Para – 15]</td></tr>
<tr><td colspan="3">When the auditor plans to rely on controls over a risk the auditor has determined to be a significant risk, the auditor shall test those controls in the current period.</td></tr>
<tr><td colspan="3"><u>G.</u> <u>Evaluation the Operating Effectiveness of Controls</u></td></tr>
<tr><td>16</td><td>Effectiveness of Controls</td><td>As per the mistake detected by substantive procedure, the auditor shall evaluate that whether the relevant controls are operating effectively or not. The absence of misstatements detected by substantive procedures, however, does not assert that controls are effective.</td></tr>
<tr><td>17</td><td>Deviation from Controls</td><td>When deviations from controls upon which the auditor intends to rely are detected, the auditor shall make specific inquiries to understand these matters and their potential consequences, and shall determine whether –
(a) The tests of controls that have been performed provide an appropriate basis for reliance on the controls;
(b) Additional tests of controls are necessary; or
(c) The potential risks of misstatement need to be addressed using substantive procedures.</td></tr>
<tr><td colspan="3"><u>H.</u> <u>Performing Substantive Procedures</u></td></tr>
<tr><td>18
&
19</td><td>Substantive Procedures are a must</td><td>Irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure. [Para – 18]
The Auditor shall consider whether External Confirmation Procedures are to be performed as SAP [Para – 19]
Note → This requirement reflects the facts that – [Para A.42]
(i) The Auditor's assessment of risk is Judgmental and may not identify all risk of Material Misstatement, and
(ii) There are Inherent Limitations to Internal Control, including Management override.</td></tr>
<tr><td>A.43</td><td>Nature and Extent</td><td><u>SPs may be any of the following –</u>
(a) Substantive Analytical Procedures [Note – They are generally more applicable to large volumes of transactions that tend to be predictable over time].</td></tr>
</table>

		(b) Test of Details – The nature of the risk and assertion is relevant to the design of test of details. For examples – test of details related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence. **(c) Combination** of Substantive Analytical Procedures and Test of Details.
A.46 & A.47	**Relationship between Risk, TOC & SPs**	Since the assessment of the risk of material misstatement takes account of internal control, the extent of substantive procedures may need to be increased when the results from tests of controls are unsatisfactory. However, increasing the extent of an audit procedure is appropriate only if the audit procedure itself is relevant to the specific risk. In designing tests of details, the extent of testing is ordinarily thought of in terms of the sample size. However, other matters are also relevant, including whether it is more effective to use other selective means of testing.
20	**SPs of FS Closing Process**	The Auditor's SPs shall include the following APs related to the FS closing process – (a) Agreeing or reconciling the financial statements with the underlying accounting records; and (b) Examining material journal entries and other adjustments made during the course of preparing the financial statements.
21	**SPs for Significant Risks**	When the assessed risk of material misstatement at the assertion level is a significant risk, the auditor shall perform substantive procedures including test of details that are specifically responsive to that risk. When the approach to a Significant Risk consists only of SPs, that procedures shall include TOD.
22 & 23	**SPs at Interim date (Timing of SPs)**	1. **Year – End Additional Procedures [Para – 22] –** When substantive procedures are performed at an interim date, the auditor shall cover the remaining period by performing – (a) Substantive procedures, combined with tests of controls for the intervening period; or (b) If the auditor determines that it is sufficient, further substantive procedures only; that provide a reasonable basis for extending the audit conclusions from the interim date to the period end. 2. **Modifications [Para – 23] –** If misstatements that the auditor did not expect when assessing the risks of material misstatement are detected at an interim date, the auditor shall evaluate whether the related assessment of risk and the planned nature, timing, or extent of substantive procedures covering the remaining period need to be modified.
I. Evaluating adequacy of Presentation and Disclosure [Para – 24]		
The auditor shall perform audit procedures to evaluate whether the overall presentation of the financial statements, including the related disclosures, is in accordance with the applicable financial reporting framework.		
J. Evaluating Sufficiency & Appropriateness of Audit Evidence		
25	**Risk Assessment**	Based on the audit procedures performed and the audit evidence obtained, the auditor shall evaluate before the conclusion of the audit whether the assessments of the risks of material misstatement at the assertion level remain appropriate.
26	**Conclusion as to Audit Evidence**	The auditor shall conclude whether sufficient appropriate audit evidence has been obtained. In forming an opinion, the auditor shall consider all relevant audit evidence, regardless of whether it appears to corroborate or to contradict the assertions in the financial statements.
27	**If SAAE is not obtained**	If the auditor has not obtained sufficient appropriate audit evidence as to a material financial statement assertion, the auditor shall attempt to obtain further audit

		evidence. If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall express a qualified opinion or a disclaimer of opinion.

6. Documentation under SA – 330

28	**Matter to be documented**	The Auditor shall document – (a) The overall responses to address the assessed risks of material misstatement at the financial statement level, and the nature, timing and extent of the further audit procedures performed; (b) The linkage of those procedures with the assessed risks at the assertion level; and (c) The results of the audit procedures, including the conclusions where these are not otherwise clear.
29	**Conclusion based on previous audit**	If the auditor plans to use audit evidence about the operating effectiveness of controls obtained in previous audits, the auditor shall document the conclusions reached about relying on such controls that were tested in a previous audit.
30	**Agreement with Books**	The auditors' documentation shall demonstrate that the financial statements agree or reconcile with the underlying accounting records.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	In the course of audit of Z Ltd, its auditor wants to **rely on audit evidence obtained in previous audit** in respect of effectiveness of internal controls instead of retesting the same during the current audit. As an advisor to the auditor kindly caution him about the **factors that may warrant a re-test of controls.**	[4 Marks] [May 2013]	**Refer Para No. 13 & 14 on Page no. 19 & 20**
2.	**As a Statutory Auditor, how would you deal with the following?** While commencing the statutory audit of B Company Limited, the auditor undertook the **risk assessment and found that the detection risk relating to certain class of transactions cannot be reduced to acceptance level.**	[4 Marks] [Nov. 2003]	**See Below**
And.	SA 315 and SA 330 establish standards on the procedures to be followed to obtain an understanding of the accounting and internal control systems and on audit risk and its components – inherent risk, control risk and detection risk. SAs 315 and 330 require that the auditor should **use professional judgement to assess audit risk and to design audit procedures to ensure that it is reduced to an acceptably low level.** "Detection risk" is the risk that an auditor's substantive procedures will not detect a misstatement that exists in an account balance or class of transactions that could be material. **The higher the assessment of inherent and control risks, the more audit evidence the auditor should obtain from the performance of substantive procedures.** When both inherent and control risks are assessed as high, the auditor needs to consider whether substantive procedures can provide s**ufficient appropriate audit evidence to reduce detection risk**, and therefore audit risk, to an acceptably low level. If it cannot be reduced to an acceptable level, the auditor should **express a qualified opinion or a disclaimer of opinion as may be appropriate.**		

Standard on Auditing (SA) 402 (Revised)
Audit Consideration relating to an Entity using a SO

1. Effective Date [Para – 6]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1, 2, 3, 4 & 5]

1. This SA deals with the user auditor's responsibility to obtain sufficient appropriate audit evidence when a user entity uses the services of one or more Service Organizations (SO).
2. Many services are given by the service organizations like information processing, maintenance of safe custody or assets, and initiation or execution of transactions. However not all may be relevant to the audit.
3. A service is relevant to financial reporting and is part of entities information system when they affect;
   a) The classes of transactions are significant.
   b) The transfer and reporting of accounting entries.
   c) The related accounting records and how information is transferred to the general ledger ;
   d) How the user entity's information system captures insignificant events and conditions ;
   e) The reporting process including significant accounting estimates and disclosures ; and
   f) Controls surrounding journal entries, including non-standard journal entries used to record non- recurring, unusual transactions or adjustments.

Note → The nature and extent of work to be performed by the user auditor regarding the services provided by a service organisation depend on the nature and significance of those services to the user entity and the relevance of those services to the audit.

Note → This SA do not cover services of Financial Institutions that are limited to processing, for an entity's account held at the financial institution, transactions that are specifically authorised by the entity (For e.g. Bank or Stock Broker). Also this SA does not cover other entities (For e.g. Partnerships, Corporations and Joint Ventures).

3. Objective [Para – 7]

(a) To **obtain** an understanding of the nature and significant of the services and their effect on the user entity's internal control relevant to the audit, sufficient to identify and assess the risks of material misstatement; and

(b) To **design and perform** audit procedures responsive to those risks.

4. Definition [Para – 8]

(a)	**Complementary User entity controls**	Controls that the service organization assumes, in the design of its service, will be implemented by user entities, and which, if necessary to achieve control objectives, are identified in the description of its system.
(b)	**Type 1 Report (Report on the description and design of controls at a service organization)**	A report that comprises – (a) A description, prepared by management of the service organization, of the service organization's system, control objectives and related controls that have been designed and implemented as at a specified date ; and (b) 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 service organization's system, control objectives and related controls and the suitability of the design of the controls to achieve the specified control objectives.

(c)	**Type 2 Report (Report on the description, design & operating effectiveness of controls at a service organization)**	A report that comprises – 1. A description, prepared by management of the service organisation, of the service organisation's 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 2. A report by the service auditor with the objective of conveying reasonable assurance that includes – (a) The service auditor's opinion on the description of the service organisation's system, control objectives and related controls, the suitability of the design of the controls to achieve the specified control objectives, and the operating effectiveness of the controls; and (b) A description of the service auditor's tests of the controls and the results thereof.
(d)	**Service Auditor**	An auditor who, at the request of the service organization, provides an assurance report on the controls of a service organization.
(e)	**Service Organisation**	A third-party organization (or segment of a third party organization) that provides services to user entities that are part of those entities' information systems relevant to financial reporting.
(f)	**Service Organisation's System**	The policies and procedures designed, implemented and maintained by the service organization to provide user entities with the services covered by the service auditor's report.
(g)	**Subservice Organisation**	A service organization used by another service organization to perform some of the services provided to user entities that are part of those user entities' information systems relevant to financial reporting.
(h)	**User Auditor**	An auditor who audits and reports on the financial statement of a user entity.
(i)	**User Entity**	An entity that uses a service organization and whose financial statements are being audited.

5. Requirement

A. Obtaining the Understanding the Services provided by a SO, including IC		
A.1 & A.2	**Sources of Information**	☞ Information on the nature of the services provided by a service organisation may be available from a wide variety of sources, such as: ✓ User manuals, ✓ System overviews, ✓ Technical manuals, ✓ The contract or service level agreement between the user entity and the service organisation, ✓ Reports by service organisations, internal auditors or regulatory authorities on controls at the service organisation, ✓ Reports by the service auditor, including management letters, if available. ☞ Knowledge obtained through the user auditor's experience with the service organisation, (for example through experience with other audit engagements).
9	**How Services are uses**	(a) The nature of service provided by the SO and significance of such services and its effect on internal control of UE; (b) The nature and materiality of the transactions processed or accounts or Financial Reporting processes affected by the SO; (c) The degree of interaction between the activities of SO and those of UE and; (d) The nature of the relationship between the UE and SO.

10	**Design and Implementation of Controls**	Evaluate the design and implementation of relevant controls at the user entity
11	**Risk Assessment**	The User Auditor shall determine whether a sufficient understanding of the nature and significance of the services provided by the SO and their effect on the UE's IC relevant to the audit has been obtained, to provide a basis for the I&A of Risks of Material Misstatement.
12.	**Additional Procedures**	If the user Auditor is unable to obtain sufficient understanding, following procedure should be done by the Users Auditor – (a) Obtaining a Type 1 or Type 2 report, if available; (b) Contacting the service organization, through the user entity, to obtain specific information; (c) Visiting the service organization and performing procedures that will provide the necessary information about the relevant controls at the service organization; or (d) Using another auditor to perform procedures that will provide the necessary information about the relevant controls at the service organization.
A.20	**SSO**	A user entity may use a service organisation that in turn uses a subservice organisation to provide some of the services provided to a user entity that are part of the user entity's information system relevant to financial reporting. In such situations, the interaction between the activities of the UE and those of the SO is expanded to include SSO's also, in order to evaluate the controls in the SSO's.
B. Using a Type 1 or Type 2 Report to support the Auditor's understanding of the SO		
13	**Sufficiency of Report**	**In determining the sufficiency and appropriateness the auditor shall –** 1. The service auditor's professional competence (except where the service auditor CA) and independence from the service organization ; and 2. The adequacy of the standards under which the Type 1 or Type 2 report was issued.
14	**Evaluation of Report**	**If auditor plan to use a Type 1 or 2 Report the auditor shall –** 1. Evaluate whether the description and design of controls is at a date or for a period that is appropriate for the user auditor's purposes; 2. Evaluate the sufficiency and appropriateness of the evidence provided by the report. 3. Determine whether complementary user entity controls identified by the service organization are relevant to the user entity and, if so, obtain an understanding of whether the user entity has designed and implemented such controls.
C. Responding to Assessed Risk of Material Misstatement – If the evidence is not sufficient conducting additional procedures or using another auditor to obtain the evidence.		
D. Test of Control		
16	**Affirmation of Operating Effectively**	**Operating effectiveness of controls can be affirmed by** (a) Obtaining a Type 2 report, if available; (b) Performing appropriate tests of controls at the service organization ; or (c) Using another auditor to perform tests of controls at the service organization on behalf of the user auditor.
E. Using Type 2 Report as Audit Evidence for Operating Effectiveness of Controls at the SO		
17	**Type 2 Report as AE for Operating Effectiveness of Controls**	(a) Evaluating whether the description, design and operating effectiveness of controls at the service organization is at a date or for a period that is appropriate for the user auditor's purposes; (b) Determining whether complementary user entity controls if any are implemented and tested ;

		(c) Evaluating the adequacy of the time period covered and the time elapsed since the performance of the tests of controls ; and (d) Evaluating whether the tests of controls are relevant to the assertions and provide sufficient basis to support the user auditor's risk assessment.
F. Evaluation of SO Auditor's Report		
A.37 & A.38	**Evaluation of So Auditor's Report**	☞ If the user auditor believes that the service auditor's report may not provide sufficient appropriate audit evidence, the User Auditor may contact the SO, through the user entity, to request a **discussion with the service auditor** about the scope and results of the service auditor's work. Also, if the user auditor believes it is necessary, the user auditor may contact the service organisation, through the user entity, to request that the service auditor perform procedures at the service organisation. **[Para A.37]** ☞ Exceptions noted by the service auditor or a modified opinion in the service auditor's Type 2 report do not automatically mean that the service auditor's Type 2 report will not be useful for the audit of the user entity's financial statements in assessing the risks of material misstatement. Rather, the exceptions and the matter giving rise to a modified opinion in the service auditor's Type 2 report are considered in the user auditor's assessment of the testing of controls performed by the service auditor. **[Para A.38]**
G. Inclusive or Carve Out Method of Reporting		
A.40	**Inclusive or Carve Out Method**	If a service organisation uses a subservice organisation, the service auditor's report may either include or exclude the subservice organisation's relevant control objectives and related controls in the service organisation's 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.
18	**Reports Carve Out of services SSO**	User Auditor plans to use a Type 1 & Type 2 Report that excludes the services provided by SSO, and those services are relevant to the audit of the UEs FSs, in this case the auditor shall apply this SA to the services of a subservice used by the user entity.
H. Fraud, Non Compliance with L&R and Uncorrected Misstatements in relation to Activities at the SO		
19	**If the above items are present at SO**	☞ The user auditor shall inquire to management and ☞ Evaluate how such matters affect the nature, timing and extent of the user auditor's further audit procedures, including the effect on the user auditor's conclusions and user auditor's report.
I. Reporting by the User Auditor		
20 To 22	**Reporting**	(a) If the user auditor is unable to obtain sufficient appropriate audit evidence regarding the services the user auditor shall modify his opinion. (b) The user auditor shall not refer a service auditor in case of unmodified opinion unless required by law or regulation, and the user auditor's report shall indicate that the reference does not diminish the user auditor's responsibility for the audit opinion. (c) 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.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	In the course of the audit of R Ltd., the audit manager of ABC & Co. observed that **R Ltd. has outsourced certain activities to an outsourcing agency.** As the engagement partner guide the audit manager in the **assessment of services provided by the outsourcing agency** in relation to the audit.	[4 Marks] [May 2011]	**Refer Para No. 9, 10 & 11 on Page no. 24 & 25**
2.	G Ltd. is a mobile phone operating company. Barring the **marketing function** it had **outsourced** the entire operations like maintenance of mobile infrastructure, customer billing, payroll, accounting functions, etc. Assist the auditor of G Ltd. as to how he can **obtain an understanding of how G Ltd. uses the services of the outsourced agency in its operations.**	[5 Marks] [Nov. 2013]	**Refer Para No. 9, 10 & 11 on Page no. 24 & 25**

Standard on Auditing (SA) 450
Evaluation of Misstatements identified during the Audit

1. Effective Date [Para – 2]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

This Standard on Auditing (SA) deals with the auditor's responsibility to evaluate the effect of identified misstatements on the audit and of uncorrected misstatements, if any, in forming an opinion on the financial statements.

3. Objectives [Para – 3]

The objective of the auditor is to evaluate –

(a) The effect of identified misstatements on the audit; and

(b) The effect of uncorrected misstatements, if any, on the financial statements.

4. Definition [Para – 4]

(a)	**Misstatement**	A difference between the amounts, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Misstatements can arise from error or fraud. When the auditor expresses an opinion on whether the financial statements give a true and fair view or are presented fairly, in all material respects, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the auditor's judgment, are necessary for the financial statements to give a true and fair view or present fairly, in all material respects.
A.1	**Reasons for Misstatement**	**Misstatements may result from –** 1. An inaccuracy in gathering or processing data from which the financial statements are prepared; 2. An Omission of an amount or disclosure; 3. An incorrect accounting estimate arising from overlooking, or clear misinterpretation of, facts; and 4. Judgments of management concerning accounting estimates that the auditor considers unreasonable or 5. The selection and application of accounting policies that the auditor considers inappropriate.
A.3	**Types of Misstatement**	**Misstatements can be Classified into –** 1. Factual misstatements are misstatements about which there is no doubt. 2. Judgmental misstatements are differences arising from the judgments of management concerning accounting estimates that the auditor considers unreasonable, or the selection or application of accounting policies that the auditor considers inappropriate. 3. Projected misstatements are the auditor's best estimate of misstatements in populations, involving the projection of misstatements identified in audit samples to the entire populations from which the samples were drawn.
(b)	**Uncorrected Misstatement**	Misstatements that the auditor has accumulated during the audit and that have not been corrected.

5. Requirements [Para – 4]

A. Accumulation of Identified Misstatement		
5	**Accumulation of Identified Misstatement**	☞ The auditor shall accumulate misstatements identified during the audit, other than those that are insignificant. [Para – 5] ☞ 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 financial statements. [Para A.2] ☞ **"Clearly trivial" is not another expression for "not material"** [Para A.2]
B. Consideration of Identified Misstatements as the Audit Progresses		
6 & 7	**Misstatement as Audit Progresses**	The auditor shall identify whether there is need to revise audit plan if the circumstances are such that there may be other misstatements, and the collective effect of such is material.
C. Communication and Correction of Misstatements		
8 & 9	**Communication & Correction**	☞ The auditor shall communicate on a timely basis all misstatements accumulated during the audit with the appropriate level of management, unless prohibited by law. ☞ If management refuses to correct the same then appropriate procedures should be followed.
D. Evaluating the effect of Uncorrected Misstatements		
10 & 11	**Evaluation of Uncorrected Misstatement**	The auditor shall reassess the materiality of misstatements and effect of those on particular classes of transactions, account balances or disclosures in the financial statements, prior period's relevant transactions and financial statements as a whole.
E. Communication with TCWG		
12 & 13	**Communication with TCWG**	**The Auditor shall –** ☞ Uncorrected misstatements and the effect that they, individually or in aggregate, may have on the opinion in the auditor's report, unless prohibited by law or regulation. The auditor's communication shall identify material uncorrected misstatements individually. The auditor shall request that uncorrected misstatements be corrected. ☞ The effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole.
F. Written Representation		
14	**WR**	The auditor shall request a written representation from management and, where appropriate, those charged with governance that whether they believe that the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the financial statements as a whole. A summary of such items shall be included in or attached to the written representation.
G. Documentation		
15	**Documentation**	(a) The amount below which misstatements would be regarded as clearly immaterial (trivial), (b) All misstatements accumulated during the audit and whether they have been corrected and (c) The auditor's conclusion as to whether uncorrected misstatements are material, individually or in aggregate and the basis for that conclusion.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	In the course of audit of T Ltd., the audit team is not sure of the **possible source of misstatements** in the financial statements. As the audit manager identify the sources of misstatements.	[4 Marks] [May 2011] & [May 2013]	**Refer Para No. A.1 on Page no. 28**
2.	The Auditor should consider the aggregate of all uncorrected mis – statements including those involving estimates in his assessment of materiality in audit. Comment. **OR** An assistant of X & Co., CAs, detected an **error of ₹ 5 per interest payment,** which **recurred a number of times.** The General Manager (Finance) of T Ltd advised him not to request for passing any adjustment entry as **individually** the **errors** were of **very small amounts.** The Company had **2000 Deposit Accounts** and interest was paid quarterly. State your views in this issue, with reasons. **OR** While auditing the accounts of a Public Limited Company for the year ended 31st March, an Auditor fount out **error in the valuation of inventory,** which **affects** the **Financial Statement materially.** Comment as per Auditing Standard.	[8 Marks] [May 2002]	**Refer Para No. 5 to 15 on Pg. no. 29**

Standard on Auditing (SA) 500 (Revised)
Audit Evidence

1. Effective Date [Para – 3]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2009.**

2. Scope of this SA [Para – 1 & 2]

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

This SA is applicable to all the audit evidence obtained during the course of the audit. Other SAs deal with specific aspects of the audit (for example, SA 315), the audit evidence to be obtained in relation to a particular topic [for example, SA 570(Revised)], specific procedures to obtain audit evidence [for example, Proposed SA 520 (Revised)], and the evaluation of whether sufficient appropriate audit evidence has been obtained {Proposed SA 200 (Revised) and SA 330].

3. Objectives [Para – 4]

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

4. Definition [Para – 5]

(a)	**Accounting Records**	The records of **initial accounting entries and supporting records**, such as checks and records of electronic fund transfers ; invoices; contracts; the general and subsidiary ledgers, journal entries and other **adjustments** to the financial statements that are not reflected in journal entries; and records such as work sheets and spreadsheets supporting cost allocations, computations, reconciliations and disclosures.
(b)	**Appropriateness of AE**	The **measure of the quality** of audit evidence; that is, its **relevance** and its **reliability** in providing support for the conclusions on which the auditor's opinion is based.
(c)	**AE**	Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information.
(d)	**Management Expert**	An individual or organization **possessing expertise in a field other than accounting or auditing**, whose work in that field is used by the entity to assist the entity in preparing the financial statements.
(e)	**Sufficiency of AE**	The **measure of the quantity** of audit evidence. The quantity of the audit evidence needed is **affected by** the **auditor's assessment of the risks of material misstatement** and also **by the quality** of such audit evidence.

5. Requirement

	A. SAAE	
6	**SAAE**	The auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.

B. Reliability of Audit Evidence [Para – 7] - – When designing and performing audit procedures, the auditor shall evaluate the relevance and reliability of the information to be used as audit evidence. The following are the principles in this regard –

I. Relevance [Para A.27 to A.30]		
(a)	**Meaning**	Relevance deals with the logical connection with, or bearing upon, the purpose of the audit procedure and, where appropriate, the assertion under consideration.
(b)	**Relevance to Audit Procedure**	☞ The relevance of information to be used as audit evidence may be affected by the direction of testing. ☞ **For example** – To test for overstatement in the existence or valuation of accounts payable (Creditor), testing the recorded accounts payable may be a relevant audit procedure. On the other hand, when testing for understatement in the existence or valuation of accounts payable, testing the recorded accounts payable would not be relevant, but testing such information as subsequent disbursements, unpaid invoices, suppliers' statements, and unmatched receiving reports may be relevant.
(c)	**Relevance to Assertion**	☞ A given set of audit procedures may provide audit evidence that is relevant to certain assertions, but not others. ☞ **For example** – The existence of inventory, is not a substitute for obtaining audit evidence regarding another assertion, for example, the valuation of that inventory. On the other hand, audit evidence from different sources or of a different nature may often be relevant to the same assertion.
(d)	**Relevance of TOCs**	☞ Tests of controls are designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level. ☞ Designing tests of controls to obtain relevant audit evidence includes identifying conditions (characteristics or attributes) that indicate performance of a control, and deviation conditions which indicate departures from adequate performance.
(e)	**Relevance of TODs**	☞ Substantive procedures are designed to detect material misstatements at the assertion level. They comprise tests of details and substantive analytical procedures. ☞ Designing substantive procedures includes identifying conditions relevant to the purpose of the test that constitute a misstatement in the relevant assertion.

II. Relevance [Para A.31 to A.33] – Reliability of AE is influenced by its source and its nature, and the circumstances under which it is obtained, including the controls over its preparation and maintenance where relevant. The general rules about the reliability of AE are –	
(a)	Reliability of AE is increased when it is obtained from independent sources outside the Entity. However, such independent external source may not be reliable if the source is not knowledgeable, or a management's expert may lack objectivity.
(b)	The reliability of audit evidence that is generated internally is increased when the related controls, including those over its preparation and maintenance, imposed by the entity are effective.
(c)	Audit evidence obtained directly by the auditor (for example, observation of the application of a control) is more reliable than audit evidence obtained indirectly or by inference (for example, inquiry about the application of a control).
(d)	Audit evidence in documentary form, whether paper, electronic, or other medium, is more reliable than evidence obtained orally
(e)	Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies or facsimiles, or documents that have been filmed, digitised or otherwise transformed into electronic form, the reliability of which may depend on the controls over their preparation and maintenance.

Four major categories of documentary evidence, which provide degree of reliability are –		
Origin	**Held by**	**Example**
Third Parties	**Third Parties**	**Title Deeds to land held by bank towards security.**
Third Parties	**Entity**	**Purchase invoices, Bills for services obtained, Bills for expenses.**
Entity	**Third Parties**	**Sales invoices, Delivery Challans.**
Entity	**Entity**	**Copy of Goods Received Note (GRN), Journal Vouchers (JV).**

C. Information to be used as AE

8	**Using M's E**	When information to be used as audit evidence has been prepared using the work of a management's expert, the auditor shall, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes – 1. Evaluate the competence, capabilities and objectivity of that expert; 2. Obtain an understanding of the work of that expert; and 3. Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion
9	**Information produced by the Entity**	When using information produced by the entity, the auditor shall evaluate whether the information is sufficiently reliable for the auditor's purposes, including as necessary in the circumstances – 1. Obtaining audit evidence about the accuracy and completeness of the information; and 2. Evaluating whether the information is sufficiently precise and detailed for the auditor's purposes.

D. Selecting Items for Testing to Obtain AE

(a) When designing tests of controls and tests of details, the auditor shall determine means of selecting items for testing that are effective in meeting the purpose of the audit procedure. [Para – 10]

(b) The means available to the Auditor for selecting items for Testing and explained below – [Para A.52]

1. Selecting All Items (100%)
2. Selecting Specific Items
3. Audit Sampling

E. Inconsistency in, or doubts over reliability of AE [Para – 11]

S.N.	Situation	The Auditor Shall
(a)	If audit evidence obtained from one source is inconsistent with that obtained from another, or	☞ Determine what modifications or additions to audit procedures are necessary to resolve the matter, and ☞ Consider the effect of the matter, if any, on other aspects of the audit.
(b)	If the auditor has doubts over the reliability of information to be used as audit evidence.	

Other Matter

Audit Procedures for Collecting AE.

1.	**Inspection**	Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset
2.	**Observation**	Observation consists of looking at a process or procedure being performed by others. E.g. The auditor's observation of inventory counting by the entity's personnel, or of the performance of control activities.
3.	**External Confirmation**	An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.
4.	**Recalculation**	Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.
5.	**Re – Performance**	Re – Performance involves the auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal control.
6.	**Analytical Procedures**	Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial and non-financial data. Analytical procedures also encompass the investigation of identified fluctuations and relationships that are inconsistent with other relevant information or deviate significantly from predicted amounts.
7.	**Inquiry**	Inquiry consists of seeking information of knowledgeable persons, both financial and non- financial, within the entity or outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures. Inquiries may range from formal written inquiries to informal oral inquiries. Evaluating responses to inquiries is an integral part of the inquiry process.
8.	**Written Representations**	In respect of some matters, the auditor may consider it necessary to obtain written representations from management and, where appropriate, those charged with governance to confirm responses to oral inquiries.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	The MD of a client Company has advised you Audit Manager that **because of the confidentiality of the Director' Salaries,** the appropriate **records** will **only** be made available **to** you as the **Partner in charge** and **not to your audit staff.** Explain the steps you will take to resolve the issue.	-----------	**Refer Para No. A.31 on Page no. 32**
2.	An assistant of X & Co. Chartered Accountants wanted to **verify the cash in hand and investment** of T Ltd. The **General Manager (Finance)** of T Ltd. **suggested** to the assistant of X & Co. that **it was not necessary as his staff has done the same only few days back and no discrepancies were noted.** Comment on the above.	---------	**Refer Para No. 7 to 9 on Page No. 31 to 32**

Standard on Auditing (SA) 501 (Revised)
Specific Considerations for Selected Items

1. Effective Date [Para – 2]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

This Standard on Auditing (SA) deals with specific considerations by the auditor in obtaining sufficient appropriate audit evidence in accordance with SA 330, SA 500 (Revised) and other relevant SAs, with respect to certain aspects of inventory, litigation and claims involving the entity, and segment information in an audit of financial statements.

3. Objectives [Para – 3]

The objective of the auditor is to obtain sufficient appropriate audit evidence regarding the –

a. Existence and condition of inventory;
b. Completeness of litigation and claims involving the entity; and
c. Presentation and disclosure of segment information in accordance with the applicable financial reporting framework.

4. Requirement

A. Inventory – The Auditors' Duties are summarized as under –		
4	**Existence and Condition**	When inventory is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of inventory by – (a) Attendance at physical inventory counting, unless impracticable, to – 1. Evaluate management's instructions and procedures for recording and controlling the results of the entity's physical inventory counting; 2. Observe the performance of management's count procedures; 3. Inspect the inventory; and 4. Perform test counts; and (b) Performing audit procedures over the entity's final inventory records to determine whether they accurately reflect actual inventory count results.
5	**Different date of Physical Count**	If physical inventory counting is conducted at a date other than the date of the financial statements, the auditor shall, in addition to the procedures mentioned above, perform audit procedures to obtain audit evidence about whether changes in inventory between the count date and the date of the financial statements are properly recorded. Relevant matters for consideration when designing audit procedures to obtain audit evidence about whether changes in inventory amounts between the count date, or dates, and the final inventory records are properly recorded include – [Para A.11] ✓ Whether the perpetual inventory records are properly adjusted. ✓ 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.
6 & 7	**Auditor not able to attend Physical**	☞ If the auditor is unable to attend physical inventory counting due to unforeseen circumstances, the auditor shall make or observe some physical counts on an alternative date, and perform audit procedures on intervening transactions.

<table>
<tr><td></td><td>Inventory Counting</td><td>☞ If attendance at physical inventory counting is impracticable, the auditor shall perform alternative audit procedures to obtain sufficient appropriate audit evidence regarding the existence and condition of inventory. If it is not possible to do so, the auditor shall modify the opinion in the auditor's report in accordance with SA 705.</td></tr>
<tr><td>8</td><td>Inventory under custody and control with Third Party</td><td>When inventory under the custody and control of a third party is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of that inventory by performing one or both of the following –
(a) Request confirmation from the third party as to the quantities and condition of inventory held on behalf of the entity.
(b) Perform inspection or other audit procedures appropriate in the circumstances.
Depending on the circumstances, for example where information is obtained that raises doubt about the integrity and objectivity of the third party, the auditor may consider it appropriate to perform other audit procedures instead of, or in addition to, confirmation with the third party. Examples of other audit procedures include – [Para A.16]
✓ Attending, or arranging for another auditor to attend, the third party's physical counting of inventory, if practicable.
✓ Obtaining another auditor's report, or a service auditor's report, on the adequacy of the third party's internal control for ensuring that inventory is properly counted and adequately safeguarded.
✓ Inspecting documentation regarding inventory held by third parties, for example, warehouse receipts.
✓ Requesting confirmation from other parties when inventory has been pledged as collateral.</td></tr>
<tr><td colspan="3"><u>B.</u> <u>Litigation and Claims</u> –</td></tr>
<tr><td>9</td><td>Identification of L&C</td><td>The auditor shall design and perform audit procedures in order to identify litigation and claims involving the entity which may give rise to a risk of material misstatement, including –
(a) Inquiry of management and, where applicable, others within the entity, including in-house legal counsel;
(b) Reviewing minutes of meetings of those charged with governance and correspondence between the entity and its external legal counsel; and
(c) Reviewing legal expense accounts.</td></tr>
<tr><td>10</td><td>Letter of Inquiry with Entity's External Legal Counsel (ELC)</td><td>☞ If the auditor assesses a risk of material misstatement regarding litigation or claims that have been identified, or when audit procedures performed indicate that other material litigation or claims may exist, the auditor shall, in addition to the procedures required by other SAs, seek direct communication with the entity's external legal counsel.
☞ The auditor shall do so through a letter of inquiry, prepared by management and sent by the auditor, requesting the entity's external legal counsel to communicate directly with the auditor.
☞ If law, regulation or the respective legal professional body prohibits the entity's external legal counsel from communicating directly with the auditor, the auditor shall perform alternative audit procedures.</td></tr>
<tr><td>A.21</td><td>Direct Communication with ELC</td><td>Direct communication with the entity's external legal counsel through a letter of general or specific enquiry assists the auditor in obtaining sufficient appropriate audit evidence as to whether potentially material litigation and claims are known and management's estimates of the financial implications, including costs, are reasonable.</td></tr>
</table>

A.23	**Letter of Inquiry to ELC**	***A letter of specific inquiry includes –*** (a) A list of litigation and claims; (b) Where available, management's assessment of the outcome of each of the identified litigation and claims and its estimate of the financial implications, including costs involved; and (c) A request that the entity's external legal counsel confirm the reasonableness of management's assessments and provide the auditor with further information if the list is considered by the entity's external legal counsel to be incomplete or incorrect.
A.24	**Meeting with ELC**	The auditor may also decide to meet the entity's external legal counsel in the case of significant or complex matters or when there is disagreement between management and the entity's external legal counsel.

