SA-200

OVERALL OBJECTIVES OF THE INDEPENDENT AUDITOR & THE CONDUCT OF AN AUDIT IN ACCORDANCE WITH SA'S.

This is very basic SA's which needs to be complying with being an Auditor for Proper & Quality audit work.

Premise of Audit

Management & TCWG is responsible for-

1) Preparation & presentation of Financial statement (Not the Auditor)
2) To Provide with information which is necessary and required by the auditor to perform his duties
3) To Design, implement & maintain I.C system of the entity (Not the auditor)

Ethical Requirements- Auditor should have these -

1) Professional Behavior
2) Due care & Professional skills
3) Confidentiality
4) Independence of mind
5) Objectivity

Professional Judgment- in arriving at decisions regarding-

1) Materiality & audit risk associated with it (Auditor can ignore immaterial items)
2) Adoption of audit procedures to obtain Sufficient and appropriate audit evidences
3) Conclusions based upon such audit evidences
4) FRF prepared by the Management

Professional Skepticism

1) An attitude that includes- a questioning mind
2) Being alert to circumstances/indicators which shows/indicates mis-statements due to error or fraud
3) An critical assessment of audit evidences

Why SA's are required?

1) Complying with SA's relevant to the audit (For proper & quality audit work)
2) Objectives stated by individual relevant SA's (It helps auditor to achieve overall objective)
3) **Note: If the auditor decides to depart from a relevant requirement inn SA, he shall perform alternatives audit procedures to achieve the overall aim.**
4) **Note: If he fails to achieve his objective and accordingly modify or withdraw from the engagement**

Inherent Limitations of Audit-

1) Nature of Financial Reporting- Ie: Accounting estimates provided by Management can not be verified accurately.
2) Nature of Audit Procedures- ie: sampling
3) If audit is to be done within stipulated time period & at a reasonable cost
4) Nature of Audit evidence (Persuasive evidence is taken by the auditor rather than conclusive evidence)

Understanding of Persuasive evidence is taken by the auditor rather than conclusive evidence)-actually what does it means?

Examples- 1) when auditors gather evidences on the basis of a test sampling
2- Peoples make mistake both client & auditor
3- Documents could be forged due to increasing in digital technology
4- The client personnel may not always tell the truth

Imp. Points-

1) The audit of the financial statement does not relieve the Management & TCWG from their duties/responsibilities.
2) Due to inherent limitations of Audit, it can not be held as an Absolute level of assurance. It provides reasonable assurance.
3) Auditor shall perform his duties under applicable/relevant SA's and laws or regulations.
4) Auditors shall form his opinion on the basis of audit done under relevant SA's, applicable laws and regulations.

SA 210

AGREEING THE TERMS OF AUDIT ENGAGEMENT

Meaning of Terms of Engagement

Terms of Engagement is a **letter written** by the **auditor to the management** describing the **Terms & Conditions of Audit, when accepted**

Scope of this S.A

- ✓ First, identifies the **Preconditions** necessary for accepting an audit.
- ✓ Second, describes the **contents of the letter** of engagement.
- ✓ Third, **Responsibilities of auditor** in case of **Recurring audit.**
- ✓ And**, duties of an auditor** where, management **changes the terms** of engagement.

Preconditions for Acceptance

The following conditions must be satisfied before accepting any audit

- ✓ Check whether the management uses an acceptable FRF (refer to below Point for detail) with reference to Nature of entity business, Purpose of Financial statement & Legal requirements?
- ✓ Check whether the management accepts the responsibility for Preparation of Financial statement, Implementation of Internal control system, Providing all the information & explanations to the auditor, full access to the accounts?
- ✓ In case management imposes any limitation on scope of Audit then, auditor should not accept the audit.

Contents of Letter of Engagement

It can be divided into 3 parts as follows-

1) Preliminary information

- ✓ Objectives and scope of the audit
- ✓ Responsibilities of Auditor & Management
- ✓ Identification for applicable FRF
- ✓ Inherent limitations of audit and disclaimer on risk of unavoidable misstatements.

2) **Management agreement Terms**
   - ✓ To provide adequate information of time
   - ✓ To inform auditors on subsequent events
   - ✓ Any restriction of the auditor liability
   - ✓ Any other agreement between the auditor & management
3) **Miscellaneous issues**
   - ✓ That audit work may be subjected to Peer review act
   - ✓ Obligations regarding Audit working papers
   - ✓ Fee & billing related matters
   - ✓ Arrangements to be made with internal auditor/Predecessor auditor/experts etc.

