

STANDARDS OF AUDITING (SA) ISSUED BY ICAI

HIGHLIGHTS OF STANDARDS ON AUDITING (SA) ISSUED BY THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

SA 200: Basic Principles Governing an Audit

Auditor, while carrying out independent audit of the financial statements should adhere to the basic principles governing an audit. These principles are integrity, objectivity and independence, confidentiality, skills and competence, work performed by others, documentation, planning, audit evidence, accounting system and internal control, and, audit conclusions and reporting.

SA 200A: Objective and Scope of the Audit of Financial Statements

Objective of an independent audit is to enable the auditor to express an opinion on the financial statements as to whether they reflect true and fair view of financial position and operating results of the enterprise and the state of affairs of the enterprise.

The primary responsibility for preparation of books of accounts is of management. The scope of audit is determined by audit engagement, pronouncements of the Institute of Chartered Accountants of India (ICAI) and legal and regulatory requirements. Auditor's opinion does not assure of future viability of the enterprise.

SA 210: Terms of Audit Engagement

Auditor and client should agree on terms of engagement. Agreed terms would need to be recorded in an audit engagement letter or other suitable form of contract. This SA is intended to assist the auditor in preparation of engagement letters relating to audits and other related services. The form and content of audit engagement letter may vary for each client, but it would generally include reference to objectives of audit; Management's responsibility for financial statements, selection and application of appropriate accounting policies and accounting standards; Making judgments and estimates, maintenance of adequate accounting records and internal controls; scope of audit: fact that due to inherent limitations of audit there is an unavoidable risk of non detection of some material misstatements. Other matters as per the circumstances should also be included. In case of recurring audits, auditor should consider whether circumstances require the terms of engagement to be revised. Where the terms of engagement are changed, auditor and client should agree on the new terms. If auditor is unable to agree to a change of engagement and is not permitted to continue the original engagement, the auditor should consider withdrawing from the engagement.

SA 220: Quality Control for Audit Work

Quality control policies and procedures should be implemented at both level – of audit firm and on individual audits.

Audit firm should implement quality control policies and procedures designed to ensure that all audits are conducted in accordance with Standards of Auditing. Objectives of quality control policies to be adopted will incorporate Professional Requirements, Skills and Competence, Assignment, Delegation, Consultation, Acceptance and Retention of Clients, Monitoring. The firm's general quality control policies and procedures should be communicated to its personnel in a manner that provides reasonable assurance that the policies and procedures are understood and implemented. Auditor should implement those quality control procedures which are, in the context of policies and procedures of the firm, appropriate to individual audit. Auditor should consider professional competence of assistants performing work delegated to them when deciding extent of direction, supervision and review appropriate for each assistant. Assistants to whom work is delegated need appropriate direction, supervision and review of audit work performed by them.

SA 230: Audit Documentation

Audit documentation that meets the requirements of this SA and the specific documentation requirements of other relevant SAs provides:

- a. Evidence of auditor's basis for a conclusion about the achievement of overall objective of audit; and
- b. Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.

Audit Documentation refers to the record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached. Preparing sufficient and appropriate audit documentation on a timely basis helps to enhance the quality of audit and facilitates effective review and evaluation of audit evidence obtained and conclusions reached before finalizing auditor's report. Auditor should document discussions of

significant matters with management, those charged with governance, and others, including the nature of significant matters discussed and when and with whom the discussions took place. Auditor may consider preparing and retaining a summary (Completion Memorandum) that describes significant matters identified during the audit and how they were addressed. SA 220 requires auditor to review audit work performed through review of audit documentation. Standards on Quality Control (SQC) 1 require firms to establish policies and procedures for timely completion of audit files. An appropriate time limit within which to complete the assembly of final audit file is ordinarily not more than 60 days after the date of auditor's report. SQC 1 requires firms to establish policies and procedures for retention of engagement documentation. Retention period for audit engagements ordinarily is no shorter than ten years from the date of auditor's report, or, if later, the date of group auditor's report

SA 240: The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements

Auditor is concerned with fraud that causes a material misstatement in financial statements. Two types of intentional misstatements are relevant – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets. Although auditor may suspect or, in rare cases, identify occurrence of fraud, auditor does not make legal determinations of whether fraud has actually occurred. Primary responsibility of prevention and detection of frauds is of the management as well as those charged with governance. It is important that management, with oversight of those charged with governance; place a strong emphasis on fraud prevention. Auditor is responsible for obtaining reasonable assurance that financial statement taken as a whole are free from material misstatement, whether caused by fraud or error. While auditor may be able to identify potential opportunities for fraud to be perpetrated, it is difficult for him to determine whether misstatements in judgment areas such as accounting estimates are caused by fraud or error. Risk of 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. Therefore, when planning and performing audit procedures and evaluating and reporting the results thereof, auditor should consider the risk of material misstatements in financial statements resulting from fraud. 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. SA 315 requires a discussion among engagement team members which shall place particular emphasis on how and where entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud might occur. 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. Auditor shall identify and assess risks of material misstatement due to fraud at financial statement level, and at assertion level for classes of transactions, account balances and disclosures. Auditor must make appropriate inquiries of the management. Auditor must discuss with those charged with governance as they have oversight responsibility for systems for accounting risk, financial control and compliance with the law.

When auditor encounters circumstances that may indicate that there is a material misstatement in financial statements resulting from fraud, s/he should perform procedures to determine whether financial statements are materially misstated.

When auditor identifies a misstatement, s/he should consider whether such a misstatement may be indicative of fraud and if there is such an indication, s/he should consider the implications of misstatement in relation to other aspects of the audit, particularly the reliability of management representations.

When the auditor identifies a misstatement resulting from fraud, or a suspected fraud, s/he should consider auditor's responsibility to communicate that information to management, those charged with governance and, in some circumstances, when so required by laws and regulations, to regulatory and enforcement authorities also. Auditor should obtain written representations from management. The auditor shall document the understanding of entity and its environment and the assessment of risks of material misstatement, responses to assessed risks of material misstatement and communications about fraud made to management, those charged with governance, regulators and others. 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 engagement, auditor shall document reasons for that conclusion.

