A COMPLETE GUIDE FOR ADVANCED AUDITING

(CA FINAL)

Applicable for CA Final November, 2016, Exams onwards

Short Notes for Quick Revision

It Covers :

> Upto date Amendments Including :
- CARO 2016
- Companies (Amendment) Act, 2015
- Companies (Audit & Auditor's) Amendment Rules, 2015
- Revised SA 610 & SAE 3420

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CA Sumit Aggarwal

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ADVANCED AUDITING

(CA FINAL)

- With solved Question Papers for Last 36 Exams
- With Short Notes for Quick Revision

By

C.A. SUMIT AGGARWAL

Foreword by

C.A. AMARJIT CHOPRA

SPIRAA PUBLISHING INC.

NEW DELHI

First Edition	:	December, 2014
Reprint Edition	:	February, 2015
Second Edition	:	July, 2015
Third Edition	:	January, 2016
Fourth Edition	:	July, 2016
ISBN	:	978-81-930580-2-2
Price	:	Rs. 610/-
Published by	:	*Spiraa Publishing Inc*
Regd. Office	:	Flat # 1, Upper Ground Floor, Front Right, Plot # 258 - 259, Sarder Patel Enclave, Gram Sabha, Pooth Kalan, Rohini Sec. 23 Extension. New Delhi -110086
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Printed at	:	Raja Offset Printers, Delhi

Dedicated to

All CA Students

&

My Family

About the Author

Sumit Kumar Aggarwal is a commerce graduate from Bikaner University, having done his graduation from Seth G.L. Bihani S.D. (P.G.) College. He qualified Chartered Accountancy Course in 2005, simultaneously; he also completed his Master in Commerce in 2005. He has cleared various exams conducted by NSE. He also qualified certification course in International Financial Reporting Standard (IFRS) from ICAI in January 2010. He is currently teaching auditing to CA Students & functioning as a Practicing Chartered Accountant. He is also a member of Institute of Certified Management Accountant, USA.

Foreword

Financial Statements are important as these reveal the state of affairs of a particular entity on a particular date as well as the performance of the entity over the accounting period. These need to be transparent and give true and fair view of the state of affairs and of profit/loss for the period. Though the responsibility for preparation of financial statements lies with the managements, the responsibility, to ensure that sound accounting policies and the relevant accounting standards have been complied with, remains with the auditor.

With a view to enable auditor to discharge his duties effectively and efficiently, Standards on Auditing have been laid down. The same are in line with the Standards laid down by International Auditing and Assurance Standards Board (IAASB). The Institute of Chartered Accountants of India have pronounced Standards on Auditing. These Standards lay down the responsibilities of the auditors and the procedures to be followed by them. Any deviation from these Standards has to be explained by the auditor giving the reasons, impact etc. In certain cases he may be required to modify his report.

I am indeed glad to know that CA Sumit Kumar Aggarwal has authored "A Complete Guide For Advanced Auditing" for CA Final students. He has covered the various Standards and other topics meticulously. He has taken pains to include topics on Professional Ethics, Bank Audit, Cost Audit etc. He has also deftly handled the questions with answers from last 34 exams. The effort is laudable and I am sure that the students would be immensely benefitted by the book.

With best wishes

CA. Amarjit Chopra,

Fellow Member ICAI

Preface to Fourth Edition

Firstly, I would like to thank the reader for the response given to earlier edition. It gives me immense pleasure in presenting the fourth edition of the book "A Complete Guide for Advanced Auditing – CA Final".

The Salient features of this books are as follow:

- Presentation of whole Syllabus in an easy language to understand the complex subject matter.
- Tabular and graphic presentation to facilitate easy understanding and learning.
- Inclusion of flowcharts on various topics, including Standards on Auditing.
- Presentation of maximum topics in point-wise manner.
- Upto date amendments including:
    - ◊ CARO 2016
    - ◊ Companies (Amendment) Act, 2015
    - ◊ Companies (Audit & Auditor's) Amendment Rules, 2015
    - ◊ Revised SA 610 & SAE 3420
- Illustration of all "Audit Report" as per SA 700, SA 705 & SA 706 at one place (See Chapter 23) for quick understanding of "Audit Report" in different situations with minimum time frame & fast understandability.
- All Example of Engagement Letter as per SA 210, SA 2400, SRE 2410, SRS 4400, SRS 4410 at one place (See Chapter - 23) for quick understanding of Engagement Letter in different situations with minimum time frame & fast understandability.
- All Illustration of Audit Report, Review Report & Certificate as per SA 800, SA 805, SRE 810, SRE 2400, SRE 2410, SAE 3400, SRS 4400, SRS 4410 at one place (See: Chapter - 23) for quick understanding of Audit Report, Review Report in different situations & their comparison with minimum time frame & fast understandability.
- Full coverage of Questions appeared in past 36 exams has been arranged in following manners:
    - ◊ Chapter wise/topic wise
    - ◊ Standard of Auditing wise
    - ◊ Accounting Standard wise
    - ◊ Clause wise & Schedule wise (Chapter – Professional Ethics)
    - ◊ Clause wise (Chapter – Audit under Fiscal Law (Form 3CD)
- Graphs at the beginning of every chapter, showing marks allotment in last twenty examinations.
- List of questions including case study's appeared in past 36 examinations given at the end of

each chapter.