Revision of letter of Engagement

In case of recurring audits, the auditor shall consider whether the LOE requires any revision as compared to previous year. It can be revised in following cases-

- ✓ Misunderstanding of the objectives and scope
- ✓ Revision in audit engagement
- ✓ Change in Ownership, Management, Nature of business, FRF & legal requirements

Revision of Terms

If after accepting the LOE, management revises the terms then the auditor shall ascertain the reasons for such revision and the same could be due to-

- ✓ A change in circumstances
- ✓ Misunderstanding of the nature of an audit as originally requested
- ✓ A restriction on the scope of the audit engagement

Note: - If auditor feels it on reasonable basis then he shall record the new terms otherwise he shall withdraw from the engagement.

Imp. Points:-

- ✓ In case of any conflict between the FRF and legal requirements, the auditor shall discuss the same with management and ensure that the same is disclosed in the Notes to accounts accordingly.
- ✓ Where the FRF followed by the entity is not acceptable, then auditor shall ensure that-
  1) The same is disclosed in Notes to accounts
  2) Include an emphasis of matters Para in audit report

3) Shall not use the words "True & Fair" in his audit report
4) These points should be intimated in the LOE itself.

- ✓ Where the audit report format prescribed by any law/regulation (Tax audit report format) does not confirms with the audit report under SA (as prescribed under SA 700 format), the user might misunderstand the audit scope report and the assurance given. In such a case he shall not state in his report that the audit has been conducted in accordance with SA's.

Financial Reporting Framework (FRF)- stands for the basis on which the financial statements are prepared-

- ✓ Accounting standards
- ✓ IFRS
- ✓ Schedule VI
- ✓ Cash or mercantile basis

Why FRF?

Following the FRF ensures that-

- ✓ All the relevant information are included in Financial statements
- ✓ FS is complete in all aspects
- ✓ FS is reliable
- ✓ FS is comparable
- ✓ FS is understandable

General clarification on SA 210 as issued by ICAI (GC-AASB/2/2004)

Query- A question that arises is whether it is necessary that the engagement letter issued by the auditor should be acknowledged by addressee and returned to the auditor to indicate that the client's understanding of the terms of the engagement is in accordance with the engagement letter issued by the auditor and to establish that the auditor has complied with the requirements of the Standard in so far as they are related to sending the audit engagement letter.

Clarification-

- ✓ The auditor and the client **should agree** on the terms of the engagement.
- ✓ The 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 the preparation of engagement letters **relating to audits of financial statements**. The Standard is also applicable to related services.

- When **other services such as tax, accounting, or management consultancy** and other services are to be provided, separate letters may be appropriate.
- Though the objective and scope of an audit and the auditor's obligations are, normally, laid down in the applicable statute or regulations and the pronouncements of the Institute of Chartered Accountants of India, the audit engagement letters would be **informative** for the clients.
- From the above it is clear that the basic purpose of issuing an engagement letter is that the auditor and the client should agree on the terms of the engagement.
- The auditor and the client are normally considered to be agreeing on the terms of the engagement if the objective and scope of an audit and the auditor's obligations are laid down in the **statute or regulations governing the engagement**.
- Examples of such engagements include audit under section 227 of the Companies Act, 1956, audit of public sector banks, etc.
- **In such cases**, it is not necessary that the engagement letter sent by the auditor in accordance with paragraph 5 of SA 210 is acknowledged by the addressee and returned to the auditor to establish that the client's understanding of the terms of the engagement is in accordance with the engagement letter issued by the auditor.
- It shall be sufficient compliance with the requirements related to sending the audit engagement letter, if an engagement letter is appropriately delivered to the client and the auditor retains the evidence for such delivery. In such cases, the audit engagement letters would be informative for the clients.
- If, however, the client seeks any further explanations or clarification in regard to any terms, conditions or other contents of the engagement letter issued, it might indicate that there exists a difference in understanding of the terms of audit engagement either on the part of the client or on the part of the auditor. The auditor, in such cases, should take necessary steps to resolve the issues, for example by appropriately replying to the issues raised by the client.
- It is also desirable that the auditor documents the evidence indicating that the issues are settled and the client and auditor agree on the terms of the engagement.
- There may be certain engagements where the objective and scope of the engagement and the auditor's obligations are not laid down in the applicable statute or regulations. In such situations, the auditor should request the client that a copy of the engagement letter be acknowledged by the addressee and returned to the auditor to establish: (a) that the client's understanding of the arrangements for the engagement is in accordance with the engagement letter issued by the auditor; and (b) that the auditor has complied with the requirements of the standard in so far as they are related to the audit engagement letter.