Note → IF – [Para – 11]

(a) Management refuses to give the auditor permission to communicate or meet with the entity's external legal counsel, or the entity's external legal counsel refuses to respond appropriately to the letter of inquiry, or is prohibited from responding; and

(b) The auditor is unable to obtain sufficient appropriate audit evidence by performing alternative audit procedures; the auditor shall modify the opinion in the auditor's report in accordance with SA 705.

A.25	**Date on Auditor's Report**	The auditor is required to date the auditor's report no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements.
12	**Written Representation**	The auditor shall request management and, where appropriate, those charged with governance to provide written representations that all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to the auditor and appropriately accounted for and disclosed in accordance with the applicable financial reporting framework.

C. Segment Information –

19	**Obtain SAAE**	The auditor shall obtain sufficient appropriate audit evidence regarding the presentation and disclosure of segment information in accordance with the applicable financial reporting framework by – (a) Obtaining an understanding of the methods used by management in determining segment information, and – 1. Evaluating whether such methods are likely to result in disclosure in accordance with the applicable financial reporting framework; and 2. Where appropriate, testing the application of such methods; and (b) Performing analytical procedures or other audit procedures appropriate in the circumstances.
A.27	**Methods used by Management in Segment Information**	Matters that may be relevant when obtaining an understanding of the methods used by management in determining segment information and whether such methods are likely to result in disclosure in accordance with the applicable financial reporting framework include – 1. Sales, transfers and charges between segments, and elimination of inter-segment amounts. 2. Comparisons with budgets and other expected results, for example, operating profits as a percentage of sales. 3. The allocation of assets and costs among segments. 4. Consistency with prior periods, and the adequacy of the disclosures with respect to inconsistencies.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	You are the auditor of Easy Communications Ltd. for the year 2012–13. The inventory as at the end of the year i.e. 31.3.13 was ₹ 2.25 Crores. **Due to unavoidable circumstances, you could not be present at the time of annual physical verification.** Under the above circumstances how would you ensure that the physical verification conducted by the management was in order?	[5 Marks] [Nov. 2008]	**Refer Para No. 6 & 7 on Page no. 36 & 37**
2.	XYZ Ltd has significant operations in a foreign country. Due to civil and political unrest in that country **physical verification of inventory and fixed assets could not carried out** and you are not in a position to obtain audit evidence through other audit procedures also. The **value of fixed assets and inventory forms part of 80% of the asset value of the company.** As the auditor of XYZ Ltd what **factors** do you **consider** in your **reporting responsibility.** Also draft a suitable report that will be incorporated in the main audit report (Reporting under CARO 03 need not be considered).	[8 Marks] [May 2013]	**See Below**

Ans.

<u>Following factors are to be considered in auditor's reporting responsibility</u> –

(a) Inventories and the Fixed Assets are material to the financial statements.

(b) Auditor is unable to attend physical verification of the inventories and fixed assets. In other words, physical verification becomes impracticable due to civil and political unrest in the foreign country, where the inventory and fixed assets are located, posing threats to the safety of auditor.

(c) Auditor failed to obtain proper and sufficient audit evidence, even by alternative audit procedures.

<u>Draft of the suitable report to be incorporated in the main audit report</u> –

"Our responsibility is to express an opinion on these financial statements based on our audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Because of the matters described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for Disclaimer of Opinion

We were appointed as auditors of the Company and we report that we could not observe the counting of physical inventories and physical verification of fixed assets due to civil and political unrest in foreign country where the company has significant operation. We were also unable to satisfy

	ourselves by alternative means concerning the inventory quantities and fixed assets of the company held at March 31st 20XX, which are stated in the Balance Sheet at ₹ XXX and ₹ XXX, respectively. ***Disclaimer of Opinion*** *Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statements.* ***Report on Other Legal and Regulatory Requirements*** As required by section 227(3) of the Companies Act, 1956, we report that – As described in the Basis for Disclaimer of Opinion paragraph, we were unable to obtain all the information and explanations which to the best of our knowledge and belief were necessary for the purpose of our audit.

Standard on Auditing (SA) 505 (Revised)
External Confirmations

1. Effective Date [Para – 4]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

- This Standard on Auditing (SA) deals with the auditor's use of external confirmation procedures to obtain audit evidence in accordance with the requirements of SA – 330 and SA – 500.
- It does not address inquiries regarding litigation and claims.

3. Objectives [Para – 5]

The objective of the auditor, when using external confirmation procedures, is to design and perform such procedures to obtain relevant and reliable audit evidence.

4. Definitions [Para – 6]

(a)	**External Confirmation**	Audit evidence obtained as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.
(b)	**Positive Confirmation Request**	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 requested information.
(c)	**Negative Confirmation Request**	A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.
(d)	**Non Response**	A failure of the confirming party to respond, or fully respond, to a positive confirmation request, or a confirmation request returned undelivered.
(e)	**Exception**	A response that indicates a difference between information requested to be confirmed, or contained in the entity's records, and information provided by the confirming party.

5. External Confirmation Procedures to Obtain Audit Evidence [Para –2 &3]

- Audit evidence in the form of external confirmations received directly by the auditor from confirming parties may be more reliable than evidence generated internally by the entity. This SA is intended to assist the auditor in designing and performing external confirmations procedures to obtain relevant and reliable audit evidence.
- Other SAs recognise the importance of external confirmations as audit evidence,(for example – SA 240/330/500).

6. Requirement

Para No.	Aspects	Descriptions
7	**Procedure / Control**	**When using external confirmation procedures, maintain control over external confirmation requests, including –** (a) Determining the information to be confirmed or requested; (b) Selecting the appropriate confirming party; (c) Designing the confirmation requests and their route such that they are properly

<table>
<tr><td></td><td></td><td>addressed and contain return information for responses to be sent directly to the auditor; and
(d) Sending the requests, including follow – up requests when applicable, to the confirming party.</td></tr>
<tr><td>8
&
9</td><td>Effect of Management 's Refusal</td><td>1. If management refuses to allow the auditor to send a confirmation request, the auditor shall –
(a) Inquire the validity and reasonableness of the reasons for their refusal;
(b) Evaluate its implications on the auditor's assessment of the relevant risks of material misstatement, including the risk of fraud, and on the nature, timing and extent of other audit procedures; and
(c) Perform alternative audit procedures to obtain relevant and reliable audit evidence.
2. Further Duties of Auditor –
<table>
<tr><th>S.N.</th><th>If the Auditor –</th><th>Then the Auditor Shall –</th></tr>
<tr><td>(a)</td><td>Concludes that management's refusal is unreasonable, or</td><td rowspan="2">☞ Communicate with those charged with governance and
☞ Also determine the implications for the audit and the auditor's opinion.</td></tr>
<tr><td>(b)</td><td>Is unable to obtain relevant and reliable audit evidence from alternative audit procedures</td></tr>
</table></td></tr>
<tr><td colspan="3">Results of External Confirmation Procedures [Para – 10 to 14]</td></tr>
<tr><td>10
&
11</td><td>Doubt or Unreliable Response</td><td>☞ If the auditor doubts or concludes that a response to a confirmation request is not reliable, then he shall obtain further audit evidence and
☞ Shall evaluate the implications on the assessment of the relevant risks of material misstatement, including the risk of fraud, and on the related nature, timing and extent of other audit procedures.</td></tr>
<tr><td>12</td><td>Non – Response</td><td>In the case of each non-response, the auditor shall perform alternative audit procedures to obtain relevant and reliable audit evidence.</td></tr>
<tr><td>13</td><td>Necessity of Positive Confirmation</td><td>☞ If the auditor has determined that a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence, alternative audit procedures will not provide the audit evidence the auditor requires.
☞ If the auditor does not obtain such confirmation, the auditor shall determine the implications for the audit and the auditor's opinion in accordance with SA 705.</td></tr>
<tr><td>14</td><td>Exceptions</td><td>The auditor shall investigate exceptions to determine whether or not they are indicative of misstatements.</td></tr>
<tr><td>15</td><td>Negative Confirmation</td><td>Negative confirmation requests should not be used as the sole substantive audit procedure to address an assessed risk of material misstatement at the assertion level unless all of the following are present –
(a) The auditor has assessed the risk of material misstatement as low and has obtained sufficient appropriate audit evidence regarding the operating effectiveness of controls relevant to the assertion;
(b) The population of items subject to negative confirmation procedures comprises a large number of small, homogeneous, account balances, transactions or conditions;
(c) A very low exception rate is expected; and
(d) The auditor is not aware of circumstances or conditions that would cause recipients of negative confirmation requests to disregard such requests.</td></tr>
</table>

16	**Evaluating Evidence Obtained**	The auditor shall evaluate whether the results of the external confirmation procedures provide relevant and reliable audit evidence, or whether performing further audit procedures is necessary.
A.48 of SA 330	**External Confirmations may be used in the following situations**	1. Bank Balances and Other Information relevant to Banking Relationships. 2. Accounts Receivables balances and items. 3. Accounts Payable balances and items. 4. Inventories held by Third Parties at Bonded Warehouses for Processing or on Consignment. 5. Property Title Deed held by Lawyers or Financers for safe custody or as security. 6. Investment held for safe – keeping by Third Parties, or Purchased from Stock – Brokers but not delivered at B/S date. 7. Amount due to Lenders, including relevant terms of repayment and restrictive covenants.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	The management of S Ltd. requests you **not to seek confirmation from its debtors.** As the auditor of S Ltd., what can be an appropriate response? **OR** The auditor of H Ltd. wanted to obtain confirmation from its creditors. But the **management made a request to the auditor not to seek confirmation from certain creditors citing disputes.** Can the auditor of H Ltd. Accede to this request?	**[6 Marks] [May 2011] & [4 Marks] [May 2013]**	**Refer Para No. 8 & 9 on Page no. 42**
2.	Moon Limited replaced its statutory auditor for the Financial year 2013 – 14. During the course of audit, the new auditor found a credit item of ₹ 5 Lakhs. On enquiry, the company explained him that it is, a very old credit balance. **The creditor had neither approached for the payment nor is he traceable.** Under the circumstances, **no confirmation of the credit balance is available.** Comment.	**[5 Marks] [Nov. 2009]**	**See Below**
Ans.	This is a case of external confirmation, covered by SA 505 "External Confirmation". The identities of creditors are not traceable to confirm the credit balance as appearing in the financial statement of the company. It is also **not a case of pending litigation.** It might be a case that an **income** of ₹ 5 Lakhs had been **hidden in previous year/s.** The statutory auditor should **examine the validity of the credit balance** as appeared in the company's financial statements. He should **obtain sufficient evidence in support of the balance.** He should **apply alternative audit procedures to get documentary proof** for the transaction/s and should **not rely entirely on the management representation.** Finally, he should include the matter y way of a qualification in his audit report to the members.		

Standard on Auditing (SA) 510 (Revised)

Initial Audit Engagements – Opening Balances

1. Effective Date [Para – 2]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

- This Standard on Auditing (SA) deals with the auditor's responsibilities relating to opening balances when conducting an initial audit engagement.
- In addition to financial statement amounts, opening balances include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

3. Objectives [Para – 3]

In conducting an initial audit engagement, the objective of the auditor with respect to opening balances is to obtain sufficient appropriate audit evidence about whether –

(a) Opening balances contain misstatements that materially affect the current period's financial statements; and

(b) Appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are properly accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

4. Definitions [Para – 4]

(a)	**Initial Audit Engagement**	An engagement in which either – (a) The financial statements for the prior period were not audited; or (b) The financial statements for the prior period were audited by a predecessor auditor.
(b)	**Opening Balance**	Those account balances that exist at the beginning of the period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.
(c)	**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.

5. Requirements

A. Audit Procedures		
5	**Reading FS**	The auditor shall read the most recent financial statements as well as the predecessor auditor's report
6 & A.2	**Procedures**	Audit shall obtain sufficient appropriate audit evidence that whether the opening balances contain misstatements that materially affect the current period's financial statements by – - Checking prior period's closing balances with current year's opening balances and other adjustments disclosed as prior period items in the current year's Statement of Profit and Loss. - Auditor should determine whether the opening balances reflect the application of appropriate accounting policies and

7		☞ Auditor should get the copies of prior period's which he should evaluate and perform specific audit procedures to obtain evidence regarding the opening balances.
7	**Misstatement**	☞ If the auditor obtains audit evidence that the opening balances contain misstatements that could materially affect the current period's financial statements, the auditor shall perform such additional audit procedures as are appropriate in the circumstances to determine the effect on the current period's financial statements. ☞ If the Auditor concludes that such Misstatement exist in the current period's FSs, the Auditor shall communicate the Misstatements as per SA – 450.

B. Special Duties –

8	**Consistency of Accounting Policies**	**The auditor shall obtain sufficient appropriate audit evidence about –** ☞ Whether the accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, and ☞ Whether changes in the accounting policies have been properly accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.
9	**Modification of Opinion in Predecessor Auditors Report**	If the prior period's financial statements were audited by a predecessor auditor and there was a modification to the opinion, the auditor shall evaluate the effect of the matter giving rise to the modification in assessing the risks of material misstatement in the current periods financial.

C. Audit Conclusions and Forms of Reporting

Para No.	Situation	Nature of Opinion
10	If the auditor is unable to obtain SAAE regarding the Opening Balances.	Qualified Opinion or a Disclaimer of Opinion as per SA – 705
11	**If the auditor concludes that –** (a) The opening balances contain a misstatement that materially affects the current period's financial statements, and (b) The effect of the misstatement is not properly accounted for or not adequately presented or disclosed	Qualified Opinion or a Disclaimer of Opinion as per SA – 705
12	**If the auditor concludes that –** (a) The current period's accounting policies are not consistently applied in relation to opening balances in accordance with the applicable financial reporting framework; or (b) A change in accounting policies is not properly accounted for or not adequately presented or disclosed in accordance with the applicable financial reporting framework.	Qualified Opinion or a Disclaimer of Opinion as per SA – 705
13	If the predecessor auditor's opinion regarding the prior period's financial statements included a modification to the auditor's opinion that remains relevant and material to the current period's financial statements	Qualified Opinion or a Disclaimer of Opinion as per SA – 705 and SA – 710

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	In an initial audit engagement the auditor will have to **satisfy about the sufficiency and appropriateness of 'Opening Balances'** to ensure that they are free from misstatements, which may materially affect the current financial statements. Lay down the audit procedure, you will follow in cases – (i) When the financial statements are **audited for the preceding period by another auditor;** and (ii) When financial statements are **audited for the first time.**	[7 Marks] [Nov. 2004]	**Refer Para No. 5 to 9 on Page no. 44 & 45**
2.	If, after performing the procedure, you **are not satisfied about the correctness of 'Opening Balances'**; what approach you will adopt in drafting your audit report in two situations mentioned in (2) above?	[7 Marks] [Nov. 2004]	**Refer Para No. 10 to 13 on Pg. no. 45**

Standard on Auditing (SA) 520 (Revised)

Analytical Procedures

1. Effective Date [Para – 2]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010.**

2. Scope of this SA [Para – 1]

- This Standard on Auditing (SA) deals with the auditor's use of analytical procedures as substantive procedures ("substantive analytical procedures"), and as procedures near the end of the audit that assist the auditor when forming an overall conclusion on the financial statements.
- The use of analytical procedures as risk assessment procedures is dealt with in SA 315. SA 330 includes requirements and guidance regarding the nature, timing and extent of audit procedures in response to assessed risks; these audit procedures may include substantive analytical procedures.

3. Objectives [Para – 3]

(a) To obtain relevant and reliable audit evidence when using substantive analytical procedures; and

(b) To design and perform analytical procedures near the end of the audit that assists the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor understanding of the entity.

4. Definitions [Para – 4]

(a)	**Analytical Procedures**	☞ For the purposes of the SAs, the term "Analytical Procedures" means evaluation 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. The auditor's choice of procedures, methods and level of application is a matter of professional judgement. Analytical procedures include the consideration of **comparisons** of the entity's financial information with – **[Para A.1]** ✓ Prior period information; ✓ Budgets, forecasts ; ✓ Similar industry information etc. **Analytical procedures also include consideration of relationships, for example – [Para A.2]** ☞ Among elements of financial information that would be expected to conform to a predictable pattern based on the entity's experience, such as gross margin percentages. ☞ Between financial information and relevant non-financial information, such as payroll costs to number of employees.

5. Requirements

A. Substantive Analytical Procedures [Para – 5] – When designing and performing substantive analytical procedures, the auditor shall –

(a)	Determine the suitability of particular substantive analytical procedures for given assertions
(b)	Develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify a misstatement.
(c)	Evaluate the reliability of data from which the auditor's expectation of recorded amounts or ratios is developed.
(d)	Determine the amount of any difference of recorded amounts from expected values that is acceptable without further investigation.

B. APs that assist when forming an Overall Conclusion [Para – 6] –

- The auditor shall design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor's understanding of the entity.
- The results of such analytical procedures may identify a previously unrecognised risk of material misstatement. These analytical procedures may be similar to those that would be used as risk assessment procedures. **[Para A.18]**

C. Investigating Results of APs [Para – 7] –

- 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 –
  - (a) **Inquiring of management** and obtaining appropriate audit evidence relevant to management's responses; and
  - (b) Performing **other audit procedures** as necessary in the circumstances.
- The need to perform other audit procedures may arise when, for example, management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate.**[Para A.21]**

Examples of Analytical Procedures

1	**Trends**	Analysing account fluctuations by comparing current year to prior year information and, also, to information derived over several years.
2	**Reasonableness Tests**	Tests are made by reviewing the relationship of certain account balances to other balances for reasonableness of amounts. Examples of accounts that may be reasonably tested are – (a) Interest expense against interest bearing obligations. (b) Raw Material Consumption to Production (quantity). (c) Wastage & Scrap % against production & raw material consumption (quantity). (d) Work-in-Progress based on issued of materials & Sales (quantity). (e) Sales discounts and commissions against sales volume. (f) Rental revenues based on occupancy of premises

3	**Analysis by Computation of Ratios**	Analysis by computation of ratios includes the study of relationships between financial statement amounts. Commonly used ratios include – (a) Elements of income or loss as a percentage of sales. (b) Gross profit turnover. (c) Accounts receivable turnover. (d) Inventory turnover. (e) Profitability, leverage, and liquidity

Sources of Information for Analytical Procedures

1	**Interim financial information**
2	**Budgets**
3	**Management Accounts**
4	**Non – Financial Information**
5	**Bank and Cash Records**
6	**VAT Returns**
7	**Board Minutes**
8	**Discussion or Correspondence with Client at year – end.**

Some Past Attempts Question

S.N.	Question	Marks and Attempt	Answer
1.	In the audit of Hotel Great Stay Ltd. its auditor wants to **use the analytical procedure as substantive procedure** in respect of room rental income as well as payroll costs. Guide him as to how it can be done.	**[4 Marks]** **[Nov. 2013]**	**See Below**
Ans.	As per **SA 520 on "Analytical Procedures",** in some cases, even an unsophisticated predictive model may be effective as an analytical procedure. ☞ **In case of Payroll cost –** Where an entity has a known number of employees at fixed rates of pay throughout the period, it may be possible for the auditor to use this data to estimate the total payroll costs for the period with a high degree of accuracy, thereby providing audit evidence for a significant item in the financial statements and reducing the need to perform tests of details on the payroll. ☞ **In case of Room Rental Income of Hotel –** Different types of analytical procedures provide different levels of assurance. Analytical procedures involving the prediction of total rental income in case of Hotel taking the room tariff rates, the number of rooms and vacancy rates into consideration, can provide persuasive evidence and may eliminate the need for further verification by means of tests of details, provided the elements are appropriately verified.		

Standard on Auditing (SA) 530 (Revised)
Audit Sampling

1. Effective Date [Para – 3]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2009.**

2. Scope of this SA [Para – 1]

- This Standard on Auditing (SA) applies when the auditor has decided to use audit sampling in performing audit procedures.
- It deals with the auditor's use of statistical and non-statistical sampling when designing and selecting the audit sample, performing tests of controls and tests of details, and evaluating the results from the sample.

3. Objectives [Para – 4]

The objective of the auditor when using audit sampling is to provide a reasonable basis for the auditor to draw conclusions about the population from which the sample is selected.

4. Definitions [Para – 5]

<table>
<tr><td>(a)</td><td>Audit Sampling (Sampling)</td><td>The application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population.</td></tr>
<tr><td>(b)</td><td>Population</td><td>The entire set of data from which a sample is selected and about which the auditor wishes to draw conclusion.</td></tr>
<tr><td>(c)</td><td>Sampling Risk</td><td>The 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. Sampling risk can lead to two types of erroneous conclusion –
<table>
<tr><th>Error Type</th><th>In case of TOCs</th><th>In case of TODs</th><th>Effect of this erroneous conclusion</th></tr>
<tr><td>Type I</td><td>That Controls are more effective than they actually are (i.e. Risk of over reliance)</td><td>That a Material Misstatement doesn't exist, when in fact it does (i.e. Risk of incorrect acceptance)</td><td>This affects audit effectiveness, and is more likely to lead to an inappropriate audit opinion.</td></tr>
<tr><td>Type 2</td><td>That Controls are less effective than they actually are (i.e. Risk of over reliance)</td><td>That a Material Misstatement does exist, when in fact it does not (i.e. Risk of incorrect rejected)</td><td>This affects audit efficiency, as it would usually lead to additional work to establish that initial conclusions were incorrect.</td></tr>
</table></td></tr>
<tr><td>(d)</td><td>Non – Sampling Risk</td><td>The risk that the auditor reaches an erroneous conclusion for any reason not related to sampling risk. (E.g. use of inappropriate audit procedures, mis – interpretation of audit evidence, failure to recognize a mis – statement or deviation, etc.)</td></tr>
<tr><td>(e)</td><td>Anomaly</td><td>A misstatement or deviation that is demonstrably not representative of misstatements or deviations in a population.</td></tr>
</table>

(f)	**Sampling Unit**	The individual items constituting a population.
(g)	**Statistical sampling**	☞ An approach to sampling that has the following characteristics – (a) Random selection of the sample items; and (b) The use of probability theory to evaluate sample results, including measurement of sampling risk. ☞ A sampling approach that does not have characteristics (i) and (ii) is considered non-statistical sampling.
(h)	**Stratification**	The process of dividing a population into sub-populations, each of which is a group of sampling units which have similar characteristics (often monetary value).
(i)	**Tolerable Mis – statement**	A monetary amount set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the monetary amount set by the auditor is not exceeded by the actual misstatement in the population.
(j)	**Tolerable Rate of Deviation**	A rate of deviation from prescribed internal control procedures set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the rate of deviation set by the auditor is not exceeded by the actual rate of deviation in the population.

5. Requirements

	A. Design, Size & Selection of Items for Testing [Para – 6 – 8]
6	When designing an audit sample, the auditor shall consider the purpose of the audit procedure and the characteristics of the population from which the sample will be drawn.
7	☞ The auditor shall determine a sample size sufficient to reduce sampling risk to an acceptably low level. ☞ The level of sampling risk that the auditor is willing to accept affects the sample size required. The lower the risk the auditor is willing to accept, the greater the sample size will need to be. [Para A.10]
8	The auditor shall select items for the sample in such a way that each sampling unit in the population has a chance of selection.
	B. Performing Audit Procedures [Para – 9 – 11]
9	The auditor shall perform audit procedures, appropriate to the purpose, on each item selected.
10	If the audit procedure is not applicable to the selected item, the auditor shall perform the procedure on a replacement item.
11	If the auditor is unable to apply the designed audit procedures, or suitable alternative procedures, to a selected item, the auditor shall treat that item as a deviation from the prescribed control, in the case of tests of controls, or a misstatement, in the case of tests of details.
	C. Nature and Cause of Deviations and Mis – statement [Para – 12 & 13]
12	The auditor shall investigate the nature and cause of any deviations or misstatements identified, and evaluates their possible effect on the purpose of the audit procedure and on other areas of the audit.
13	In the extremely rare circumstances when the auditor considers a misstatement or deviation discovered in a sample to be an anomaly, the auditor shall obtain a high degree of certainty that such misstatement or deviation is not representative of the population. The auditor shall obtain this degree of certainty by performing additional audit procedures to obtain sufficient appropriate audit evidence that the misstatement or deviation does not affect the remainder of the population.
	D. Projecting Mis - Statements [Para – 14]
14	For tests of details, the auditor shall project misstatements found in the sample to the population. Note – If a misstatement / deviation is categorized as an anomaly, it may be excluded from being projected on to the population.

E. Evaluating Results of Audit Sampling [Para – 15] – The Auditor shall evaluate –	
15	(a) The results of the sample; and (b) Whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

F. Conclusions on Audit Sampling [Para A.21, A.22] – The Auditor shall evaluate –	
TOCs	A high sample deviation rate may lead to an increase in the assessed risk of material misstatement
TODs	☞ A high Mi – Statement amount in a sample may cause the Auditor to believe that a class of transactions or account balance is materially misstated. ☞ When the auditor's best estimate of misstatement in the population (i.e., projected misstatement plus anomalous misstatement) > tolerable misstatement, the sample does not provide a reasonable basis for conclusions about the population that has been tested. ☞ The closer the projected misstatement plus anomalous misstatement is to tolerable misstatement, the more likely that actual misstatement in the population may exceed tolerable misstatement. ☞ If the projected misstatement is > the auditor's expectations of misstatement used to determine the sample size, the auditor may conclude that there is an unacceptable sampling risk that the actual misstatement in the population exceeds the tolerable misstatement.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	While planning the audit of S Ltd. you want to apply sampling techniques. What are the **risk factors you should keep in mind?**	**[4 Marks]** **[May 2010]**	**Refer Para No. 5 (C) on Page no. 50**
2.	Write short note on **Sampling Risk.**	**[4 Marks]** **[Nov. 2006]**	**Refer Para No. 5 (C) on Page no. 50**

Standard on Auditing (SA) 540 (Revised)

Auditing Accounting Estimates, including Fair Value Accounting Estimates & Related Disclosures

1. Effective Date [Para – 5]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2009.**

2. Scope of this SA [Para – 1]

- This SA deals with the auditor's responsibilities regarding accounting estimates, including fair value accounting estimates, and related disclosures in an audit of financial statements.
- It includes requirements and guidance on misstatements of individual accounting estimates, and indicators of possible management bias.

3. Objectives [Para – 6]

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

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

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

4. Nature of Accounting Estimates [Para – 2, 3 & 4]

- The nature and reliability of information available to management to support the making of an accounting estimate varies widely, which thereby affects the degree of estimation uncertainty associated with accounting estimates.
- The degree of estimation uncertainty affects, in turn, the risks of material misstatement of accounting estimates, including their susceptibility to unintentional or intentional management bias.
- A difference between the outcome of an accounting estimate and the amount originally recognized or disclosed in the financial statements does not necessarily represent a misstatement of the financial statements. This is particularly the case for fair value accounting estimate.

5. Definitions [Para – 7]

(a)	**Accounting Estimate**	An approximation of a monetary amount in the absence of a precise means of measurement. This term is used for an amount measured at fair value where there is estimation uncertainty, as well as for other amounts that require estimation.
(b)	**Estimation Uncertainty**	The susceptibility of an accounting estimate and related disclosures to an inherent lack of precision in its measurement.
(c)	**Auditor's Point Estimate or Auditor's Range**	The amount, or range of amounts, respectively, derived from audit evidence for use in evaluating management's point estimate.
(d)	**Management bias**	A lack of neutrality by management in the preparation and presentation of information.
(e)	**Management's Point Estimate**	The amount selected by management for recognition or disclosure in the financial statements as an accounting estimate.
(f)	**Outcome of an Accounting Estimate**	The actual monetary amount which results from the resolution of the underlying transaction(s), event(s) or condition (s) addressed by the accounting estimate.

6. Requirements

<table>
<tr><td colspan="3"><u>A. Risk Assessment Procedures and Related Activities</u> –</td></tr>
<tr><td>8</td><td>Understanding the Entity</td><td>The Auditor shall obtain an understanding of the following in order to provide a basis for the identification and assessment of the risks of material misstatement for Accounting Estimates –
(a) The requirements of the applicable financial reporting framework relevant to accounting estimates, including related disclosures.
(b) How management identifies those transactions, events and conditions that may give rise to the need for accounting estimates to be recognised or disclosed in the financial statements. In obtaining this understanding, the auditor shall make inquiries of management about changes in circumstances that may give rise to new, or the need to revise existing, accounting estimates How management makes the accounting estimates, and an understanding of the data on which they are based, including –
1. The method, including where applicable the model, used in making the accounting estimate;
2. Relevant controls;
3. Whether management has used an expert;
4. The assumptions underlying the accounting estimates;
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. Whether and, if so, how management has assessed the effect of estimation uncertainty</td></tr>
<tr><td>9</td><td>Review of Prior Period Estimates</td><td>☞ The auditor shall review the outcome of accounting estimates included in the prior period financial statements, or, where applicable, their subsequent re-estimation for the purpose of the current period.
☞ The nature and extent of the auditor's review takes account of the –
1. Nature of the Accounting Estimates, and
2. Whether the information obtained from the review would be relevant to identifying and assessing risks of material misstatement of accounting estimates made in the current period financial statements.
☞ The review is not intended to call into question (evaluate) the judgments made in the prior periods that were based on information available at that time.</td></tr>
<tr><td colspan="3"><u>B. Identifying and Assessing RMM</u> –</td></tr>
<tr><td>10</td><td colspan="2">In identifying and assessing the risks of material misstatement, the auditor shall evaluate the degree of estimation uncertainty associated with an accounting estimate.</td></tr>
<tr><td>11</td><td colspan="2">The auditor shall determine whether, in the auditor's judgment, any of those accounting estimates that have been identified as having high estimation uncertainty give rise to significant risks.</td></tr>
<tr><td colspan="3"><u>C. Response to the Assessed RMM</u> –</td></tr>
<tr><td>12</td><td>Determining Compliance</td><td><u>Based on the assessed risks of material misstatement, the auditor shall determine-</u>
☞ Whether management has appropriately applied the requirements of the applicable financial reporting framework relevant to the accounting estimate; and
☞ Whether the methods for making the accounting estimates are appropriate and have been applied consistently, and whether changes, if any, in accounting estimates or in the method for making them from the prior period are appropriate in the circumstances.</td></tr>
</table>

13	**Responding to Risks**	**In responding to the assessed risks of material misstatement, the auditor shall –** **1.** Determine whether events occurring up to the date of the auditor's report provide audit evidence regarding the accounting estimate. **2.** Test that whether the method of measurement and the assumptions used by the management in making accounting estimates are reasonable and appropriate. **3.** Test the operating effectiveness of the controls over how management made the accounting estimate, together with appropriate substantive procedures. **4.** Develop a point estimate or a range to evaluate management's point estimate.
14	**Special Skills**	While responding to the assessed risks of material misstatement the auditor shall consider whether specialized skills or knowledge in relation to one or more aspects of the accounting estimates are required in order to obtain sufficient appropriate audit evidence.

D. Further Substantive Procedures to respond to Significant Risks –

15 & 16	**Estimation Uncertainly**	(a) For accounting estimates that give rise to significant risks, the auditor shall evaluate the following – ☞ How management has considered **alternative assumptions**, outcomes and estimation uncertainty in making the accounting estimate. ☞ Whether the significant **assumptions** used by management **are reasonable.** ☞ Appropriate application of the financial reporting framework, and in this respect, **management's intent** to carry out specific courses of action and its **ability** to do so. (b) If, in the auditor's judgment, management has not adequately addressed the effects of estimation uncertainty on the accounting estimates that give rise to significant risks, the auditor shall, if considered necessary, **develop a range** with which to evaluate the reasonableness of the accounting estimate.
17	**Recognition and Measurement Criteria**	For accounting estimates that give rise to significant risks, the auditor shall obtain sufficient appropriate audit evidence whether the following are in accordance with the requirements of the applicable financial reporting framework – (a) Management's decision regarding recognition of accounting estimates in the financial statements; and (b) The selected measurement basis for the accounting estimates.

E. Evaluating Reasonableness of Accounting Estimates and Determining Mis – Statements – The auditor shall evaluate, based on the audit evidence, whether the accounting estimates in the financial statements are either reasonable in the context of the applicable financial reporting framework, or are misstated. **[Para – 18]**

F. Disclosures Related to Accounting Estimates –

(a) The auditor shall obtain sufficient appropriate audit evidence about whether the disclosures in the financial statements related to accounting estimates are in accordance with the requirements of the applicable financial reporting framework. **[Para – 19]**

(b) 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 financial statements in the context of the applicable financial reporting framework. **[Para – 20]**

G. Indicators of Possible Management Bias – The auditor shall review the judgments and decisions made by management in the making of accounting estimates to identify whether there are indicators of possible management bias. Indicators of possible management bias do not themselves constitute misstatements for the purposes of drawing conclusions on the reasonableness of individual accounting estimates. **[Para – 21]**

H. Written Representations – The auditor shall obtain written representations from management whether management believes that significant assumptions used by it in making accounting estimates are reasonable. **[Para – 22]**

I. Documentation – The audit documentation shall include –

(a) The basis for the auditor's conclusions about the reasonableness of accounting estimates and their disclosure that give rise to significant risks; and

(b) Indicators of possible management bias, if any.