- Short Notes of all Chapters given at the end of the book (See Chapter – 25) for Quick revision.

I am thankful to my students and colleagues for their valuable suggestions while presenting this fourth edition of the book.

I also grateful to ***"Spiraa Publishing Inc."*** for their efforts in publishing the second edition of the book.

Suggestions and criticism from all readers would be highly appreciated and acknowledged.

Finally, I hope that students will find this book beneficial from exam point for view. In case of any suggestion, please feel free in writing to me at **cacma.sumit@gmail.com**.

I look forward the views and suggestions from the readers which would help towards further improvement of the book.

Wishing every success to the readers.

CA Sumit Kumar Aggarwal

Syllabus

(Applicable for May 2015 Exams & Onwards)
[As per ICAI Notification dated May 20, 2014]

Paper 3: Advanced Auditing and Professional Ethics

(One Paper - Three hours - 100 marks)

Level of Knowledge: Advanced knowledge

Objectives:

(a) To gain expert knowledge of current auditing practices and procedures and apply them in auditing engagements.

(b) To develop ability to solve cases relating to audit engagements.

Contents:

1. **Auditing Standards, Statements and Guidance Notes**

   Auditing and Assurance Standards (AASs) ; Statements and Guidance Notes on Auditing issued by the ICAI; Significant differences between Auditing and Assurance Standards and International Standards on Auditing.

2. **Audit strategy, planning and programming**

   Planning the flow of audit work; audit strategy, planning programme and importance of supervision: review of audit notes and working papers; drafting of reports; principal's ultimate responsibility; extent of delegation; control over quality of audit work; reliance on the work of other auditor, internal auditor or an expert.

3. **Risk Assessment and Internal Control**

   Evaluation of internal control procedures; techniques including questionnaire, flowchart; internal audit and external audit, coordination between the two.

4. **Audit under Computerized Information System (CIS) environment**

   Special aspects of CIS Audit Environment, need for review of internal control especially procedure controls and facility controls. Approach to audit in CIS Environment, use of computers for internal and management audit purposes, audit tools, test packs, computerized audit programmes; Special Aspects in Audit of E-Commerce Transaction.

5. **Special audit techniques**

   (a) Selective verification; statistical sampling: Special audit procedures; physical verification of assets, direct confirmation of debtors and creditors

   (b) Analytical review procedures

   (c) Risk-based auditing.

6. **Audit of limited companies**

   Relevant Provisions under the Companies Act, 2013 relating to Audit and Auditors and Rules made there under; Audit of branches joint audits; Dividends and divisible profits- financial, legal, and policy considerations.

7. Rights, duties, and liabilities of auditors; third party liability.

8. Audit reports; Qualifications, notes on accounts, distinction between notes and qualifications, detailed observations by the statutory auditor to the management vis-a-vis obligations of reporting to the members.

9. Audit Committee and Corporate Governance.

10. **Provisions under the Companies Act, 2013 in respect of Accounts of Companies and Rules made there under**: Audit of Consolidated Financial Statements, Audit Reports and Certificates for Special Purpose engagements; Certificates under the Payment of Bonus Act, import/ export control authorities, etc.; Specific services to

non-audit clients; Certificate on Corporate Governance.

11. Special features of audit of banks, insurance companies, co-operative societies and Non banking financial companies.

12. Audit under Fiscal Laws, viz., Direct and Indirect Tax Laws.

13. Cost audit.

14. Special audit assignments like audit of bank borrowers, audit of stock and commodity exchange intermediaries and depositories; inspection of special entities like banks, financial institutions, mutual funds, stock brokers.

15. Special features in audit of public sector companies. Directions of Comptroller and Auditor General of India to statutory auditors Concepts of propriety and efficiency audit.

16. **Internal audit, management and operational audit :** Nature and purpose, organization, audit programme, behavioral problems; Internal Audit Standards issued by the ICAI; Specific areas of management and operational audit involving review of internal control, purchasing operations, manufacturing operations, selling and distribution, personnel policies, systems and procedures. Aspects relating to concurrent audit.

17. Investigation and Due Diligence.

18. Concept of peer review.

19. Salient features of Sarbanes - Oxley Act, 2002 with special reference to reporting on internal control.

20. **Professional Ethics**

Code of Ethics with special reference to the relevant provisions of The Chartered Accountants Act, 1949 and the Regulations there under.

Note:

(I) The provisions of the Companies Act, 1956 which are still in force would form part of the syllabus till the time their corresponding or new provisions of the Companies Act, 2013 are enforced.

(II) If new legislations are enacted in place of the existing legislations, the syllabus would include the corresponding provisions of such new legislations with effect from a date notified by the Institute.

CA (Final) May 2016 Examination

Paper 3: Advanced Auditing and Professional Ethics

Question No. 1 compulsory. Attempt any five questions from the remaining six questions.