SA 250: CONSIDERATION OF LAWS AND REGULATIONS IN AN AUDIT OF FINANCIAL STATEMENTS

Auditor should recognise that non-compliance by entity with laws and regulations may materially affect financial statements. It is management's responsibility to ensure that entity's operations are conducted in accordance with laws and regulations. Auditor is not responsible for preventing non-compliance. Auditor should plan and perform the audit recognising that it may reveal conditions or events that would lead to questioning whether an entity is complying with laws and regulations. Risk of non detection of material misstatements is higher with regard to material misstatements resulting from non-compliance with laws and regulations due to various factors. Auditor should obtain a general understanding of legal and regulatory framework applicable to the entity and how it is complying with that framework. After obtaining general

understanding, auditor should perform procedures to identify instances of non-compliance with these laws and regulations where non-compliance should be considered when preparing financial statements. Further, auditor should obtain sufficient appropriate audit evidence about compliance with those laws and regulations generally recognised by Auditor to have an effect on determination of material amounts and disclosures in financial statements. Auditor should obtain written representations that management has disclosed all known actual or possible non-compliance with laws and regulations whose effects should be considered when preparing financial statements. This SA does not apply to other assurance engagements in which auditor is specifically engaged to test and report separately on compliance with specific laws and regulations. Whether an act constitutes a non-compliance can be determined only by a court of law. The Standard envisages "engaging a legal advisor to assist in monitoring legal requirements" instead of "establishing a legal department" as one of the policies to ensure compliance with laws and regulations. The Standard, in larger entities, also envisages existence of a separate "compliance function" in addition to internal audit function and audit committee to supplement policies and procedures for ensuring compliance with laws and regulations.

SA 260: Communication With those Charged With Governance

The auditor shall communicate with those charged with governance, auditor's responsibilities in relation to financial statements audit, an overview of planned scope and timing of audit and significant findings from the audit. Auditor shall communicate to those charged with governance, auditor's responsibilities in relation to the financial statements audit, audit matters, as also significant difficulties encountered during audit. Such matters include: Overall scope of audit; selection of/ changes in significant accounting policies; potential effect on financial statements of any significant risks and exposures, such as pending litigation; adjustments to financial statements arising out of audit that have a significant effect on entity's financial statements; material uncertainties related to events and conditions that may cast significant doubt on entity's ability to continue as a going concern, disagreements with management about matters that could be significant to entity's financial statements or auditor's report; expected modifications to auditor's report. Auditors should communicate matters of governance interest on timely basis. Auditor's communication may be made orally or in writing. In case of oral communication, auditor should document their oral communications and response thereof

SA 299: Responsibility of Joint Auditors

Where joint auditors are appointed, they should, by mutual discussion, divide audit work among themselves. Division of work would usually be in terms of audit of identifiable units or specified areas. In some cases, due to the nature of business of entity under audit, such a division of work may not be possible. In such situations, division of work may be with reference to items of assets or liabilities or income or expenditure or with reference to periods of time. Where, in the course of his work, a joint auditor comes across matters which are relevant to areas of responsibility of other joint auditors and which deserve their attention, or which require disclosure or discussion with, or application of judgment by, other joint auditors, he should communicate the same to all other joint auditors in writing prior to finalisation of audit. Certain areas of work, owing to their importance or owing to the nature of work involved, would often not be divided and would have to be covered by all joint auditors. Each joint auditor is responsible only for the work allocated to them, whether or not s/he has prepared a separate report on work performed by them. All joint auditors are jointly and severally responsible in respect of the audit work which is not divided amongst them. For examining that the financial statements of the entity comply with disclosure requirements of relevant statute, for ensuring that audit report complies with the requirements of relevant statute and in respect of matters which are brought to the notice of joint auditors by any one of them and on which there is an agreement among joint auditors. Each joint auditor is entitled to assume that other joint auditors have carried out their part of audit work in accordance with generally accepted audit procedures. Normally, joint auditors are able to arrive at an agreed report. However, where joint auditors are in disagreement with regard to any matters to be covered by the report, each one of them should express their own opinion through a separate report

SA 300: Planning an Audit of Financial Statements

Planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. The objective of auditor is to plan the audit so that it will be performed in an effective manner. Once the overall audit strategy has been established, an audit plan can be developed to address various matters identified in the overall audit strategy, considering the need to achieve the audit objectives through efficient use of auditor's resources. Auditor should consider various matters in developing the overall plan like: terms of engagement; nature and timing of reports; applicable legal or statutory requirements; accounting policies adopted by the client; identification of significant audit areas; setting of materiality levels, etc. Auditor needs to obtain a level of knowledge of client's business that will enable them to identify events, transactions and practices that, in their judgment, may have a significant effect on financial information. Audit plan is more detailed than overall audit strategy that includes the nature, timing and extent of audit procedures to be performed by engagement team members. Engagement partner and other key members of engagement team shall be involved in planning the audit, including planning and participating in the discussion among engagement team members so as to enhance effectiveness and efficiency of planning process. Auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and review of their work. Auditor shall document overall audit strategy, audit plan and any significant changes made during

audit engagement to the overall audit strategy or audit plan, and reasons for such changes.

Audit planning ideally commences at the conclusion of previous year's audit, and along with related programme, it should be reconsidered for modification as the audit of their compliance and substantive procedures progress. For an initial audit, auditor may need to expand the planning activities because the auditor does not ordinarily have previous experience with the entity that is considered when planning recurring engagements

SA 310: KNOWLEDGE OF THE BUSINESS

Auditor should obtain knowledge of the business in performing an audit of financial statements, sufficient to enable the auditor to identify and understand events, transactions and practices that, in auditor's judgment, may have a significant effect on financial statements or on examination or audit report. Such knowledge is used by the auditor in assessing inherent and control risks and in determining the nature, timing and extent of audit procedures. Obtaining required knowledge of business is a continuous and cumulative process of gathering and assessing information and relating the resulting knowledge to audit evidence and information at all stages of audit. Preliminary knowledge is obtained prior to acceptance of engagement. More detailed knowledge is obtained after acceptance. Auditor can obtain knowledge of the industry and entity from a number of sources. Understanding business and using this information appropriately assists the auditor in assessing risks and identifying problems, planning and performing audit effectively and efficiently and evaluating audit evidence

SA 315: Understanding the Entity and its Environment and Assessing the Risk of Material Misstatement

Auditors cannot approach their work with a fixed audit program which they expect will work in all circumstances. They must understand their client, identify and assess audit risk, and plan their work accordingly. SA 315 deals with understanding and assessing risk.