Some Past Attempts Question

S.N.	Question	Marks and Attempt	Answer
1.	While auditing Z Ltd., you observe **certain material financial statement assertions have been based on estimates** made by the management. As the auditor how do you minimize the risk of material misstatements?	**[6 Marks] [May 2011]**	**Refer Para No. 8 & 9 on Page no. 54**

Standard on Auditing (SA) 550 (Revised)
Related Parties

1. Effective Date [Para – 8]

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2008.**

2. Scope of this SA [Para – 1]

This SA deals with the auditor's responsibilities regarding RPRs and transactions of the FSs.

3. Objectives [Para – 6]

The auditor must obtain an in-depth and comprehensive understanding of the related party relationships and transactions, in order to be able to –

1. To recognize the fraud risk factors from related party relationships and transactions, that are relevant to the identification and assessment of material misstatements due to fraud; and
2. To conclude whether the financial statements, insofar as they are affected by those relationships and transactions –
   a. Achieve a true and fair presentation.
   b. Are not misleading.

4. Definitions [Para – 10]

(a)	**Parties are related when**	If at any time during the reporting period, one party has the ability to control or exercise significant influence over the other party in making financial and/or operating decisions
(b)	**Arm's length transaction**	It refers to one, in the ordinary course of business, between consenting parties, the consent being free from any influence, who endeavors to safeguard their own legitimate interests.

6. Requirements

S.N.	Aspects	Descriptions
1.	**Understand the Entity's Related Party Relationships and Transactions**	**<u>In order to understand the auditor shall require</u> –** (a) The identity of the entity's related parties, including changes from the prior period. (b) The nature of the relationships between the entity and these related parties. (c) Whether the entity entered into any transactions with these related parties during the period. (d) The auditors shall inquire and perform other risk assessment procedures, to test internal controls, in order to – 1. Identify, account for and disclose related party relationships and transactions. 2. Authorize and approve significant transactions and arrangements with the related parties. 3. Authorize and approve significant transactions and arrangements outside the normal course of business.
2.	**Be alert for Related Party Information when reviewing**	It is a genuine possibility that the auditor may not have all the information regarding related parties made available or for may conceal the related parties transaction in such a case the auditor shall inspect the following indications for the existence of related party relationships or transactions that the management may not have

	records or documents	identified or disclosed – 1. Bank, legal and third party confirmations. 2. Minutes of meetings of shareholders and those charged with governance. 3. Other records or documents. In case the auditor identifies significant transactions outside the entity's normal course of business, he shall inquire management about – (a) The nature of the transactions. (b) Involvement of related parties.
3.	**Identification and Assessment of the risks of material misstatement associated with Related Party transactions and relationships**	Related party relationships and transactions can be both harmless as well as harmful to the truth and fairness of the transactions and the financial statements. There are sufficient cases to prove that related party transactions have been arranged to circumvent rules and regulations on the milder side, and even perpetrate deceit and fraud on the extreme side. For this purpose, the auditor shall – (a) Identify and assess the risk of material misstatement associated with related party transactions. (b) Determine whether the risks derived are significant risks. If the auditor identifies fraud risk factors, he shall identify and assess the risk of material misstatement due to fraud in accordance with SA 240.
4.	**Respond to the risks of material misstatement associated with related party relationships and transactions**	The response of the auditor to these situations is of significant importance. As a part of his response to the possibility of these misstatements, the auditor should design and perform further audit procedure, to obtain sufficient appropriate audit evidence about the assessed risks of material misstatement associated with related party relationships and transactions.
5.	**Identify previously unidentified or undisclosed related parties or significant transactions**	In case of abnormal transactions arranged either to avail benefits by avoiding taxes and other regulations or to window-dress the financial statements for various purposes, that the management may not disclose such relationships. There may be genuine mistake by management or the auditor the transactions may not have been identified. However this standard emphasizes on the **intentional concealment** of such information. If the auditor has significant related party transactions that the management has not previously identified or disclosed. The auditor shall – 1. Promptly communicate to the members of the engagement team where financial reporting framework establishes related party requirements, 2. Request management to identify all transactions with newly identified related parties. 3. Inquire as to why the controls over related party relationships and transactions were unable to identify and/or disclose the same – (a) Perform substantive procedures relating to newly identified related parties or significant related party transactions. (b) Reconsider the risk that other related parties or transactions may exist, that the management has not previously identified or disclosed to the auditor. (c) If the non-disclosure by management appears intentional, evaluate implications of the same on the audit.
6.	**Identified significant related party transactions outside the entity's normal course of**	For identified significant related party transactions outside the entity's normal course of business, the auditors shall – 1. Inspect underlying contracts or agreements and evaluate whether – a. Business rationale of transactions suggests intention of fraudulent financial reporting or concealment of misappropriation of assets. b. Terms of transactions are consistent with management's explanations

	business	c. Transactions have been appropriately accounted for and disclosed. 2. Obtain audit evidence that the transactions have been appropriately authorized and approved.
7.	**Assertions that related party transactions were conducted on terms equivalent to those prevailing in an arm's length transaction**	In case of management assertions that related party transactions are devoid of fraudulent malafide intent, the auditor shall evaluate that whether – (a) The related party transactions were conducted on terms suitable to the company. (b) The related party transactions were conducted at arms length price.
8.	**Evaluation of the accounting for and disclosure of identified related party relationships and transactions**	In forming an opinion on the financial statements, the auditor shall evaluate – (a) Whether the identified related part relationships and transactions have been appropriately accounted for and disclosed. (b) Whether the effects of the related party relationships and transactions 1. Prevent financial statements from achieving true and fair presentation, 2. Cause the financial statements to be misleading.
9.	**Written Representations**	If the financial reporting framework establishes related party requirements, the auditor shall obtain written representations from management that – (a) They have disclosed to the auditor the identity of the related parties and the related party relationships and transactions, (b) They have appropriately accounted for and disclosed such relationships and transactions.
10.	**Communication with those charged with those charged with governance**	The Auditor shall communicate with those charged with governance significant matters arising during the audit in connection with the entity's related parties.
11.	**Documentation**	**The auditor shall include in the audit documentation** – (a) The names of the identified related parties, (b) The nature of related party relationships.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	In the course of audit of Q Ltd, its statutory auditor wants to be sure of the **adequacy of related party disclosures?** Kindly guide the auditor in identifying the **possible source of related party information.**	[8 Marks] [May 2012]	**Refer Point No. 6 – S.N. (1, 2, 5, 6 & 9) on Page no. 57 & 58**
2.	How can an Auditor **identify Related Parties?**	[8 Marks] [Nov. 2002]	

Standard on Auditing (SA) 560 (REVISED)
SUBSEQUENT EVENTS

1. Effective Date

This Standard on Auditing becomes operative for all audits relating to accounting periods beginning **on or after 1st April, 2009.**

2. Scope of this SA

(SA) deals with the auditor's responsibilities relating to subsequent events in an audit of financial statements i.e. the auditor has considered the effect of the event and transactions that occur upto the date of auditor report.

3. Objectives

The objectives of the auditor are to –

(i) Obtain sufficient appropriate audit evidence of the subsequent events occurring that require adjustments or disclosure in the financial statements and

(ii) Respond appropriately to facts which may have caused the auditor to amend the report if were known at the time of reporting.

4. Definitions

(a) ***Date of the financial statements***- The last date of the financial statements.

(b) ***Date of approval of the financial statements*** – The date on which recognized authority have asserted that they have taken responsibility for those financial statements.

(c) ***Date of the auditor's report*** – The date the auditor dates the report.

(d) ***Date the financial statements are issued*** – The date on which auditor's report and the audited financial statements are made available to third parties.

5. Subsequent Events

Events occurring between the date of the financial statements and the date of the auditor's report, and facts that become known to the auditor after the date of the auditor's report.

6. Events occurring Between the Date of the Financial Statements and the Date of the Auditor's Report

The auditor shall perform audit procedures to obtain and identify sufficient appropriate audit evidence that require adjustments of or disclosure in the financial statements. The auditor shall assess the risk in determining the nature and extent of audit procedures which shall include –

(a) Obtain an understanding of whether the management has identified any subsequent event.

(b) Inquire whether any subsequent events have occurred which might affect the financial statements.

(c) The auditor must go through the minute's book and also inquire of meeting for which minutes are yet not prepared.

(d) Reading the entity's latest subsequent interim financial statements, if any.

Note → The events which require adjustments of or disclosure should be appropriately reflected in the financial statements. For this the auditor should request written representation.

7. Facts Which Become Known to the Auditor After the Date of the Auditor's Report but Before the Date the Financial Statements are Issued

Such events which may cause the auditor to amend the report the auditor shall discuss and determine whether financial statements need amendments and if so how the management is planning to address the matter in the financial statements.

1. If management amends the financial statements, the auditor shall extend the audit procedures to the date of the new amended report. When law or regulation or the financial reporting framework does not prohibit management from restricting the amendment the auditor can restrict the audit procedures to the new amended date. In such case the auditor shall –
   (a) Amend the report to include an additional date and indicate that the audit procedures are restricted to the amendments in the financial statements of the financial statements. OR
   (b) Provide a new or amended auditor's report that includes a statement in an Emphasis of Matter paragraph or Other Matter that conveys that auditor's procedures on subsequent events are restricted solely to the amendment of the financial statements.
2. In some entities, when there is need to amend financial statements but the same is not permitted by law or regulation then;
   (a) If the report is not given auditor shall modify his opinion.
   (b) If report is given but before making available to third party than auditor shall notify management to issue amended financial statement.
   (c) If the financial statements are issued without amendments the auditor shall take appropriate action to prevent reliance on his report.

8. Facts which become known to the Auditor after the Financial Statements have been issued

The auditor has no obligation to perform any audit procedures but such events which may have caused to amend report the auditor shall –

(a) Discuss and determine whether financial statements need amendments and if so, how the management is planning to address the matter in the financial statements.
(b) If management amends the financial statements, the auditor shall extend the audit procedures to the date of the new amended report and amend the report to include an additional date and indicate that the audit procedures are restricted to the amendments in the financial statements give a note of reason of amendments.
(c) If management does not amend financial statement where auditor believes they need to be amended, auditor will seek to prevent future reliance on the auditor's report. OR
(d) If the financial statements are issued without amendments the auditor shall take appropriate action to prevent reliance on his report.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	Briefly explain the **audit procedures on subsequent events?**	[4 Marks] [Nov. 2009]	**Refer Point No. 5 & 6 on Page no. 60**
2.	Briefly describe the **auditor's responsibility regarding subsequent events.**	[10 Marks] [May 2001]	**Refer Point No. 5, to 8 on Page no. 60 & 61**

Standard on Auditing (SA) 570 (REVISED)
GOING CONCERN

1. Effective Date

This Standard on Auditing becomes operative for all audits relating to accounting periods beginning **on or after 1st April, 2009.**

2. Scope of this SA

This (SA) deals with the auditor's responsibility in the audit of financial statements with respect to management's use of the going concern assumption in the preparation and presentation of the financial statements.

3. Going Concern Assumption

Under this going concern assumption entity is viewed as continuing in business for the foreseeable future for preparation of financial statements, and the assets & liabilities will be able to realize and discharge its liabilities in the normal course of business.

4. Responsibilities of Management

Going concern assumption is the fundamental principle in the preparation of the financial statements of the entity. For this the management responsibility is making a judgment of the entity's ability to continue in the uncertain future outcomes of events or conditions.

☞ **Factors relevant to management judgment are –**

(a) The degree of uncertainty associated with the outcome of the event or condition

(b) The size and complexity of the entity.

(c) The nature and condition of the business.

(d) Information available at the time of making judgment.

5. Responsibilities of the Auditor

The auditor's responsibility is to –

(a) To obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements;

(b) To conclude, based on the audit evidence obtained, whether 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; and

(c) To determine the implications for the auditor's report. Due to inherent limitations of the auditor's ability to predict future events or conditions, the absence of any reference to going concern uncertainty in an auditor's report cannot be viewed as a guarantee as to the entity's ability to continue as a going concern.

6. Risk Assessment Procedures and Related Activities

The auditor shall consider whether there are events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. In so doing, he shall –

(a) discuss the assessment with management on the significant doubt on the entity's ability to continue as going concern and whether the management has planned to address; or

(b) If not done, he shall discuss with the management on whether the events or conditions that exists will cast doubt on going concern of the entity.

Note → The 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.

7. Evaluating Management's Assessment

The auditor shall –

a. Evaluate management's assessment of the entity's ability to continue as a going concern and shall cover the same period as that used by management and in case the period is less than 12 months from the date of financial statement he should request to extend the same to atleast 12 months.

b. All relevant information should be considered of which the auditor is aware as a result of the audit.

8. Period Beyond Management's Assessment

The auditor shall inquire of events or conditions beyond the period of management's assessment that may cast significant doubt on the entity's ability to continue as a going concern.

9. Additional Audit Procedures When Events or Conditions are Identified

When events or conditions have been identified the auditor need to determine whether or not a material uncertainty exists. These additional procedures shall include –

1. Requesting management to start the assessment when the same has not been performed.
2. Evaluating management's future plans to determine whether this would improve the situations and are feasible in such circumstances.
3. While analyzing the cash flow forecast evaluating the –
   (a) Reliability of the data.
   (b) Determining adequate support for the forecast.
   (c) Considering additional information since the date of last assessment
   (d) Requesting written representation regarding future plans of actions and its feasibility.

10. Audit Conclusions and Reporting

Based on the audit evidence obtained, the auditor shall conclude whether, a material uncertainty exists related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern. Appropriate disclosure of the nature and in case of existence of material uncertainty appropriate disclosures should be made.

11. Use of Going Concern Assumption Appropriate but a Material Uncertainty exists

In this situation the auditor shall determine whether the Financial Statements –

1. Describe the principal events or condition and disclose that it may be unable to realize its assets and discharge liabilities in normal course of business.
2. In case appropriate disclosure is made the auditor shall express unmodified opinion and highlight the existence of material uncertainty by referring to the disclosures made in the financial statements **(i.e. Emphasis On Matter Para as per SA – 706)** .
3. If adequate disclosure is not made in the financial statements, the auditor shall express a qualified or adverse opinion as appropriate.
4. If use of Going Concern Assumption is inappropriate, in this case the auditor shall express an adverse opinion.
5. If management is unwilling to Make or Extend its Assessment- In this case the auditor shall consider the implication of the management unwillingness to extend or make the assessment.
6. **Communication with Those Charged with Governance-** When all those charged with governance are involved in managing the entity, the communication shall include –
   (a) Whether the events or conditions constitute a material uncertainty;

(b) Whether the use of the going concern assumption is appropriate;

(c) The adequacy of related disclosures in the financial statements.

12. Significant Delay in the Approval of Financial Statements

When there is significant delay the auditor shall inquire the reasons and perform additional audit procedures to conclude the existence of a material uncertainty in the financial statements.

13. Events or condition that may cast doubt on going concern Assumptions

☞ **Financial**

(a) Net liability or net current liability position.

(b) Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment; or excessive reliance on short-term borrowings to finance long-term assets.

(c) Indications of withdrawal of financial support by creditors.

(d) Negative operating cash flows indicated by historical or prospective financial statements. "Adverse key financial ratios.

(e) Substantial operating losses or significant deterioration in the value of assets used to generate cash flows.

(f) Arrears or discontinuance of dividends.

(g) Inability to pay creditors on due dates.

(h) Inability to comply with the terms of loan agreements.

(i) Change from credit to cash-on-delivery transactions with suppliers

(j) Inability to obtain financing for essential new product development or other essential investments.

☞ **Operating**

(a) Management intentions to liquidate the entity or to cease operation.

(b) Loss of key management without replacement.

(c) Loss of a major market, key customer (s), franchise, license, or principal supplier (s).

(d) Labour difficulties.

(e) Shortages of important supplies.

(f) Emergence of a highly successful competitor.

☞ **Other**

(a) Non- compliance with capital or other statutory requirements.

(b) 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.

(c) Changes in law or regulation or government policy expected to adversely affect the entity.

(d) Uninsured or underinsured catastrophes when they occur.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	A Company's **net worth is eroded and creditors are unpaid due to liquidity constraints.** The management represents to the statutory auditor that the **promoter's wife is expected to give an unsecured loan** to meet the liquidity constraints and that **negotiations are underway to secure large export orders.** Comment.	[4 Marks] [June 2009]	**Refer Point No. 5 & 10 on Page no. 62 & 63**
Ans.	In this case, it is subjective, but prima-facie a mere expectation of future cash flows from the promoter's wife without any firm commitment and the possibility of an export order being negotiated, may not that be sufficient appropriate audit evidence of mitigating factors for resolving the going concerns question under SA 570 "Going Concern".		
3.	R & Co. is the statutory auditor of S Ltd. For the financial year ended on 31st March 2012, S Ltd had disclosed in the notes (Note No. X) **"The state pollution control board had ordered the closure of the company's only manufacturing plant on the ground that it is environmentally damaging, which the company had challenged in a law suit.** Pending the outcome of the law suit the financial statements are prepared on a going concern basis". Further the financial statements prepared by the management of S Ltd **include financial statements of certain branches which are audited by other auditors.** What are the reporting responsibilities of R & Co?	[10 Marks] [May 2012]	**Refer Point No. 10 & 11 on Pg no. 63 Also Refer Below**
Ans.	<u>**This question involves two broad aspects with respect to reporting requirements i.e.**</u> (i) One which deals with Going Concern aspect where the company has gone for legal suit and (ii) Other is work done by other auditors. **(i) As per SA 620, "Using the Work of an Auditor's Expert",** if expertise in a field is necessary to obtain sufficient appropriate audit evidence, he may determine to use the work of an auditor's expert. On the basis of expert's opinion he may decide to rely or not on assessment of management. **(ii) Please See SA – 600 for Ans. of 2nd Part.**		
3.	While examining the going concern assumption of an entity, **what important indications should be evaluated and examined?**	[5 Marks] [Nov. 2005]	**Refer Point No. 13 on Page no. 64**

Standard on Auditing (SA) 580 (REVISED)
WRITTEN REPRESENTATIONS

1. Effective Date

This Standard on Audit becomes operative for all audits relating to accounting periods beginning **on or after 1st April, 2009.**

2. Scope of this SA

Auditor's responsibility to obtain written representation and where appropriate, those charged with governance. Written representations are the audit evidence as they provide necessary information in connection with the audit of the entity, although they do not provide sufficient appropriate audit evidence on their own about any matter which the auditor has to deal with. Also this does not affect the nature and extent of other audit evidence which the auditor needs to obtain to fulfill

3. Objective of the Standard is to -

(a) Obtain written representation from the management that the management believes that it has fulfilled the fundamental responsibilities that constitute the premise / basis on which audit is conducted.

(b) Support other audit evidence relevant to the financial statements or specific assertions in the financial statements.

(c) Respond appropriately to written representations provided by management and also if management does not provide the written representations requested by the auditor.

4. Definition

- **Written Representations** – A written statement provided by the management to the auditor to confirm certain matters or to support other audit evidence but do not include financial statements, the assertions therein, or supporting books and records. Auditor shall send request to management with appropriate responsibilities and knowledge of matters concerned.

5. Responsibility of Management

In the case of a fair presentation framework, management is responsible for the preparation and *fair* presentation of the financial statements in accordance with the applicable FRF, or the preparation of financial statements ***that give a true and fair view*** in accordance with the applicable financial reporting framework.

6. Nature of Written Representation as a Audit Evidence

(a) Audit evidence is all the information used by the auditor in arriving at the conclusions on which the audit opinion is based. Written representations are **necessary information** that the auditor requires in connection with the audit of the entity's financial statements. Accordingly, similar to responses to inquiries, written representations are audit evidence

(b) Although written representations provide necessary audit evidence, they do **not provide sufficient appropriate audit evidence** on their own about any of the matters with which they deal.

(c) The fact that management has provided reliable written representations does **not affect the nature or extent of other audit evidence** that the auditor obtains about the fulfillment of management's responsibilities, or about specific assertions.

7. Requirements

S.N.	Aspects	Descriptions
1.	**Written Representations about management's responsibilities**	a. **Preparation and Presentation of Financial Statements** – The auditor shall obtain a written representation that the management has fulfilled its responsibility for the preparation and presentation of financial statements as set out in the terms of audit engagement. b. **Information provided to auditor** – The auditor shall obtain written representation that management has provided the auditor with the relevant information and that all transactions have been recorded and are reflected in the financial statements. c. **Description of management's responsibilities** – Management's responsibilities shall be described in the representations.
2.	**Other Written Representations**	In case auditors determines that it is necessary to obtain more other written representation, as required by other SA's to support other audit evidence, he can request for such other representations also.
3.	**Date and period covered of representations**	The date of the representations shall be, as near as possible near to the date of audit report and in no case should be after the date of audit report.
4.	**Form of representations**	(a) It should be in the form of representation letter addressed to the auditor. (b) In case if any law or regulations requires management to made written public statements about its responsibilities, them such matter need be included in the representation letters.
5.	**Doubt as to reliability of written representations**	(a) If the auditor has concerns about the **competence, integrity, ethical values or diligence** of the management, or about its commitment to or enforcement or these, he shall determine the effect that such concerns may have in the reliability of representations (oral or written) and audit evidence in general. (b) If representations are **inconsistent** with other audit evidence, the auditor shall perform audit procedures to **attempt to resolve** the matter or reconsider the assessment of the management. (c) If the auditor concludes that these are **unreliable**, he shall take appropriate actions, including determining the possible effect on the opinion in the auditor's report.
6.	**Requested representations not provided**	**If the management does not provide one or more of the requested written representations, the auditor shall –** (a) Discuss with management. (b) Re-evaluate the integrity of management and evaluate the effect on reliability of the representations (oral or written). (c) Take appropriate actions and consider the effect on reports.
7.	**Representations about management's responsibilities effect on Audit Report**	**The auditor shall disclaim an opinion on the financial statements if –** (a) He concludes that there is **sufficient doubt** about the integrity of the management, and reliability of their written representations or (b) Management does **not provide** the written representations.

<table>
<tr><th colspan="4"><u>Some Past Attempts Questions</u></th></tr>
<tr><th>S.N.</th><th>Questions</th><th>Marks and Attempt</th><th>Answer</th></tr>
<tr><td>1.</td><td>In the course of audit of ABC Ltd. its management refuses to provide written representations. As an auditor what is your duty?</td><td>[4 Marks]
[May 2010]</td><td>Refer Point No. 7 – S.N. 6 & 7 on Page no. 67</td></tr>
<tr><td>2.</td><td>Explain what is meant by "Written Representations" and indicate to what extent an auditor can place reliance on such representations?</td><td>[6 Marks]
[May 2006]</td><td>Refer Point No. 5 & 6 on Page no. 66</td></tr>
<tr><td>Ans.</td><td colspan="3"><u>Conclusion</u> – It must be note that representations by the management cannot be the substitute for other audit evidence that the auditor could reasonably expected to be available. For example, a representation by the management as to existence, quantity and cost of inventories is not substitute for adopting audit procedures regarding verification and valuation of inventories.

If a representation by management is contradicted by other evidence, the auditor should examine the circumstances and, when necessary, reconsider the reliability of other representations made by the management as well.</td></tr>
<tr><td>3.</td><td>What are your views on the following?

An auditor of Sagar Ltd. was not able to get the confirmation about the existence and value of certain machineries. However, the management gave him a certificate to prove the existence and value of the machinery as appearing in the books of account. The auditor accepted the same without any further procedure and signed the audit report. Is he right in his approach?</td><td>[5 Marks]
[Nov. 2004]</td><td>Refer Point No. 5 & 6 on Page no. 66</td></tr>
<tr><td>Ans.</td><td colspan="3"><u>Conclusion</u> – If the auditor is unable to obtain sufficient appropriate audit evidence that he believes would be available regarding a matter, which has or may have a material effect on the financial information, this will constitute a limitation on the scope of his examination even if he has obtained a representation from management on the matter. Therefore, the approach adopted by the auditor is not right.</td></tr>
</table>

Standard on Auditing (SA) 600 (Revised)
USING THE WORK OF ANOTHER AUDITOR

1. Effective Date –

This Standard on Auditing becomes operative for all audits relating to accounting periods beginning **on or after 1st April, 2002**.

2. Introduction –

The auditor while relying on the work performed by others he should exercise adequate skill and care on which he relied and has no reason to believe that he should not have relied. This SA is applied to where an auditor uses the work of another auditor but does not apply to joint auditor. When the auditor concludes that the financial statement of a component is immaterial, SA would not apply. Whereas several components, individually though immaterial, together may be material for the entity as a whole, the SA would apply.

Note → When the principal auditor uses the work of another auditor, the principal auditor should determine how the work of the other auditor will affect the audit.

3. Definition –

(a) **"Principal auditor"** means the auditor with responsibility for reporting on the financial information of an entity when that financial information includes the financial information of one or more components audited by another auditor.

(b) **"Other auditor"** means an auditor, other than the principal auditor, with responsibility for reporting on the financial information of a component which is included in the financial information audited by the principal auditor.

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

4. Acceptance as Principal Auditor-

For this purpose the auditor would consider –

(a) The materiality of the portion of the financial information which he audits;
(b) His degree of knowledge regarding the business of the components;
(c) The risk of material misstatements in the financial information of the component audited by the other auditor; and
(d) The performance of additional procedures as set out in this SA regarding the components audited by other auditor resulting him having significant participation in such audit.

5. The Principal auditor's Procedures-

When planning to use the work of another auditor, the principal auditor may consider –

(a) The professional competence of the other auditor in the context of specific assignment

(b) Evaluate the work performed by another to obtain sufficient appropriate audit evidence.

(c) Advise the other auditor of the use that is to be made of his work and report.

(d) Inform the other auditor of matters such as areas requiring special consideration, procedures for the identification of inter component transactions that may require disclosure and the time-table for completion of audit;

(e) Advise the other auditor of the significant accounting, auditing and reporting requirements

(f) The nature, timing and extent of procedures which will depend on the circumstances of the engagement and the principal auditor's knowledge of the professional competence of the other auditor.

(g) The principal auditor should consider the significant findings of the other auditor.

(h) He may also decide that supplemental tests of the records or the financial statements of the component are necessary.

6. *Documentation-*

The principal auditor should document in his working papers the –

(a) The components whose financial information was audited by other auditors;

(b) Their significance to the financial information of the entity as a whole;

(c) The names of the other auditors;

(d) And any conclusions reached that individual components are not material.

(e) The principal auditor should also document the procedures performed and the conclusions reached.

7. *Co-ordination Between Auditors for this purpose-*

(a) The principal auditor may find it necessary to issue written communications (s) to the other auditor so that there is proper coordination between the two.

(b) The other auditor, knowing the context in which his work is to be used by the principal auditor, should co-ordinate with the principal auditor.

(c) The principal auditor may require the other auditor to answer a detailed questionnaire regarding matters on which the principal auditor requires information for discharging his duties.

8. *Reporting Considerations*

(a) When the principal auditor concludes, that the work of the other auditor cannot be used and he has not been able to perform sufficient additional procedures regarding the financial information of the component audited by the other auditor, he should express a qualified opinion or disclaimer of opinion because there is a limitation on the scope of audit.

(b) In all circumstances, if the other auditor issues, or intends to issue, a modified auditor's report, the principal auditor should consider whether the subject of the modification is of such nature and significance, in relation to the financial information of the entity on which the principal auditor is reporting, that it requires a modification of the principal auditor's report. **[Refer Appendix also]**

9. *Division of Responsibility*

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

(b) Information of the entity by indicating the extent to which the financial information of components audited by the other auditors have been included in the financial information of the entity, e.g., the number of divisions/branches/subsidiaries or other components audited by other auditors.

Appendix

Announcement

SA – 600 (R) – Using the work of another Auditor

Manner of Disclosure in the Auditor's Report of the Fact of Inclusion of Unaudited Financial Statements/ Information of Component/s in the Financial Statements Audited by the Principal Auditor(s)

……………………………………………………………………………………………

1. An **Independent Auditor** of the Financial Statements of an entity may, at times, need to **rely upon work of the other auditors.**

   For example, in an audit of the stand alone financial statements of an entity the Independent Auditor thereof (the Principal Auditor) may need to rely upon the Financial Statements of the entity's component/s such as branch/es, division/s, etc., which have been audited by other Independent Auditor/s.

   Similarly, in an audit of the consolidated financial statements of a group, the independent auditor thereof (the Principal Auditor), may need to rely upon the work of the independent auditors of the components of the group such as subsidiary/ies, joint venture/s, associate/s, etc., whose audited financial statements/ information have been included in the consolidated financial statements and have been audited by their respective independent auditors (the Component Auditors).

2. There may also be **a situation** where the financial statements of one or more components included in the stand alone financial statements of an entity/ consolidated financial statements of a group have **not been audited either by the Principal Auditor or the Component Auditor/s.**

3. Members have sought **guidance on the appropriate manner of disclosure of information in the independent auditor's report of the Principal Auditor about the fact** that the financial statements/ information pertaining to certain/ all components, included in the stand alone financial statements of an entity/ consolidated financial statements of a group are unaudited.

4. The **Council at its 331st meeting** held on 10th Feb., 2014 considered the above matter and decided as under –

<table>
<tr><th>S. N.</th><th>Situation</th><th>Disclosures in the Principle Auditor's Report</th></tr>
<tr><td>1.</td><td>Component/s is/are unaudited and such component/s is/are not material to the Financial Statements of the Entity/ Consolidated Financial Statements of the Group.</td><td rowspan="2">The Principal Auditor may or may not disclose the fact of such component/s in the Principal Auditor's report. In case the Principal Auditor decided to make such disclosure, the same would be done under the "Other Matters" paragraph, pursuant to SA 706, Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report. An illustrative manner of reporting is given in Ill. 2 in the Appendix of SA – 706.</td></tr>
<tr><td>2.</td><td>Component/s is/are audited by auditor/s other than the Principal Auditor and such component/s is/are not material to the Financial Statements of the entity/ Consolidated Financial Statement of the Group.</td></tr>
</table>

3.	Component/s is/are **audited** by auditor/s other than the Principal Auditor **and** such component/s **is/ are material** to the Financial Statements of the entity/ Consolidated Financial Statements of the Group	The principal auditor would **need to disclose the fact** of such component/s in the Principal Auditor's report. Such disclosure would be done under the "Other Matters" paragraph, pursuant to SA 706, ***Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report.*** An Illustrative manner of reporting is given in Illustration 2 in the Appendix to SA 706.
4.	Component/s is/are **unaudited and** such component/s **is/are material** to the Financial Statements of the entity/ Consolidated Financial Statements of the Group	The Principal Auditor **needs to consider** its/ their **impact on the auditor's opinion** on the Financial Statements of the entity/ Consolidated Financial Statements of the Group, in terms of the principles laid down in SA 705, ***Modifications to the Opinion in the Independent Auditor's Report.***

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	R & Co. is the statutory auditor of S Ltd. For the financial year ended on 31st March 2012, S Ltd had disclosed in the notes (Note No. X) **"The state pollution control board had ordered the closure of the company's only manufacturing plant on the ground that it is environmentally damaging, which the company had challenged in a law suit.** Pending the outcome of the law suit the financial statements are prepared on a going concern basis". Further the financial statements prepared by the management of S Ltd **include financial statements of certain branches which are audited by other auditors.** What are the reporting responsibilities of R & Co?	[10 Marks] [May 2012]	See Below
Ans.	<u>**This question involves two broad aspects with respect to reporting requirements i.e.**</u> **(i) One which deals with Going Concern aspect where the company has gone for legal suit and** **(ii) Other is work done by other auditors.** **(i) Please See SA – 570 for Ans. of 1st Part.** **(ii) As per Sec. 227** of the Companies Act, 1956, the auditor has to state that whether the report on the accounts of any branch office audited under section 228 by a person other than the company's auditor has been forwarded to him and how he has dealt with the same in preparing the auditor's report. Further, as per **SA 600 Using the work of Another Auditor,** When the principal auditor has to base his opinion on the financial information of the entity as a whole relying upon the statements and reports of the other auditors, his report should state clearly the division of responsibility for the financial information of the entity by indicating the extent to which the financial information of components audited by the other auditors have been included in the financial information of the entity, e.g., the number of divisions/ branches/ subsidiaries or other components audited by other auditors.		
2.	"There should be **sufficient liaison between a principal auditor and other auditors".** Discuss the above statement and state in this context the reporting considerations, when the **auditor uses the work performed by other auditor.**	[8 Marks] [Nov. 2002]	Refer Point No. 7 & 8 on Page no. 70 And also Appendix also to point no. 8 on Page no. 71 & 72

Standard on Auditing (SA) 610 (REVISED)
USING THE WORK OF INTERNAL AUDITORS

1. Effective Date

This Standard on auditing becomes operative for all audits relating to accounting periods beginning **on or after 1st April 2010**.

2. Scope

(a) This SA deals with the external auditor's (EA) responsibilities regarding the work of internal auditors (IA) when the ***external auditor has determined, in accordance with SA 315 Risk of Material Misstatement***, that the internal audit function is likely to be relevant to the audit. But it does not cover when IA is not permitted to provide access to his papers or when IA gives direct assistance to EA.

(b) ***Relationship between the Internal Audit Function and the External Auditor -*** though the objectives of the internal audit function and the external auditor are different, some of the ways in which they achieve their respective objectives may be similar. The EA has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the EAs use of the work of the IAs.

3. Objectives

The objectives of the EA, are to determine –

(a) Whether, and to what extent, to use specific work of the IA's and

(b) If so, whether such work is adequate for the purposes of the audit.

4. Definitions

(a) ***Internal audit function –*** An appraisal activity established or provided as a service to the entity. Its functions include, amongst other things, examining, evaluating and monitoring the adequacy and effectiveness of internal control.

