

AUDIT DOCUMENTATION
[With Specific Reference to Audit
under section 44AB of the Income-tax Act, 1961]

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INTRODUCTION:

Peer Review, as per ICAI Peer Review Manual, means 'an examination and review of the systems and procedures to determine whether they have been put in place by the practice unit for ensuring the quality of attestation services as envisaged and implied/mandated by the Technical Standards and whether these were effective or not during the period under review'.

Therefore, peer review visualises two items, viz.,

- Existence of systems and procedures in Practising Firms, designed to ensure the quality of assurance services, and
- Effective implementation of (Compliance with) these systems and procedures.

Auditing and Assurance Standard (AAS), now Standards on Auditing (SA), is being formulated by the Auditing and Assurance Standards Board on various topics, to help the auditors in performing their attest functions in accordance with generally accepted audit procedures.

To ensure quality in such attestation services, AAS 17 (SA 220), 'Quality Control for Audit Work' has been issued by the institute, which requires establishment of standards by the auditor on the quality control relating to –

- Policies and procedures of an audit firm regarding audit work generally, and
- Procedures regarding the work delegated to assistants of an individual audit.

This Documentation Model aims at providing some standard procedures to help the Auditors in completing their tax audits of Small & Medium Enterprises in accordance with the generally accepted audit practices, together with the documentation of such audit work.

DOCUMENTATION:

Paragraph 11 of AAS 1 (SA 200), "Basic Principles Governing an Audit" states that, "The auditor should document matters which are important in providing evidence that the audit was carried out in accordance with the basic principles."

Documentation, vide AAS 3 (SA 230), refers to the working papers prepared or obtained by the auditor and retained by him, in connection with the performance of his audit.

Working paper is the only asset of, or source to, an auditor in satisfying the questions raised, or relating to, effective execution of audit. Working papers aid in –

- ♦ documenting the proper acceptance of audit, including 'check on independence';
- ♦ planning the audit;
- ♦ performance (including supervision and review) of the audit work; and
- ♦ providing evidence of the audit work performed to support the auditor's opinion.

ACCEPTANCE/RETENTION OF AUDIT:

Independence is a state of mind. Independence is to be ensured in order to have integrity on the opinion expressed by the auditor on the financial statements. A condition table is enclosed in Annexure A which gives the conditions, upon which it has to be decided whether an audit is to be accepted or not. Such a check of independence shall be made every year before accepting the re-appointment [vide Guidance Note (GN) on "Independence of Auditors"].

As a matter of professional ethics, it is required that the consent of the previous auditor(s) of the client is sought. An audit can be accepted, when there is expressive consent from the previous auditor(s) about the 'No Objection' on the successor's acceptance of audit or where there is no reply from the previous auditor(s) even after the lapse of reasonable time.

On acceptance of the audit, the following are required to be documented: -

- Appointment letter from the Client.
- Resolution passed by the Client duly signed by the authorised person(s) in the case of Firms/AoPs/Companies. In any case, signature from more than 51% of the interest holders would avoid dispute on appointment in later days.
- Communication with the previous Auditor of the Client, including the proof of despatch of communication and his reply (if any received).
- Office copy of the Acceptance Letter.
- Audit Engagement Letter (Refer Annexure B) – (vide AAS 26).
- Form 23B in case of Companies (only if you are statutory auditor of the company).

SCOPE OF AUDIT:

The scope of the audit, vide AAS 2 (SA 200A), cannot be reduced by the Management below the statutory requirements. However, it can be enhanced to include for separate reports to management, etc.

Scope of tax audit requires the auditor to perform two main functions, viz., ensuring true and fair view of the financial statements (Form 3CA/3CB) and certifying certain information (Form 3CD). This cannot be reduced (for ex.: the client cannot restrict the auditor as to he should not report on related party transactions, loans and advances, etc.). However, it may be extended by the terms of engagement to cover further certificates under the Act (for ex.: certificate under section 80IA, etc.)