To provide a basis for identification and assessing of risks of material misstatement, the auditor shall perform risk assessment procedures. Thus procedures shall include: Inquires with management; Analytical Procedures; Observation and Inspection.

Where Auditor has performed other engagements with the entity, auditor shall consider whether information obtained is relevant for identifying the risk of material misstatement.

Also, if Auditor intends to use his previous experiences with the entity, he shall determine whether changes have occurred since previous audit that may affect its relevance on current audit.

Auditor shall obtain an understanding of the following: Industry, regulatory and other external factors; Nature of entity; Objectives and strategies and related business risks; Measurement and review of entity's financial performance; Internal control.

SA 315 sets out five components of Internal control: Control environment; Entity's risk assessment process; the information system, including related business processes, relevant to financial reporting and communication; Control activities; Monitoring controls.

Usually, those controls which pertain to entity's objective of preparing financial statements are subject to risk assessment procedures.

Obtaining an understanding of entity and its environment including entity's internal control is a continuous, dynamic process of gathering, updating and analyzing information through out the audit.

Auditor should identify and assess risks of material misstatement at financial statement level, and at assertion level for classes of transactions, account balances and disclosures

Auditors are required to: Relate identified risks to what can go wrong at assertion level; Consider potential magnitude of risks in the context of financial statements; Consider the likelihood that risks could result in a material misstatement of financial statements.

Documentation should cover: Discussion among engagement team; Key elements of understanding obtained; Sources of information; Risk assessment process; the identified and assessed risks; Significant risks evaluated; Risks evaluated for which substantive procedures done.

Auditor uses professional judgment to determine the extent of understanding required. Auditors primary consideration is whether the understanding that has been obtained is sufficient to meet the objective stated in the SA

SA 320: Audit Materiality

Information is material if its misstatement (i.e. omission or erroneous statement) could influence economic

decisions of users taken on the basis of financial information. Materiality depends on size and nature of item, judged in particular circumstances of its misstatement. Concept of materiality recognises that some matters, either individually or in aggregate, are relatively important for true and fair presentation of financial information in conformity with recognised accounting policies and practices. Auditor considers materiality at both, overall financial information level and in relation to individual account balances and classes of transactions. Materiality may also be influenced by other considerations, such as legal and regulatory requirements, non-compliance with which may have a significant bearing on financial information, and considerations relating to individual account balances and relationships. Materiality should be considered by the auditor when determining the nature, timing and extent of audit procedures and while evaluating the effect of misstatements. There is an inverse relation between materiality and audit risk. Auditor takes this relationship into account when determining nature, timing and extent of audit procedures. Auditor's assessment of materiality and audit risk may be different at the time of initially planning the engagement from that at the time of evaluating results of their audit procedures. Auditor may, in planning audit work, intentionally set acceptable cut off level for verifying individual transactions at a lower level than is intended to be used to evaluate results of the audit. In forming his/ her opinion on financial information, auditor should consider whether effect of aggregate uncorrected misstatements on financial information is material. If the aggregate of uncorrected misstatements that the auditor has identified approaches materiality level, or if auditor determines that aggregate of uncorrected misstatements causes financial information to be materially misstated, s/he should consider requesting management to adjust financial information or extending their audit procedures

SA 330: The Auditor's Responses to Assessed Risks

This Standard deals with auditor's responsibility to design and implement responses to risks of material misstatement identified and assessed by the auditor in accordance with SA 315, in a financial statement audit. The objective is to obtain sufficient appropriate audit evidence about assessed risks of material misstatement, through designing and implementing appropriate responses to those risks.

Auditor shall design and implement overall responses to address assessed risks of material misstatement at financial statement level.

Auditor shall design and perform further audit procedures whose nature, timing and extent are based on and are responsive to assessed risks of material misstatement at assertion level.

In designing further audit procedures to be performed, the auditor shall:

- a. Consider reasons for the assessment given to risk of material misstatement at the assertion level for each class of transactions, account balance, and disclosure
- b. Obtain more persuasive audit evidence the higher the auditor's assessment of risk

When the auditor obtains audit evidence about 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 additional audit evidence to be obtained for the remaining period

Based on the audit procedures performed and audit evidence obtained, auditor shall evaluate before conclusion of audit whether assessments of risks of material misstatement at assertion level remain appropriate.

Auditor shall conclude whether sufficient appropriate audit evidence has been obtained. In forming an opinion, auditor shall consider all relevant audit evidence, regardless of whether it appears to corroborate or contradict assertions in financial statements.

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, auditor shall express a qualified opinion or a disclaimer of opinion.

If Auditor plans to use audit evidence about operating effectiveness of controls obtained in previous audits, auditor shall document conclusion reached about relying on such controls that were tested in a previous audit.

SA 402: Audit Considerations relating to Entities using Service Organisations

Auditor should consider how a service organisation affects client's accounting and internal control systems so as to plan the audit and develop an effective audit approach. The policies and procedures established and executed by service organisations are physically and operationally separate from client's organisation. When service organisation executes client's transactions and maintains accountability, the client may deem it necessary to rely on policies and procedures of the service organisation. If the auditor concludes that activities of service organisation are significant to the entity and relevant to audit, auditor should obtain sufficient

information to understand accounting and internal control systems of service organisation and to assess control risk. When using a service organisation auditor's report, auditor should consider the nature and content of that report. The report of the service organisations auditor will ordinarily be one of two types: Type A – Report on Suitability of Design – giving an understanding of accounting and internal control systems installed by service organisation; Type B – Report on Suitability of Design and Operating Effectiveness – giving an understanding of accounting and internal control systems installed by service organisation and effectiveness of such system.