(b) ***Internal auditors (IA) -*** Those individuals who perform the activities of the internal audit function. Internal auditors may belong to an internal audit department or equivalent function.

5. Requirements

EA has to determine whether and to What Extent to Use the Work of the IA;

1. Whether the work of the IA is likely to be ***adequate for purposes of the audit***; and
2. If so, the planned effect of the work of the ***IA on the nature, timing or extent of his procedures***.
3. To determine the adequacy of the work of IA the ***EA shall evaluate*** –
   (a) The objectivity of the internal audit function;
   (b) The technical competence of the IA;
   (c) Whether the work of the IA is likely to be carried out with due professional care; and
   (d) Whether there is likely to be effective communication between the IA and the EA.
4. In determining the ***effect of IAs work on audit procedures of EA***, he shall consider:
   (a) The nature and scope of specific work performed, or to be performed, the IA;
   (b) The assessed risks of material misstatement at the assertion level for particular classes of transactions, account balances, and disclosures; and

(c) The degree of subjectivity involved in the evaluation of the audit evidence gathered by the IA in support of the relevant assertions.

5. To determine the ***adequacy of specific work performed by the IA for the EAs purposes***, EA shall evaluate whether –

(a) The work was performed by IA having ***adequate technical training and proficiency***;

(b) The work was ***properly supervised, reviewed and documented***;

(c) ***Adequate audit evidence*** has been obtained to enable the IA's ***to draw reasonable conclusions***;

(d) Conclusions reached are appropriate in the circumstances and any reports prepared by the IA's are consistent with the results of the ***work performed; and***

(e) Any ***exception or unusual matters disclosed*** by the IA's are properly resolved.

6. Documentation

When the EA uses specific work of the IA, he shall document conclusion regarding the evaluation of the adequacy of the work of the IA, and the audit procedures performed by the EA on that work.

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	You are appointed statutory auditor of X Ltd. X Ltd. has an internal audit system and reports for the same are given to you. Mention the **factors** you will consider **to ensure** that the said **system of internal audit** of X Ltd. **is commensurate with the size of the company and nature of its business.**	[8 Marks] [June 2009]	**Refer Audit Under Co's Act, 1956 Para 4 (vii) of CARO – 2003 on Page no. 49 & 50**
2.	In the course of the statutory audit of Z Ltd, its statutory auditors, having determined that the work of internal auditor is likely to be adequate for the purpose of statutory audit, wanted to **use the work of internal auditor in respect of physical verification of fixed assets.** How an evaluation of this specific work done by the internal auditor can be done?	[5 Marks] [May 2012]	**Refer Point No. 5 Requirements – (1, 2, 3, 4 & 5) on Page no. 74 & 75**
3.	Enumerate, in brief, the important **aspects to be evaluated by the external auditor** in determining the efficiency and extent of reliance to be placed on the work and function of an Internal Auditor.	[6 Marks] [May 2005]	**Refer Point No. 5 Requirements – (1, 2, 3, 4 & 5) on Page no. 74 & 75**

Standard on Auditing (SA) 620 (Revised)
Using the Work of an Auditor's Expert

1. Effective Date –

This SA is effective for audits of financial statements for periods beginning **on or after April 1, 2010**.

2. Scope of this SA –

This Standard on Auditing (SA) deals with the auditor's responsibilities regarding the use of an individual or organisation's work in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence. This SA does not deal with –

(a) Situations where the engagement team includes a member with expertise in specialised area of accounting or auditing, which is dealt with in SA 220 (Revised) ;or

(b) The auditor's use of the work of an individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements (a management's expert), which is dealt with in SA 500 (Revised) .

3. Objectives –

The objectives of the auditor are –

(a) To determine whether to use the work of an auditor's expert; and

(b) If using the work of an auditor's expert, to determine whether that work is adequate for the auditor's purposes.

4. The Auditor's Responsibility for the Audit Opinion –

The auditor has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the auditor's use of the work of an auditor's expert. Nonetheless, if the auditor concludes that the work of that expert is adequate for the auditor's purposes, the auditor may accept that expert's findings or conclusions in the expert's field as appropriate audit evidence.

5. Definitions

(a) **Auditor's expert** – An individual or organisation possessing **expertise** in a field other than accounting or auditing, whose work in that field is used by the auditor to assist the auditor in obtaining sufficient appropriate audit evidence.

Note →An auditor's expert may be either an auditor's internal expert (who is a partner or staff, including temporary staff, of the auditor's firm or a network firm), or an auditor's external expert.

(b) **Expertise** – Skills, knowledge and experience in a particular field.

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

6. Determining the need for an auditor's expert –

If expertise in a field other than accounting or auditing is necessary to obtain sufficient appropriate audit evidence, the auditor shall determine whether to use the work of an auditor's expert.

7. The competence, capabilities and objectivity of the auditor's expert –

The auditor shall evaluate whether the auditor's expert has the necessary competence, capabilities and objectivity for the auditor's purposes.

8. Obtaining an understanding of the field of expertise of the auditor's expert –

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

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

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

9. Agreement with the Auditor's Expert –

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

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

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

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

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

10. Evaluating the Adequacy of the Auditor's Expert's Work –

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

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

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

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

(d) If the auditor determines that the work of the auditor's expert is **not adequate** for the auditor's purposes, the auditor shall –

1. Agree with that expert on the nature and extent of **further work** to be performed by **that expert**; or
2. Perform **further audit procedures** appropriate to the circumstances.

11. Nature, timing and extent of audit procedures –

The nature, timing and extent of the auditor's procedures with respect to the requirements in para 7-10 above, will vary depending on the circumstances. In determining the nature, timing and extent of those procedures, the auditor shall consider matters including –

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

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

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

12. Reference to the auditor's expert in the auditor's report

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

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

Some Past Attempts Question

S.N.	Question	Marks and Attempt	Answer
1.	Y Ltd. engaged an actuary to ascertain its employee cost, gratuity and leave encashment liabilities. As the auditor of Y Ltd., you would like to use the report of the actuary as audit evidence. How do you **evaluate the work of the actuary?**	**[8 Marks] [May 2011] & [Nov. 2002]**	**See Below, but Students can also Refer Point No. 6 to 10 on Page no. 76 & 77**

Ans.

As per SA 620 "Using the Work of an Auditor's Expert", when management has used a management's expert in preparing the financial statements, the auditor's decision on whether to use an auditor's expert may also be influenced by such factors as –

(a) The nature, scope and objectives of the management's expert's work.

(b) Whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services.

(c) The extent to which management can exercise control or influence over the work of the management's expert.

(d) The management's expert's competence and capabilities.

(e) Whether the management's expert is subject to technical performance standards or other professional or industry requirements.

(f) Any controls within the entity over the management's expert's work.

However, an evaluation of the work of an expert can be done considering the following facts –

1. When the auditor plans to use the expert's work as audit evidence, he should satisfy himself as to the expert's skills and competence by considering the expert's –
   - Professional qualifications, licence or membership in an appropriate professional body, and
   - Experience and reputation in the field in which the evidence is sought.
2. The **objectives and scope** of the experts' work.
3. A **general outline** as to specific items in the expert's report.
4. **Confidentiality** of the client's information used by the expert.
5. The **source data used**.
6. The **assumptions and methods** used and, if appropriate, their comparison with the prior period.
7. The results of the expert's work in the light of auditor's **overall knowledge of the business** and of the results of his audit procedures.
8. The auditor should also **satisfy** himself that the substance of the expert's findings **is properly reflected in the financial statements**.
9. Consider whether the expert has **used the appropriate source data**, by **making inquiries** of the expert.
10. **Conducting audit procedures** on the data by the client to the expert to obtain **reasonable assurance that the data are appropriate.**

2.	While doing audit, Ram, the Auditor requires reports from experts for the purpose of Audit evidence. What types of reports/opinions he can obtain and to what extent he can rely upon the same?	**[4 Marks]** **[Nov. 2010]**	**See Below**
Ans.	As per SA 620, "Using the Work of an Auditor's Expert", during the audit, the auditor may seek to obtain, in conjunction with the client or independently, audit evidence in the form of reports, opinions, valuations and statements of an expert. While doing audit, Ram, the auditor can obtain the following types of reports, or options or statements of an expert for the purpose of audit evidence – (a) Valuations of certain types of assets, for example, land and buildings, plant and machinery, works of art, and precious stones. (b) Determination of quantities or physical condition of assets, for example, minerals stored in stockpiles, mineral and petroleum reserves, and the remaining useful life of plant and machinery. (c) Determination of amounts using specialised techniques or methods, for example, an actuarial valuation. (d) The measurement of work completed and to be completed on contracts in progress for the purpose of revenue recognition. (e) Legal opinions concerning interpretations of agreements, statutes, regulations, notifications, circulars, etc. When the auditor intends to use the work of an expert, he should seek reasonable assurance that the expert's work constitutes appropriate audit evidence in support of the financial information, by considering the sufficiency, relevance and reliability of source data used, the assumptions and methods used and, if appropriate, their consistency with the prior period, and the results of the expert's work in the light of the auditor's overall knowledge of the business and of the results of his audit procedures.		
3.	Z Ltd. had appointed an **outside expert to assess accrued gratuity liability** of the company. Based on the said report, the company provides ₹ 80 Lakhs as gratuity in the financial statements. Comment.	**[5 Marks]** **[June 2011]**	**Same as given in 1. Or Students can Refer Below Ans. also.**
Ans.	**(a)** SA 620 states that while using the work of an expert, auditor should consider the **materiality** of the item, nature and complexity of the item, the other audit evidence available and **professional qualifications, experience and reputation in the field of the concerned expert.** (b) The auditor should ensure that the expert has used appropriate source data, has made consistent **assumptions, has applied correct methods and that results of expert's work are in line with auditor's overall knowledge of the business and match with results of his audit procedures.** (c) The auditor should also ensure that substance **of expert's findings is properly reflected in the financial information.**		

Section – III

Standard on Auditing (SA) 700 (Revised) Forming an Opinion and Reporting on Financial Statements

1. Effective Date –

This SA is effective for audits of financial statements for periods beginning on or after **April 1, 2011**.

2. Scope of this SA –

This Standard on Auditing (SA) deals with –

i. The auditor's responsibility to form an opinion on the financial statements.

ii. The form and content of the auditor's report issued as a result of an audit of financial statements.

Note → This SA is written in the context of a complete set of general purpose financial statements. This SA promotes consistency in the auditor's report which in turn helps to promote the user's understanding and to identify unusual circumstances when they occur.

3. Objectives –

The objectives of the auditor are to –

(a) Form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained; and

(b) Express clearly that opinion through a written report that also describes the basis for the opinion.

4. Definitions –

For purposes of the SAs, the following terms have the meanings attributed below –

(a) **General purpose financial statements –** Financial statements prepared in accordance with a general purpose framework. Reference to "financial statements" in this SA means "a complete set of general purpose financial statements, including the related notes" comprising a summary of significant accounting policies and other explanatory information.

(b) **General purpose framework –** A financial reporting framework designed to meet the common financial information needs of a wide range of users. The financial reporting framework may be –

- **Fair Presentation Framework** - a financial reporting framework that requires compliance with the requirements of the framework and –

  (i) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework;

  OR

  (ii) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements.

- **Compliance Framework** - a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (i) or (ii) above.

(c) **Unmodified opinion –** The opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

5. Requirements

i) **Forming an Opinion on the Financial Statements -** The auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework by obtaining reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error.

That conclusion shall take into account –

(a) Whether sufficient appropriate audit evidence has been obtained (SA 330);

(b) Whether uncorrected misstatements are material, individually or in aggregate (SA 450);

(c) Whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework.

(d) Whether in view of the requirements of the applicable financial reporting framework – **(FS Evaluation)**

- The financial statements adequately disclose the significant accounting policies selected and applied;
- The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;
- The accounting estimates made by management are reasonable;
- The information presented in the financial statements is relevant, reliable, comparable and understandable;
- The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and
- The terminology used in the financial statements, including the title of each financial statement, is appropriate.

(e) When the financial statements are **prepared in accordance** with a fair presentation framework, the evaluation required by paragraphs (c) and (d) shall also include whether the financial statements achieve fair presentation by considering – **(Fair Presentation)**

- The overall presentation, structure and content of the financial statements; and
- Whether the financial statements, including the related notes, represent the underlying transactions and events in a manner that achieves fair presentation.

(f) Whether the financial statements **adequately** refer to or describe the applicable financial reporting framework.

- ✓ A description that the financial statements are prepared in accordance with a particular applicable financial reporting framework is appropriate only if the financial statements comply with all the requirements of that framework that are effective during the period covered by the financial statements.
- ✓ In some cases, the financial statements may represent that they are prepared in accordance with two financial reporting frameworks (e.g., the national framework and International Financial Reporting Standards).
- ✓ This may be because management is required, or has chosen, to prepare the financial statements in accordance with both frameworks, in which case both are applicable financial reporting frameworks.
- ✓ Such description is appropriate only if the financial statements comply with each of the frameworks individually.
- ✓ To be regarded as being prepared in accordance with both frameworks, the financial statements need to comply with both frameworks simultaneously and without any need for reconciling statements.

ii) Form of Opinion –

S. No.	Conditions	Type of Opinion / Course of Action
1.	When the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework	Unmodified opinion

2.	**When the auditor** – (a) Concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or (b) Is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement,	Modify the opinion in auditor's report as per SA 705
3.	When financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation.	The auditor shall discuss the matter with management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, shall determine whether it is necessary to modify the opinion in the auditor's report in accordance with SA 705
4.	When the financial statements are prepared in accordance with a compliance framework.	The auditor is not required to evaluate whether the financial statements achieve fair presentation. (However, if in extremely rare circumstances the auditor concludes that such financial statements are misleading, the auditor shall discuss the matter with management and, depending on how it is resolved, shall determine whether, and how, to communicate it in the auditor's report.)

iii) Auditor's Report – [8 Marks, Nov. 2004]

- The auditor's report shall be **in writing.**
- **Title** - The auditor's report shall have a title that clearly indicates that it is the report of an independent auditor. For Eg. – **"Independent Auditor's Report"**
- **Addressee** - The auditor's report shall be addressed as required by the circumstances of the engagement. The law or regulation applicable to the entity often specifies to whom the auditor's report is to be addressed. The auditor's report is normally addressed to those for whom the report is prepared, often either to the shareholders or to those charged with governance of the entity whose financial statements are being audited.
- **Introductory Paragraph** - The introductory paragraph in the auditor's report shall –
  - (a) Identify the entity whose financial statements have been audited;
  - (b) State that the financial statements have been audited;
  - (c) Identify the title of each statement that comprises the financial statements;
  - (d) Refer to the summary of significant accounting policies and other explanatory information; and
  - (e) Specify the date or period covered by each financial statement comprising the financial statements.

Note → When the auditor is aware that the audited financial statements will be included in a document that **contains other information**, such as an annual report, the auditor may consider, if the form of presentation allows, **identifying the page numbers on which the audited financial statements are presented.** This helps users to identify the financial statements to which the auditor's report relates.

- **Management's Responsibility for the Financial Statements** - This section of the auditor's report describes the responsibilities of those in the organisation that are responsible for the preparation of the financial statements. The auditor's report need not refer specifically to "management", but shall use the term that is appropriate in the context of the legal and/or regulatory framework applicable to the entity. In case of some entities, the appropriate reference may be to those charged with governance. The auditor's report shall describe management's responsibility for the preparation of the financial statements in the manner in which that responsibility is described in the terms of the audit engagement.

Where the financial statements are prepared in accordance with a fair presentation framework, the explanation of management's responsibility for the financial statements in the auditor's report shall refer to "the preparation and fair presentation of these financial statements" or "the preparation of financial statements that give a true and fair view", as appropriate in the circumstances.

- **Auditor's Responsibility** –

1. **Responsibility** – The auditor's report shall include a section with the heading "Auditor's Responsibility" stating that the **responsibility** of the auditor is **to express an opinion** on the financial statements based on the audit.

2. **Compliance with SA –** The auditor's report shall state that the audit was **conducted in accordance with Standards on Auditing** issued by the Institute of Chartered Accountants of India.

3. **Compliance with Ethics –** The auditor's report shall also explain that those Standards require that the auditor **comply with ethical requirements** and that the auditor plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

4. **Description of Audit –** The auditor's report shall describe an audit by stating that –

   (a) An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements;

   (b) The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. In circumstances when the auditor also has a responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the financial statements, the auditor shall omit the phrase that the auditor's consideration of internal control is not for the purpose of expressing an opinion on the effectiveness of internal control; and

   (c) An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made by management, as well as the overall presentation of the financial statements.

5. **Fair Presentation –** Where the financial statements are prepared in accordance with a fair presentation framework, the description of the audit in the auditor's report shall refer to "the entity's preparation and fair presentation of the financial statements" or "the entity's preparation of financial statements that give a true and fair view", as appropriate in the circumstances.

6. **Audit Evidence –** The auditor's report shall state whether the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's opinion.

- **Auditor's Opinion -** The auditor's report shall include a section with the heading "Opinion". When expressing an unmodified opinion on financial statements prepared in accordance with a fair presentation framework, the auditor's opinion shall, unless otherwise required by law or regulation, use one of the following phrases, which are regarded as being equivalent –

(a) The financial statements present fairly, in all material respects, in accordance with [the applicable financial reporting framework]; or

(b) The financial statements give a true and fair view of in accordance with [the applicable financial reporting framework].

- ✓ When expressing an unmodified opinion on financial statements prepared in accordance with a compliance framework, the auditor's opinion shall be that the financial statements are prepared, in all material respects, in accordance with [the applicable financial reporting framework].
- ✓ **Identification of applicable FRF –** If the reference to the applicable financial reporting framework, in the auditor's opinion, is not to the Accounting Standards promulgated by the Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India (ICAI) or Accounting Standards, notified by the Central Government by publishing the same as the Companies (Accounting Standards) Rules, 2006, or the Accounting Standards for Local Bodies promulgated by the Committee on Accounting Standards for Local Bodies (CASLB) of the Institute of Chartered Accountants of India, as may be applicable, the auditor's opinion shall identify the jurisdiction of origin of the framework.
- ✓ SA 210 (Revised) explains that, in some cases, law or regulation prescribes the wording of the auditor's report (which in particular includes the auditor's opinion) in terms that are significantly different from the requirements of SAs. In these circumstances, SA 210 (Revised) requires the auditor to evaluate –
  - (a) Whether users might misunderstand the assurance obtained from the audit of the financial statements and, if so,
  - (b) Whether additional explanation in the auditor's report can mitigate possible misunderstanding.
- ✓ If the auditor concludes that additional explanation in the auditor's report cannot mitigate possible misunderstanding, SA 210 (Revised) requires the auditor not to accept the audit engagement, unless required by law or regulation to do so.
- ✓ In accordance with SA 210 (Revised), an audit conducted in accordance with such law or regulation does not comply with SAs. Accordingly, the auditor does not include any reference in the auditor's report to the audit having been conducted in accordance with Standards on Auditing, "Present fairly, in all material respects" or "give a true and fair view"

- **Other Reporting Responsibilities -** If the auditor addresses other reporting responsibilities in the auditor's report on the financial statements that are in addition to the auditor's responsibility under the SAs to report on the financial statements, these other reporting responsibilities shall be addressed in a separate section in the auditor's report that shall be sub-titled "Report on Other Legal and Regulatory Requirements," or otherwise as appropriate to the content of the section. In case of some entities, the auditor may have additional responsibilities to report on other matters that are supplementary to the auditor's responsibility under the SAs to report on the financial statements. In some cases, the relevant law or regulation may require or permit the auditor to report on these other responsibilities within the auditor's report on the financial statements. In other cases, the auditor may be required or permitted to report on them in a separate report. If the auditor's report contains a separate section on other reporting responsibilities, the headings, statements and explanations referred to in aforesaid paragraphs shall be under the sub-title "Report on the Financial Statements." The "Report on Other Legal and Regulatory Requirements" shall follow the "Report on the Financial Statements."
- **Signature of the Auditor -** The auditor's report shall be signed by the auditor in his personal name along with his membership no. allotted by ICAI. Where the firm is appointed as the auditor, the report is signed in the personal name of the auditor and in the name of the audit firm.
- **Date of the Auditor's Report -** The auditor's report shall be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements, including evidence that –
  - (a) All the statements that comprise the financial statements, including the related notes, have been prepared; and
  - (b) Those with the recognised authority have asserted that they have taken responsibility for those financial statements.

  The date of the auditor's report informs the user of the auditor's report that the auditor has considered the effect of events and transactions of which the auditor became aware and that occurred up to that date.
- **Place of Signature -** The auditor's report shall name specific location, which is ordinarily the city where the audit report is signed.

iv) Auditor's Report Prescribed by Law or Regulation - If the auditor is required by any law or regulation to use a specific layout or wording of the auditor's report, the auditor's report shall refer to Standards on Auditing only if the auditor's report includes, at a minimum, each of the following elements –

(a) A title;

(b) An addressee, as required by the circumstances of the engagement;

(c) An introductory paragraph that identifies the financial statements audited;

(d) A description of the responsibility of management (or other appropriate term) for the preparation of the financial statements;

(e) A description of the auditor's responsibility to express an opinion on the financial statements and the scope of the audit, that includes –

- ✓ A reference to Standards on Auditing and the law or regulation; and
- ✓ A description of an audit in accordance with those Standards;

(f) An opinion paragraph containing an expression of opinion on the financial statements and a reference to the applicable financial reporting framework used to prepare the financial statements (including identifying the jurisdiction of origin of the financial reporting framework ;)

(g) The auditor's signature;

(h) The date of the auditor's report; and

(i) The place of signature.

v) Auditor's Report for Audits Conducted in Accordance with Both Auditing Standards issued by the Institute of Chartered Accountants of India and International Standards on Auditing –

- **Situation –** An auditor may be required to conduct an audit in accordance with the auditing Standards issued by the Institute of Chartered Accountants of India (the "national auditing standards"), but may additionally have complied with the International Standards on Auditing (ISAs) in the conduct of the audit. If this is the case, the auditor's report may refer to International Standards on Auditing in addition to the national auditing standards, but the auditor shall do so only if –

(a) There is **no conflict** between the requirements in the national auditing standards and those in ISAs that would lead the auditor –

(i) To form a different opinion, or

(ii) Not to include an Emphasis of Matter paragraph that, in the particular circumstances, is required by ISAs; and

(b) The auditor's report includes, at a minimum, each of the elements set out in paragraph – (iv) points (a)-(i) when the auditor uses the layout or wording specified by the national auditing standards.

(c) When the auditor's report refers to both the national auditing standards and International Standards on Auditing, the auditor's report shall identify the national auditing standards being the Standards on Auditing issued by the Institute of Chartered Accountants of India.

vi) Supplementary Information Presented with the Financial Statements –

- **Need –** If supplementary information that is not required by the applicable financial reporting framework is presented with the audited financial statements, (e.g. to enhance a User's understanding of applicable FRF).

- **Auditor's Duties –**

(a) The auditor shall evaluate whether such supplementary information is clearly differentiated from the audited financial statements.

(b) If such supplementary information is not clearly differentiated from the audited financial statements, the auditor shall ask management to change how the unaudited supplementary information is presented. This can be done by –

- ✓ **Removing any cross references** from the financial statements to unaudited supplementary schedules or unaudited notes so that the demarcation between the audited and unaudited information is sufficiently clear.

- ✓ **Placing the unaudited supplementary information outside of the financial statements** or, if that is not possible in the circumstances, at a minimum, place the unaudited notes together at the end of the required notes to the financial statements and clearly label them as unaudited. Unaudited notes that are intermingled (combine) with the audited notes can be misinterpreted as being audited.

(c) If management refuses to do so, the auditor shall **explain in the auditor's report** that such supplementary information has **not been audited.** The **fact that** supplementary information is **unaudited does not relieve the auditor of the responsibility** to read that information to identify material inconsistencies with the audited financial statements. The auditor's responsibilities with respect to unaudited supplementary information are consistent with those described in SA 720.

(d) Supplementary information that is not required by the applicable financial reporting framework but is nevertheless an integral part of the financial statements because it cannot be clearly differentiated from the audited financial statements due to its nature and how it is presented shall **be covered by the auditor's opinion.**

(e) Supplementary information that is covered by the auditor's opinion does not need to be specifically referred to in the introductory paragraph of the auditor's report when the reference to the notes in the description of the statements that comprise the financial statements in the introductory paragraph is sufficient.

....

Appendix

Auditor Report Format

Illustration 1 – Circumstances include the following –

- Audit of a complete set of separate general purpose financial statements of a company prepared under the Companies Act, 1956 financial reporting framework, which is a fair presentation framework.
- The terms of the audit engagement reflect description of management's responsibility for the financial statements in SA 210 (Revised).
- The report is unmodified and does not include either an Emphasis of Matter paragraph or an Other Matter(s) paragraph.
- In addition to the audit of financial statements, the auditor has other reporting responsibilities required under the Companies Act, 1956 and/or other regulatory requirements.

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Financial Statements

We have audited the accompanying financial statements of ABC Company Limited ("the Company"), which comprise the Balance Sheet as at March 31, 20XX, and the Statement of Profit and Loss and Cash Flow Statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation of these financial statements that give a true and fair view of the financial position, financial performance and cash flows of the Company in accordance with the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act"). This responsibility includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of the financial statements that give a true and fair view and are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, **but not**

for the purpose of expression an opinion on the effectiveness of the Companies internal control (Newly Interested Line). An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of the accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion and to the best of our information and according to the explanations given to us, the financial statements give the information required by the Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India –

(a) In the case of the Balance Sheet, of the state of affairs of the Company as at March 31, 20XX;

(b) In the case of the Profit and Loss Account, of the profit/ loss for the year ended on that date; and

(c) In the case of the Cash Flow Statement, of the cash flows for the year ended on that date.

Report on Other Legal and Regulatory Requirements –

1. As required by the Companies (Auditor's Report) Order, 2003 ("the Order") issued by the Central Government of India in terms of sub-section (4A) of section 227 of the Act, we give in the Annexure a statement on the matters specified in paragraphs 4 and 5 of the Order.
2. As required by section 227(3) of the Act, we report that –
   (a) We have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purpose of our audit;
   (b) In our opinion proper books of account as required by law have been kept by the Company so far as appears from our examination of those books [and proper returns adequate for the purposes of our audit have been received from branches not visited by us];
   (c) The Balance Sheet, Statement of Profit and Loss, and Cash Flow Statement dealt with by this Report are in agreement with the books of account [and with the returns received from branches not visited by us];
   (d) In our opinion, the Balance Sheet, Statement of Profit and Loss, and Cash Flow Statement comply with the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956;
   (e) On the basis of written representations received from the directors as on March 31, 20XX, and taken on record by the Board of Directors, none of the directors is disqualified as on March 31, 20XX, from being appointed as a director in terms of clause (g) of sub-section (1) of section 274 of the Companies Act, 1956.
   (f) Since the Central Government has not issued any notification as to the rate at which the cess is to be paid under section 441A of the Companies Act, 1956 nor has it issued any Rules under the said section, prescribing the manner in which such cess is to be paid, no cess is due and payable by the Company.

For XYZ and Co.

Chartered Accountants

Place of Signature **Firm's Registration Number**

Signature

Date **(Name of the Member Signing the Audit Report)**

(Designation)

Membership Number

Standard on Auditing (SA) 705
Modifications to the Opinion in the Independent Auditor's Report

1. Effective Date

This SA is effective for audits of financial statements for periods beginning on or after **April 1, 2011**.

2. Scope of this SA

This Standard on Auditing (SA) deals with the auditor's responsibility to issue an appropriate report in circumstances when, in forming an opinion in accordance with SA 700 (Revised), the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary.

3. Types of Modified Opinions

This SA establishes three types of modified opinions, namely, a qualified opinion, an adverse opinion, and a disclaimer of opinion. The decision regarding which type of modified opinion is appropriate depends upon:

(a) The nature of the matter giving rise to the modification, that is, whether the financial statements are materially misstated or, in the case of an inability to obtain sufficient appropriate audit evidence, may be materially misstated; and

(b) The auditor's judgment about the pervasiveness of the effects or possible effects of the matter on the financial statements.

4. Objective

The objective of the auditor is to express clearly an appropriately modified opinion on the financial statements that are necessary when –

(a) The auditor concludes based on the audit evidence obtained, that the financial statements as a whole are not free from material misstatement; or

(b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

5. Definitions

For purposes of the SAs, the following terms have the meanings attributed below –

(a) Pervasive –

- A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence.
- Pervasive effects on the financial statements are those that, in the auditor's judgment –
  1. Are **not confined to specific elements**, accounts or items of the financial statements;
  2. If so confined, represent or could represent a **substantial proportion** of the financial statements; o
  3. In relation to disclosures, are **fundamental** to users' understanding of the financial statements.

(b) Modified opinion – A qualified opinion, an adverse opinion or a disclaimer of opinion.

6. Requirements

i) Circumstances When a Modification to the Auditor's Opinion Is Required –

The auditor shall modify the opinion in the auditor's report when –

(a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or

(b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

Note → SA 450 defines a misstatement as a difference between the amounts, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework.

Accordingly, a material misstatement of the financial statements may arise in relation to –

(a) The appropriateness and application of the selected accounting policies; or

(b) The appropriateness or adequacy of disclosures in the financial statements.

Note → The auditor's **inability to obtain sufficient appropriate audit evidence** (also referred to as a limitation on the scope of the audit) may arise from –

(a) Circumstances **beyond the control** of the entity;
(b) Circumstances relating to **the nature or timing of the auditor's work**; or
(c) **Limitations imposed by management.**

ii) Determining the Type of Modification to the Auditor's Opinion –

Nature of Matter Giving Rise to the Modification	Auditor's Judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements	
	Material but Not Pervasive	**Material and Pervasive**
Financial statements are materially misstated	**Qualified opinion**	**Adverse opinion**
Inability to obtain sufficient appropriate audit evidence	**Qualified opinion**	**Disclaimer of opinion**

- **Qualified Opinion** - The auditor shall express a qualified opinion when:
  1. The auditor, having obtained sufficient appropriate audit evidence, concludes that **misstatements**, individually or in the aggregate, **are material, but not pervasiv**e, to the financial statements; or
  2. The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.
- **Adverse Opinion** - The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that **misstatements**, individually or in the aggregate, are **both material and pervasive** to the financial statements.
- **Disclaimer of Opinion** –

  (a) The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, **could be both material and pervasive.**

  (b) The auditor shall disclaim an opinion when, in extremely rare circumstances involving **multiple uncertainties**, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is **not possible** to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.

iii) Consequence of an Inability to Obtain Sufficient Appropriate Audit Evidence Due to a Management-Imposed Limitation after the Auditor Has Accepted the Engagement –

(a) If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall **request** that management **remove the limitation.**

(b) If management refuses to remove such limitation, the auditor shall **communicate** the matter to those charged with governance and determine whether it is possible to perform **alternative procedures** to obtain sufficient appropriate audit evidence.

(c) If the auditor is **unable to obtain sufficient appropriate audit evidence**, the auditor shall determine the implications as follows –

1. If the auditor concludes that the **possible effects** on the financial statements of undetected misstatements, if any, **could be material but not pervasive**, the auditor shall **qualify** the opinion; or
2. If the auditor concludes that the **possible effects** on the financial statements of undetected misstatements, if any, **could be both material and pervasive** so that a **qualification** of the opinion would be **inadequate** to communicate the gravity of the situation, the auditor shall –
   (i) **Resign** from the audit, where practicable and not prohibited by law or regulation (If the auditor so resigns, he shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion); or
   (ii) If resignation from the audit before issuing the auditor's report is not practicable or possible, **disclaim an opinion** on the financial statements.

iv) Other Considerations Relating to an Adverse Opinion or Disclaimer of Opinion –

Unmodified Opinion on Single FS/Specific Items not Possible –

- When the auditor considers it necessary to express an adverse opinion or disclaim an opinion on the financial statements as a whole, the auditor's report shall not also include an unmodified opinion with respect to the same financial reporting framework on a single financial statement or one or more specific elements, accounts or items of a financial statement.
- To include such an unmodified opinion in the same report in these circumstances would contradict the auditor's adverse opinion or disclaimer of opinion on the financial statements as a whole.

v) Form and Content of the Auditor's Report When the Opinion Is Modified

1. ***Basis for Modification Paragraph*** **–** When the auditor modifies the opinion on the financial statements, the auditor shall, in addition to the specific elements required by the SA 700 (Revised), include a paragraph in the auditor's report that provides a description of the matter giving rise to the modification.
2. ***Placement & Heading*** **–** The auditor shall place this paragraph immediately before the opinion paragraph in the auditor's report and use the heading "Basis for Qualified Opinion", "Basis for Adverse Opinion", or "Basis for Disclaimer of Opinion", as appropriate.
3. ***Quantification*** **–**
   (a) If there is a material misstatement of the financial statements that relates to specific amounts in the financial statements (including quantitative disclosures), the auditor shall include in the basis for modification paragraph a description and quantification of the financial effects of the misstatement, unless impracticable.
   (b) If it is not practicable to quantify the financial effects, the auditor shall so state in the basis for modification paragraph.
4. **Narrative Disclosure –** If there is a material misstatement of the financial statements that relates to narrative disclosures, the auditor shall include in the basis for modification paragraph an explanation of how the disclosures are misstated.
5. **Non – Disclosure of Information –** If there is a material misstatement of the financial statements that relates to the non- disclosure of information required to be disclosed, the auditor shall –
   (a) Discuss the non-disclosure with those charged with governance;
   (b) Describe in the basis for modification paragraph the nature of the omitted information; and

(c) Unless prohibited by law or regulation, include the omitted disclosures, provided it is practicable to do so and the auditor has obtained sufficient appropriate audit evidence about the omitted information.

6. **Inability to obtain evidence** – If the modification results from an inability to obtain sufficient appropriate audit evidence, the auditor shall include in the basis for modification paragraph, the reasons for that inability.