No.		Questions	Marks
1	**(a)**	Mr. Z who is appointed as auditor of Elite Co. Ltd. wants to use confirmation request as audit evidence during the course of audit. What are the factors to be considered by Mr. Z when designing a confirmation request ? Also state the effect of using positive external confirmation request by Mr. Z.	**5**
	(b)	R& M Co. wants to be alert on the possibility of non-compliance with Laws and Regulations during the course of audit of SRS Ltd. R & M Co. seeks your guidance for identifying the indications of non compliance w.i.th Laws and Regulations.	**5**
	(c)	The management of CSITA Ltd. has prepared its summary financial statements for the year 2015-16 to be provided to its investors. Consequently the company wants to appoint you for conducting audit of summary financial statements. What are the procedures that you will perform and consider necessary as the basis for forming an opinion on the summary financial statements?	**5**
	(d)	The financial statements of Ace Ltd. have been' prepared by the management in accordance with special purpose frame work to meet the financial reporting provisions of a regulator. As art auditor, what considerations would be undertaken while planning and performing an audit in case of such special purpose frame work?	**5**
2	**(a)**	ENP Ltd. engaged actuary to ascertain its employee cost, gratuity and leave encashment liabilities. As an auditor of ENP Ltd., you would like to use the report of the actuary as an audit evidence. How would you evaluate the work of the actuary?	**4**
	(b)	KSY & Co. Chartered Accountants is an audit firm having two partners CA K and CA Y. KSY & Co. is already holding appointment as auditors of 36 public companies. KSY & Co. seeks your advice in the following situations: KSY & Co. has been offered the appoiritment as Auditors of 7 more Private Limited Companies. Of the seven, one is a company with a paid up share capital of Rs. 150 crores, five are "Small companies" as per the Act and one is a " Dormant Company". (ii) Would your answer be different, if out of those 7 Private Companies, 3 Companies have paid up capital of Rs. 90 crores each?	**4**
	(c)	What are the General Steps in the conduct of Risk based Audit?	**4**
	(d)	State the key requirements of auditing standards of Public Company Accounting oversight board.	**4**
3	**(a)**	KG Ltd. wants to provide prospective Financial Information to its investors with information about future expectations of the company. You are engaged by KG Ltd. to examine the Projected Financial Information and give report thereon. What will you consider in assessing the presentation and disclosure of the prospective Financial Information and the underlying assumptions?	**4**
	(b)	M/s IO Ltd. is registered with Registrar of Companies on 1st of May 2014. The Company's 27% of paid up share capital is held by Central Government; 28% by State Government and the remaining 45% by public. The Board of Directors appointed RMG, Chartered Accountants as statutory auditors for the financial year 2014-15 by passing a resolution at the Board Meeting held on 25th May, 2014. Comment whether appointment is valid or not.	**4**

	(c)	M/s ME Ltd. is a manufacturing company of MIs Bars and Rods. The turnover of the company for financial year 2014-15 was Rs. 870 crores. The audit committee has appointed M/s MK Associates, Chartered Accountants as an internal, auditor of the company for the financial year 2015-16. As an auditor of ME Ltd., draw out' the internal audit plan specifying the coverage of area.	4
	(d)	The Board of Directors of ACP Ltd. has recommended the dividend of 15% on paid up share capital of Rs. 450, crores for the year ended 31st March, 2015, at their meeting held on 1st of May, 2015 when the accounts for the financial year 2014-15 were approved. The Board of Directors when they met on 7th July, 2015 for the review of first quarter accounts, they, realized that results were negative for the first quarter. Therefore, the Board has decided to rescind their decision to recommend dividend. The notice for AGM to be held on 14.8.2015 was sent on 15th July, 2015 without any recommendation for dividend. At the AGM, the members asked the management how they can rescind the declaration of dividend once recommended. Comment.	4
4	(a)	Mr. Arjun, a newly qualified Chartered Accountant started his practice wants to specialize in Audits of corporates and requires your advice on criminal liabilities of an auditor under the Companies Act, 2013. Kindly guide him.	4
	(b)	During the course of audit of M/s CT Ltd. for the financial year 2014-15, it has noticed that Rs. 2.00 lakhs of employee contribution and Rs. 9.50 lakhs of employer contribution towards employee state insurance contribution have been accounted in the books of accounts in respective heads. Whereas, it was found that Rs. 4.00 lakhs only has been deposited with ESIC department during the year ended 31st March, 2015. The Finance Manager informed the auditor that due to financial crunch they have not deposited the amount due, but will deposit the amount overdue along with interest as and when financial position improves. Comment as a statutory auditor.	4
	(c)	Kalmani & Co. Chartered Accountants have been appointed by C & AG for performance audit of a sugar industry. What factors should be considered by Kalmani & Co., while planning a performance audit of a sugar industry?	4
	(d)	B Pvt. Ltd. started stock broking activities in 2015 and for which it acquired membership of a stock exchange for Rs. 150 lakhs. While finalizing the accounts, the company disclosed 'the above amount under fixed assets schedule as "Stock Exchange Membership Rights'. The company also did not write off any amount since the rights would enable the company to perpetually carry on its business. As a statutory auditor how would you deal with the above situation?	4
5	(a)	Mr. Ankit, who passed his CA examination of ICAI on 18th July, 2015 had started his practice from 15th August, 2015. On 16th August, 2015 one candidate approached him for articleship. Mr. Ankit decided to give her 1% profits of his CA firm in addition to monthly stipend. She agreed to take both 1% 'of profits and prescribed stipend. The ICAI had sent a letter to Mr. Ankit objecting the payment of 1% profits. Mr. Ankit replied stating that sharing 1% profits is over and above the stipend to help the articled clerk to overcome her financial crisis. Is Mr. Ankit liable for Professional mis-conduct?	4
	(b)	Mr X is a practicing Chartered Accountant. Mr. Y is a practicing Advocate representing matters in the court of law. X and Y decided to help each other in the matters involving their professional expertise. Accordingly, Mr. X recommends Mr. Y in all litigation matters in the court of law and Y consults X in all matters relating to finance and other related matters, which comes to him in arguing various cases. Consequently they started sharing profits of their professional work. Is Mr. X liable for professional misconduct?	4