SA 500: Audit Evidence

Auditor is required to obtain sufficient appropriate audit evidence to enable them to draw reasonable conclusions on which they can base their opinion on financial information. Auditor normally relies on evidence that is persuasive rather than conclusive in nature. Auditor may obtain evidence on a selective basis by way of either judgmental or statistical sampling procedures. Evidence is obtained through performance of compliance and substantive procedures. Compliance procedures are tests designed to obtain reasonable assurance that internal controls on which audit reliance is placed are in effect. Substantive procedures are designed to obtain evidence as to completeness, accuracy and validity of data produced by accounting system. Obtaining audit evidence from compliance procedures is intended to reasonably assure the auditor in respect of assertions of existence, effectiveness and continuity. Obtaining audit evidence from substantive procedures is intended to reasonably assure the auditor in respect of assertions of existence, rights and obligations, occurrence, completeness, valuation, measurement, presentation and disclosure. To test the reliability, few generalisations are useful such as external evidence is more reliable than internal evidence, written evidence is more reliable than oral evidence and self obtained evidence is more reliable than obtained through the entity. Auditor gains increased assurance when audit evidence obtained from different sources is consistent. Various methods for obtaining audit evidence include inspection, observation, inquiry and confirmation, computation and analytical review. Emphasis is to be laid on considering relevance and reliability of audit evidence obtained during the course of audit, and focus is to be laid on designing and performing audit procedures to obtain relevant and reliable audit evidence.

SA 501: Audit Evidence – Additional Consideration for Specific Items

The objective of this standard is to establish standards on auditor's responsibilities, audit procedures and provide guidance, in addition to that provided in SA 500, "Audit Evidence", with respect to certain specific financial statement amounts and other disclosures. It provides guidance with respect to definition, procedures, management representations and audit conclusions and reporting for each of following parts. This standard assists the auditor to obtain audit evidence with respect to following aspects:

Part A: Attendance at Physical Inventory Counting

Management ordinarily establishes procedures under which inventory is physically counted at least once in a year to serve as a basis for preparation of financial statements or to ascertain reliability of perpetual inventory system. When inventory is material to financial statements, auditor should obtain sufficient appropriate audit evidence regarding its existence and condition by attendance at physical inventory counting unless impracticable. If unable to attend physical inventory count on the date planned due to unforeseen circumstances, auditor should take or observe some physical counts on an alternative date and where necessary, perform alternative audit procedures to assess whether changes in inventory between date of physical count and period end date are correctly recorded.

Part B: Inquiry regarding Litigation and claims

Auditor should carry out audit procedures in order to become aware of any litigation and claims involving the entity which may have a material effect on the financial statements. The letter seeking direct communication with entity's lawyers and such other professionals to whom the entity engages for litigation and claims should be prepared by management. If management refuses to give the auditor permission to communicate with entity's lawyers, this would constitute a limitation on the scope of auditor's work.

Part C: Valuation and Disclosure of Long Term Investments

Audit procedures regarding long-term investments ordinarily include obtaining audit evidence with respect to their ownership and existence as to whether the entity has the ability to continue to hold investments on a long term basis and discussing with management whether the entity will continue to hold investments as long-term investments and obtaining written representations to that effect.

Part D: Segment Information

Auditor considers segment information in relation to financial statements taken as a whole, and is not required to apply auditing procedures that would be necessary to express an opinion on segment information standing alone. Audit procedures regarding segment information ordinarily consist of analytical procedures and other audit tests appropriate in the circumstances.

SA 505: External Confirmations

External confirmation is the process of obtaining and evaluating audit evidence through a direct communication from a third party in response to a request for information about a particular item. Before making use of external confirmations, auditor should consider materiality, the assessed level of inherent and control risk, and how the evidence from other planned audit procedures will reduce audit risk to an acceptably low level. Auditor should employ external confirmation procedures in consultation with the management. External confirmations are mostly sought for account balances and their components but they are not to be restricted to these items only. The use of confirmation procedures may be effective in providing sufficient appropriate audit evidence when auditor determines higher level of assessed inherent and control risk. The request for confirmations is to be made either at the date of financial statements or at a date close to it. Requests are to be designed to specific audit objectives. Auditor's understanding of client's arrangements and transactions with third parties is important in determining the information to be confirmed. Auditor may use positive or negative external confirmation requests or a combination of both. The former request asks the respondent to reply to Auditor in all cases either by indicating respondent's agreement with the given information, or by asking the respondent to fill in information. Latter asks the respondent to reply only in the event of disagreement with information provided in the request. Auditor should perform alternative procedures where no response is received to a positive external confirmation request. Auditor should consider whether there is any indication that external confirmations received may not be reliable. Auditor should evaluate the conformity between results of external confirmation process together with results from any other procedures performed. If Auditor seeks for an external confirmation and management requests the auditor not to do so, auditor should consider whether there are valid grounds for such a request and obtain evidence to support validity of management's requests.

SA 510: Initial Audit Engagements – Opening Balances

This Standard deals with auditor's responsibilities relating to opening balances when conducting an initial audit engagement. In conducting an initial audit engagement, the auditor should obtain sufficient appropriate audit evidence that closing balances of preceding period have been correctly brought forward to current period, the opening balances do not contain misstatements that materially affect financial statements for the current period and appropriate accounting policies are consistently applied. Auditor should consider whether accounting policies followed in preceding period, based on which opening balances have been arrived at, were appropriate and that those policies are consistently applied. If the auditor concludes that the accounting policies have not been consistently applied or properly accounted for, the auditor has to express either a qualified or adverse opinion, as may be appropriate. Ordinarily, current auditor can place reliance on closing balances contained in financial statements for preceding period, except when during performance of audit procedures for current period the possibility of misstatements in opening balances is indicated. If the auditor concludes that a misstatement exists in the current period's financial statements, the auditor requires communicating the same to the appropriate level of management and those charged with governance. When financial statements of preceding period were not audited, auditor must adopt other procedures such as for current assets and liabilities. Some audit evidence can ordinarily be obtained as part of audit procedures performed during the current period and for non-current assets and liabilities such as fixed assets, investments and long-term debt, the auditor could ordinarily examine records underlying the opening balances. The auditor should evaluate matters giving rise to modifications in prior period's financial statements for assessing the risk of material misstatements.