7. **In case of Adverse Opinion/ Disclaimer** – Even if the auditor has expressed an adverse opinion or disclaimed an opinion on the financial statements, the auditor shall describe in the basis for modification paragraph the reasons for any other matters of which the auditor is aware that would have required a modification to the opinion, and the effects thereof.

vi) Form and Content of Opinion Paragraph, in case of Modification

1. **Heading** – When the auditor modifies the audit opinion, the auditor shall use the heading "Qualified Opinion", "Adverse Opinion", or "Disclaimer of Opinion", as appropriate, for the opinion paragraph.

2. **Qualified Opinion – Form and Contents** – When the auditor expresses a qualified opinion due to a material misstatement in the financial statements, the auditor shall state in the opinion paragraph that, in the auditor's opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion paragraph –

   (a) The financial statements present fairly, in all material respects (or give a true and fair view) in accordance with the applicable financial reporting framework when reporting in accordance with a fair presentation framework; or

   (b) The financial statements have been prepared, in all material respects, in accordance with the applicable financial reporting framework when reporting in accordance with a compliance framework.

   Note → **When the modification arises from an inability to obtain sufficient appropriate audit evidence, the auditor shall use the corresponding phrase "except for the possible effects of the matter(s)..." for the modified opinion. When the auditor expresses a qualified opinion, it would not be appropriate to use phrases such as "with the foregoing explanation" or "subject to" in the opinion paragraph as these are not sufficiently clear or forceful.**

3. **Adverse Opinion – Form and Content** – When the auditor expresses an adverse opinion, the auditor shall state in the opinion paragraph that, in the auditor's opinion, because of the significance of the matter(s) described in the Basis for Adverse Opinion paragraph –

   (a) The financial statements do not present fairly (or give a true and fair view) in accordance with the applicable financial reporting framework when reporting in accordance with a fair presentation framework; or

   (b) The financial statements have not been prepared, in all material respects, in accordance with the applicable financial reporting framework when reporting in accordance with a compliance framework.

4. **Disclaimer of Opinion – Form and Content** – When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall state in the opinion paragraph that –

   (a) Because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion paragraph, the auditor has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion; and, accordingly,

   (b) The auditor does not express an opinion on the financial statements.

vii) Description of Auditor's Responsibility–

(a) **When the Auditor Expresses a Qualified or Adverse Opinion** When the auditor expresses a qualified or adverse opinion, the auditor shall amend the description of the auditor's responsibility to state that the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's modified audit opinion.

(b) **When the Auditor Disclaims an Opinion –**

- When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall amend the introductory paragraph of the auditor's report to state that the auditor was engaged to audit the financial statements.
- The auditor shall also amend the description of the auditor's responsibility and the description of the scope of the audit to state only the following –

  "Our responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with Standards on Auditing issued by the Institute of Chartered Accountants of India. Because of the matter(s) described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion".

viii) Communication with Those Charged with Governance –

When the auditor expects to modify the opinion in the auditor's report, the auditor shall communicate with those charged with governance the circumstances that led to the expected modification and the proposed wording of the modification, in order to enable –

(a) The auditor to give notice to those charged with governance of the intended modification(s) and the reasons (or circumstances) for the modification(s);
(b) The auditor to seek the concurrence of those charged with governance regarding the facts of the matter(s) giving rise to the expected modification(s), or to confirm matters of disagreement with management as such; and
(c) Those charged with governance to have an opportunity, where appropriate, to provide the auditor with further information and explanations in respect of the matter(s) giving rise to the expected modification(s).

....

Appendix
Qualified Report

Illustration 1 – Circumstances for Qualified Report include the following –

- Audit of a complete set of separate general purpose financial statements of a company prepared under the Companies Act, 1956 financial reporting framework.
- The terms of the audit engagement reflect description of management's responsibility for the financial statements in SA 210 (Revised).
- Inventories are misstated. The misstatement is deemed to be material but not pervasive to the financial statements. The audit opinion is qualified for the misstatement.
- In addition to the audit of financial statements, the auditor has other reporting responsibilities required under the Companies Act, 1956 and/or other regulatory requirements.

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Financial Statements

We have .... summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible .... free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express................. basis for our audit opinion.

Basis for Qualified Opinion

The Company's inventories are carried in the Balance Sheet at ₹ XXX. Management has not stated the inventories at the lower of cost and net realisable value but has stated them solely at cost, which constitutes a departure from the Accounting Standards referred to in sub-section (3C) of section 211 of the Act. The Company's records indicate that had management stated the inventories at the lower of cost and net realisable value, an amount of ₹ XXX would have been required to write the inventories down to their net realisable value. Accordingly, cost of sales would have been increased by ₹ XXX, and income tax, net profit and shareholders' funds would have been reduced by ₹ XXX, Rs. XXX and ₹ XXX, respectively.

Qualified Opinion

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 paragraph,, the financial statements give the information required by the Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India –

(d) In the case of the Balance Sheet, of the state of affairs of the Company as at March 31, 20XX;
(e) In the case of the Profit and Loss Account, of the profit/ loss for the year ended on that date; and
(f) In the case of the Cash Flow Statement, of the cash flows for the year ended on that date.

Report on Other Legal and Regulatory Requirements –

3. As required by .... paragraphs 4 and 5 of the Order.
4. As required by section 227(3) of the Act, we report that –
   (g) We have obtained .... our audit;
   (h) In our opinion .... not visited by us];
   (i) The Balance Sheet, ... visited by us];
   (j) Except for the effects of the matter described in the Basis for Qualified Opinion paragraph, in our opinion, the Balance Sheet, Statement of Profit and Loss and Cash Flow Statement comply with the accounting standards referred to in sub-section (3C) of section 211 of the Act;
   (k) On the basis .... 274 of the Companies Act, 1956.
   (l) Since the .... due and payable by the Company.

For XYZ and Co.
Chartered Accountants

Place of Signature **Firm's Registration Number**

Signature

Date **(Name of the Member Signing the Audit Report)**
(Designation)

Membership Number

Adverse Report

Illustration 2 – Circumstances for Adverse Report include the following –

- Audit of a complete set of consolidated general purpose financial statements of a parent company prepared under accounting principles generally accepted in India (as required for compliance with SEBI's regulatory requirement).
- The terms of the group audit engagement reflect description of management's responsibility for the financial statements in SA 210 (Revised).
- The financial statements are materially misstated due to the non-consolidation of a subsidiary. The material misstatement is deemed to be pervasive to the financial statements. The effects of the misstatement on the financial statements have not been determined because it was not practicable to do so. An adverse audit opinion is given under the circumstances.

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Financial Statements
We have .... summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements
Management is responsible .... free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express................ basis for our audit opinion.

Basis for Adverse Opinion
As explained in Note X, the Company has not consolidated the financial statements of subsidiary ABC Company it acquired during 20XX because it has not yet been able to ascertain the fair values of certain of the subsidiary's material assets and liabilities at the acquisition date. This acquisition is therefore accounted for as an investment. Under the accounting principles generally accepted in India, the subsidiary should have been consolidated because it is controlled by the Company. Had ABC been consolidated, many elements in the accompanying financial statements would have been materially affected. The effects on the financial statements of the failure to consolidate have not been determined.

Adverse Opinion
In our opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion paragraph, the Consolidated financial statements do not give a true and fair view in conformity with the accounting principles generally accepted in India –

(a) In the case of the Balance Sheet, of the state of affairs of the Company as at March 31, 20XX;
(b) In the case of the Profit and Loss Account, of the profit/ loss for the year ended on that date; and
(c) In the case of the Cash Flow Statement, of the cash flows for the year ended on that date.

Report on Other Legal and Regulatory Requirements –

1. As required by .... paragraphs 4 and 5 of the Order.

2. As required by section 227(3) of the Act, we report that –
   (a) We have obtained .... our audit;
   (b) In our opinion .... not visited by us];
   (c) The Balance Sheet, ... visited by us];
   (d) Except for the effects of the matter described in the Basis for Qualified Opinion paragraph, in our opinion, the Balance Sheet, Statement of Profit and Loss and Cash Flow Statement comply with the accounting standards referred to in sub-section (3C) of section 211 of the Act;
   (e) On the basis .... 274 of the Companies Act, 1956.
   (f) Since the .... due and payable by the Company.

For XYZ and Co.

Chartered Accountants

Place of Signature **Firm's Registration Number**

Signature

Date **(Name of the Member Signing the Audit Report)**

(Designation)

Membership Number

....

Disclaimer of Opinion for Single Element of the FS

Illustration 3 – Circumstances for Disclaimer of Opinion include the following –

- Audit of a complete set of separate general purpose financial statements of a company prepared under the Companies Act, 1956 financial reporting framework.
- The terms of the audit engagement reflect description of management's responsibility for the financial statements in SA 210 (Revised).
- The auditor was unable to obtain sufficient appropriate audit evidence about a single element of the financial statements. That is, the auditor was unable to obtain audit evidence about the financial information of a joint venture investment that represents over 90% of the Company's net assets. The possible effects of this inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the financial statements. A disclaimer of audit opinion is given in the circumstances.
- In addition to the audit of financial statements, the auditor has other reporting responsibilities required under the Companies Act, 1956 and/or other regulatory requirements.

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Financial Statements
We have .... summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements
Management is responsible .... free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Because of the matter described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for Disclaimer of Opinion
The Company's investment in its joint venture ABC Company is carried at ₹ XXX in the Company's Balance Sheet, which represents over 90% of the Company's net assets as at March 31, 20XX. We were not allowed access to the management and the auditors of ABC Company. As a result, we were unable to determine whether any adjustments were necessary in respect of the Company's proportional share of ABC Company's assets that it controls jointly, its proportional share of ABC Company's liabilities for which it is jointly responsible, its proportional share of ABC Company's income and expenses for the year, and the elements making up the Cash Flow Statement.

Disclaimer of Opinion
Because of the significance of the matter described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statements.

Report on Other Legal and Regulatory Requirements –

1. As required .... paragraphs 4 and 5 of the Order.
2. As required by section 227(3) of the Companies Act, 1956, we report that –
   (a) As described in the Basis for Disclaimer of Opinion paragraph, we were unable to obtain all the information and explanations which to the best of our knowledge and belief were necessary for the purpose of our audit;
   (b) Due to the possible effect of the matter described in the Basis for Disclaimer of Opinion paragraph, we are unable to state whether proper books of account as required by law have been kept by the Company so far as appears from our examination of those books [and proper returns adequate for the purposes of our audit have been received from branches not visited by us];
   (c) The Balance Sheet, ... not visited by us];
   (d) Due to the possible effects of the matter described in the Basis for Disclaimer of Opinion paragraph, we are unable to state whether the Balance Sheet, Statement of Profit and Loss and Cash Flow Statement comply with the accounting standards referred to in sub-section (3C) of section 211 of the Act;
   (e) On the basis........... Section 274 of the Act.
   (f) Since the............. no cess is due and payable by the Company.

For XYZ and Co.
Chartered Accountants
Firm's Registration Number

Place of Signature

Signature

Date

(Name of the Member Signing the Audit Report)
(Designation)
Membership Number

Disclaimer of Opinion for Multi Element of the FS

Illustration 4 – Circumstances for Disclaimer of Opinion include the following –

- Audit of a complete set of separate general purpose financial statements of a company prepared under the Companies Act, 1956 financial reporting framework.
- The terms of the audit engagement reflect description of management's responsibility for the financial statements in SA 210 (Revised).
- The auditor was unable to obtain sufficient appropriate audit evidence about multiple elements of the financial statements. That is, the auditor was unable to obtain audit evidence about the entity's inventories and accounts receivable. The possible effects of this inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the financial statements. A disclaimer of audit opinion is given in the circumstances.
- In addition to the audit of financial statements, the auditor has other reporting responsibilities required under the Companies Act, 1956 and/or other regulatory requirements.

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Financial Statements – **See Illustration 1 above**

Management's Responsibility for the Financial Statements – **See Illustration 1 above**

Auditor's Responsibility – **See Illustration 3 above**

Basis for Disclaimer of Opinion

We were appointed as auditors of the Company after March 31, 20XX and thus could not observe the counting of physical inventories at the beginning and end of the year. Accordingly, we were unable to satisfy ourselves by alternative means concerning the inventory quantities held at December 31, 20X0 and March 31, 20X1 which are stated in the Balance Sheet at ₹ XXX and ₹ XXX, respectively.

In addition, the introduction of a new computerised accounts receivable system in September 20X1 resulted in numerous errors in accounts receivable. As of the date of our audit 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 ₹ 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 Profit and Loss and Cash Flow Statement.

Disclaimer of Opinion

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statements.

Report on Other Legal and Regulatory Requirements – **See Illustration 4 above**

For XYZ and Co.
Chartered Accountants
Place of Signature **Firm's Registration Number**

Signature

Date **(Name of the Member Signing the Audit Report)**
(Designation)
Membership Number

Standard on Auditing (SA) 706
Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report

1. Effective Date

This SA is effective for audits of financial statements for periods beginning on or after **April 1, 2011.**

2. Scope of this SA/ Objectives of the Auditor

This Standard on Auditing (SA) deals with additional communication in the auditor's report when the auditor considers it necessary to draw users' attention

- To any matter presented or disclosed in the financial statements which may be **fundamental** to users' understanding of the financial statements;
- or any matter or matters other than those presented or disclosed in the financial statements that are **relevant** to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

3. Definitions

For the purposes of the SAs, the following terms have the meanings attributed below –

(a) **Emphasis of Matter paragraph** – A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements.

(b) **Other Matter paragraph** – A paragraph included in the auditor's report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

4. Requirements

i) Emphasis of Matter Paragraphs in the Auditor's Report –

- **Meaning –** If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is **fundamental** to user's understanding of the financial statements, the auditor shall include an Emphasis of Matter paragraph in the auditor's report provided the auditor has obtained sufficient appropriate audit evidence that the matter is **not** materially misstated in the financial statements. Such a paragraph shall refer **only** to information presented or disclosed in the financial statements.

ii) When the auditor includes an Emphasis of Matter paragraph in the auditor's report, the auditor shall–

(a) Include it immediately after the Opinion paragraph in the auditor's report;

(b) Use the heading "Emphasis of Matter", or other appropriate heading;

(c) Include in the paragraph a clear reference to the matter being emphasised and to where relevant disclosures that fully describe the matter can be found in the financial statements; and

(d) Indicate that the auditor's opinion is not modified in respect of the matter emphasised.

iii) The inclusion of an Emphasis of Matter paragraph in the auditor's report *does not affect* the auditor's opinion. An Emphasis of Matter paragraph is *not* a substitute for either –

(a) The auditor expressing a qualified opinion or an adverse opinion, or disclaiming an opinion, when required by the circumstances of a specific audit engagement; or

(b) Disclosures in the financial statements that the applicable financial reporting framework requires management to make.

iv) Other Matter Paragraphs in the Auditor's Report –

- **Meaning –** If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of – (a) the audit, or (b) the auditor's responsibilities or (c) the auditor's report **AND**
- This is not prohibited by law or regulation,
- **Heading –** The auditor shall do so in a paragraph in the auditor's report, with the heading "Other Matter", or other appropriate heading.
- **Place –** The auditor shall include this paragraph immediately after the Opinion paragraph and any Emphasis of Matter paragraph, or elsewhere in the auditor's report if the content of the Other Matter paragraph is relevant to the Other Reporting Responsibilities section.
- **Effect of Law, Regulation, etc. –** Law, regulation or generally accepted practice in a jurisdiction may require or permit the auditor to elaborate on matters that provide further explanation of the auditor's responsibilities in the audit of the financial statements or of the auditor's report thereon. Where relevant, one or more sub-headings may be used that describe the content of the Other Matter paragraph.

v) Content of Other Matter Paragraph

(a) The content of an Other Matter paragraph reflects clearly that such other matter is **not** required to be presented and disclosed in the financial statements.

(b) An Other Matter paragraph does not include information that the auditor is prohibited from providing by law, regulation or other standards, for example, ethical standards relating to confidentiality of information.

(c) An Other Matter paragraph also does not include information that is required to be provided by management.

vi) Inclusion in Auditor's Report

(a) The placement of an Other Matter paragraph depends on the nature of the information to be communicated.

(b) When an Other Matter paragraph is included to draw users' attention to a matter relevant to their understanding of the audit of the financial statements, the paragraph is included immediately after the Opinion paragraph and any Emphasis of Matter paragraph.

(c) When an Other Matter paragraph is included to draw users' attention to a matter relating to Other Reporting Responsibilities addressed in the auditor's report, the paragraph may be included in the section sub-titled "Report on Other Legal and Regulatory Requirements".

(d) Alternatively, when relevant to all the auditor's responsibilities or users' understanding of the auditor's report, the Other Matter paragraph may be included as a separate section following the Report on the Financial Statements and the Report on Other Legal and Regulatory Requirements.

vii) Communication with Those Charged with Governance -

1. If the auditor expects to include an Emphasis of Matter or an Other Matter paragraph in the auditor's report, the auditor shall communicate with those charged with governance regarding this expectation and the proposed wording of this paragraph.
2. Such Communication enables TCWG to make them aware of the nature of any specific matters that the auditor intends to highlight in the auditor's report, and provides them with an opportunity to obtain further clarification from the auditor where necessary.

....

Appendix

Emphasis of Matter Para

Illustration 1 – Circumstances include the following –

- Audit of a complete set of separate general purpose financial statements of a company prepared under the Companies Act, 1956 financial reporting framework.
- The terms of the audit engagement reflect description of management's responsibility for the financial statements in SA 210 (Revised).
- Inventories are misstated. The misstatement is deemed to be material but not pervasive to the financial statements. The audit opinion is qualified for the misstatement.
- There is uncertainty relating to a pending exceptional litigation matter. This is highlighted in the auditor's report by an Emphasis of Matter paragraph.
- In addition to the audit of financial statements, the auditor has other reporting responsibilities required under the Companies Act, 1956 and/or other regulatory requirements.

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Financial Statements –	**See Illustration 1 above of SA – 705**
Management's Responsibility for the Financial Statements –	**See Illustration 1 above of SA – 705**
Auditor's Responsibility –	**See Illustration 1 above of SA – 705**
Basis for Disclaimer of Opinion –	**See Illustration 1 above of SA – 705**
Opinion –	**See Illustration 1 above of SA – 705**

Emphasis of Matter

We draw attention to Note X to the financial statements which describe the uncertainty related to the outcome of the lawsuit filed against the Company by XYZ Company. Our opinion is not qualified in respect of this matter.

Report on Other Legal and Regulatory Requirements – **See Illustration 1 above of SA – 705.**

For XYZ and Co.
Chartered Accountants
Firm's Registration Number
Signature
(Name of the Member Signing the Audit Report)
(Designation)
Membership Number

Place of Signature

Date

Other Matter Para

Illustration 2 – Circumstances include the following –

- Audit of a complete set of consolidated general purpose financial statements of a parent company prepared under accounting principles generally accepted in India, as required for compliance with SEBI's regulatory requirement, which is a fair presentation framework.
- The terms of the group audit engagement reflect description of management's responsibility for the financial statements in SA 210 (Revised).
- The report includes an Other Matter paragraph in respect of the auditor's responsibility in respect of subsidiaries not audited by him but which form part of the consolidated financial statements under report.

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Financial Statements –	**See Illustration 1 above of SA – 700**
Management's Responsibility for the Financial Statements –	**See Illustration 1 above of SA – 700**
Auditor's Responsibility –	**See Illustration 1 above of SA – 700**
Basis for Disclaimer of Opinion –	**See Illustration 1 above of SA – 700**

Opinion –

In our opinion and to the best of our information and according to the explanations given to us and based on the consideration of the reports of the other auditors on the financial statements of the subsidiaries as noted below, the consolidated financial statements give a true and fair view in conformity with the accounting principles generally accepted in India –

(a) In the case of the consolidated Balance Sheet, of the state of affairs of the Company as at March 31, 20XX;
(b) In the case of the consolidated Profit and Loss Account, of the profit/ loss for the year ended on that date; and
(c) In the case of the consolidated Cash Flow Statement, of the cash flows for the year ended on that date.

Other Matter –

We did not audit the financial statements of certain subsidiaries, whose financial statements reflect total assets (net) of ₹ XXXX as at March 31, 20XX, and total revenues of ₹ XXXX and net cash outflows are amounting to ₹ XXXX for the year then ended. These financial statements have been audited by other auditors whose reports have been furnished to us by the Management, and our opinion is based solely on the reports of the other auditors. Our opinion is not qualified in respect of this matter.

For XYZ and Co.
Chartered Accountants
Firm's Registration Number

Place of Signature

Signature

Date

(Name of the Member Signing the Audit Report)
(Designation)
Membership Number

Standard on Auditing (SA) 710 (Revised) Comparative Information— Corresponding Figures and Comparative Financial Statements

1. Effective Date

This SA is effective for audits of financial statements for periods beginning on or after **April 1, 2011.**

2. Scope of this SA

This Standard on Auditing (SA) deals with the auditor's responsibilities regarding comparative information in an audit of financial statements. When the financial statements of the prior period have been audited by a predecessor auditor or were not audited, the requirements and guidance in SA 510 (Revised) regarding opening balances also apply.

3. The Nature of Comparative Information

Audit Approach – The nature of the comparative information that is presented in an entity's financial statements depends on the requirements of the applicable financial reporting framework. There are two different broad approaches to the auditor's reporting responsibilities in respect of such comparative information –

(a) **Corresponding figures -** For corresponding figures, the auditor's opinion on the financial statements refers to the current period only

(b) **Comparative financial statements -** For comparative financial statements, the auditor's opinion refers to each period for which financial statements are presented.

Note → The approach to be adopted is often specified by law or regulation but may also be specified in the terms of engagement.

4. Objectives

The objectives of the auditor are –

(a) To obtain sufficient appropriate audit evidence about whether the comparative information included in the financial statements has been presented, in all material respects, in accordance with the requirements for comparative information in the applicable financial reporting framework; and

(b) To report in accordance with the auditor's reporting responsibilities.

5. Definitions

For purposes of the SAs, the following terms have the meanings attributed below –

(a) **Comparative information –** The amounts and disclosures included in the financial statements in respect of one or more prior periods in accordance with the applicable financial reporting framework.

(b) **Corresponding figures –** Comparative information where amounts and other disclosures for the prior period **are included as an integral part** of the current period financial statements, and are intended to be read only in relation to the amounts and other disclosures relating to the current period (referred to as "current period figures"). The level of detail presented in the corresponding amounts and disclosures is dictated primarily by its relevance to the current period figures.

(c) **Comparative financial statements –** Comparative information where amounts and other disclosures for the prior period are included for comparison with the financial statements of the current period but, if audited, are referred to in the auditor's opinion. The level of information included in those comparative financial statements is comparable with that of the financial statements of the current period.

6. Requirements

i) Audit Procedures

1. **Basic Evaluation of Comparative Information –**

   (a) The auditor shall determine whether the financial statements **include** the comparative information required by the applicable financial reporting framework and whether such information is appropriately **classified.**

   (b) For this purpose, the auditor shall evaluate whether –

   i. The comparative information **agrees** with the amounts and other disclosures presented in the prior period; and

   ii. The accounting policies reflected in the comparative information are **consistent** with those applied in the current period or, if there have been changes in accounting policies, whether those changes have been properly accounted for and adequately **presented and disclosed.**

2. **Additional Procedures in case of Material Misstatement** –

   (a) If the auditor becomes aware of a possible material misstatement in the comparative information while performing the current period audit, the auditor shall perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence to **determine whether a material misstatement exists.**

   (b) If the auditor had audited the prior period's financial statements, the auditor shall also follow the relevant requirements of SA 560 (Revised).

3. **Written Representation –** As required by SA 580 (Revised), the Auditor shall –

   (a) Request written representations for **all periods** referred to in the auditor's opinion.

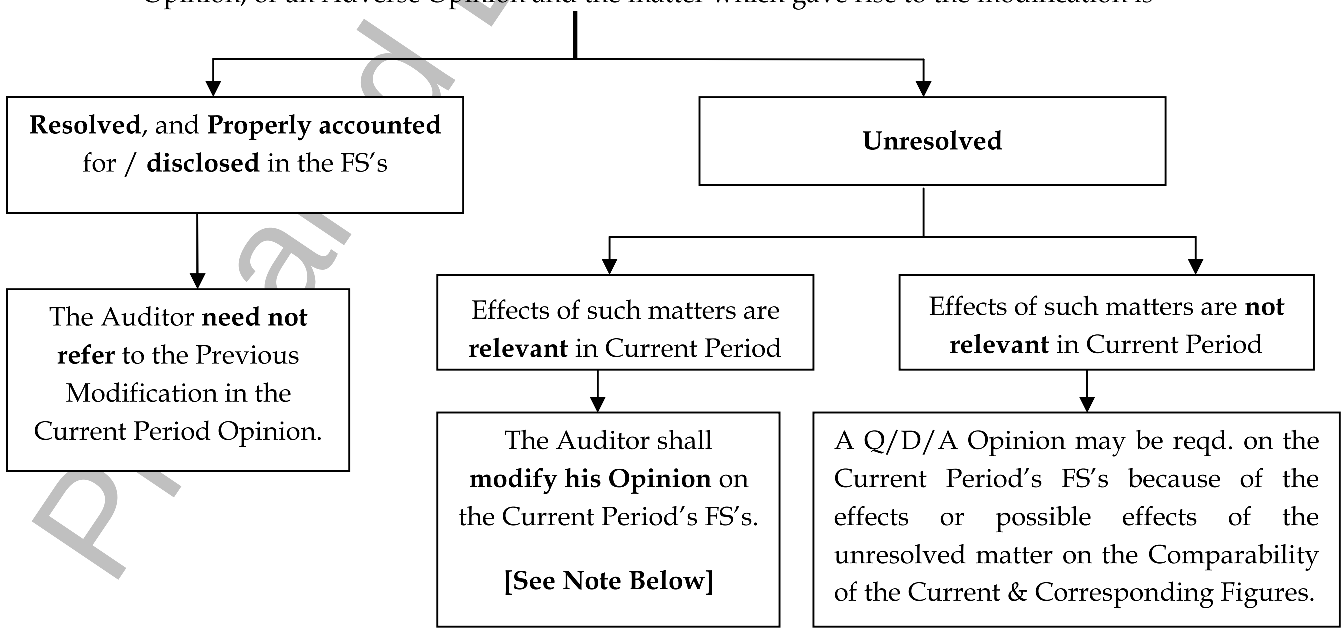
   (b) Obtain a **Specific written representation** regarding any **Prior Period Item** that is separately disclosed in the current year's statement of profit and loss.

ii) Audit Reporting for Corresponding Figures –

1. **Basic Principle -** When corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures because the auditor's opinion is on the current period financial statements as a whole, including the corresponding figures, (except in the following circumstance is discussed below)

2. **Effect of Prior Period Modified Report –**

If the Auditor's Report on the prior period, as previously issued, included a Qualified Opinion, a Disclaimer of Opinion, or an Adverse Opinion and the matter which gave rise to the modification is –



Note → In the Basis for Modification paragraph in the auditor's report, the auditor shall either –

1. Refer to both the current period's figures and the 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

2. 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.

3. **Prior Period Material Misstatement –** If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements on which an unmodified opinion has been previously issued, the auditor shall –

(a) Verify whether the misstatement has been dealt with as required under the applicable financial reporting framework and,

(b) If that is not the case, the auditor shall express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, **Modified with respect to the Corresponding Figures** included therein.

Note → When the prior period financial statements that are misstated have not been amended and an Auditor's Report thereon has not been issued in accordance with the requirements of SA 560 (Revised), "Subsequent Events", but the corresponding figures have been properly dealt with as required under the applicable FRF and the appropriate disclosures have been made in the Current Period Financial Statements, the Auditor's Report may include an **Emphasis of Matter Paragraph** describing the circumstances and referring to, where relevant, disclosures that fully describe the matter that can be found in the Financial Statements.

4. **Prior Period Financial Statements Audited by a Predecessor Auditor -** If the financial statements of the prior period were audited by a predecessor auditor and the auditor is permitted by law or regulation to refer to the predecessor auditor's report on the Corresponding Figures and decides to do so, the auditor shall state in an **Other Matter Paragraph** in the Auditor's Report –

(a) That the financial statements of the prior period were audited by the predecessor auditor;

(b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefore; and

(c) The date of that report.

5. **Prior Period FS's Not Audited –**

(a) If the prior period financial statements were **not au**dited, the auditor shall –

- ✓ Request the management to **disclose this fact** on the face of the Current Period Financial Statements with respect to the Corresponding Figures.
- ✓ State in an **Other Matter Paragraph** in the auditor's report that the Corresponding Figures are **unaudited.**

(b) Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements.

iii) Audit Reporting for Comparative Financial Statements –

1. **Basic Principle –**

(a) When comparative financial statements are presented, the auditor's opinion shall refer to **each period** for which financial statements are presented and on which an audit opinion is expressed.

(b) Since the auditor's report on Comparative Financial Statements applies to the financial statements for **each of the periods presented,** the auditor may express a qualified opinion or an adverse opinion, disclaim an opinion, or include an Emphasis of Matter paragraph with respect to one or more periods, while expressing a different auditor's opinion on the financial statements of the other period.

2. **Difference in Opinion –** When reporting on prior period financial statements in connection with the current period's audit, if the auditor's opinion on such prior period financial statements differs from the opinion the auditor previously expressed, the auditor shall **disclose the substantive reasons** for the different opinion in an **Other Matter Paragraph** in accordance with SA 706.

3. **Prior Period Financial Statements Audited by a Predecessor Auditor –**

(a) If the financial statements of the prior period were audited by a predecessor auditor, in addition to expressing an opinion on the current period's financial statements, the auditor shall state in an Other Matter paragraph –

- ✓ That the financial statements of the prior period were audited by a predecessor auditor;
- ✓ The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons there for; and
- ✓ The date of that report, unless the predecessor auditor's report on the prior period's financial statements is revised with the financial statements.

Unless the Predecessor AR's on the P's FS's is revised with the FS's

(b) If the Auditor concludes that a material misstatement exists that affects the Prior Period Financial Statements on which the predecessor auditor had previously reported **without modification**, the auditor shall **communicate** the misstatement with the appropriate level of management and those charged with governance and request that the Predecessor Auditor be informed.

(c) If the Prior Period Financial Statements are **amended,** and the Predecessor Auditor agrees to issue a new **Auditor's Report** on the amended Financial Statements of the prior period, the auditor shall report only on the Current Period.

4. **Prior Period Financial Statements Not Audited –**

(a) If the prior period financial statements were not audited, the auditor shall state in an Other Matter paragraph that the comparative financial statements are **unaudited.**

(b) Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements.

………………………………………………………………………………………………

Appendix

Corresponding Figures

Illustration 1 – Circumstances include the following –

- The auditor's report on the prior period, as previously issued, included a qualified opinion.
- The matter giving rise to the modification is unresolved.
- The effects or possible effects of the matter on the current period's figures are material and require a modification to the auditor's opinion regarding the current period figures.

INDEPENDENT AUDITOR'S REPORT

(Refer the Format of Audit Report – 7000)

Basis for Qualification Opinion

As discussed in Note X to the financial statements, no depreciation has been provided in the financial statements which constitutes a departure from the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act"). This is the result of a decision taken by management at the start of the preceding financial year and caused us to qualify our audit opinion on the financial statements relating to that year. Based on the straight-line method of depreciation and annual rates of 5% for the building and 20% for the equipment, the loss for the year should be increased by ₹ XXX in 20X1 and ₹ XXX in 20X0, property, plant and equipment should be reduced by accumulated depreciation of ₹.XXX in 20X1 and ₹ XXX in 20X0, and the accumulated loss should be increased by ₹ XXX in 20X1 and ₹ XXX in 20X0.

Qualified Opinion

In our opinion, except for the effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements give a true and fair view of the state of affairs of the Company as of March 31, 20X1, and of its results of operations and its cash flows for the year then ended in accordance with the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act").

Illustration 2 – Circumstances include the following –

- The auditor's report on the prior period, as previously issued, included a qualified opinion.
- The matter giving rise to the modification is unresolved.
- The effects or possible effects of the matter on the current period's figures are immaterial but require a modification to the auditor's opinion because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.

Basis of Qualification Opinion

Because we were appointed auditors of the Company during 20X0, we were not able to observe the counting of the physical inventories at the beginning of that period or satisfy ourselves concerning those inventory quantities by alternative means. Since opening inventories affect the determination of the results of operations, we were unable to determine whether adjustments to the results of operations and opening retained earnings might be necessary for 20X0. Our audit opinion on the financial statements for the year ended 31 March, 20X0 was modified accordingly. Our opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures and the corresponding figures.

Qualified Opinion

In our opinion, except for the possible effects on the corresponding figures of the matter described in the Basis for Qualified Opinion paragraph, the financial statements give a true and fair view of the state of affairs of the Company as of March 31, 20X1, and of its results of operations and its cash flows for the year then ended in accordance with the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act").

Corresponding Figures

Illustration 3 – Circumstances include the following –

- Auditor is required to report on both the current period financial statements and the prior period financial statements in connection with the current year's audit.
- The financial reporting framework used in preparing the financial statements is other than accounting principles generally accepted in India. However, the audit is performed in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India.
- The auditor's report on the prior period, as previously issued, included a qualified opinion.
- The matter giving rise to the modification is unresolved.
- The effects or possible effects of the matter on the current period's figures are material to both the current period financial statements and Prior Period Financial Statements and require a modification to the auditor's opinion.

Basis of Opinion

As discussed in Note X to the financial statements, no depreciation has been provided in the financial statements which constitutes a departure from the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act"). Based on the straight-line method of depreciation and annual rates of 5% for the building and 20% for the equipment, the loss for the year should be increased by ₹ XXX in 20X1 and ₹ XXX in 20X0, property, plant and equipment should be reduced by accumulated depreciation of ₹ XXX in 20X1 and ₹ XXX in 20X0, and the accumulated loss should be increased by ₹ XXX in 20X1 and ₹ XXX in 20X0.