	(c)	CA Raghu is practicing in the field of Income-tax over a period of 12 years. He has gained experience in this domain over others. Sam, a student of Chartered. Accountancy Course is very much impressed with the knowledge of CA Raghu. He approached CA Raghu to take guidance on some topics of .Income-tax related to his course. CA Raghu, on request decided to spare time and started providing private tutorship to Sam and some of his friend's along with. However, he forgot to take specific permission from the ICAl, for such private tutorship. Is CA Raghu, professionally liable for misconduct?	4
	(d)	CA P and CA Q are running a firm of Chartered Accountants in the name of M/s. PQ & Co. On 21.06.2015 they included the name of CA R a practicing CA, without his knowledge, as a partner while submitting an application for empanelment as auditors for public sector banks branches to the institute. Whether CA P and CA Q are professionally liable for misconduct?	**4**
6	**(a)**	K Ltd. changed its employee remuneration policy from I" of April . 2015 to provide for 12% contribution to provident fund on leave .encashment also. The leave encashment policy provides that employees can either utilize or encash it. As at 31st March" 2016, the company obtained an actuarial valuation for leave .encashment liability. However, it did not provide for 12% PF contribution on it. The auditor of the company wants it to be provided but the management replied that as and when the employees availed leave encashment, the provident fund contribution would be made. It is further contended that this treatment is correct as it is not sure whether employees will avail leave encashment or utilize it. Comment.	**4**
	(b)	While auditing Suryakiran Insurance Ltd. as on 31st March, 2015, you observed that there is one policy which has been issued on 25th March, 2015 towards fire risk favouring one of the leading corporate houses in the country without the actual receipt of premium and it was reflected as premium receivable. It is the usual practice maintained by the company in respect of big customers that they would issue the policy before receiving the premium. The premium money was collected on 5th of April 2015. It is further noticed that there was a fire accident in the premises of insured on 31st March, and a claim was lodged. The insurance company also provided for the same. How would you respond ?	**4**
	(c)	ABC Pvt. Ltd. and XYZ Pvt. Ltd. are the Companies in which public are not substantially interested. During the previous year 2015-16, ABC Pvt. Ltd., received some property being shares of XYZ Pvt. Ltd. The details of which are provided below: No. of Shares 1000 Face Value Rs. 10 per share Aggregate Fair Market Value Rs. 1,00,000 Consideration Value Nil As the tax auditor how would you deal with the situation?	**4**
	(d)	You are appointed as tax auditor of Mr. X, a practicing advocate in Agra. During the previous year he collected Service Tax of Rs. 7 lakhs but utilized for personal use. The Commissioner of Central Excise issued a show cause notice to him why the tax collected by him is not deposited to the Government account. He appeared before the Commissioner and stated his inability to pay the sum due to financial crisis. The proceedings are still pending. Mr. X requests you not to disclose his Service Tax registration details while filling particulars to be furnished in Form No. 3CD. As a tax auditor how would you deal with this?	**4**
7		Write short notes on any four of the following:	
	(a)	Deferred Taxation	4
	(b)	Exception to the General Rule of treating advances as Non performing Assets.	4
	(c)	Advantages that accrue because of cost audit.	4

	(d)	Matters to be included in Auditor's Report in case of NBFC not accepting deposits.	4
	(e)	Areas to be reviewed in the assessment of independence of the practicing unit, while conducting peer review.	4

STUDY PLAN – KEY TO EFFECTIVE LEARNING

While studying the subject of Auditing, students should also draw their knowledge from the other subjects (Accounting, Management Accounting, Company Law, Taxation and Other subjects) and adopt an integrated approach for the purpose as this is the subject which involves application of theoretical knowledge of other subjects.

For the purpose of its full coverage student should segregate the syllabus of this paper into seven parts for preparation.

Part 1:

- Auditing & Assurance Standard
- Guidance Note

Part 2:

- Audit Strategy, Planning And Programming
- Risk Assessment, Internal Control & The Sarbane -Oxley Act Of 2002
- Audit Under Computerised Information System (CIS) Environment
- Special Audit Techniques

While doing preparation for this part, student may interlink it with Auditing Standards, specially the series of SA 300 – 499 i.e. Risk Assessment and Response to Assessed Risks and series of SA 500 – 599 Audit Evidence.

Part 3:

In this part, student should cover chapter related to Company Audit. For better understanding of this chapter, student must have good knowledge of the Companies Act, 2013 which is pre-requisite.