SA 520: Analytical Procedures

Auditor should apply analytical procedures at the planning and overall review stages of audit. Analytical procedures are analysis of significant ratios and trends including resulting investigation of fluctuations and relationships that are inconsistent with other relevant information or which deviate from predicted amounts. Auditor should apply analytical procedures at planning and overall review stages of audit as well as while applying substantive procedures. Analytical procedures in planning the audit use both financial and non-financial information. Application of analytical procedures is based on the expectation that relationships among data exist and continue in absence of known conditions to the contrary. Presence of these relationships provides audit evidence as to completeness, accuracy and validity of data produced by the accounting system. However, reliance on results of analytical procedures will depend on auditor's assessment of the risk that analytical procedures may identify relationships as expected when, in fact, a material misstatement exists. When analytical procedures identify significant fluctuations or relationships that are inconsistent with other relevant information or that deviate from predicted amounts, the auditor should investigate and obtain adequate explanations and appropriate corroborative evidence.

SA 530: Audit Sampling

When using either statistical or non-statistical sampling methods, auditor should design and select an audit sample, perform audit procedures thereon, and evaluate sample results so as to provide sufficient appropriate audit evidence. The objective of the auditor when using audit sampling is to provide a reasonable basis to draw conclusions about the population from which the sample is selected. When designing an audit sample, auditor

should consider the objectives of the audit procedure and characteristics of the population when designing an audit sample. To assist in efficient and effective design of sample, stratification may be appropriate. Stratification is the process of dividing a population into sub-populations. When determining sample size, auditor should consider sampling risk, tolerable error, and expected error. Tolerable error is the maximum error in population that the auditor would be willing to accept and still conclude that the result from sample has achieved audit objective. If Auditor expects error to be present in the population, a larger sample needs to be examined to conclude that actual error in the population is not greater than planned tolerable error. Auditor should select sample items in such a way that the sample can be expected to be representative of the population. This requires that all items in the population have an opportunity of being selected. After having carried out those audit procedures on each sample item that are appropriate to particular audit objective, auditor should analyse any errors detected in the sample, project the errors found in the sample to the population and reassess sampling risk. Auditor should investigate the nature and cause of any deviations or misstatements identified, and their possible effect on the objective of the particular audit procedure or other areas of audit. In order to conclude that a misstatement or deviation is an anomaly, the auditor is required to obtain a high degree of certainty that the misstatement or deviation is not representative of the population.

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

Auditor should obtain sufficient appropriate audit evidence regarding reasonableness of accounting estimates including fair value accounting estimate and related disclosure in financial statements are adequate. Accounting estimate means an approximation of amount of an item in absence of a precise means of measurement. Determination of an accounting estimate may be simple or complex, depending upon the nature of item. Auditor should adopt one or a combination of following approaches in the audit of an accounting estimate:

- (a) review and test process used by management to develop the estimate;
- (b) use an independent estimate for comparison with that prepared by management; or
- (c) review subsequent events which confirm the estimate made

Auditor should make a final assessment of reasonableness of estimate based on auditor's knowledge of the business and whether the estimate is consistent with other audit evidence obtained during audit. When there is a difference between auditor's estimate of the amount best supported by available audit evidence and the estimated amount included in financial statements, auditor should consider whether the amount requires adjustment and report accordingly.

Auditor should adopt a risk-based approach to the responsibilities regarding accounting estimates, including fair value accounting estimates and related disclosures. A difference between the outcome of an accounting estimate and amount originally recognized or disclosed in financial statements does not necessarily represent a misstatement of financial statements. Auditor should review the outcome of accounting estimates included in prior period financial statements. Auditor should obtain written representations from management whether management believes significant assumptions used by it in making accounting estimates are reasonable.

Audit documentation should include the basis for auditor's conclusions about reasonableness of accounting estimates and their disclosure that give rise to significant risks; and Indicators of possible management bias, if any.

SA 550: Related Parties

Auditor should perform audit procedures designed to obtain sufficient appropriate audit evidence regarding identification and disclosure by management of related parties and the related party transactions that are material to financial statements. Definitions regarding related parties are given in Accounting Standard 18 and are adopted for the purposes of this SA. Management is responsible for identification and disclosure of related parties and transactions with such parties. This responsibility requires management to implement adequate accounting and internal control systems to ensure that transactions with related parties are appropriately identified in accounting records and disclosed in financial statements. Auditor should review information provided by directors and management identifying names of all known related parties and should perform other procedures in respect of completeness of this information. S/he should consider adequacy of control procedures over authorisation and recording of related party transactions. In examining identified related party transactions, auditor should obtain sufficient appropriate audit evidence as to whether these transactions have been properly recorded and disclosed. Auditor should obtain a written representation from management concerning completeness of information provided regarding identification of related parties and adequacy of related party disclosures in financial statements. If auditor is unable to obtain sufficient appropriate audit evidence concerning related parties and transactions with such parties or s/he concludes that their disclosure in financial statements is not adequate, s/he should express a qualified opinion or a disclaimer of opinion in the audit report. Focus is now more on identification and assessment of risks of material misstatement associated with related party relationships and transactions, and on responses to such risks. It emphasizes

particular skepticism required in the context of related parties and also deals with auditor's procedure in case of identification of previously unidentified or undisclosed Related Parties or Significant Related Party Transactions.