Qualified Opinion

In our opinion, except for the effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements give a true and fair view of the state of affairs of the Company as of March 31, 20X1 and 20X0 and of its results of operations and its cash flows for the years then ended in accordance with the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act").

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	What are the **auditor's responsibilities in respect of corresponding figures?**	[4 Marks] [May 2010]	**Refer Point No. 6 – i) Audit Procedures – 1, 2 & 3 on Pg. No. 27**
2.	The audit report of P Ltd. for the year 2012 – 13 contained a **qualification regarding non – provision of doubtful debts.** As the statutory auditor of the company for the year 2013 – 14, how would you report, if – (a) The company **does not make provision** for doubtful debts in 2013 – 14 (b) The company **makes adequate provision** for doubtful debts in 2013 – 14?	[8 Marks] [June 2009]	**Refer Point No. 6 – ii) Audit Reporting for Corresponding Figures – 1 & 2 on Pg. no. 27** **For Conclusion See Below**

Conclusion – In the instant Case, if P Ltd. –

(a) Does not make provision for doubtful debts the auditor will have to **modify his report for both current and previous year's figures** as mentioned in **Point No. 6 – ii) Audit Reporting for Corresponding Figures – 1 & 2 on Pg. no.** .

(b) If however, the provision is made, the auditor need **not refer to the earlier year's modification.**

S.N.	Questions	Marks and Attempt	Answer
3.	Write Short Note on Corresponding Figures.	[4 Marks] [May 2013]	**Refer Point No. 5 (b) on Page no. 26**
4.	Write Short Note on Auditor's Responsibilities regarding comparatives.	[4 Marks] [Nov. 2006]	**Refer Point No. 6 on Page no. 27**

Standard on Auditing (SA) 720

Auditor's responsibility in relation to other information in documents containing auditor's financial statements

1. Effective Date

This Standard on Auditing becomes operative for all audits relating to accounting periods beginning **on or after 1st April, 2010.**

2. Introduction

1. For auditors it will be a wider role in the affairs of a company and apart from financial statements, also to inspect 'other information' to look for **possible material inconsistencies** to make the audit reports fool-proof.
2. It will also help auditors **"to go beyond receiving the evidences** by valuating them on prudence principles."

3. Objective

The objective of the auditors is to respond appropriately when documents containing audited financial statements and the auditor's report thereon include **Other Information that could undermine the credibility** of those financial statements and the auditor's report.

4. Definitions

(a) **Other information** – Financial and non-financial information (other than the financial statements and the auditor's report thereon) which is included, either by law, regulation or custom, in a document containing audited financial statements and the auditor's report thereon.

(b) **Inconsistency** – Other information that contradicts information contained in the audited financial statements. A material inconsistency may raise doubt about the audit conclusions drawn from audit evidence previously obtained and, possibly, about the basis for the auditor's opinion on the financial statements.

(c) **Misstatement of fact** – Other information that is unrelated to matters appearing in the audited financial statements that is incorrectly stated or presented which may undermine the credibility of the document containing audited financial statements.

5. Other Information comprises of:-

1. **A report by management or those charged with governance on operations.**
2. **Financial summaries or highlights.**
3. **Planned capital expenditures.**
4. **Financial ratios.**
5. **Selected quarterly data.**
6. **However if does not encompass:-**
   - A press release or a transmittal memorandum, e.g. a covering Letter with audited financial statements and the auditor's report.
   - Information contained in analyst briefings.
   - Information on entity's web site.

6. Scope

Consideration Specific to Smaller Entities –

- Only if required law or regulations e.g. A document where a legal requirement exists for an accompanying report by those charged with governance.

- In case of certain entities such as, Central/State governments and related government entities (for example, agencies, boards, commissions), withdrawal from the engagement may not be an option. In such cases the auditor may issue a report to the appropriate statutory body giving details of the inconsistency.

7. Material Inconsistencies

When management agrees to revise the inconsistencies, the auditor shall review the steps taken by the management and ensure that the users of FS are informed of the revision. When the management refuses to make the revisions, the auditor shall communicate this matter to those charged with governance; and

1. Include in the auditor's report an Other Matter(s) paragraph describing the material inconsistency;
2. Where withdrawal is legally permitted, withdraw from the engagement.
3. The auditor may base any decision on what further action to take on advice from the auditor's legal counsel.

8. Auditors report

When the auditor concludes that there is a material misstatement of face in the other information which management refuses to correct, the auditor shall notify those charged with governance of the auditor's concern regarding the other information and take any further appropriate action.

Section – IV

S. No.	Standard on Auditing	Page No.
1.	SA – 800	194 – 199
2.	SA – 805	200 – 207
3.	SA – 810	208 – 213

Standard on Auditing (SA) 800
Special Considerations — Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks

1. Effective Date –

This SA is effective for audits of financial statements for periods beginning on or after **April 1, 2011**.

2. Scope of this SA –

This SA deals with special considerations in the application of the SAs (in 100-700 series) to an audit of financial statements prepared in accordance with a special purpose framework. This SA does not override the requirements of the other SAs; nor does it purport to deal with all special considerations that may be relevant in the circumstances of the engagement.

3. Objectives –

The objective of the auditor, when applying SAs in an audit of financial statements prepared in accordance with a special purpose framework, is to address appropriately the special considerations that are relevant to –

(a) The **acceptance** of the engagement;

(b) The **planning and performance** of that engagement; and

(c) **Forming an opinion and reporting** on the financial statements.

4. Definitions –

For purposes of the SAs, the following terms have the meanings attributed below –

(a) Special purpose financial statements – Financial statements prepared in accordance with a special purpose framework. Examples of special purpose frameworks are –

1. The cash receipts and disbursements basis of accounting for cash flow information that an entity may be requested to prepare for creditors;
2. The financial reporting provisions established by a regulator to meet the requirements of that regulator; or
3. The financial reporting provisions of a contract, such as a bond indenture, a loan agreement, or a project grant.

(b) Special purpose framework – A financial reporting framework designed to meet the financial information needs of **specific users.** The financial reporting framework may be a fair presentation framework or compliance framework.

4.1 Features of Special Purpose Frameworks

☞ **Specific Users –** Special Purpose Framework is a Financial Reporting Framework designed to meet the financial information needs of Specific Users. [See examples in Table above]

☞ **Special / Unique Feature –**

(a) When a special purpose framework is based on some authorised financial reporting framework, but does not comply with all the requirements of that framework. Then, in this case, with respect to the special purpose engagement, it would be inappropriate to imply full compliance of such authorised financial reporting framework.

(b) The **special purpose framework may not be a fair presentation framework** even if the financial reporting framework on which it is based is a fair presentation framework. This is because the special purpose framework may not comply with all the requirements of the financial reporting framework established by the authorized or recognized standards setting organization or by law or regulation that are necessary to achieve fair presentation of the financial statements.

☞ **Special Purpose Financial Statements only prepared –** If the Financial statements prepared in accordance with a special purpose framework may be the only financial statements an entity prepares, those financial statements may be **used by users other than those for whom the financial reporting framework is designed.** Despite the broad distribution of the financial statements in those circumstances, the financial statements are still considered to be special purpose financial statements for purposes of the SAs. The requirements in paragraphs **13-14 are designed to avoid misunderstandings** about the purpose for which the financial statements are prepared.

☞ **Notes & Disclosures –** The related notes ordinarily comprise **a summary of significant accounting policies and other explanatory information.** The requirements of the applicable financial reporting framework determine the form and content of the financial statements, and what constitutes a complete set of financial statements.

5. Requirements

A. Acceptability of the Financial Reporting Framework –

1. **Auditor's Duties –** In an audit of special purpose financial statements, the auditor shall obtain an understanding of –
   (a) The purpose for which the financial statements are prepared
   (b) The financial information needs of the intended users are a key factor in determining the acceptability of the financial reporting framework applied in the preparation of the financial statements.
   (c) The steps taken by management to determine that the applicable financial reporting framework is acceptable in the circumstances.

B. Considerations When Planning and Performing the Audit –

1. **Accounting policies –** In planning and performing an audit of special purpose financial statements, the auditor shall determine whether application of the SAs requires special consideration in the circumstances of the engagement. SA 315 requires the auditor to obtain an understanding of the entity's selection and application of accounting policies. In the case of financial statements prepared in accordance with the provisions of a contract, the auditor shall obtain an understanding of any significant interpretations of the contract that management made in the preparation of those financial statements.

2. **Compliance with SAs –** SA 200 requires an auditor to comply with all the ethical requirements and all SAs, while performing the audit. In exceptional circumstances, the auditor may judge it necessary to depart from a relevant requirement in an SA by performing alternative audit procedures to achieve the aim of that requirement. Application of some of the requirements of the SAs in an audit of special purpose financial statements may require special consideration by the auditor.

   For examples –

   ✓ **Judgements regarding materiality (SA – 320)** of an item can be based on the consideration of the financial information needs of the intended users.

   ✓ In the case of special purpose financial statements, those charged with governance may not have the responsibility for overseeing the preparation of financial statements. In such cases, the requirements of **SA 260 (Revised) (Communication with those charged with governance)** may not be relevant to the audit of the special purpose financial statements, except when the auditor is also responsible for the audit of the entity's general purpose financial statements or, **for example**, has agreed with those charged with governance of the entity to communicate to them relevant matters identified during the audit of the special purpose financial statements.

C. Forming an opinion and Reporting Considerations –

1. **Basic Principle –** When forming an opinion and reporting on special purpose financial statements, the auditor shall apply the requirements in SA 700 (Revised). (Forming an Opinion and Reporting on Financial Statements)

2. **Reporting Requirements –** SA 700 (Revised) requires the auditor to evaluate whether the financial statements adequately refer to or describe the applicable financial reporting framework or the provisions of a contract, as the case may be.(Describing thereby significant interpretations of the contract).

   In the case of an auditor's report on special purpose financial statements following matters should be included as per SA 700 – **[Para 13]**

   (a) The auditor's report shall also describe the purpose for which the financial statements are prepared and, if necessary, the intended users, or refer to a note in the special purpose financial statements that contains that information; and

   (b) If management has a choice of financial reporting frameworks in the preparation of such financial statements, the explanation of management's responsibility for the financial statements shall also make reference to its responsibility for determining that the applicable financial reporting framework is acceptable in the circumstances.

3. **Alerting Readers that the Financial Statements Are Prepared in Accordance with a Special Purpose Framework – [Para 14]**

   a. The auditor's report on special purpose financial statements shall include an **Emphasis of Matter paragraph** alerting users of the auditor's report that the financial statements are prepared in accordance with a special purpose framework and that, as a result, the financial statements may not be suitable for another purpose. The auditor shall include this paragraph under an appropriate heading.

   b. In addition to the alert, the auditor may consider it appropriate to indicate that the **auditor's report is intended solely for the specific users.**

Appendix

Auditor Report Format

Illustration 1 – Circumstances include the following –

- The financial statements have been prepared by management of the entity in accordance with the financial reporting provisions of a contract (i.e., a special purpose framework) to comply with the provisions of that contract. Management does not have a choice of financial reporting frameworks.
- The applicable financial reporting framework is a **compliance framework.**
- The terms of the audit engagement reflect the description of management's responsibility for the financial statements in SA 210 (Revised).
- **Distribution** and use of the auditor's report are **restricted.**

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addresses]

We have audited the accompanying financial statements of ABC Company Ltd., which comprise the balance sheet as at March 31, 20XX, and the statement of profit and loss, and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information. The financial statements have been prepared by management of ABC Company Ltd. based on the financial reporting provisions of section/ clause Z of the contract dated July 1, 20XX between ABC Company Ltd. and DEF Company Ltd. ("the contract").

Management's Responsibility for the Financial Statements

Management is responsible for the preparation of these financial statements in accordance with the financial reporting provisions of section/ clause Z of the contract; this includes the design, implementation and maintenance of internal control relevant to the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, **<u>but not for the purpose of expression an opinion on the effectiveness of the Companies internal control.</u>** An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of the accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements of ABC Company Ltd. for the year ended March 31,20XX are prepared, in all material respects, in accordance with the financial reporting provisions of section/ clause Z of the contract.

Basis of Accounting and Restriction on Distribution and Use

Without modifying our opinion, we draw attention to Note X to the financial statement, which describes the basis of accounting. The financial statements are prepared to assist ABC Company Ltd. 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 ABC Company Ltd. and DEF Company Ltd. and should not be distributed to or used by parties other than ABC Company Ltd. or DEF Company Ltd.

For XYZ and Co.

Chartered Accountants

Place of Signature **Firm's Registration Number**

Signature

Date **(Name of the Member Signing the Audit Report)**

(Designation)

Membership Number

Illustration 2 – Circumstances include the following –

- The financial statements have been prepared by management of the entity in accordance with the financial reporting provisions established by a regulator (i.e., a special purpose framework) to meet the requirements of that regulator. Management does not have a choice of financial reporting frameworks.
- The applicable financial reporting framework is a **fair presentation framework.**
- The terms of the audit engagement reflect the description of management's responsibility for the financial statements in SA 210 (Revised).
- **Distribution** and use of the auditor's report are **not restricted.**
- **The Other Matter paragraph** refers to the fact that the auditor has also issued an auditor's report on financial statements prepared by ABC Company Ltd. for the same period in accordance with a general purpose framework.

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addresses]

We have audited the accompanying financial statements of ABC Company Ltd., which comprise the balance sheet as at March 31, 20X1, and the statement of profit and loss, and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information. The financial statements have been prepared by management based on the financial reporting provisions of Section Y of Regulation Z.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation of these financial statements that give a true and fair view of the state of affairs, results of operations and cash flows of the Company in accordance with the financial reporting provisions of Section Y of Regulation Z; this includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of the financial statements that give a true and fair view and are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, **but not for the purpose of expression an opinion on the effectiveness of the Companies internal control.** An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of the accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion and to the best of our information and according to the explanations given to us, the financial statements give a true and fair view of the state of affairs of ABC Company Ltd. as at March 31, 20X1, and of its results of operations and its cash flows for the year then ended in accordance with the financial reporting provisions of Section Y of Regulation Z.

Basis of Accounting and Restriction on Distribution and Use

Without modifying our opinion, we draw attention to Note X to the financial statements, which describe the basis of accounting. The financial statements are prepared to assist ABC Company Ltd. to meet the requirements of Regulator DEF. As a result, the financial statements may not be suitable for another purpose.

Other Matter

ABC Company Ltd. has prepared a separate set of financial statements for the year ended March 31, 20XX in accordance with the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act") on which we issued a separate auditor's report to the shareholders of ABC Company Ltd. dated June 30, 20XX.

For XYZ and Co.
Chartered Accountants

Place of Signature **Firm's Registration Number**

Signature

Date **(Name of the Member Signing the Audit Report)**
(Designation)
Membership Number

Standard on Auditing (SA) 805

Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement

1. Effective Date –

This SA is effective for audits of single financial statements or of specific elements, accounts or items for periods beginning on or after **April 1, 2011**.

2. Scope of this SA –

This SA deals with special considerations in the application of the SAs (in 100 – 700 series) to an audit of a single financial statement or of a specific element, account or item of a financial statement. The single financial statement or the specific element, account or item of a financial statement may be prepared in accordance with a general or special purpose framework. If prepared in accordance with a special purpose framework, SA 800 also applies to the audit.

Note → This SA does not apply to the report of a component auditor, issued as a result of work performed on the financial information of a component at the request of a group engagement team for purposes of an audit of group financial statements.

3. Objectives –

The objective of the auditor, when applying SAs in an audit of a single financial statement or of a specific element, account or item of a financial statement, is to address appropriately the special considerations that are relevant to –

(a) The **acceptance** of the engagement;

(b) The **planning and performance** of that engagement; and

(c) **Forming an opinion and reporting** on the single financial statement or on the specific element, account or item of a financial statement.

4. Definitions -

For purposes of this SA, reference to –

(a) **Element of a Financial Statement – "Element of a financial statement"** or "**element**" means an "element, account or item of a financial statement";

(b) **Financial Reporting Standards – "Financial Reporting Standards"** means**(Various accounting standards pronounced by different bodies of ICAI)** the Accounting Standards promulgated by the Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India (ICAI) or Accounting Standards, notified by the Central Government by publishing the same as the Companies (Accounting Standards) Rules, 2006, or the Accounting Standards for Local Bodies promulgated by the Committee on Accounting Standards for Local Bodies (CASLB) of the Institute of Chartered Accountants of India, as may be applicable.

(c) **Single Financial Statements –** A single financial statement (for example, a cash flow statement) or to a specific element of a financial statement (for example, cash and bank balances) includes the related notes. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information relevant to the financial statement or to the element.

Examples of Specific Elements, Accounts or Items of a Financial Statement

(a) Accounts receivable, allowance for doubtful accounts receivable, inventory, the liability for accrued benefits of a private pension plan, the recorded value of identified intangible assets, or the liability for "incurred but not reported" claims in an insurance portfolio, including related notes.

(b) A schedule of externally managed assets and income of a private pension plan, including related notes.

(c) A schedule of net tangible assets, including related notes.

(d) A schedule of disbursements in relation to a lease property, including explanatory notes.

(e) A schedule of profit participation or employee bonuses, including explanatory notes.

5. Requirements –

A. Considerations When Accepting the Engagement –

(a) **Basic Principle –** In the case of an audit of a single financial statement or of a specific element of a financial statement, auditor needs to comply with all SAs relevant to the audit (as per SA 200), irrespective of whether the auditor is also engaged to audit the entity's complete set of financial statements.

(b) **If the Auditor is not engaged for audit of Complete Financial Statements –** If the auditor is **not** also engaged to audit the entity's complete set of financial statements, the auditor shall determine whether the audit of a single financial statement or of a specific element of those financial statements in accordance with **SAs is practicable.**

Compliance with the requirements of SAs relevant to the audit of a single financial statement or of a specific element of a financial statement may not be practicable when the auditor is not also engaged to audit the entity's complete set of financial statements. In such cases, the auditor may discuss with management whether **another type of engagement might be more practicable.**

B. Acceptability of the Financial Reporting Framework –

- ✓ SA 210 (Revised) requires the auditor to determine the acceptability of the financial reporting framework applied in the preparation of the financial statements.
- ✓ In such audits, this shall include whether application of the financial reporting framework will result in a presentation that provides **adequate disclosures** to enable the intended users to understand the information conveyed in the financial statement or the element, and **the effect of material transactions and events** on the information conveyed in the financial statement or the element.

C. Form of Opinion –

(a) SA 210 (Revised) requires that the agreed terms of the audit engagement include the expected form of any reports to be issued by the auditor. In such audits, auditor shall consider whether the expected form of **opinion is appropriate** in the circumstances.

(b) The auditor's decision as to the expected form of opinion is a matter of professional judgment. It may be affected by whether use of the phrases presents fairly, in all material respects", or "gives a true and fair view" in the auditor's opinion on a single financial statement or on a specific element of a financial statement prepared in accordance with a fair presentation framework is generally accepted in the particular jurisdiction.

(c) If necessary to **achieve fair presentation**, provide **disclosures beyond those specifically** required by the framework or, in exceptional circumstances, depart from a requirement of the framework.

D. Considerations When Planning and Performing the Audit –

1. **Adaptation of SA's –** In planning and performing such audits, the **auditor shall adapt all SAs relevant** to the audit as necessary in the circumstances of the engagement. Even when only a specific element of a financial statement is the subject of the audit, SAs such as SA 240 (Revised) {A*uditor's Responsibilities relating to Fraud in an Audit of Financial Statements*}, SA 550 (Revised) {*Related Parties*} and SA 570 (Revised) 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 financial reporting framework.

2. **Inter – Relationship between Items –** The individual financial statements that comprise a complete set of financial statements, and many of the elements of those financial statements, including their related notes, are

interrelated. Consequently, the auditor may need to **perform procedures in relation to the interrelated items to meet the objective of the audit.**

3. **Materiality** – The materiality determined for a single financial statement or for a specific element of a financial statement may **be lower than the materiality determined** for the entity's complete set of financial statements; this will affect the nature, timing and extent of the audit procedures and the evaluation of uncorrected misstatements.

E. Forming an Opinion and Reporting Considerations –

(a) Basic principle –

- ✓ When forming an opinion and reporting on a single financial statement or on a specific element of a financial statement, the auditor shall apply the requirements in SA 700 (Revised) ***{Forming an Opinion and Reporting on Financial Statements}***, adapted as necessary in the circumstances of the engagement.
- ✓ In the case of a single financial statement or of a specific element of a financial statement, it is important that it provides **adequate disclosures** to enable the intended users to understand the information conveyed in the financial statement or the element, and the effect of material transactions and events on the information conveyed in the financial statement or the element.

(b) Reporting on the Entity's Complete Set of Financial Statements and on a Single Financial Statement or on a Specific Element of Those Financial Statements –

1. **Separate opinion** – If the auditor undertakes an engagement to report on a single financial statement or on a specific element of a financial statement in conjunction with an engagement to audit the entity's complete set of financial statements, the auditor shall express a separate opinion for each engagement.
2. **Differentiation** –
   - ✓ An audited single financial statement or an audited specific element of a financial statement may be published together with the entity's audited complete set of financial statements.
   - ✓ Presentation of the single financial statement or of the specific element of a financial statement should be sufficiently differentiated from the complete set of financial statements and if it is not done so the auditor shall ask management to rectify the situation and
   - ✓ Shall not issue the auditor's report containing the opinion on the single financial statement or on the specific element of a financial statement until satisfied with the differentiation.

(c) Modified Opinion, Emphasis of Matter Paragraph or Other Matter Paragraph in the Auditor's Report on the Entity's Complete Set of Financial Statements –

If the **opinion** in the auditor's report on an entity's **complete set of financial statements is modified**, or that **report includes an Emphasis of Matter paragraph or an Other Matter paragraph**

⇩

The auditor shall **determine the effect** that this may have on the auditor's report on a single financial statement or on a specific element of those financial statements.

⇩

When deemed appropriate, the auditor shall **modify the opinion** on the single financial statement or on the specific element of a financial statement, or include an Emphasis of Matter paragraph or an Other Matter paragraph in the auditor's report, accordingly.

Even when the modified opinion on the entity's complete set of financial statements, Emphasis of Matter paragraph or Other Matter paragraph does not relate to the audited financial statement or the audited element, the auditor may still **deem it appropriate** to refer to the modification in an Other Matter paragraph in an auditor's report on the financial statement or on the element because the auditor judges it to be relevant to the users' understanding of the audited financial statement or the audited element or the related auditor's report.

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If the auditor concludes that it is necessary to express an adverse opinion or disclaim an opinion on the entity's complete set of financial statements as a whole

⇩

SA 705 **{ *Modifications to the Opinion in the Independent Auditor's Report*}** does not permit the auditor to include in the same auditor's report an **unmodified opinion** on a single financial statement that forms part of those financial statements or on a specific element that forms part of those financial statements.

⇩

This is because such an unmodified opinion would **contradict** the adverse opinion or disclaimer of opinion on the entity's complete set of financial statements as a whole.

In the auditor's report on an entity's complete set of financial statements, the expression of a disclaimer of opinion regarding the results of operations and cash flows, where relevant, and an unmodified opinion regarding the state of affairs is permitted since the disclaimer of opinion is being issued in respect of the results of operations and cash flows only and not in respect of the financial statements as a whole.

⇩

If the auditor concludes that it is necessary to express an adverse opinion or disclaim an opinion on the entity's complete set of financial statements as a whole but, in the context of a separate audit of a specific element that is included in those financial statements, the auditor wants to express an unmodified opinion on that single element,

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The auditor shall only do so if –

(a) The auditor is not prohibited by law or regulation from doing so;

(b) That opinion is expressed in an auditor's report that is not published together with the auditor's report containing the adverse opinion or disclaimer of opinion; and

(c) The specific element does not constitute a major portion of the entity's complete set of financial statements.

⇩

Adverse Opinion or Disclaimer of Opinion on the Complete Set of Financial Statements –

(a) The auditor shall not express an unmodified opinion on a single financial statement of a complete set of financial statements if the auditor has expressed an adverse opinion or disclaimed an opinion on the complete set of financial statements as a whole.

(b) This is the case even if the auditor's report on the single financial statement is not published together with the auditor's report containing the adverse opinion or disclaimer of opinion. This is because a single financial statement is deemed to constitute a major portion of those financial statements.

Appendix

Auditor Report Format

Illustration 1 – Circumstances include the following –

- Audit of a **Balance Sheet** (i.e., a single financial statement).
- The balance sheet has been prepared by management of the entity in accordance with the requirements of the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act") relevant to preparing a balance sheet.
- The applicable financial reporting framework is **a fair presentation framework** designed to meet the common financial information needs of a wide range of users.
- The terms of the audit engagement reflect the description of management's responsibility for the financial statements in SA 210 (Revised).
- The auditor has determined that it is appropriate to use the phrase "presents a true and fair view", in the auditor's opinion.

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addresses]

We have audited the accompanying balance sheet of ABC Company Ltd. as at March 31, 20XX and a summary of significant accounting policies and other explanatory information (together "the financial statement").

Management's Responsibility for the Financial Statements

Management is responsible for the preparation of these financial statements that give a true and fair view of the financial position, financial performance and cash flows of the Company in accordance with the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act"). This responsibility includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of the financial statements that give a true and fair view and are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, **but not for the purpose of expression an opinion on the effectiveness of the Companies internal control.** An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of the accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statement presents a true and fair view of the state of affairs of ABC Company Ltd. as at March 31, 20XX in accordance with those requirements of the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956 ("the Act"), relevant to preparing such a financial statement.

For XYZ and Co.

Chartered Accountants

Place of Signature **Firm's Registration Number**

Signature

Date **(Name of the Member Signing the Audit Report)**

(Designation)

Membership Number

Illustration 2 – Circumstances include the following –

- Audit of a statement of **cash receipts** and disbursements (i.e., a single financial statement).
- The financial statement has been prepared by management of the entity in accordance with the cash receipts and disbursements basis of accounting to respond to a request for cash flow information received from a creditor. Management has a choice of financial reporting frameworks.
- The applicable financial reporting framework is a fair presentation framework designed to meet the financial information needs of specific users.
- The auditor has determined that it is appropriate to use the phrase "true and fair view" in the auditor's opinion.
- **Distribution** or use of the auditor's report is **not restricted.**

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addresses]

We have audited the accompanying statement of cash receipts and disbursements of ABC Company Ltd. for the year ended March 31, 20XX and a summary of significant accounting policies and other explanatory information (together "the financial statement"). The financial statement has been prepared by management using the cash receipts and disbursements basis of accounting described in Note X.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of this financial statement in accordance with the cash receipts and disbursements basis of accounting described in Note X; this includes determining that the cash receipts and disbursements basis of accounting is an acceptable basis for the preparation of the financial statement in the circumstances, and the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of the financial statement that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, **but not for the purpose of expression an opinion on the effectiveness of the Companies internal control.** An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of the accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statement presents a true and fair view of the cash receipts and disbursements of ABC Company Ltd. for the year ended March 31, 20XX in accordance with the cash receipts and disbursements basis of accounting described in Note X.

Basis of Accounting

Without modifying our opinion, we draw attention to Note X to the financial statement, which describes the basis of accounting. The financial statement is prepared to provide information to XYZ Creditor. As a result, the statement may not be suitable for another purpose.

For XYZ and Co.

Chartered Accountants

Place of Signature **Firm's Registration Number**

Signature

Date **(Name of the Member Signing the Audit Report)**

(Designation)

Membership Number

Standard on Auditing (SA) 810
Engagements to Report on Summary Financial Statements

1. Effective Date –

This SA is effective for engagements for periods beginning on or after **April 1, 2011**.

2. Scope of this SA –

This Standard on Auditing (SA) deals with the auditor's responsibilities when undertaking an engagement to report on summary financial statements derived from financial statements audited in accordance with SAs by that same auditor.

3. Objectives –

The objectives of the auditor are to –

(a) Determine whether it is appropriate to accept the engagement to report on summary financial statements;

(b) Form an opinion on the summary financial statements based on an evaluation of the conclusions drawn from the evidence obtained; and

(c) Express clearly that opinion through a written report that also describes the basis for that opinion.

4. Definitions –

For purposes of this SA, the following terms have the meanings attributed below –

(a) **Applied criteria** –The criteria applied by management in the preparation of the summary financial statements.

(b) **Audited financial statements** – Financial statements audited by the auditor in accordance with SAs, and from which the summary financial statements are derived.

(c) **Summary financial statements** – Historical financial information that is derived from financial statements but that contains less detail than the financial statements, while still providing a structured representation consistent with that provided by the financial statements of the entity's economic resources or obligations at a point in time or the changes therein for a period of time. Different jurisdictions may use different terminology to describe such historical financial information.

5. Requirements –

A. Engagement Acceptance –

1. **Basic principle –** The auditor shall, ordinarily, accept an engagement to report on summary financial statements in accordance with this SA only when the auditor has been engaged to conduct an audit in accordance with SAs of the financial statements from which the summary financial statements are derived.

2. **Preliminary Aspects –** Before accepting an engagement to report on summary financial statements, the auditor shall –

   (a) Determine whether the **applied criteria are acceptable**;

   (b) Obtain the **agreement of management** that it acknowledges and understands its responsibility:

      (i) For the **preparation of the summary financial statements** in accordance with the applied criteria;

      (ii) To make the **audited financial statements** available to the intended users of the summary financial statements **without undue difficulty;** and

      (iii) To include the **auditor's report on the summary financial statements** in any document that contains the summary financial statements and that indicates that the auditor has reported on them.

   (c) Agree with management the **form of opinion** to be expressed on the summary financial statements.

(d) **Management is responsible** for the determination of the information that needs to be reflected in the summary financial statements so that they are consistent, in all material respects, with or represent a fair summary of the audited financial statements. Because summary financial statements by their nature contain aggregated 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 financial statements do not exist.

(e) **Factors** that may affect the auditor's determination of the acceptability of the **applied criteria** include –

- ✓ The **nature** of the entity;
- ✓ The **purpose** of the summary financial statements;
- ✓ The **information** needs of the intended users of the summary financial statements; and
- ✓ Whether the applied criteria will result in summary financial statements that are not **misleading** in the circumstances.

3. Effect of unacceptable Criteria or Management Agreement not obtained –

- ✓ If the Auditor concludes that the **applied criteria is unacceptable** or is unable to **obtain the agreement of management set out in above point 2**. Its responsibility, the auditor shall not accept the engagement to report on the summary financial statements, unless required by law or regulation to do so.
- ✓ An engagement conducted in accordance with such law or regulation does not comply with this SA. Accordingly, the auditor's report shall include appropriate reference to this fact in the terms of the engagement. The auditor shall also determine the effect that this may have on the engagement to audit the financial statements from which the summary financial statements are derived.

B. Nature of Procedures – 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 financial statements:

(a) Evaluate whether the summary financial statements adequately **disclose their summarised nature and identify** the audited financial statements.

(b) When summary financial statements are not accompanied by the audited financial statements, evaluate whether they **describe clearly –**

1. From whom or where the audited financial statements are available; or
2. The law or regulation that specifies that the audited financial statements need not be made available to the intended users of the summary financial statements and establishes the criteria for the preparation of the summary financial statements.

(c) Evaluate whether the summary financial statements adequately **disclose the applied criteria.**

(d) Compare the summary financial statements with the related information in the audited financial statements to determine whether the summary financial statements **agree with or can be re-calculated** from the related information in the audited financial statements (Agreement with audited financial statements).

(e) Evaluate whether the summary financial statements are **prepared in accordance with the applied criteria.**

(f) Evaluate, in view of the purpose of the summary financial statements, whether the summary financial statements contain the information necessary, and are at an appropriate level of aggregation, so as **not to be misleading** in the circumstances.

(g) Evaluate whether the audited financial statements are available to the intended users of the summary financial statements **without undue difficulty,** unless law or regulation provides that they need not be made available and establishes the criteria for the preparation of the summary financial statements.

C. Form of Opinion –

(a) **Phrasing of Unmodified Opinion as per SA –** When the auditor has concluded that an unmodified opinion on the summary financial statements is appropriate, the auditor's opinion shall, unless otherwise required by law or regulation, use one of the following phrases –

1. The summary financial statements are **consistent,** in all material respects, with the audited financial statements, in accordance with **the applied criteria**; or

2. The summary financial statements are a **fair summary** of the audited financial statements, in accordance with the **applied criteria.**

(b) Phrasing of Unmodified Opinion as per Law or Regulation – If law or regulation prescribes the wording of the opinion on summary financial statements in terms that are different from those described before, the auditor shall –

1. Apply the procedures and any further procedures necessary to enable the auditor to express the prescribed opinion; and

2. Evaluate whether users of the summary financial statements might misunderstand the auditor's opinion on the summary financial statements and, if so, whether **additional explanation** in the auditor's report on the summary financial statements can mitigate possible misunderstanding.

(c) Where Additional Explanation is not sufficient –

1. If, in this case, the auditor concludes that additional explanation in the auditor's report on the summary financial statements cannot mitigate possible misunderstanding, the auditor shall not accept the engagement, unless required by law or regulation to do so.

2. An engagement conducted in accordance with such law or regulation does not comply with this SA. Accordingly, the auditor's report on the summary financial statements shall not indicate that the engagement was conducted in accordance with this SA.

D. Timing of Work and Events Subsequent to the Date of the Auditor's Report on the Audited Financial Statements –

(a) The auditor's report on the summary financial statements may be **dated later than** the date of the auditor's report on the audited financial statements. In such cases, the auditor's report on the summary financial statements shall state that the summary financial statements and audited financial statements do not reflect the effects of events that occurred subsequent to the date of the auditor's report on the audited financial statements that may require adjustment of, or disclosure in, the audited financial statements.