- Company Accounts
- Schedule III Of Companies Act, 2013
- Company Auditors
- Audit of Dividends
- Audit Committee and Corporate Governance (Clause 49 Of Listing Agreement)
- Audit of Consolidated Financial Statements
- Accounting Standard
- Cost Audit
- Audit Report

While doing study of Audit Reports, student may interlink this with series of SA 700-799 i.e. Audit Conclusion and Reporting, and Statement on Reporting under The Companies Act, 2013. Students are also required to practice the drafting of qualifications. Student may also scan through the Annual Financial Statements of Companies to analyse the notes and qualifications, if any, incorporated by the Auditors in their Audit Report.

Part 4:

- Audits of Banks
- Audit of General Insurance Companies
- Audit of Co-Operative Societies

- Audit of Non Banking Financial Companies

Part 5:

In part five, student should include following miscellaneous chapter namely:

- Audit Under Fiscal Laws (Tax Audit & Vat Audit)
- Audit of Public Sector Undertaking
- Special Audit Assignments
    - ◊ Audit of Member Of Stock Exchanges
    - ◊ Audit of Mutual Funds
    - ◊ Audit of Depositories
    - ◊ Environmental Auditing
    - ◊ Energy Audit
    - ◊ Audit of Accounts of Non Corporate Entities (Bank Borrowers)

For the preparation of part five, deep knowledge of statutory requirements is a pre-requisite for validation of adherence to the business with applicable laws. For this student should follow a check-list approach ensuring completeness of compliance validations. Further, student should update yourself with latest notification, circulars etc. Student may also interlink the above part with guidance notes already covered in part one.

Part 6:

In part six, student should cover following chapters namely:

- Internal Audit, Management & Operational Audit
- Investigation and Due Diligence
- Liabilities of Auditor
- Peer Review

Part 7:

in the seventh part student may prepare ***Professional Ethics.*** Generally it has been observed that there is one question i.e. case studies based question of 16 marks in the examination paper.

General Approach to Preparation:

- As in all other subjects of CA course, to excel in Audit, proper preparation and planning is very much important to avoid failure. Further Audit is a paper which requires a practical approach towards actual Audit work.
- Student should in the first instance focus on studying Auditing concepts, procedures and techniques (Part 1 & Part 2). The knowledge being so derived may be related by the students to the practical work in the field of Auditing which they do as part of their Articles training.
- Students are advised not to count the total number of pages before preparing for the paper/chapter.
- While reading the chapters, student should try to highlight the important lines or make appropriate headings and sub-headings. It will help you a lot in the last few days of the exams to have a quick view.
- After reading each chapter student should try to solve the case studies. While answering the case study based question, answer should be split in to two parts, first one is facts of the case and second one is the relevant concept and finally give your own conclusion. In this manner, the case study and application oriented theory questions can be answered.
- It is also advisable to mention applicable Engagement Quality Control Standards or Accounting Standards or Sections in audit paper wherever required. Answers should be crisp, precise and to the point to secure good marks.
- Student should also practice well the latest case laws and amendments. Do not add anything new near the exams.

- Audit is a subject which requires a lot of quick and logical application of mind to answer practical problems. Finally student should not forget to revise as revision is also very important to crack the examination.
- My personal view is that while studying audit paper student should consider yourself as an auditor and analyze and comment on the situation as an auditor. Be practical and think like a CA.

Some Other Important Points:

Exam strategy: At the time of taking exam student should try to attempt all the questions and start attempting the easy and short questions first and then devote time to the tough questions. Do not answer the questions in essay type presentation make precise points headings and sub-headings while writing the exam.

Preparation and Application of SA and AS in Audit: Special attention to SA and AS is required to be given. Along with good knowledge of SA and AS the technique to apply SA and AS in audit practical problems should also be clear to you all. It is also advisable to mention SA in audit paper wherever required just like sections. For example if some where going concern word is used in the context of Audit, you may mention the relevant SA/AS no. where "going concern" is defined and explain the same if you have time.

Answering Practical Questions: Practical questions play an important role in audit paper. These Practical questions mostly based on Accounting Standards and Standard of Auditing. Always remember good command over Accounting standards and Standard of Auditing and its application to practical questions are the real key to score in audit. Further Accounting Standards are also mandatory to prepare for Financial Reporting paper or Accounting paper. So give special attention to AS.

Timely revision: Another basic study point is to give ample emphasis to a good revision plan. There is nothing is this world which can substitute a good revision plan. To succeed revision is must. It is important to have good materials (notes) for last minutes revisions to secure maximum marks. Short Notes have been given at the end of this book.

Good presentation of theory: Lack of good presentation especially in theory paper is one of the major drawbacks for most of the students. In theory subjects good presentation of theory is must along with mentioning case laws and sections etc. So I'd request you all to take note of the same.

Some Important Topics for Exams

- Standard of Auditing & Guidance Notes
- Accounting Standards
- Company Audit
- Audit Report
- Professional Ethics
- Peer Review

Happy Reading and Best Wishes!

How to prepare for Theory Subjects

Time may change, technology may change, methodology of teaching and training and many other aspects of CA curriculum may change but as far as human brain is concerned, it follows some basic fundamental principles for remembering and recalling the things that has been learnt by an individual. As per my observations, I noticed some terrible mistakes that are being done by many students which I feel should be avoided.