PLAN YOUR WORK:

PLANNING:

Objectives of planning, vide AAS 8 (SA 300), broadly fall into the following classification:

- a. Acquiring knowledge of the client's business, accounting systems, policies and internal control procedures;
- b. Establishing the expected degree of reliance to be placed on internal control system and internal auditors;
- c. Determining and programming the nature, timing and extent of the audit procedures to be performed; &
- d. Deciding the audit team and coordinating the work to be performed.

While planning, the following considerations shall be borne: -

- a. To ensure compliance with Auditing Standards.
- b. To ensure proper documentation of audit evidences and to assure quality in the audit.
- c. To direct the audit approach and to determine where Standard Audit Programmes are required and where Specific Audit Programmes are required.
- d. To design the audit procedure to ensure that the entity is not susceptible to material misstatements or frauds, vide AAS 4 (SA 240).

KNOWLEDGE OF BUSINESS:

In case of initial assignments, and in case of re-appointment - any changes, shall be recorded in relation to the: -

- a. Nature of business
- b. Constitution of the entity and its period of existence
- c. Accounting Systems/Policies/Methods
- d. Internal Control
- e. Managerial Personnel (especially Accounting Department) and
- f. Legal Provisions affecting the entity

It is also important that the inherent business risk is evaluated based on the internal and external factors affecting the company, vide AAS4 (SA 240), AAS 6 (SA 400) & AAS 20 (SA 310).

ASSESSMENT OF ACCOUNTING SYSTEM AND INTERNAL CONTROL:

Receive the Accounting Manual or Record the Accounting System and Record Internal Control Questionnaire (refer Institute's pronouncement in this regard).

Evaluate the Accounting System and Internal Control, vide AAS 6 (SA 400). Check the reliability and decide as to whether to -

- a. Perform Compliance Test and reduce Substantive Test, or
- b. Ignore Systems and Control and do high Substantive Test.

Where there is an extensive computerisation of the accounting system and internal control, the additional controls in the system should be evaluated and wherever necessary the need to involve an expert should be considered, vide AAS 29 (SA 401).

It is important to note that whenever, service organisations are involved in the Accounting System, then the nature of such service together with its extent of accountability shall be studied in relying on the internal control, vide AAS 24 (SA 402).

MATERIALITY, ANALYTICAL REVIEW AND SAMPLING:

Undertake Analytical Review, vide AAS 14 (SA 520) based on last year Audited Financial Statements and current year Draft/Final Accounts. Determine, whether any area require higher or lower Substantive Procedure.

Determine the Materiality Level for the Entity, for Assets, Liabilities, Income and Expense and on Overall basis, vide AAS 13 (SA 320).

Determine, whether sampling, vide AAS 15 (SA 530) can be applied and if so; determine the Sample Size.

WORK YOUR PLAN:

PROGRAMMING:

Ensure that wherever required the following are obtained before the Audit is commenced: -

- a. Letter of Confirmation from the Client that all the books and records are ready for audit.
- b. Authorisation letter for entry to restricted areas, where audit/inspection has to be carried out.
- c. Attendance at Physical Stock-taking at year-end or surprise check.
- d. Bank, Debtor's and Creditor's Confirmation Letter circulation, vide AAS 30 (SA 505)

Allocate Personnel for the Audit and form the Audit Team. Ensure that the Audit Team comprises of staffs possessing adequate skills to carry out the audit, either by way of qualification or experience or training or any combination thereof.

GENERAL EXECUTION RESPONSIBILITIES:

The auditor shall direct the assistants (qualified or otherwise), which includes –

- a. informing the assistants of their responsibilities and the objectives of the procedures they are to perform;
- b. informing the nature of entity's business and possible accounting or auditing problems that may affect the nature, timing and extent of audit procedures with which they are involved;
- c. issuing orders/guidance in the course of the execution of the audit programme;
- d. ensuring that the documentation is proper and adequate;
- e. ensuring that all the significant audit matters have been resolved or are reflected in audit conclusions;
- f. ensuring that the audit conclusions expressed are consistent with the results of the work performed and support the audit opinion;
- g. reviewing the work carried out by the assistants; and
- h. ensuring the achievement of the independent objectives.