(b) When the auditor reports on the summary financial statements after the completion of the audit of the financial statements, the auditor is not required to obtain additional audit evidence on the audited financial statements, or report on the effects of events that occurred subsequent to the date of the auditor's report on the audited financial statements since the summary financial statements are **derived** from the audited financial statements and **do not update them.**

(c) The auditor may become aware of facts that existed at the date of the auditor's report on the audited financial statements, but of which the auditor previously was unaware. In such cases, the auditor shall not issue the auditor's report on the summary financial statements until the auditor's consideration of such facts in relation to the audited financial statements in accordance with SA 560 (Revised) {*Subsequent Events}* has been completed.

E. Elements of the Auditor's Report on Summary Financial Statements – The auditor's report on summary financial statements shall include the following elements–

(a) A **TITLE** clearly indicating it as the report of an independent auditor.

(b) An **ADDRESSEE.**

(c) An **INTRODUCTORY PARAGRAPH** that –

(i) Identifies the summary financial statements on which the auditor is reporting including the title of each statement included in the summary financial statements;

(ii) Identifies the audited financial statements;

(iii) Refers to the auditor's report on the audited financial statements, the date of that report, and, **subject to Point F**, the fact that an unmodified opinion is expressed on the audited financial statements;

(iv) If the date of the auditor's report on the summary financial statements is later than the date of the auditor's report on the audited financial statements, states that the summary financial statements and the audited financial statements do not reflect the effects of events that occurred subsequent to the date of the auditor's report on the audited financial statements; and

(v) A statement indicating that the summary financial statements do not contain all the disclosures required by the financial reporting framework applied in the preparation of the audited financial statements, and that reading the summary financial statements is not a substitute for reading the audited financial statements.

(d) A description of **MANAGEMENT'S RESPONSIBILITY** for the summary financial statements, explaining that management is responsible for the preparation of the summary financial statements in accordance with the applied criteria.

(e) A statement that the **AUDITOR IS RESPONSIBLE** for expressing an opinion on the summary financial statements based on the procedures required by this SA.

(f) A paragraph clearly expressing an **OPINION.**

(g) The **AUDITOR'S SIGNATURE** along with the firm registration number, wherever applicable, and the membership number assigned by the Institute of Chartered Accountants of India (ICAI).

(h) The **DATE** of the auditor's report.

(i) The place of **SIGNATURE.**

F. Modifications to the Opinion, Emphasis of Matter Paragraph or Other Matter Paragraph in the Auditor's Report on the Audited Financial Statements –

Situation	Treatment – In addition to the elements in the above Point E
When the auditor's report on the audited financial statements contains a **Qualified Opinion, An Emphasis Of Matter Paragraph, Or An Other Matter Paragraph,** but the auditor is satisfied that the summary financial statements are consistent, in all material respects, with or are a fair summary of the audited financial statements, in accordance with the applied criteria.	The Auditor's Report on the summary financial statements shall, in addition to the elements in Form of opinion paragraph – (a) State that the auditor's report on the audited financial statements contains a qualified opinion, an Emphasis of Matter paragraph, or an Other Matter paragraph; and (b) Describe – (i) The basis for the qualified opinion on the audited financial statements, and that qualified opinion; or the emphasis of Matter or the Other Matter paragraph in the auditor's report on the audited financial statements; and (ii) The effect thereof on the summary financial statements, if any.
When the auditor's report on the audited financial statements contains an **Adverse Opinion Or A Disclaimer Of Opinion**	The auditor's report on the summary financial statements shall, in addition to the elements in Form of opinion paragraph – (a) State that the auditor's report on the audited financial statements contains an adverse opinion or disclaimer of opinion; (b) Describe the basis for that adverse opinion or disclaimer of opinion; and (c) State that, as a result of the adverse opinion or disclaimer of opinion, it is inappropriate to express an opinion on the summary financial statements.

G. Modified Opinion on the Summary Financial Statements –

Situation	Treatment
1. If the summary financial statements are **not consistent,** in all material respects, with or are **not a fair summary** of the audited financial statements, in accordance with the Applied Criteria, **and** 2. Management does **not** agree to make the necessary changes,	**The auditor shall express an adverse opinion on the summary financial statements.**
Note →Restriction on Distribution or Use or Alerting Readers to the Basis of Accounting - When distribution or use of the auditor's report on the audited financial statements is **restricted**, or the auditor's report on the audited financial statements **alerts readers** that the audited financial statements are prepared in accordance with a special purpose framework, the auditor shall **include a similar restriction or alert** in the auditor's report on the summary financial statements.	

H. Comparatives –

Aspects	Description
Omission of Comparatives	1. If the Audited Financial Statements contain Comparatives, there is **presumption** that the Summary Financial Statements also would contain comparatives. 2. If the audited financial statements contain comparatives, but the summary financial statements do not, the auditor shall determine whether such **omission is reasonable** in the circumstances of the engagement. 3. The auditor shall determine the effect of an **unreasonable omission** on the auditor's report on the summary financial statements. 4. Circumstances that may affect the auditor's determination whether an omission of comparatives is reasonable include the nature and objective of the summary financial statements, the applied criteria, and the information needs of the intended users of the summary financial statements.
Another Auditor	If the summary financial statements contain comparatives that were reported on by another auditor, the auditor's report on the summary financial statements shall also contain the matters that SA 710 (Revised) **{*Comparative Information—Corresponding Figures and Comparative Financial Statements*}** requires the auditor to include in the auditor's report on the audited financial statements.

I. Unaudited Supplementary Information Presented with Summary Financial Statements –

The auditor shall evaluate whether any unaudited supplementary information presented with the summary financial statements is clearly differentiated from the summary financial statements. If the auditor concludes that the entity's presentation of the unaudited supplementary information is not clearly differentiated from the summary financial statements, the auditor shall ask management to change the presentation of the unaudited supplementary information. If management refuses to do so, the auditor shall explain in the auditor's report on the summary financial statements that such information is not covered by that report.

J. Other Information in Documents Containing Summary Financial Statements –

The auditor shall read other information included in a document containing the summary financial statements and related auditor's report to identify material inconsistencies, if any, with the summary financial statements. If, on reading the other information, the auditor identifies a material inconsistency, the auditor shall determine whether the summary financial statements or the other information needs to be revised. If, on reading the other information, the auditor becomes aware of an apparent material misstatement of fact, the auditor shall discuss the matter with management.

K. Auditor Association –

1. Management does not include Auditor's Report in the document containing Summary Financial Statements –

(a) If the auditor becomes aware that the entity plans to state that the auditor has reported on summary financial statements in a document containing the summary financial statements, but does not plan to include the related auditor's report, the auditor shall request management to include the auditor's report in the document.

(b) If management does not do so, the auditor shall determine and carry out other appropriate actions designed to prevent management from inappropriately associating the auditor with the summary financial statements in that document.

(c) Other appropriate actions the auditor may take when management does not take the requested action may include informing the intended users and other known third-party users of the inappropriate reference to the auditor. The auditor's course of action depends on the auditor's legal rights and obligations. Consequently, the auditor may consider it appropriate to seek legal advice.

2. Auditor not engaged to report on Summary Financial Statements –

(a) The auditor may be engaged to report on the financial statements of an entity, while not engaged to report on the summary financial statements If, in this case, the auditor becomes aware that the entity plans to make a statement in a document that refers to the auditor and the fact that summary financial statements are derived from the financial statements audited by the auditor, the auditor shall be satisfied that –

1. The reference to the auditor is made in the context of the auditor's report on the audited financial statements; and
2. The statement does not give the impression that the auditor has reported on the summary financial statements.

(b) If (a) or (b) are not met, the auditor shall request management to change the statement to meet them, or not to refer to the auditor in the document. Alternatively, the entity may engage the auditor to report on the summary financial statements and include the related auditor's report in the document.

(c) If management does not (a) change the statement, (b) delete the reference to the auditor, or (c) include an auditor's report on the summary financial statements in the document containing the summary financial statements, the auditor shall advise management that the auditor disagrees with the reference to the auditor, and the auditor shall determine and carry out other appropriate actions designed to prevent management from inappropriately referring to the auditor.

Section – V		
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Standard on Review Engagements (SRE) 2400 (Revised)
Engagements to Review Financial Statements

1. Effective Date –

This SRE is effective for reviews of financial statements for periods beginning on or after **April 1, 2010**.

2. Introduction –

A practitioner, who is not the auditor of an entity, undertakes an engagement to review financial statements and on the form and content of the report that the practitioner issues in connection with such a review. Also to engagements to review other historical financial information.

3. Objective of a Review Engagement –

Review engagement is carried out with an objective to provide **negative assurance** that nothing has come to the practitioner's attention that causes the practitioner to believe that the financial statements are not prepared, in all material respects, in accordance with the applicable financial reporting framework .

4. General Principles of a Review Engagement –

Ethical principles governing the practitioner's professional responsibilities are –

(a) Independence;
(b) Integrity;
(c) Objectivity;
(d) Professional competence and due care;
(e) Confidentiality;
(f) Professional behaviour; and
(g) Technical standards.

5. Engagements to Review Financial Statements –

The practitioner should obtain sufficient appropriate evidence primarily through inquiry and analytical procedures to be able to draw conclusions.

6. Scope of a Review –

The procedures should be determined relevant professional bodies, legislation, regulation and, where appropriate, the terms of the review engagement and reporting requirements.

7. Moderate Assurance –

A review engagement provides a moderate level of assurance that the information subject to review is free of material misstatement; this is expressed in the form of negative assurance.

8. Terms of Engagement –

Matters to be included in the engagement letter –

1. The objective of the service being performed.
2. Management's responsibility for the financial statements.
3. The scope of the review,
4. Unrestricted access to whatever records, documentation and other information requested in connection with the review.

5. The anticipated form and content of the report to be issued, including the identity of the addressee of the report.
6. Non reliability of engagement to disclose errors, illegal acts or other irregularities, for example, fraud or defalcations that may exist.
7. A statement that an audit is not being performed and that an audit opinion will not be expressed.

9. Planning

The practitioner should obtain or update the knowledge of the business including consideration of the entity's organisation, accounting systems, operating characteristics and the nature of its assets, liabilities, revenues and expenses.

10. Work Performed by Others –

When using work performed by another practitioner or an expert, the practitioner should be satisfied that such work is adequate for the purposes of the review.

11. Documentation –

The practitioner should document matters which are important in providing evidence to support the review report, and evidence that the review was carried out in accordance with this SRE.

12. Procedures and Evidence –

The practitioner should apply judgment in determining the specific nature, timing and extent of review procedures. Although there is a greater risk that misstatements will not be detected in a review.

☞ **Procedures for the review of financial statements will ordinarily include the following –**

1. Obtaining an understanding of the entity's business and the industry in which it operates.
2. Inquiries concerning the entity's accounting principles, practices, data classification procedures, material assertions in the financial statements and actions taken at the meetings.
3. Analytical procedures designed to identify relationships and individual items that appear unusual. Such procedures would include –
   - ✓ Comparison of the financial statements with statements for prior periods.
   - ✓ Comparison of the financial statements with anticipated results and financial position.
   - ✓ Study of the relationships of the elements of the financial statements that would be expected to conform to a predictable pattern based on the entity's experience or industry norm.
4. Reading the financial statements to consider, on the basis of information coming to the practitioner's attention, whether the financial statements appear to conform with the basis of accounting indicated.
5. Obtaining reports from other practitioners, if any and if considered necessary, who have been engaged to audit or review the financial statements of components of the entity.
6. Inquiries of persons having responsibility for financial and accounting matters concerning, for example –
   - ✓ Whether all transactions have been recorded.
   - ✓ Whether the financial statements have been prepared in accordance with the basis of accounting indicated.
   - ✓ Changes in the entity's business activities and accounting principles and practices.
   - ✓ Matters as to which questions have arisen in the course of applying the foregoing procedures.
   - ✓ Obtaining written representations from management when considered appropriate.
7. The practitioner should inquire about events subsequent to the date of the financial statements that may require adjustment of or disclosure in the financial statements. And not after the date of the review report.

8 The practitioner should carry out additional or more extensive procedures as are necessary to be able to express negative assurance or to confirm that a modified report is required.

13. Conclusions and Reporting –

☞ **The review report should contain a clear written expression of negative assurance. Generally should contain –**

(a) Title;

(b) Addressee;

(c) Opening or introductory paragraph including –

- ✓ Identification of the financial statements on which the review has been performed; and
- ✓ A statement of the responsibility of the entity's management and the responsibility of the practitioner;

(d) Scope paragraph, describing the nature of a review, including –

- ✓ A reference to this SRE applicable to review engagements, or to relevant national standards or practices;
- ✓ A statement that a review is limited primarily to inquiries and analytical procedures; and
- ✓ A statement that an audit has not been performed, that the procedures undertaken provide less assurance than an audit and that an audit opinion is not expressed;

(e) Statement of negative assurance;

(f) Date of the report;

(g) Place of Signature;

(h) Practitioner's signature and membership number assigned by ICAI; and

(i) The Firm's registration number allotted by ICAI.

☞ **The review report should –**

(a) State that nothing has come to the practitioner's attention based on the review that causes the practitioner to believe the financial statements do not give a true and fair view (or are not presented fairly, in all material respects) in accordance with the applicable financial reporting framework (negative assurance); or

(b) If matters have come to the practitioner's attention, describe those matters that impair a true and fair view, and either –

1. Express a qualification of the negative assurance provided; or
2. When qualification is not adequate, disclose the misleading or incomplete nature of the financial statements with an adverse statement; or

(c) If there has been a material scope limitation, describe the limitation and either –

1. Express a qualification of the negative assurance provided regarding the possible adjustments to the financial statements that might have been determined to be necessary had the limitation not existed; or
2. When the possible effect of the limitation is so significant and pervasive that the practitioner concludes that no level of assurance can be provided, not provide any assurance.

Note → The practitioner should date the review report as of the date the review is completed, which includes performing procedures relating to events occurring up to the date of the report. Not earlier than the date on which the financial statements were approved by management.

Illustration 1 – Form of Unqualified Report

REVIEW REPORT TO...

We have reviewed the accompanying balance sheet of ABC Company as at March 31, 20XX, and related statement of profit and loss, and the cash flow statement for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to issue a report on these financial statements based on our review.

We conducted our review in accordance with the Revised Standard on Review Engagements (SRE) 2400, "Engagements to Review Financial Statements", issued by the Institute of Chartered Accountants of India (ICAI). This Standard requires that we plan and perform the review to obtain moderate assurance as to whether the financial statements are free of material misstatement. A review is limited primarily to inquiries of company personnel and analytical procedures applied to financial data and thus provide less assurance than an audit. We have not performed an audit and, accordingly, we do not express an audit opinion.

Based on our review, nothing has come to our attention that causes us to believe that the accompanying financial statements do not give a true and fair view (or are not presented fairly, in all material respects) in accordance with the Financial Reporting Standards.

For XYZ and Co.
Chartered Accountants
Place of Signature – **Firm's Registration Number**

Signature

Date – **(Name of the Member Signing the Audit Report)**
(Designation)
Membership Number

Illustration 2 – Review Repots Other than Unqualified

A. Qualification for a Departure from Financial Reporting Standards

REVIEW REPORT TO...

We have reviewed the accompanying balance sheet of ABC Company as at March 31, 20XX, and the related statement of profit and loss, and the cash flow statement for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to issue a report on these financial statements based on our review.

We conducted our review in accordance with the Revised Standard on Review Engagements (SRE) 2400, "Engagements to Review Financial Statements", issued by the Institute of Chartered Accountants of India (ICAI). This Standard requires that we plan and perform the review to obtain moderate assurance as to whether the financial statements are free of material misstatement. **A review is limited primarily to inquiries of company personnel and analytical procedures applied to financial data and thus provide less assurance than an audit. We have not performed an audit, and, accordingly, we do not express an audit opinion.**

Management has informed us that inventory has been stated at its cost, which is in excess of its net realisable value. Management's computation, which we have reviewed, shows that inventory, if valued at the lower of cost and net realisable value as required by Accounting Standard (AS) 2, "Valuation of Inventories" notified by the Central Government under the Companies (Accounting Standards) Rules, 2006, would have been decreased by Rs. X, and net profit and reserves would have been decreased by ₹ XXX.

Based on our review, except for the effects of the overstatement of inventory described in the previous paragraph, nothing has come to our attention that causes us to believe that the accompanying financial statements do not give a true and fair view (or are not presented fairly, in all material respects) in accordance with the aforesaid Rules, 2006.

<u>Bottom lines will be same as given in Illustration 1 of SRE</u> – <u>2400</u>

<u>Illustration 2</u> – <u>Review Repots Other than Unqualified</u>

B. <u>Adverse Report for a Departure from Financial Reporting Standards</u>

REVIEW REPORT TO...

We have reviewed the accompanying balance sheet of ABC Company as at March 31, 20XX, and the related statement of profit and loss, and the cash flow statement for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to issue a report on these financial statements based on our review.

We conducted our review in accordance with the Revised Standard on Review Engagements (SRE) 2400, "Engagements to Review Financial Statements", issued by the Institute of Chartered Accountants of India (ICAI). This Standard requires that we plan and perform the review to obtain moderate assurance as to whether the financial statements are free of material misstatement. **A review is limited primarily to inquiries of company personnel and analytical procedures applied to financial data and thus provide less assurance than an audit. We have not performed an audit and, accordingly, we do not express an audit opinion.**

As noted in note X, the Company has adopted the method of taking entire profits on construction contracts to the statement of profit and loss on entering into the contract. This has resulted in anticipating the profit in cases where the contracts have not even been commenced or where only a very minor part of the expenditure relating to the construction contracts has been incurred. This method of accounting is contrary to the requirements of Accounting Standard (AS) 7, "Accounting for Construction Contracts", notified by the Central Government under the Companies (Accounting Standards) Rules, 2006.

Based on our review, because of the pervasive effect on the financial statements of the matter discussed in the preceding paragraph, the accompanying financial statements do not give a true and fair view (or are not presented fairly, in all material respects) in accordance with the aforesaid Rules, 2006.

<u>Bottom lines will be same as given in Illustration 1 of SRE</u> – <u>2400</u>

Standard on Review Engagements (SRE) 2410
Review of Interim Financial Information Performed by the Independent Auditor of the Entity

1. Effective Date –

This SRE is effective for reviews of interim financial information for periods beginning on or after April 1, 2010.

2. Objective –

- To establish standards and provide guidance on the auditor's professional responsibilities when the auditor undertakes an engagement to review interim financial information of an audit client, and on the form and content of the report.
- Interim financial information is financial information that is prepared and presented in accordance with an applicable financial reporting framework and comprises either a complete or a condensed set of financial statements for a period that is shorter than the entity's financial year.
- This SRE is applied, adapted as necessary in the circumstances, when an entity's auditor undertakes an engagement to review historical other than interim financial information of an audit client.

3. General Principles of a Review of Interim Financial Information –

The auditor should –

(a) Comply with the ethical requirements ,

(b) Implement quality control procedures ,

(c) Plan and perform the review with an attitude of professional skepticism, .

4. Objective of an Engagement to Review Interim Financial Information

To express a conclusion whether, on the basis of the review, anything has come to the auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with an applicable financial reporting framework. A review, in contrast to an audit, is not designed to obtain reasonable assurance that the interim financial information is free from material misstatement

5. Terms of the Engagement –

Ordinarily terms of engagement are as follows –

- ✓ The objective of a review of interim financial information.
- ✓ The scope of the review.
- ✓ Management's responsibility for the
- ✓ Interim financial information,
- ✓ Internal control,
- ✓ Ensuring availability of records to the auditor and
- ✓ For providing written representations to the auditor.
- ✓ The anticipated form and content of the report to be issued, including the identity of the addressee of the report.
- ✓ The review report of entities auditor, if any.

.

6. Procedures for a Review of Interim Financial Information

☞ **Understanding the Entity and its Environment, Including its Internal Control**, so as to be able to:

1. Identify the types of potential material misstatement and consider the likelihood of their occurrence; and
2. Select the inquiries, analytical and other review procedures to update the understanding of the entity and its environment, including its internal control, ordinarily include the following –
   (a) **Reading** the documentation, of the preceding year's audit and reviews of prior interim period(s) of the current year and corresponding interim period(s) of the prior year, and
   (b) The most recent annual and comparable prior period interim financial information.

Considering –

1. Any significant risks, including the risk of management override of controls that were identified in the audit of the prior year's financial statements.
2. Materiality to assist in determining the nature and extent of the procedures to be performed and evaluating the effect of misstatements.
3. The nature of any corrected material and any identified uncorrected immaterial misstatements in the prior year's financial statements.
4. Significant financial accounting and reporting matters that may be of continuing significance such as material weaknesses in internal control.
5. The results of any audit procedures performed with respect to the current year's financial statements.
6. The results of any internal audit performed and the subsequent actions taken by management.

Inquiring –

1. The results of management's assessment of the risk that the interim financial information may be materially misstated as a result of fraud.
2. The effect of changes in the entity's business activities.
3. Any significant changes in internal control and the potential effect of any such changes .
4. The process of preparation and the reliability of the underlying accounting records .

☞ **Inquiries, Analytical and Other Review Procedures** –

(a) Reading the minutes of the meetings of shareholders, those charged with governance, and other appropriate committees and inquiring about other matters dealt with at meetings.

(b) Considering the effect, if any, of matters giving rise to a modification '

(c) Communicating, where appropriate, with other auditors

(d) Inquiring of members of management responsible for financial and accounting matters, and others as appropriate about the following, **whether –**

- ✓ It has been prepared and presented in accordance with the applicable financial reporting framework.
- ✓ There have been any changes in accounting principles or in the methods of applying them.
- ✓ Any new transactions have necessitated the application of a new accounting principle.
- ✓ It contains any known uncorrected misstatements.
- ✓ Unusual or complex situations that may have affected the interim financial information, such as a business combination or disposal of a segment of the business.
- ✓ Significant assumptions that is relevant to the fair value measurement or disclosures and management's intention and ability to carry out specific courses of action on behalf of the entity.
- ✓ Whether related party transactions have been appropriately accounted for and disclosed.

- ✓ Significant changes in commitments and contractual obligations.
- ✓ Significant changes in contingent liabilities including litigation or claims.
- ✓ Compliance with debt covenants.
- ✓ Matters about which questions have arisen in the course of applying the review procedures.
- ✓ Significant transactions occurring in the last several days of the interim period or the first several days of the next interim period.
- ✓ Knowledge of any fraud or suspected fraud affecting the entity involving –
  - ➢ Management;
  - ➢ Employees who have significant roles in internal control; or
  - ➢ Others where the fraud could have a material effect on the interim financial information.
- ✓ Knowledge of any allegations of fraud, or suspected fraud, communicated by employees, former employees, analysts, regulators, or others.
- ✓ Knowledge of any actual or possible noncompliance with laws and regulations.
- ✓ Analytical procedures may include ratio analysis and statistical techniques such as trend analysis or regression analysis.

(e) Reading the interim financial information to ensure preparation of financial information in accordance with the applicable reporting financial framework.

(f) The auditor performing the review of interim financial information is also engaged to perform an audit of the annual financial statements of the entity.

(g) Direct communication with the entity's lawyer with respect to litigation or claims.

(h) The auditor should obtain evidence.

(i) The accounting records, such as the general ledger, or a consolidating schedule that agrees or reconciles with the accounting records; and

☞ **<u>Other supporting data in the entity's records as necessary</u> –**

1. It is not necessary for the auditor to perform other procedures to identify events occurring after the date of the review report.
2. When the auditor becomes aware of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, he should –
   (a) Inquire as to plans for future actions based on its going concern the feasibility of these plans, and whether management believes that the outcome of these plans will improve the situation; and
   (b) Consider the adequacy of the disclosure about such matters in the interim financial information.
3. When a matter comes to the auditor's attention that leads the auditor to question whether a material adjustment should be made for the interim financial information to be prepared, in all material respects, in accordance with the applicable financial reporting framework, the auditor should make additional inquiries or perform other procedures to enable the auditor to express a conclusion in the review report.

☞ **<u>Evaluation of Misstatements</u> -** The auditor exercises professional judgment in evaluating the materiality of any misstatements that the entity has not corrected. But is not designed to obtain reasonable assurance that the interim financial information is free from material misstatement.

☞ **<u>Management Representations</u> - written representation from management that:**

(a) It acknowledges its responsibility for the design and implementation of internal control to prevent and detect fraud and error;

(b) Is prepared and presented in accordance with the applicable financial reporting framework;

(c) It believes the effect of the uncorrected misstatements aggregated are immaterial A summary of such items is included in or attached to the written representations;

(d) Disclosed all significant facts relating to any frauds or suspected frauds ;

(e) Disclosed the results of its assessment of the risks as a result of fraud ;

(f) Disclosed all known actual or possible noncompliance with laws and regulations and

(g) Disclosed significant subsequent events after BS date upto review date.

7. Auditor's Responsibility for Accompanying Information –

- If the auditor identifies a material inconsistency, which needs to be amended.& management refuses to make the amendment, he should consider including in the review report an additional paragraph describing the material inconsistency, or taking other actions, such as withholding the issuance of the review report or withdrawing from the engagement.

- In case of material misstatement of **fact,** the auditor should discuss the matter with the entity's management and where valid differences of judgment or opinion exist consult qualified third party. if management refuses to make the amendment, he shall consider taking further action as appropriate, such as notifying those charged with governance and obtaining legal advice.

8. Communication to the appropriate level of management.

- When, in the auditor's judgment, management does not respond appropriately within a reasonable period of time, the auditor should inform those charged with governance either orally or in writing. If the information is communicated orally, the auditor documents the communication.

- When, in the auditor's judgment, those charged with governance do not respond appropriately within a reasonable period of time, the auditor should consider –
  (a) Whether to modify the report; or
  (b) The possibility of withdrawing from the engagement; and
  (c) The possibility of resigning from the appointment to audit the annual financial statements.

- In case of the existence of fraud or non compliance by the entity with laws and communicate the matter to the appropriate level of management.

- In case of matters of governance interest communicate to those charged with governance.

9. Reporting the Nature, Extent and Results of the Review of Interim Financial

- **Information –** In written report-
  (a) An appropriate title.
  (b) An addressee, as required by the circumstances of the engagement.
  (c) Identification of the interim financial information reviewed, title of each of the statements contained in the complete or condensed set of financial statements and the date and period.
  (d) A statement that management is responsible for the preparation and fair presentation with the applicable financial reporting framework.
  (e) A statement that the auditor is responsible for expressing a conclusion on the interim financial information based on the review.
  (f) A statement that the review was done on basis of this standard.
  (g) A statement that a review is substantially less in scope than an audit.
  (h) A conclusion as to whether anything has come to the auditor's attention that causes the auditor to believe that the interim financial information does not give a true and fair view, or does not present fairly, in all material respects, in accordance with the applicable financial reporting.
  (i) The date of the report.
  (j) Place of Signature.

(k) The auditor's signature and membership number assigned by ICAI.

(l) The Firm's registration wherever applicable, as allotted by ICAI.

10. Departure from the Applicable Financial Reporting Framework –

The auditor should express a qualified or adverse conclusion .And when a qualified conclusion is not adequate to disclose the misleading or incomplete nature of the interim financial information, the auditor expresses an adverse conclusion.

11. Limitation on Scope –

When the auditor is unable to complete the review, the auditor should communicate, in writing, to the appropriate level of management and to those charged with governance the reason why the review cannot be completed, and consider whether it is appropriate to issue a report.

12. Limitation on Scope Imposed by Management –

- ✓ At first instance should not accept the engagement.
- ✓ If, after accepting the engagement, should request the removal of that limitation. On refusal communicate, in writing, to the appropriate level of management and those charged with governance the reason why the review cannot be completed.
- ✓ The auditor also considers the legal and regulatory responsibilities, to report, report the reason why the review cannot be completed.
- ✓ The auditor may also communicate material adjustments necessary a matter in the report.

13. Other Limitations on Scope –

A limitation on scope may occur due to other circumstances like limitation on the scope of annual audit. And it auditor considers whether that limitation on scope still exists and, if so, the implications for the review report.

14. Going Concern and Significant Uncertainties –

- ☞ The auditor may have modified a prior audit or review report by adding an emphasis of matter paragraph to highlight a material uncertainty relating to an event or condition that may cast significant doubt on the entity's ability to continue as a going concern.
- ☞ If not adequately disclosed, the auditor should express a qualified or adverse conclusion, as appropriate. The report should include specific reference to the fact that there is such a material uncertainty.
- ☞ The auditor should consider modifying the review report by adding a paragraph to highlight a significant uncertainty other than a going concern problem.

15. Other Considerations –

- ☞ If the management does not include the modified review report issued by auditor, then auditor shall seek legal advice to assist in determining the appropriate course of action in the circumstances, and the possibility of resigning from the appointment to audit the annual financial statements.
- ☞ The auditor shall consider whether, without a reference to the latest audited financial statements, the interim financial information is misleading in the circumstances, and the implications for the review report.

16. 16. Documentation –

Sufficient documents to provide evidence that the review was performed in accordance with this SRE and applicable legal and regulatory requirements.

Standard on Assurance Engagement (SAE) 3400
The examination of prospective financial information

- **FS Financial Statements**
- **FI Financial Information**
- **PFI Prospective Financial Information**

1. Effective Date –

This SAE is effective in relation to reports on projections/forecasts, issued **on or after April 1, 2007.**

2. Introduction –

The purpose is to establish standards and provide guidance on engagements to examine and report on PFI including examination procedures for best-estimate and hypothetical assumptions.

3. Scope –

In an engagement to examine PFI, the auditor should obtain sufficient appropriate evidence as to whether –

(a) Mgt's best-estimate assumptions on which the PFI is based are not unreasonable and, in the case of hypothetical assumptions, such assumptions are consistent with the purpose of the information;

(b) The PFI is properly prepared on the basis of the assumptions;

(c) The PFI is properly presented and all material assumptions are adequately disclosed, including a clear indication as to whether they are best-estimate assumptions or hypothetical assumptions; and

(d) The PFI is prepared on a consistent basis with historical FS, using appropriate accounting principles.

4. Definitions

1. ***"PFI"*** means FI based on assumptions about events that may occur in the future and possible actions by an entity. E.g.; forecast, a projection, or a combination of both.
2. **A *"forecast"*** means PFI prepared on the basis of assumptions as to future events which Mgt expects to take place and take action as of the date the information is prepared (best-estimate assumptions).
3. A ***"projection"*** means PFI prepared on the basis of –

   (a) hypothetical assumptions about future events and mgt actions which are not necessarily expected to take place

   (b) a mixture of best-estimate and hypothetical assumptions.

5. PFI can include FS or one or more elements of FS and may be prepared –

(a) As an internal Mgt tool, for e.g., to assist in evaluating a possible capital investment; or

(b) For the distribution/submission to third parties in, for e.g. –

- ✓ A prospectus to provide potential investors with information about future expectations.
- ✓ An annual report to provide information to shareholders, regulatory bodies and other interested parties.
- ✓ A document, for e.g., cash flow forecasts, for the information of lenders.

<u>Note</u> → Mgt is responsible for the preparation and presentation of the PFI, identification and disclosure of the sources of information, the basis of forecasts and the underlying assumptions.

6. The Auditor's Assurance Regarding PFI –

The types of evidence available in assessing the assumptions on which the PFI is based, it may be difficult for the auditor to draw opinion on such evidence hence the auditor provides only a moderate level of assurance.

7. Acceptance of Engagement –

The Auditor would consider –

- ✓ The intended use of the information;
- ✓ Whether the information will be for general or limited distribution;
- ✓ The nature of the assumptions, that is, whether they are best-estimates or hypothetical assumptions;
- ✓ The elements to be included in the information; and
- ✓ The period covered by the information.

Note → The auditor should not accept, or should withdraw from, an engagement when the assumptions are clearly unrealistic or when the auditor believes that the PFI will be inappropriate for its intended use.

8. Knowledge of the Business –

- ☞ The auditor should obtain a sufficient level of knowledge of the business to be able to evaluate whether all significant assumptions required for the preparation of the PFI have been identified. Also consider –
  - (a) The internal controls over the system used to prepare PFI and the expertise and experience of the persons preparing the PFI.
  - (b) The nature of the documentation prepared by the entity supporting Mgt's assumptions.
  - (c) The extent to which statistical, mathematical and computer-assisted techniques are used.
  - (d) The methods used to develop and apply assumptions.
  - (e) The accuracy of PFI prepared in prior periods, if any, and the reasons for any significant variances therein.
- ☞ The auditor should consider the extent to which reliance on the entity's historical FI is justified to assess whether the PFI are consistent with it.
- ☞ If the audit or review report on prior period historical FI was other than a clean report or if the entity is in a startup/ expansion phase, the auditor would consider the relevant facts and the effect on the examination of the PFI.

9. Period Covered –

The auditor should consider the period of time covered by the PFI. The period should not extend beyond the time for which Mgt has a reasonable basis for the assumptions. Some relevant factors are –

(a) The operating cycle

(b) The degree of reliability of assumptions

(c) The needs of users,

10. Examination Procedures –

When determining the nature, timing and extent of examination procedures, the auditor should consider matters such as –

(a) The knowledge obtained during any previous engagements;

(b) Mgt's competence regarding the preparation of profit;

(c) The likelihood of material misstatement;

(d) The extent to which the profit 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 stability of entity's business; and

(g) The engagement team's experience with the business and the industry in which the entity operates and with reporting on PFI.

Note → The auditor should obtain written representations from Mgt regarding the intended use of the PFI, the completeness of significant Mgt assumptions and Mgt's acceptance of its responsibility for the PFI.

11. Presentation and Disclosure –

When assessing the presentation and disclosure of the PFI and the underlying assumptions, in addition to the specific requirements of any relevant statutes, regulations as well as the relevant professional pronouncements, the auditor will need to consider whether –

(a) The presentation of PFI is informative and not misleading;

(b) The accounting policies are clearly disclosed in the notes to the PFI;

(c) The assumptions are adequately disclosed in the notes to the PFI

(d) The date as of which the PFI was prepared is disclosed.