The basic mistake I observed in those students who have the habit of not revising and not trying to recapitulate the things that they have just learnt. For example, you study Audit for the full day and will feed your brain the whole day about Audit. Now, you need to analyse how much you are able to recollect, isn't it? Or else what is the use of reading for 12 hours if you are not able to recall even the simplest of the things being read by you.

I want to give a simple example here, if you are using computer regularly, you will easily correlate this example with what I want to convey about human brain. Take an example where you are working on a file lets say this file 'Study Plan – Key to Effective Learning' and you saved it on some folder in your computer. Let's say C:\Users\Administrator\Dropbox\ Study Plan – Key to Effective Learning. Now you want to access that file and refer to this file, let's say after 3-4 months. In this case, it might be possible that you may have forgotten where you have kept this particular file unless you have accessed the file for at least 2-3 times. When you access it often, it becomes well printed in your brain where you have kept this file.

Similar to above example, our brain is also such that it can stores whatever you want to store in it; however, the retrieval power differs from person to person. The timely retrieval of information and knowledge depends on how much recalling practice you have. I was reading somewhere about human brain capacity of storage. The article revealed that human brain can store videos of around 300 years. Now, imagine what the sizes of our CA books are as compared to capacity we have got. You will wonder that human brain may be capable to even store all the existing books on this earth, you never know.

Now, the crux of the matter I want to convey you is that retrievability power. Retrievability power is our capacity to recall the stored data and knowledge as per our wish, on the day and time we want it.

Now let us analyse what our brain does when we are writing our exams? Our brain encounters a question and the answer is based on the vast amount of knowledge stored in our brain. Just like Google/Yahoo, our brain starts searching for the answer from the existing database and information bank inside itself. The more practice we have for recalling, the easier it becomes to reproduce it when required. Just stuffing the books in the storage (brain) does not help.

I want readers to do is to practice retrieval of data and information from brain. I want them to practice those things which actually matters in exams, the things that they actually do in exams. It will be much beneficial for you if you practice what you are really going to do in exams. For theory subjects, what you are going to do in exams is to face a question and retrieve relevant section or text/point from your brain in order to present your answer. It requires practice to do this in smooth manner. Retrieval practice is most important part of your preparation. Just evaluate, how much time you are dedicating for recalling and how much time you are spending in dumping the data and information in your brain. Make your own choice and chose your own result.

To put it in a summary, you are going to retrieve your knowledge based on the questions you face in exams. So, how can you imagine doing it directly in examination hall without practicing the same, without trying to get hang of the recall process and recall practice.

Below mentioned are some simple steps which everyone should follow in order to remember more and more. (What I mean by remembering is the power of retrievability and the power to recall the things when required).

Step 1: Read and Recall every hour: Take any theory subject you want to prepare, read it for an hour or so and then ask yourself what you can recall from last one hour reading. Initially it will take more time to recall but as you practice this method, it will become easier. So, don't worry and keep trying. No effort goes waste; every try of recollecting makes your brain stronger with each passing moment.

Note: Please note that those people who doesn't have any practice of this method will find it frustrating because they have never asked themselves these questions about how much they can recall. I personally have felt this frustration because I couldn't recall even the smallest of the matter in the beginning, but gradually, it became very easy with each passing day. If there is a will, there is a way. So keep trying and trying.

Step 2: Note down important points in your own words: Try to jot down those points on a page in your own words. This practice is required because what we do in exam is to write something in our own language and express. This practice will be very very useful for effective writing in exams. It's also required for efficient brain and hand synchronization while writing. Our brain can think much faster than our writing speed, so we tend to skip a word or sentences while writing. You may have experienced this while re-reading your own answers. I am sure all must have experienced this some time in their student life.

Note: Please note that jotting down points after each hour may not be feasible because of time constraints, hence, points should be noted only when you come across some important parts of your chapter or after the full reading of each chapter.

Step 3: Repeat the process of Recalling and its importance: Every hour or after two hours, repeat the process of recalling. This will make your brain super active while reading. The neurons and cells of your brain that are employed for recalling process become more and more efficient with each passing hour(s) and with each additional practice. If you keep on asking your brain what it has remembered, it will certainly understand that whatever being read is important and it will apply all its possible energy in storing and retrieving.

Table Showing Importance of Chapter on the Basis of Marks Allotment in Past Examinations