SA 560: Subsequent Events

Subsequent events are significant events occurring between balance sheet date and the date of auditor's report. Auditor should consider effect of subsequent events on financial statements and on auditor's report. Auditor should perform procedures designed to obtain sufficient appropriate audit evidence that all events up to the date of auditor's report that may require adjustment of, or disclosure in financial statements have been identified. Procedures to identify events that may require adjustment of, or disclosure in financial statements would be performed as near as practicable to the date of auditor's report. When Auditor becomes aware of events which materially affect financial statements, the auditor should consider whether such events are properly accounted for in financial statements. When the management does not account for such events that auditor believes should be accounted for, auditor should express a qualified opinion or an adverse opinion, as appropriate.

SA 570: Going Concern

Going concern assumption is a fundamental principle in the preparation of financial statements. Management should assess entity's ability to continue as a going concern even if the applicable financial reporting framework does not include an explicit requirement. Auditor should evaluate appropriateness of management's use of going concern assumption in preparation of financial statements and conclude whether there is a material uncertainty about entity's ability to continue as a going concern that need to be disclosed in financial statements. When planning and performing audit procedures and in evaluating the results thereof, auditor should perform further audit procedures when events or conditions are identified that cast significant doubt on the entity's ability to continue as a going concern. Indications of risk that continuance as a going concern may be questionable could come from financial statements, operational activities or from other sources. These may be financial indicators, operating indicators or other indicators. If, on the presence of such indication, a question arises regarding appropriateness of going concern assumption, auditor should gather sufficient appropriate audit evidence to attempt to resolve, to the auditor's satisfaction, the question regarding entity's ability to continue in operation for foreseeable future. After procedures considered necessary have been carried out, all information required has been obtained, and effect of any plans of management and other mitigating factors have been considered, auditor should decide whether the question raised regarding going concern assumption has been satisfactorily resolved. Auditor, on the basis of his/ her judgment and audit evidence will report, as deemed appropriate. In case where use of going concern assumption is appropriate but a material uncertainty exists, then (i) if adequate disclosure is made in financial statements, auditor should express an unmodified opinion but include an Emphasis of Matter paragraph in the auditor's report; (ii) if adequate disclosure is not made in financial statements, auditor should express a qualified or adverse opinion, as appropriate. In case where entity will not be able to continue as a going concern, auditor should express an adverse opinion if financial statements have been prepared on a going concern basis. Auditor should communicate with those charged with governance when there are identified events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.

SA 580: Written Representations

Written representations – are written statements used to corroborate the validity of the premises, relating to management's responsibilities, on which an audit is conducted; and other audit evidence obtained with regard to specific assertions in financial statements. Written representations in this context do not include financial statements, the assertions therein, or supporting books and records. The auditor should request general and specific written representations from management with appropriate responsibilities for financial statements and knowledge of matters concerned. The auditor should request management to provide a general written representation that it has fulfilled its responsibility for the preparation and presentation of the financial statements in accordance with the applicable financial reporting framework; designing, implementing and maintaining of adequate internal control system; and completeness of information made available to the auditor. Auditor should determine relevant parties from whom general and specific written representations are to be requested. Auditor should evaluate the reliability of written representations and in case of doubt, should reconsider the reliability of other written representations and, take appropriate action. A management representation letter should be addressed to the auditor containing relevant information and be appropriately dated and signed. A management representation letter should ordinarily be signed by members of management who have primary responsibility for the entity and its financial aspects, e.g., Managing Director, Finance Director. Auditor should disclaim an opinion on financial statements when the requested general written representations are not provided or are unreliable, and the auditor is unable to obtain sufficient appropriate audit evidence.

SA 600: Using the Work of another Auditor

When the principal auditor uses the work of another auditor, the principal auditor should determine how the

work of other auditor will affect the audit. Auditor should consider professional competence of other auditor in the context of specific assignment if the other auditor is not a Chartered Accountant. Auditor should inform other auditor of matters such as areas requiring special consideration, procedures for identification of inter-component transactions and significant accounting, auditing and reporting requirements. Auditor should consider significant findings of other auditor. There should be proper co-ordination and communication between the two auditors. When the principal auditor concludes that work of other auditor cannot be used and s/he has not been able to perform sufficient additional procedures regarding financial information of the component audited by other auditor, s/he should express a qualified opinion or disclaimer of opinion. The principal auditor would not be responsible in respect of the work entrusted to other auditors.

SA 610: Relying Upon the Work of an Internal Auditor

External auditor should, as part of their audit, evaluate the internal audit function to the extent they consider that it will be relevant in determining the nature, timing and extent of their compliance and substantive procedures. Depending upon such evaluation, external auditor may be able to adopt less extensive procedures than would otherwise be required. External auditor's general evaluation of internal audit function will assist them in determining the extent to which s/he can place reliance upon the work of internal auditor. Important aspects to be considered in this context are organisational status of the entity; nature and depth of internal audit assignment; technical competence of internal audit staff and the degree of due professional care taken by internal audit staff. External auditor must ascertain internal auditor's tentative plan for the year and discuss it with them at an early stage to determine areas where they could consider relying upon the work of internal auditor. Coordination with internal auditor is usually more effective when meetings are held at appropriate intervals during the year. Where, following the general evaluation, external auditor intends to rely upon specific internal audit work, s/he should review internal auditor's work, considering the scope of work and related audit programmes; whether the work was properly planned and work of assistants was properly supervised, reviewed and documented; whether sufficient appropriate evidence was obtained to afford a reasonable basis for the conclusions reached; whether conclusions reached are appropriate in the circumstances and whether any exceptions or unusual matters disclosed by internal auditor's procedures have been properly resolved.