The auditor shall supervise the specific audit, if the above responsibility has been delegated to an Audit Manager. Supervision is closely related to both direction and review. The work of the auditor, in such cases, involves –

- a. monitoring the progress of the audit to consider whether –
 - i. personnel in the audit team have the necessary skills and competence to carry out the independent objectives;
 - ii. personnel understand the audit directions; and
 - iii. the work is carried out in accordance with the overall audit plan and the audit programme;
- b. resolving any differences of professional judgement between personnel and consider the level of consultation that is appropriate;
- c. becoming informed of and addressing significant accounting and auditing questions raised during the audit, by assessing their significance and modifying the overall plan and the audit programme as appropriate;
- d. reviewing on timely basis –
 - i. the work of the assistants, based on the report submitted from the working papers.

- ii. assessment of inherent and control risks, including the results of tests of control and the modifications, if any, made to the overall audit plan and the audit programme as a result of performance of tests of control;
- iii. documentation of the audit evidence obtained from substantive procedures and the conclusions drawn there from, including the results of consultations; and
- iv. financial statements, proposed adjustments in financial statements arising out of the audit, and the auditor's proposed observations/report.

SPECIFIC EXECUTION OF AUDIT:

Approach the Audit using an Audit Checklist. Prepare and review the Permanent Audit File as the audit progresses. If required, modify the audit programme.

In case of initial engagement, the AAS 22 (SA 510), "Initial Engagements – Opening Balances" shall be applied.

Besides, the following AAS (SA) shall be considered in the execution of the Audit for any year, whenever they are applicable to the entity: -

- Going Concern (AAS 16 – SA 570)
- Consideration of Laws and Regulations in an Audit of Financial Statements (AAS 21 – SA 250)
- Auditing of Accounting Estimates (AAS 18 – SA 540)
- External Confirmations (AAS 30 – SA 505)
- Subsequent Events (AAS 19 – SA 560)
- Related Parties (AAS 23 – SA 550)

CONSULTATIONS AND REVIEW:

Wherever necessary the auditor shall consult with the other senior partner(s) [hereinafter 'Reviewer'] in the firm. Auditor, if necessary (including cases of individual practitioners), should obtain an opinion –

- by consulting with other chartered accountants, firms or entities having appropriate expertise, and/or
- of the Expert Advisory Committee of the Institute.

It would be a healthy practice to have the work done by one partner to be reviewed by another partner of the same firm. This would ensure that the system in the firm is complied with.

REPORTING:

Once the audit objectives are achieved, the auditor should prepare either an audit report for issue to the client or a draft audit report, only if necessary, for the discussion with the client (vide AAS 27 – SA 260).

All the opinions expressed shall be supported by sufficient and appropriate audit evidence (vide AAS 5 – SA 500 and AAS 34 – SA 505).

While issuing the Final Audit Report, due considerations shall be laid on AAS 28 'The Auditor's Report on Financial Statements' and AAS 25 'Comparatives'.

Further, he shall document the manner in which he has dealt with the reports: -

- from Internal Auditor – Relying upon the Work of (AAS 7 – SA 610)
- from Expert – Using the work of (AAS 9 – SA 620)
- from another Auditor – Using the work of (AAS 10 – SA 600)
- of the Joint Auditor – Responsibility (AAS 12 – SA 299)

Wherever, in the audit report, the auditor has relied on the representations from the Management, he shall receive a Management Representation Letter from the Client (AAS 11 – SA 580).

CONCLUSION:

Model Documentation Booklet for 'Tax Audits' has been enclosed, which has been prepared at the minimal level, to cover all the generally accepted auditing procedures. However, this may require modification based on the specific execution of the audit.

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