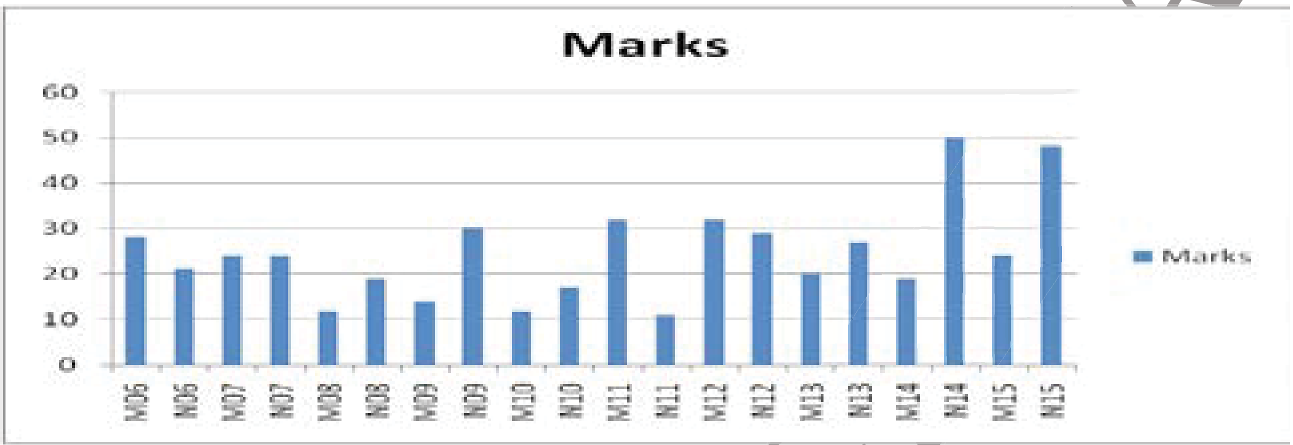
No.	Chapter	M11	N11	M12	N12	M13	N13	M14	N14	M15	N15	Total	Avg.
1	Auditing & Assurance Standard and Guidence Note	32	11	32	29	20	27	19	50	24	48	**292**	**29.2**
2	Audit Strategy, Planning and Programming	8	8	0	0	0	0	0	0	6	0	**22**	**2.2**
3	Risk Assessment, Internal Control & The Sarbane -Oxley Act Of 2002	0	9	0	0	8	4	8	4	10	4	**47**	**4.7**
4	Audit under Computerised Information System (CIS) Enviroment	4	5	6	8	4	4	4	4	0	0	**39**	**3.9**
5	Company Audit (Including Accounting Standards)	20	27	13	29	31	14	23	17	26	8	**213**	**21.3**
6	Audit Committee and Corporate Governance	0	0	4	0	0	8	4	0	0	4	**20**	**2**
7	Audit of Consolidated Financial Statements	0	0	0	4	4	9	6	0	6	4	**33**	**3.3**
8	Cost Audit	0	0	4	0	0	4	0	4	0	0	**12**	**1.2**
0	Audits of Banks	8	5	10		8	4	10	0	4	0	**49**	**4.9**
10	Audit of General Insurance Companies	4	4	4	0	5	4	6	6	4	4	**41**	**4.1**
11	Audit of Co-Operative Societies	4	0	0	0	4	4	0	4	0	4	**20**	**2**
12	Audit of Non Banking Financial Companies (NBFC)	0	0	0	6	0	0	4	0	4	4	**18**	**1.8**
13	Audit under Fiscal Laws (Tax Audit & Vat Audit)	4	15	6	4	4	4	0	4	4	4	**49**	**4.9**
14	Audit of Public Sector Undertaking	4	4	0	8	0	0	6	0	0	0	**22**	**2.2**
15	Special Audit Assignments	4	9	8	8	4	4	0	4	0	8	**49**	**4.9**
16	Internal Audit, Management & Operational Audit	4	0	4	0	4	4	3	0	4	4	**27**	**2.7**
17	Investigation and Due Diligence	4	0	8	8	4	4	4	0	4	8	**44**	**4.4**
18	Liabilities of Auditor	0	0	0	0	0	4	4	0	0	0	**8**	**8.0**
19	Peer Review	0	4	4	0	4	4	3	0	4	0	**23**	**2.3**
20	Professional Ethics	16	16	16	16	16	16	16	23	20	12	**167**	**16.7**

Contents at a Glance

List of Abbreviations

A/c	Accounts	GTD	Good till Days/Date Order
AAS	Auditing & Assurance Standard	HC	Historical Cost
AFS	Audited Financial Statement	I.Act	Insurance Act
AGM	Annual General Meeting	IC	Insurance Company
AO	Assessing Officer	IFI	Interim Financial Information
AOA	Article of Association	IOC	Immediate or Cancel Order
AON	All or None order	IR	Inherent Risk
AOP	Association of Person	IT	Income Tax
AP	Accounting Principle	LLP	Limited Lialibility Partnership
AR	Audit Report	MD	Managing Director
ARP	Analytical Review Procedures	MF	Minimum fill Order
AS	Accounting Standard	MOA	Memorandum of Association
B&P	Business & Profession	MR	Representation
BS	Balance Sheet	MRL	Management Representation Letter
BM	Board Meeting	MSCOS	Multi State Co-operative Societies Act
BOD	Board of Directors	MWCB	Market Wide Circuit Breakers
BOLT	BSE on Line Trading System	NA	Not Applicable
BSE	Bombay Stock Exchange	NEAT	National Exch. for Automated Trading system
C&AG	Comptroller and Auditor General of India	NFRA	National Financial Reporting Authority
CAAT	Computer Assisted Audit Technique	NI	Necessary Information
CEO	Chief Executive Officer	NSE	National Stock Exchange
CF	Circuit Filters	NTE	Nature, Timing & Extent
CFO	Chief Financial Officer	OLRT	On Line Real Time
CFS	Consolidate Financial Statement	OM	Other Matter Paragraph
CG	Central Government	OP	Outstanding Premium
CIS	Computer Information System	OPC	One Person Company
CLB	Company Law Board	OR	Ordinary Resolution
CN	Contract Notes	OS	Other Source
Co	Company	PM	Practice Manual
COP	Certificate of Practice	PR	Peer Review
CoR	Certificate of Registration	PRB	Peer Review Board
CR	Control Risk	PU	Practice Unit
CSR	Corporate Social Responsibility	PY	Previous Year
CY	Current Year	QC	Qualitiy Control
DQ	Disclosed Quantity Order	R&P	Receipts & Payments
DR	Detection Risk	ROC	Reigstrar of Companies
DRR	Debenture Redemption Reserve	RSS	Rolling Settlement System
DTA	Deferred Tax Assets	SFS	Summary Financial Statement
DTL	Deferred Tax Liabilities	SG	State Government
EOM	Emphasis of Matter Paragraph	SLM	Straight Line Method
FV	Fair Value	SM	Solvancy Margin
FA	Fixed Assets	SOA	Statement of Accounts
FRF	Financial Reporting Framework	SPF	Special Purpose Framwork
FRS	Financial Reporting Standard	SR	Special Resolution
FS	Financial Statements	STT	Security Transaction Tax
FY	Financial Year	TB	Trial Balance
GC	Government Company	TCWG	Those Charged with Governance
GIC	General Insurance Companies	WDV	Written Down Value
GM	General Meeting	w.e.f.	With Effect from
GMCS	General Management & Communication Skills	WR	Written Representation
GOI	Government of India	w.r.t.	With Respect to
GTC	Good till Cancelled Order	WTD	Whole time Director