(e) The basis of establishing points in a range is clearly indicated and the range is not selected in a biased or misleading manner when results shown in the PFI are expressed in terms of a range; and

(f) There is any change in the accounting policy of the entity from that disclosed in the most recent historical FS and whether reason for the change and the effect of such change on the PFI has been adequately disclosed.

12. Documentation –

The working papers will include the sources of information, basis of forecasts and the assumptions made in arriving the forecasts, hypothetical assumptions, evidence supporting the assumptions, Mgt representations regarding the intended use and distribution of the information, completeness of material assumptions, Mgt's acceptance of its responsibility for the information, audit plan, the nature, timing and extent of examination procedures performed, and, in case the auditor expresses a modified opinion or withdraws from the engagement, the reasons forming the basis of such decision.

13. Report on Examination of PFI –

The report by an auditor on an examination of PFI should contain the following –

(a) Title;

(b) Addressee;

(c) Identification of the PFI;

(d) Reference to the Standards on Auditing applicable to the examination of PFI;

(b) Statement that Mgt is responsible for the PFI including the underlying assumptions;

(c) When applicable, a reference to the purpose and/or restricted distribution of the PFI;

(d) 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;

(e) Statement of negative assurance as to whether the assumptions provide a reasonable basis for the PFI ;

(f) Opinion as to whether the PFI is properly prepared on the basis of the assumptions and is presented in accordance with the relevant financial reporting framework;

(g) Appropriate caveats concerning the achievability of the results indicated by the PFI;

(h) Date of report (which should be the date procedures have been completed);

(i) Place of signature; and

(j) Signature.

- When the auditor believes that the presentation and disclosure of the PFI is not adequate, the auditors should express a qualified or adverse opinion in the report on the PFI, or withdraw from the engagement as appropriate

- When the auditor believes that one or more significant assumptions do not provide reasonable basis for the PFI, the auditor should either express an adverse opinion setting out the reasons in the report on the PFI, or withdraw from the engagement.

- When the examination is affected by conditions that preclude application of one or more procedures considered necessary in the circumstances, the auditor should either withdraw from the engagement or disclaim the opinion and describe the scope limitation in the report on the PFI.

Standard on Assurance Engagement (SAE) 3402
Assurance Reports on Controls at a Service Organisation

1. Effective Date –

This SAE is applicable to all agreed upon procedures beginning **on or after 1st April 2011.**

2. Scope –

(a) This Standard on Assurance Engagements (SAE) deals with assurance engagements undertaken by a professional accountant in public practice [1] to provide a report for use by user entities and their auditors on the controls at a service organization that provides a service to user entities that is likely to be relevant to user entities' internal control as it relates to financial reporting.

(b) It complements SA 402, in that reports prepared in accordance with this SAE are capable of providing appropriate evidence under SA 402.

3. Auditor's Objectives –

To obtain reasonable assurance about whether, in all material respects, based on suitable criteria –

(a) The service organization's **description** of its system fairly presents the system as designed and implemented throughout the specified period (or in the case of a type 1 report, as at a specified date);

(b) The controls related to the control objectives stated in the service organization's description of its system were **suitably designed** throughout the specified period (or in the case of a type 1 report, as at a specified date);

(c) Where included in the scope of the engagement, the controls **operated effectively** to provide reasonable assurance that the control objectives stated in the service organization's description of its system were achieved throughout the specified period.

4. Framework for Assurance Engagement –

The "Framework for Assurance Engagements" states that an assurance engagement may be –

(a) Either a "reasonable assurance" engagement or a "limited assurance" engagement;

(b) Either an "assertion-based" engagement or a "direct reporting" engagement; and

(c) That the assurance conclusion for an assertion-based engagement can be worded either in terms of the responsible party's assertion or directly in terms of the subject matter and the criteria.

Note → This SAE only deal with assertion-based engagements that convey reasonable assurance, with the assurance conclusion worded directly in terms of the subject matter and the criteria

5. Exclusion –

(a) This SAE applies only when the service organization is responsible for, or otherwise able to make an assertion about, the suitable design of controls.

(b) This SAE does not deal with the following assurance engagements –

(i) To report only on whether controls at a S O's operated as described **(i.e. Operating Effectiveness),** or

(ii) To report only on controls at a service organization **other than those related to a service** that is likely to be relevant to user entities' internal control as it relates to financial reporting (for example, controls that affect user entities' production or quality control).

6. Definition –

S.N.	Aspects	Definition
1.	**Carve out method**	Method of dealing with the services provided by a subservice organization, whereby the service organization's description of its system includes the nature of the services provided by a subservice organization, but that subservice organization's relevant control objectives and related controls are excluded from the service organization's description of its system and from the scope of the service auditor's engagement. The service organization's description of its system and the scope of the service auditor's engagement include controls at the service organization to monitor the effectiveness of controls at the subservice organization, which may include the service organization's review of an assurance report on controls at the subservice organization.
2.	**Complementary UE Control**	Controls that the service organization assumes, in the design of its service, will be implemented by user entities, and which, if necessary to achieve control objectives stated in the service organization's description of its system, are identified in that description.
3.	**Control Objective**	The aim or purpose of a particular aspect of controls. Control objectives relate to risks that controls seek to mitigate.
4.	**Control at the S O**	Controls over the achievement of a control objective that is covered by the service auditor's assurance report.
5.	**Control at S S O**	Controls at a subservice organization to provide reasonable assurance about the achievement of a control objective.
6.	**Criteria**	Benchmarks used to evaluate or measure a subject matter including, where relevant, benchmarks for presentation and disclosure.
7.	**Inclusive Method**	Method of dealing with the services provided by a subservice organization, whereby the service organization's description of its system includes the nature of the services provided by a subservice organization, and that subservice organization's relevant control objectives and related controls are included in the service organization's description of its system and in the scope of the service auditor's engagement.
8.	**Report on the description and design of controls at a service organization referred to in this SAE as a "type 1 report")**	**<u>A report that comprises</u> –** 1. The service organization's description of its system; 2. A written assertion by the service organization that, in all material respects, and based on suitable criteria – (a) The description fairly presents the service organization's system as designed and implemented as at the specified date; (b) The controls related to the control objectives stated in the service organization's description of its system were suitably designed as at the specified date; and 3. A service auditor's assurance report that conveys reasonable assurance about the matters in 2 above.

9.	**Report on the description, design and operating effectiveness of controls at a service organization (referred to in this SAE as a "type 2 report")**	**A report that comprises –** 1. The service organization's description of its system; 2. A written assertion by the service organization that, in all material respects, and based on suitable criteria – (a) The description fairly presents the service organization's system as designed and implemented throughout the specified period; (b) The controls related to the control objectives stated in the service organization's description of its system were suitably designed throughout the specified period; and (c) The controls related to the control objectives stated in the service organization's description of its system operated effectively throughout the specified period; and 3. A service auditor's assurance report that – (a) Conveys reasonable assurance about the matters in 2. above; and (b) Includes a description of the tests of controls and the results thereof.
10.	**S O's System (or the System)**	The policies and procedures designed and implemented by the service organization to provide user entities with the services covered by the service auditor's assurance report. The service organization's description of its system includes identification of: the services covered; the period, or in the case of a type 1 report, the date, to which the description relates; control objectives; and related controls.
11.	**Test of Control**	A procedure designed to evaluate the operating effectiveness of controls in achieving the control objectives stated in the service organization's description of its system.

7. Requirements – The duties of a Professional Accountant under this SAE can be broadly classified into –

		A. Preliminary Engagement Activities
1.	**Framework for Assurance Engagement**	The service auditor shall not represent compliance with this SAE unless the service auditor has complied with the requirements of this SAE and the requirements of the Framework for Assurance Engagements.
2.	**Ethical Requirements**	The service auditor shall comply with relevant ethical requirements, including those pertaining to independence, relating to assurance engagements
3.	**Management & TCWG**	Where this SAE requires the service auditor to inquire of, request representations from, communicate with, or otherwise interact with the service organization, the service auditor shall determine the appropriate person(s) within the service organization's management or governance structure with whom to interact. This shall include consideration of which person(s) have the appropriate responsibilities for and knowledge of the matters concerned.

<table>
<tr>
<td>4.</td>
<td>Precondition for Acceptance</td>
<td>Before agreeing to accept, or continue, an engagement the service auditor shall –

(a) <u>Determine whether</u> –
(i) The service auditor has the capabilities and competence to perform the engagement;
(ii) The criteria to be applied by the service organization to prepare the description of its system will be suitable and available to user entities and their auditors; and
(iii) The scope of the engagement and the service organization's description of its system will not be so limited that they are unlikely to be useful to user entities and their auditors.

(b) Obtain the agreement of the service organization that it acknowledges and understands its responsibility</td>
</tr>
<tr>
<td>5.</td>
<td>Acceptance of a Change in the Terms of the Engagement</td>
<td>If the service organization requests a change in the scope of the engagement before the completion of the engagement, the service auditor shall be satisfied that there is a reasonable justification for the change.</td>
</tr>
<tr>
<td colspan="3">
<table>
<tr><th>Examples – Not Reasonable Justification</th><th>Examples – Reasonable Justification</th></tr>
<tr>
<td>The request is made to exclude certain control objectives from the scope of the engagement because of the likelihood that the service auditor's opinion would be modified; or the service organization will not provide the service auditor with a written assertion and the request is made to perform the engagement under Framework for Assurance Engagements.</td>
<td>The request is made to exclude from the engagement a subservice organization when the service organization cannot arrange for access by the service auditor, and the method used for dealing with the services provided by that subservice organization is changed from the inclusive method to the carve-out method.</td>
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<tr>
<td rowspan="2">6.</td>
<td>Assessing the Suitability of the Criteria</td>
<td>As required by Framework for Assurance Engagements, the service auditor shall assess whether the service organization has used suitable criteria in preparing the description of its system, in evaluating whether controls are suitably designed, and, in the case of a type 2 report, in evaluating whether controls are operating effectively.</td>
</tr>
<tr>
<td colspan="2">A. In assessing the suitability of the criteria to evaluate the service organization's description of its system, the service auditor shall determine if the criteria encompass, at a minimum –

(a) Whether the description presents how the service organization's system was designed and implemented, including, as appropriate –

1. The types of services provided, including, as appropriate, classes of transactions processed;
2. The procedures, within both information technology and manual systems, by which services are provided, including, as appropriate, procedures by which transactions are initiated, recorded, processed, corrected as necessary, and transferred to the reports and other information prepared for user entities;
3. The related records and supporting information, including, as appropriate, accounting records, supporting information and specific accounts that are used to initiate, record, process and report transactions; this includes the correction of incorrect information and how information is transferred to the reports and other information prepared for user entities;
4. How the service organization's system deals with significant events and</td>
</tr>
</table>

conditions, other than transactions;

5. The process used to prepare reports and other information for user entities;
6. The specified control objectives and controls designed to achieve those objectives;
7. Complementary user entity controls contemplated in the design of the controls; and
8. Other aspects of the service organization's control environment, risk assessment process, information system (including the related business processes) and communication, control activities and monitoring controls that are relevant to the services provided.

(b) In the case of a type 2 report, whether the description includes relevant details of changes to the service organization's system during the period covered by the description.

(c) Whether the description omits or distorts information relevant to the scope of the service organization's system being described, while acknowledging that the description is prepared to meet the common needs of a broad range of user entities and their auditors and may not, therefore, include every aspect of the service organization's system that each individual user entity and its auditor may consider important in its particular environment.

B. In assessing the suitability of the criteria to evaluate the design of controls, the service auditor shall determine if the criteria encompass, at a minimum, whether –

(a) The service organisation has indentified the risks that threaten achievement of the control objectives stated in the description of its system; and

(b) The controls identified in that description would, if operated as described, provide reasonable assurance that those risks do not prevent the stated control objectives from being achieved.

<u>Note</u> → In assessing the suitability of the criteria to evaluate the operating effectiveness of controls in providing reasonable assurance that the stated control objectives identified in the description will be achieved, the service auditor shall determine if the criteria encompass, at a minimum, whether the controls were consistently applied as designed throughout the specified period. This includes whether manual controls were applied by individuals who have the appropriate competence and authority.

B. <u>Review of Controls and Engagement Activities</u>

1.	**Materiality**	When planning and performing the engagement, the service auditor shall consider materiality with respect to the fair presentation of the description, the suitability of the design of controls and, in the case of a type 2 report, the operating effectiveness of controls.
2.	**Obtaining an Understanding of the SO's System**	The service auditor shall obtain an understanding of the service organization's system, including controls that are included in the scope of the engagement.
3.	**Obtaining Evidence Regarding the Description of Controls**	**<u>The service auditor shall –</u>** (a) **Obtain and read** the service organization's **description** of its system, (b) **Evaluate** whether those aspects of the description included in the scope of the engagement are **fairly presented**, This shall include – (i) Control objectives stated in the service organization's description of its system are reasonable in the circumstances; (ii) Controls identified in that description were implemented;

<table>
<tr><td></td><td></td><td colspan="4">(iii) Complementary user entity controls, if any, are adequately described; and
(iv) Services performed by a subservice organization, if any, are adequately described, including whether the inclusive method or the carve-out method has been used in relation to them.
(c) Determine, whether the service organization's system has been implemented. (through enquiry, observation, and inspection of records and other documentation, etc)</td></tr>
<tr><td>4.</td><td>Obtaining Evidence regarding Design of Controls</td><td colspan="4">The service auditor shall determine which of the controls at the service organization are necessary to achieve the control objectives stated in the service organization's description of its system, and shall assess whether those controls were suitably designed. This determination shall include –
(a) Identifying the risks that threaten the achievement of the control objectives stated in the service organization's description of its system; and
(b) Evaluating the linkage of controls identified in the service organization's description of its system with those risks.</td></tr>
<tr><td>5.</td><td colspan="5">Obtaining Evidence regarding Operating Effectiveness of Controls</td></tr>
<tr><td>6.</td><td>Sampling</td><td>7.</td><td>Nature and Cause of Deviations</td><td>8.</td><td>Using the Work of Internal Audit Function</td></tr>
</table>

<table>
<tr><td colspan="2">C. <u>Content of the Service Auditor's Assurance Report</u> – The Service Auditor's Assurance Report shall include the following basic elements –</td></tr>
<tr><td>1.</td><td>A Title that clearly indicates the report is an independent service auditor's assurance report.</td></tr>
<tr><td>2.</td><td>An Addressee.</td></tr>
<tr><td>3.</td><td>Identification of SO's description of its system.</td></tr>
<tr><td>4.</td><td>Identification of the criteria, and the party specifying the control objectives.</td></tr>
<tr><td>5.</td><td>A statement that the report is intended only for User Entity.</td></tr>
<tr><td>6.</td><td>Management Responsibility for the description of the system and design, control of the system.</td></tr>
<tr><td>7.</td><td>Service auditor's responsibility.</td></tr>
<tr><td>8.</td><td>A statement that the engagement was performed in accordance with SAE – 3402.</td></tr>
<tr><td>9.</td><td>A summary of the services auditor's procedures to obtain reasonable assurance.</td></tr>
<tr><td>10.</td><td>Limitations of controls in the case of a Type 2 report.</td></tr>
<tr><td>11.</td><td>The service auditor's opinion.</td></tr>
<tr><td>12.</td><td>The date of the service auditor's assurance report.</td></tr>
<tr><td>13.</td><td>The place of signature.</td></tr>
</table>

Standard on Related Services (SRS) 4400
Engagements to perform agreed upon procedures regarding financial information

1. Effective Date –

This Standard on Related Services is applicable to all agreed upon procedures beginning **on or after 1st April 2004.**

2. Introduction (Scope)–

To establish standard and provide guidance on the auditor's professional responsibilities and on the form and content of the report that the auditor issues in connection with such an engagement..

3. Meaning of Agreed Upon Procedures –

- In an engagement to perform agreed upon procedures, the auditor is engaged by the client issue a report of factual findings, based on specified subject matter of specified elements, accounts or items of a FS. For e.g. - A/c's Payable, A/c's Receivable, purchases from related parties, etc.
- This SRS may also provide useful guidance for engagement to perform agreed upon procedures regarding Non FI, provided he has adequate knowledge of the subject matter and reasonable criteria exist on which to base his findings.

4. Objective of an Agreed Upon Procedures Agreement –

- The objective of such an engagement is for the auditor to carry out procedures of an audit nature to which the auditor and the entity and any appropriate third parties have agreed and to report on factual findings.
- The auditor simply has to report the factual findings and, no assurance is expressed by him in his report. The report is restricted to those parties that have agreed to the procedures to be performed since others, unaware of the reasons for the procedures, may misinterpret the result.

5. General Principles of an Agreed Upon Procedures Agreement –

The auditor should comply with the Code of Ethics, issued by ICAI. The ethical principles are –

(a) Integrity
(b) Objectivity;
(c) Professional competence and the care;
(d) Confidentiality
(e) Professional conduct; and
(f) Technical Standards.

Note → When the auditor is not independent, a statement to that effect should be made in the report of factual findings.

6. Defining the Terms of Engagement between the Agreed Parties –

The nature to be agreed include the following –

(a) Nature of the engagement
(b) Stated purpose for the engagement

(c) Identification of the FI to which he agreed upon procedures will be applied.

(d) Nature, timing and extent of the specific procedures to be applied.

(e) Limitations on distribution of the report of factual findings. When such limitation would be in conflict with legal requirements, the auditor would not accept the engagement. The auditor should send an engagement letter documenting the key terms of the appointment

7. Planning & Documentations –

The auditor should plan the work so that an effective engagement will be performed in providing evidence to support the report of factual findings, and evidence that the engagement was carried out in accordance with this SRS and the terms of the engagement.

8. Procedures & Evidence –

The auditor carries out the procedures agreed upon and use the evidence obtained as the basis for the report of factual findings. **The procedures may includes –**

(d) Inquiry and analysis.

(e) Recompilation, comparison and other clerical accuracy checks.

(f) Observation

(g) Inspection

(h) Obtaining confirmations.

9. Reporting –

The report needs to describe the purpose and agreed upon procedures in detail to enable the extent of work performed. And also clearly mention that no audit or review work has been performed. **The report should contain –**

(a) Title

(b) Addressee (ordinarily the appointing authority);

(c) Identification of specific financial or non-financial information

(d) A statement that the procedures performed were those agreed upon with the recipient;

(e) A statement that the engagement was performed in accordance with this SRS.

(f) Identification of the purpose for which the agreed upon procedures were performed;

(g) A listing of the specific procedures performed.

(h) A description of the auditor's factual findings.

(i) A statement that procedures performed does not constitute either an audit or a review, and, as such, no assurance is expressed.

(j) A statement that had the auditor performed additional procedures, an audit or a review, other matters might have come to light that would have been reported;

(k) A statement that the report is restricted to those parties that have agreed to the procedures to be performed.

(l) A statement (when applicable) that the report relates only to the elements, accounts, items or financial or non-financial information specified and that it does not extent to the entity's FS taken as a whole;

(m) Date of the report;

(n) Place of signature;

(o) **<u>Auditor signature</u>** – The report should be signed by the auditor in his personal name. When a firm is appointed the report signed in the personal name of the auditor & M No .and the firm name.

Appendix

Illustration 1 – Engagement Letter for an Agreed-upon Procedures Engagement

Date – ______

To the Board of Directors (or other appropriate representatives of the client who engaged the auditor),

This is in reference to your letter dated ___________, appointing us to perform agreed-upon procedures in respect of ________________ ***(identify the items, e.g., sales, profit of a segment, accounts receivables, etc., of the entity).***

This letter is to confirm our understanding of the terms and objectives of our engagement and the nature and limitations of the services that we will provide.

Our engagement will be conducted in accordance with the Standard on Related Services (SRS) 4400, "Engagements to Perform Agreed-upon Procedures regarding Financial Information", issued by the Institute of Chartered Accountants of India and we will indicate so in our report.

We have agreed to perform the following procedures and report to you the factual findings resulting from our work –

(Describe the nature, timing and extent of the procedures to be performed, including specific reference, where applicable, to the identity of documents and records to be read, individuals to be contacted and parties from whom confirmations will be obtained.)

The procedures that we will perform are solely to assist you in _________________________ *(state purpose)*. Our report is not to be used for any other purpose and is solely for your information, and/ or for use by ________________ ***(in case the terms of reference so require).***

The procedures that we will perform will not constitute an audit or a review made in accordance with the generally accepted auditing standards in India and, consequently, no assurance will be expressed.

We look forward to your full cooperation and trust that you will make available to us whatever records, documentation and other information requested in connection with our engagement.

Our fees will be billed as work progresses.

Please sign and return the attached copy of this letter to indicate that it is in accordance with your understanding of the terms of the engagement including the specific procedures, which we have agreed will be performed.

For XYZ and Co.

Chartered Accountants

Signature

(Name of the Member)

(Designation)

Membership Number

Date –
Address –

Acknowledged on behalf of ABC Company by
(Signed)

Name and Title

Date –

Address –

Illustration 2 – Report of Factual Findings in Connection with Accounts Receivable

CONFIDENTIAL

Report of Factual Findings in Connection with Agreed – upon Procedures Assignment Related To Accounts Receivable

To (Those who engaged the auditor)

We have performed the procedures agreed with you and enumerated below with respect to the accounts receivable of ABC Company as at __________*(date)*, set forth in the accompanying schedules *(not shown in this example)*. Our engagement was undertaken in accordance with the Standard on Related Services (SRS) 4400, "Engagements to Perform Agreed-upon Procedures regarding Financial Information", issued by the Institute of Chartered Accountants of India. The procedures were performed solely to assist you in evaluating the validity of the accounts receivable and are summarized as follows –

1. We obtained and checked the addition of the trial balance of accounts receivable as at _________ ***(date),*** prepared by ABC Company and we compared the total to the balance in the related general ledger account.
2. We compared the attached list ***(not shown in this example)*** of major customers and the amounts outstanding at __________ ***(date)*** to the related names and amounts in the trial balance.
3. We obtained customers' statements or confirmations from customers to confirm balances outstanding at ___________ ***(date).***
4. We compared such statements or confirmations to the amounts referred to in 2 above. For amounts which did not agree, we obtained reconciliations from ABC Company. For reconciliations obtained, we identified and listed outstanding invoices, debit notes and outstanding cheques, each of which was greater than ₹ XXX. We located and examined such invoices and debit notes subsequently raised and cheques subsequently received and we ascertained that they have been rightly listed as outstanding on the reconciliations.

We report our findings below –

(a) With respect to item 1, we found the addition to be correct and the total amount to be in agreement.

(b) With respect to item 2, we found the amounts compared to be in agreement.

(c) With respect to item 3, we found there were suppliers' statements for all such customers.

(d) With respect to item 4, we found the amounts agreed, or with respect to amounts which did not agree, we found the Company had prepared reconciliations and that the debit notes, invoices and outstanding cheques over Rs. XXX were appropriately listed as reconciling items with the following exceptions –
(Detail the exceptions)

Because the above procedures do not constitute either an audit or a review made in accordance with the generally accepted auditing standards in India, we do not express any assurance on the accounts receivable as at ________ *(date)*.

Had we performed additional procedures or had we performed an audit or review of the financial statements in accordance with the generally accepted auditing standards in India, other matters might have come to our attention that would have been reported to you.

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose or to be distributed to any other parties. This report relates only to the accounts and an item specified above and does not extend to any financial statements of ABC Company, taken as a whole.

For XYZ and Co.
Chartered Accountants

Place of Signature

Signature

Date **(Name of the Member)**
(Designation)
Membership Number

Standard on Related Services (SRS) 4410

Engagements to compile financial information

1. Effective Date –

This Standard on Related Services is applicable to all compilation engagements beginning **on or after 1st April 2004.**

2. Introduction –

To establish standards on professional responsibilities of an accountant with such an engagement of work and when he issues report on the compilation.

3. Objectives of a Compilation Engagement –

The accountant has to use accounting expertise, as opposed to auditing expertise, to **Collect, Classify & Summarize** FI without the requirement to test the assertions underlying that information.

4. General Principles of a Compilation Engagement –

The accountant should comply with the "Code of Ethics" issued by ICAI. The ethical principles are-

(a) Integrity;

(b) Objectivity;

(c) Professional Competence and due care;

(d) Confidentiality;

(e) Professional conduct; and

(f) Technical Standards

Note → If the accountant is not independent, a statement to that fact should be made in the accountant's report to compilation work.

5. Responsibility of Management –

It includes –

(a) Ensuring that the financial information generated in the entity is correct, complete and reliable.

(b) Maintaining adequate accounting and other records and internal controls.

(c) Selecting and applying appropriate accounting policies.

(d) Establishing controls designed to safeguard the assets of the entity.

(e) To detect fraudulent or other dishonest conduct and to detect any fraud that occurs.

Note → The accountant should obtain an acknowledgement from the management of its responsibility for the appropriate preparation and presentation of FS or other information.

6. Defining the Terms of the Engagement –

The accountant should ensure the objective and scope of the engagement and the extent of the auditor's responsibilities. The engagement letter would include –

(a) Nature of the engagement

(b) Fact that the engagement can't be relied upon the disclose frauds or defalcations

(c) Nature of the information to be supplied by the client.

(d) Fact that the management is responsible for –

i. Accuracy and completeness of the information supplied including maintenance of adequate accounting records and internal control.

ii. Preparation and presentation of FS in accordance with applicable laws.

iii. Safeguarding the assets of the entity and preventing and detecting fraud and other irregularities.

iv. Ensuring that activities of the entity are carried in accordance with applicable laws and regulations.

v. Ensuring complete disclosure of all material and relevant information to the accountant.

(e) Intended use and distribution of the information, once compiled.

(f) Basic of accounting on which financial information is to be compiled.

(g) The fact that the management is responsible to the users for the information to be compiled by the accountant.

(h) Basis on which fees would be computed and any billing arrangements.

(i) Request for the client to confirm the forms of engagement by acknowledging the receipt of the engagement letter.

7. *Planning & Documentation –*

The accountant should plan the work so that an effective engagement will be performed. He should document matters which are important in providing evidence that the engagement was carried out in accordance SRS.

8. *Procedures –*

(a) The accountant should obtain a general knowledge of the business and operation of the entity and should be familiar with the accounting and practice of the industry in which the entity operates.

(b) He should be familiar with the form and the content of FS / other FI which is appropriate in the circumstances.

(c) He should request mgt representation letter covering significant information or explanations given orally on which he considers representations are required.

(d) If he becomes aware that the information supplied by mgt is incorrect, incomplete or unsatisfactory, he should consider performing additional procedures, e.g. making inquiries, assessing internal controls, etc.

(e) If the management refuses to provide additional information, he should withdraw from the engagement.

(f) He should read the compiled information and consider whether it appears to be appropriate in form and free from obvious material misstatements. Else disclose the departures.

9. *Special Considerations –*

(a) **Clients having an Identified Reporting Framework** – in this case, the accountant should ensure that FS or other FI compiled comply with the requirements of the identified financial reporting framework. If case of any material departure, the fact should be stated in the notes to the Accounts and report of compilation.

(b) **Clients having no Identified Financial Reporting Framework** – Since A/c's are normally assumed to be compliant with the generally accepted accounting practices, including the ASs issued by ICAI, the different basis should be set out in the Notes to A/c's and report of compilation.

(c) **Non-Compliance with the Accounting Standards** – If the accountant becomes aware of material non-compliance with the relevant ASs, the same shall be rectified by Mgt, if not; it should be included in the Notes to the A/c's and the compilation report of the accountant.

(d) **Accounting Estimates made by Clients** – If it appears that certain estimates made by the client are unreasonable, the accountant should draw these to the attention of the mgt for consideration.

10. Reporting on Compilation Engagement –

It is essential that the accountant clearly brings out the nature of work with the FS and the nature of work performed by him. The report on compilation should be in following lay out –

(a) **Title** – The title should be "Accountant's Report on compilation of unaudited Financial Statements" (and not "Auditor's Report").

(b) **Addressee –** The report should be addressed to the appointing authority.

(c) Identification of the FI.

(d) When relevant, a statement that the accountant is not independent of the entity.

(e) A statement that Mgt is responsible for –

- (i) Completeness and accuracy of the underlying data and complete disclosure of all material and relevant information.
- (ii) Maintaining adequate accounting and other records and internal control.
- (iii) Selecting and applying appropriate accounting policies.
- (iv) Preparation of FS and other information in accordance with applicable laws and regulations, if any.
- (v) Establishing controls to safeguard the assets of the entity and preventing and detecting fraud or other irregularities.
- (vi) Establishing controls for ensuring that activities of the enterprise and carried out in accordance with applicable laws and regulations.

(f) A statement that the engagement was performed in accordance with SRS

(g) A statement that neither an audit nor a review has been carried out and that according no assurance is expressed on the FI.

(h) Date of report

(i) Place of signature, and

(j) **Accountant's signature** – the report should be signed by the accountant in his personal name. Where a firm is appointed, the report should be signed in the personal name of the accountant and in the name of the firm. The membership number assigned by ICAI should be mentioned.

Appendix

Illustration 1 – Engagement Letter for an Compilation Engagement

Date – ______

To the Board of Directors (or other appropriate representatives of senior management),

You have, vide your letter dated _________ requested that we compile the balance sheet of __________ (name of the company) as at ___________ (date) and the related profit and loss account and the (cash flow statement) for the year ended on that date. We are pleased to confirm our acceptance and understanding of the engagement by means of this letter. As no audit or review engagement procedures would be carried out, no opinion on the financial statements will be expressed. Further, our engagement cannot be relied upon to disclose whether frauds or defalcations, or illegal acts exist. However, we will inform you of any such matters which might come to our attention in the course of the engagement.

As management, you are responsible for –

(a) The accuracy and completeness of the information supplied to us, including maintenance of adequate accounting records and internal controls and selection and application of appropriate accounting policies.

(b) Preparation and presentation of the financial statements of the entity, in accordance with the applicable laws and regulations, if any.

(c) Safeguarding the assets of the entity and also establishing appropriate controls designed to prevent and detect fraud and other irregularities.

(d) Ensuring that the activities of the entity are carried in accordance with applicable laws and regulations and that it institutes appropriate controls to prevent and detect any non-compliance.

You will confirm that events and transactions are recorded in accordance with the applicable Accounting Standard(s), issued by the Institute of Chartered Accountants of India and other recognised accounting principles and practices and inform us of any departures therefrom.

As part of our normal procedures, we may request you to provide written confirmations of any information or explanations given to us orally during the course of our work.

We understand that the intended use and distribution of the information we have compiled is ________________ (Specify).

We look forward to full cooperation with your staff and we trust that they will make available to us whatever records, documentation and other information requested in connection with our engagement.

Our fee will billed as the work progresses.

Please sign and return the attached copy of this letter to indicate that it is in accordance with your understanding of the arrangements for our compilation of your financial statements.

Bottom lines will be same as given in Illustration 1 of SRS – 4400

Illustration 2 –Report on compilation of Financial Statements

Accountant's Report on Compilation of Unaudited Financial Statements.

To…….

On the basis of the accounting records and other information and explanations provided to us by the management, we have compiled, the unaudited balance sheet of ……………….*(name of the entity)* as at March 31, XXXX and the related profit and loss account and the cash flow statement[6] for the period then ended.
The management of the _________ *(name of the entity)* is responsible for –

(a) Completeness and accuracy of the underlying data and complete disclosure of all material and relevant information to the accountant.

(b) Maintaining adequate accounting and other records and internal controls and selecting and applying appropriate accounting policies;

(c) Preparation and presentation of financial statements in accordance with the applicable laws and regulations, if any.

(d) Establishing controls to safeguard the assets of the entity and preventing and detecting frauds or other irregularities.

(e) Establishing controls for ensuring that the activities of the entity are carried out in accordance with the applicable laws and regulations and preventing and detecting any non compliance.

The compilation engagement was carried out by us in accordance with the Standard on Related Services (SRS) 4410 , "Engagements to Compile Financial Information", issued by the Institute of Chartered Accountants of India.

The balance sheet and the profit and loss account are in agreement with the books of account. We have not audited or reviewed these financial statements and accordingly express no opinion thereon.

Bottom lines will be same as given in Illustration 2 of SRS – 4400

Some Past Attempts Questions

S.N.	Questions	Marks and Attempt	Answer
1.	You are appointed to **compile financial statements of Y & Co. for tax purposes.** During the course of work, you learn that the inventory is grossly understated. On pointing the same, the partners of Y & Co. tell you that since you are not conducting an audit, the said figures duly certified by the firm should be accepted. Comment.	[5 Marks] [June 2009]	**Refer Point No. 8 (d) & (e) & 9 (c) on Page no. 28**
Ans.	According to SRS 4410, "Engagement to Compile Financial Information" if an accountant becomes aware of material misstatements, the accountant should persuade (convince) the **management to carry out necessary amendments** in the financial statements or other compiled financial information. If such amendments are **not made** and the financial statements are still considered to be misleading the accountant should **withdraw** from the engagement. **Hence, in this case, there is a clear violation of SRS 4410.**		
2.	Write short note on **Reporting on compilation engagement.**	[4 Marks] [Nov. 2006]	**Refer Point No. 10 on Page no. 29**
3.	While compiling the financial statements of a concern, you observed that the **input information supplied by the concern is incomplete, incorrect and few of the Accounting Standards have not been followed.** Describe, in brief, the procedure you will follow in the above.	[5 Marks] [May 2005]	**Refer Point No. 8 (d) & (e) & 9 (c) on Page no. 28**
4.	As a chartered accountants firm **draft an engagement letter** to the Board of Directors **for the compilation of financial statements** of XYZ Ltd. as at 31.3.2014.	[16 Marks] [May 2007]	**Refer appendix Illustration–1 on Pg. no. 30**