SA 620: Using the Work of an Expert

When auditor uses work of an expert employed by them, s/he is using that work in employee's capacity as an expert rather than delegating the work to an assistant on the audit. Accordingly, in such circumstances, s/he should apply relevant procedures. Before asking for an expert's opinion, auditor should satisfy themselves about the skills and competence of that expert. Auditor should also consider objectivity of the expert. Auditor should seek reasonable assurance that the expert's work constitutes appropriate audit evidence in support of the financial information. Auditor should consider whether the expert has used source data which are appropriate in the circumstances. The appropriateness and reasonableness of assumptions and methods used and their application are the responsibility of the expert. Auditor does not have the same expertise and, therefore, cannot always challenge expert's assumptions and methods. If auditor concludes that the work of expert is inconsistent with information in financial statements or that the work of expert does not constitute sufficient appropriate audit evidence (e.g. where the work of expert involves highly technical matters or where, on grounds of confidentiality, the expert refuses to make available to Auditor the source data used by them) s/he should express a qualified opinion, a disclaimer of opinion or an adverse opinion, as may be appropriate. When expressing an unqualified opinion, auditor should not refer to the work of an expert in his/her report. If auditor decides to express other than an unqualified opinion, it may be beneficial to reader of the report if the auditor, in explaining the nature of their reservation, refers to or describes the work of expert.

SA 700: The Auditor's Report on Financial Statements

(Revised Exposure draft "Forming an Opinion and Reporting on Financial Statements" issued by ICAI for Members' comments)

Auditor should review and assess conclusions drawn from audit evidence obtained as the basis for clearly written expression of an opinion on financial statements. Auditor's report includes basic elements such as Title, Addressee, Opening or introductory paragraph, Scope paragraph (describing the nature of an audit), Opinion paragraph, Date of the report, Place of signature, and Auditor's signature. Auditor should incorporate in the audit report, matters specified by statute or regulator and report in the form prescribed by them in addition to requirements of this SA. Unqualified opinion should be expressed when auditor concludes that the financial statements give a true and fair view. Auditor's report is considered to be modified when it includes emphasis of matter when it does not affect auditor's opinion. Auditor's report is considered to be qualified, disclaimer or adverse when it contains matters which affect their opinion. Auditor should modify auditor's report by adding a paragraph to highlight a material matter regarding a going concern problem where the going concern question is not resolved and adequate disclosures have been made in financial statements. A qualified opinion should be expressed when Auditor concludes that an unqualified opinion cannot be expressed but that the effect of any disagreement with management is not so material and pervasive as to require an adverse opinion. A

disclaimer of opinion should be expressed when the limitation on scope is so material that the auditor has not been able to obtain sufficient appropriate audit evidence and is unable to express an opinion on financial statements. An adverse opinion should be expressed when the effect of a disagreement is so material that auditor concludes that a qualification of the report is not adequate.

SA 705: "MODIFICATIONS TO THE OPINION IN THE INDEPENDENT AUDITOR'S REPORT"

Exposure draft issued by ICAI for Members' Comments

SA 706: "Emphasis of Matter Paragraphs and Other Matter in the Independent Auditor's Report"

Exposure draft issued by ICAI for Members' comments

SA 710: Comparatives

Existence of differences in financial reporting frameworks results in comparative financial information being presented differently in each framework. The frameworks and methods of presentation that are referred to in this SA are corresponding figures where amounts and other disclosures for preceding period are included as part of current period financial statements and Comparative Financial Statements where amounts and other disclosures for preceding period are included for comparison with financial statements of current period. Auditor should obtain sufficient appropriate audit evidence that the corresponding figures meet the requirements of relevant financial reporting framework. This involves verifying whether accounting policies used for corresponding figures are consistent with those of current period and whether corresponding figures agree with amounts and other disclosures presented in prior period. When previous year's audit was done by another auditor, the incoming auditor too must comply with these conditions along with the procedures set out by SA 510 "Initial Engagements-Opening Balances". When auditor's report on prior period, as previously issued, included a qualified opinion and concerned matter is not resolved, auditor's report should also be modified regarding corresponding figures. When prior period financial statements are not audited, incoming auditor should state the fact in auditor's report.

SA 720: The Auditors Responsibility in Relation to Other Information in Documents containing Audited Financial Statements

The objective of the auditor is to respond appropriately when documents containing audited financial statements and auditor's report thereon include other information that could undermine the credibility of those financial statements and the auditor's report. The auditor is not required to give his opinion on other information, not having any responsibility of determining whether or not other information is properly stated, if there is no separate requirement in particular circumstance of the engagement. However, the auditor reads other information because the credibility of audited financial statements may be undermined by material inconsistencies between audited financial statements and other information and if found, to determine whether the audited financial statements or other information needs to be revised. Auditor should make appropriate arrangements with management or those charged with governance to obtain the other information prior to the date of the auditor's report. If material inconsistencies are identified prior to the date of audit, and the revision of audited financial statement is necessary and the management refuses to make the revision, auditor is required to modify his opinion. Further, if revision of other information is necessary, and management refuses to make the revision, auditor is required to communicate the matter to those charged with governance and also provide paragraph in the auditor's report on other matter; or withdraw from the engagement, if permitted by laws or regulations. If material inconsistencies are identified subsequent to the date of the audit, and revision of audited financial statement is necessary, the auditor is required to perform the procedures given in SA 560, "Subsequent Events". If, on reading other information for the purpose of identifying material inconsistencies, auditor becomes aware of an apparent material misstatement of fact, auditor should discuss the matter with management and if the management refuse to correct it, communicate the same to those charged with governance and take further appropriate actions.

STANDARD ON REVIEW ENGAGEMENTS (SRE) 2400: Engagements to Review Financial Statements

(Revised Exposure draft "Engagements to Review Financial Statements" issued by ICAI for comments of Members)

This standard provides extensive guidance on procedures and enquiries to be employed by auditors on quarterly unaudited financial results of companies listed on stock exchanges in India which are subject to limited review by Chartered Accountants. Unlike an audit, a review engagement is based mainly on analytical procedures and inquiries conducted by the auditor. This standard establishes standards and provides guidance on auditor's professional responsibilities and on the form and content of report that the auditor issues in connection with a review. This standard deals with issues such as scope of review engagement, level of assurance, terms of engagement, planning, documentation, review procedures, conclusions and reporting requirements in review engagements. This standard also illustrates format of engagement letter to be issued, review procedures to be applied and format of Review reports to be issued for qualified as well as unqualified

opinion. Auditor should plan and perform the review with an attitude of professional skepticism recognising that circumstances may exist which cause financial statements to be materially misstated.

For the purpose of expressing negative assurance in review report, auditor should obtain sufficient appropriate evidence primarily through inquiry and analytical procedures to be able to draw conclusions.

The scope of a review is substantially narrower as compared to an audit in accordance with the generally accepted auditing standards for expression of an opinion on financial statements. A review engagement provides a moderate level of assurance. In planning a review of financial statements, auditor should obtain or update knowledge of business including consideration of entity's organisation, accounting systems, operating characteristics and nature of its assets, liabilities, revenues and expenses.

Auditor should apply judgment in determining the specific nature, timing and extent of review procedures.

Auditor should apply the same materiality considerations as would be applied if an audit opinion on financial statements were being given. If Auditor has reason to believe that the information subject to review may be materially misstated, s/he 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. The review report should contain a clear written expression of negative assurance.

If Auditor is unable to agree to a change of the engagement and is not permitted to continue the original engagement, s/he should withdraw and consider whether there is any obligation, either contractual or otherwise, to report the circumstances necessitating withdrawal to other parties, such as board of directors or shareholders.

Standard on Assurance Engagements (SAE) 3400 : The Examination of Prospective Financial Information

In an engagement to examine prospective financial information, auditor should obtain sufficient appropriate evidence as to whether:

- a. management's best-estimate assumptions are not unreasonable and, in the case of hypothetical assumptions, such assumptions are consistent with the purpose of information,
- b. prospective financial information is properly prepared on the basis of assumptions,
- c. prospective financial information is properly presented and all material assumptions are adequately disclosed, including whether they are best-estimate assumptions or hypothetical assumptions, and
- d. prospective financial information is prepared on a consistent basis with historical financial statements, using appropriate accounting principles.

While evidence may be available to support assumptions on which prospective financial information is based, such evidence is itself generally future-oriented and, therefore, speculative in nature, as distinct from evidence ordinarily available in examination of historical financial information. Auditor is, therefore, not in a position to express an opinion as to whether the results shown in prospective financial information will be achieved

Auditor should:

- not accept, or should withdraw from, an engagement when assumptions are clearly unrealistic or when s/he believes that prospective financial information will be inappropriate for its intended use;
- obtain a sufficient level of knowledge of business and become familiar with entity's process to be able to evaluate whether all significant assumptions required for preparation of prospective financial information have been identified;
- consider extent to which reliance on entity's historical financial information is justified. Auditor should consider period of time covered by prospective financial information. Sufficient appropriate evidence supporting such assumptions would be obtained from internal and external sources;
- would consider whether, when hypothetical assumptions are used, all significant implications of such assumptions have been taken into consideration;
- should obtain written representations from management regarding intended use of prospective financial information, completeness of significant management assumptions and management's acceptance of its responsibility for prospective financial information;
- should assess the presentation and disclosures in prospective financial statement are adequate;
- should document matters, which are important in providing evidence to support his report on examination of prospective financial information, and evidence that such examination was carried out in

accordance with this SA.

When auditor believes that presentation and disclosure of prospective financial information is not adequate, the auditor should express a qualified or adverse opinion in the report on prospective financial information, or withdraw from engagement as appropriate. When auditor believes that one or more significant assumptions do not provide a reasonable basis for prospective financial information prepared on basis of best-estimate assumptions or that one or more significant assumptions do not provide a reasonable basis for prospective financial information given the hypothetical assumptions, the auditor should either express an adverse opinion setting out reasons in the report on prospective financial information, or withdraw from engagement. When examination is affected by conditions that preclude application of one or more procedures considered necessary in the circumstances, auditor should either withdraw from engagement or disclaim the opinion and describe the scope limitation in the report on prospective financial information

Standards on Related Services (SRS) 4400: Engagements to Perform Agreed-upon Procedures regarding Financial Information

In an engagement to perform agreed-upon procedures, auditor is engaged by client to issue a report of factual findings, based on specified procedures performed on specified matters of a financial statement. As the auditor simply provides a report of factual findings of agreed-upon procedures, no assurance is expressed by them in the report. Report is restricted to those parties that have agreed to procedures to be performed since others, unaware of reasons for the procedures, may misinterpret results. Auditor should comply with *Code of Ethics*, issued by ICAI. Where Auditor is not independent, a statement to that effect should be made in the report of factual findings. Terms of engagement should be well defined so as to avoid any misunderstandings. Auditor should plan the work so that an effective engagement will be performed and documentation of important matters to be done which provides evidence to support the report of factual findings. The report describes the purpose and agreed-upon procedures of engagement in sufficient detail to enable the reader to understand the nature and extent of work performed. The report should also clearly mention that no audit or review has been performed

SRS 4410: Engagements to Compile Financial Information

In such types of engagements, accountant uses accounting expertise as against auditing expertise to collect, classify and summarise financial information. The accountant should comply with the "Code of Ethics", issued by ICAI. However, where accountant is not independent, a statement to that effect should be made in the accountant's report. It should be ensured that there is a clear understanding between the client and accountant regarding terms of engagement by means of an engagement letter or such other suitable form of contract. Accountant should obtain an acknowledgement from management of its responsibility for appropriate preparation and presentation of financial statements or other information and of its approval of such information to be compiled. Accountant should also obtain an acknowledgement from management of its responsibility for accuracy and completeness of underlying accounting data and complete disclosure of all material and relevant information. Accountant should plan the work so that an effective engagement will be performed. Accountant should obtain a general knowledge of business and operations of the entity and should be familiar with accounting principles. Accountant should request management representation letter covering significant information or explanations given orally on which they consider representations are required. There are few special considerations which the accountant has to take care of i.e. s/he should ensure that financial statements or other financial information compiled, comply with requirements of identified financial reporting framework & where there is no specific financial reporting framework, client may specify that accounts should be compiled on, for example, based on requirements of Income Tax Act. If any accounting standard is not complied with, the fact should be disclosed in the notes to accounts. If accountant becomes aware of any material misstatement, s/he must report this to management or must withdraw from engagement if management doesn't act. Financial information compiled should be approved by client before compilation report is signed by accountant.