1A AUDITING AND ASSURANCE STANDARDS



SRS 4400	Engagements to Perform Agreed-upon Procedures Regarding Financial Information (w.e.f. Ist April' 2004)	1.147
SRS 4410	Engagements to Compile Financial Information (w.e.f. Ist April' 2004)	1.149
	General Clarification	
	General Clarification (GC)-AASB/2/2004 on SA 210 (Refer SA 210)	
	General Clarification (GC)-AASB/1/2002 on SA 620 (Refer SA 620)	

SQC 1 — QUALITY CONTROL FOR FIRMS THAT PERFORM AUDITS AND REVIEWS OF HISTORICAL FINANCIAL INFORMATION AND OTHER ASSURANCE AND RELATED SERVICES ENGAGEMENTS. (W.E.F. IST APRIL' 2009)

1. Introduction

The objective of the SQC is to implement quality control procedures at the firm level that provide reasonable assurance that:

- The firm performs engagements in accordance with professional standards and regulatory and legal requirements, and
- Enable the firm to issue reports that are appropriate in the circumstances.

2. Element of Quality Control

The firms system of quality control should include policies and procedures w.r.t. following:

- Leadership responsibilities for quality within the firm
- Ethical requirements
- Independence
- Acceptance & continuance of client relationship & specified engagements
- Human resources
- Engagement performance
- Monitoring

2.1. Leadership Responsibilities for Quality of an audit

The engagement partner should take responsibility for the overall quality on each audit engagement to which that partner is assigned. Engagement team should have appropriate competence and capabilities to perform the audit engagement in accordance to the professional standards and regulatory and legal requirements.

2.2. Ethical Requirements

The firm should establish policies & Procedures to ensure compliance with relevant ethical requirements which include:

- Integrity
- Objectivity
- Professional competence & due care
- Confidentiality
- Professional behavior

2.3. Independence

Firm should establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and where applicable, other subject to independence requirements, maintain independence where required. For that purpose:

- Firm should communicate Independence requirements to personnel.

	• Identify circumstances that create threats to Independence. • Take appropriate action to eliminate those threats or reduce them to an acceptable level or if considered appropriate, to withdraw from engagements. • At least annually, firm should obtain written confirmation of compliance with independence from relevant firm personnel. • For listed entity, audit engagement partner should be rotated after pre-defined period (maximum 7 Years). • For all audit or attestation engagements where regulatory or other authorities require the rotation of personnel after a specified period, the firm's policies and procedures should address these requirements.
2.4	**Acceptance and Continuance of Client Relationship and Specified Engagements**
	• Firm should ensure that it will undertake / continue relationships only where it: ◊ Has considered integrity of client. ◊ Is competent to perform the engagement. ◊ Can comply with legal and ethical requirements • When issues have been identified, and the firm has decided to accept or continue the engagement, the firm should document how the issues were resolved. • After taking up work, if firm obtains information that would have caused it to decline an engagement, if information had been available earlier, then consider: ◊ Communicating it to appointing authority & regulatory authority; & ◊ Possibility of withdrawing from the engagement or from both the engagement & client relationship.
2.5.	**Human Resources**
	• Firm should establish policies & Procedures which provide a reasonable assurance that it has sufficient personnel (capable, competent & committed) to perform its engagement as per professional standard & regulatory requirements & to issue appropriate reports. • Firm should assign appropriate staff to perform engagements.
2.6.	**Engagement Performance - Consultation**
	Consultation includes discussion, at the appropriate level, with individuals within or outside the firm who have relevant specialized expertise. Firm should establish policies and procedures designed to provide it with reasonable assurance that: • Appropriate consultation takes place on different matters • The nature and scope of such consultations are documented; and • The conclusions resulting from such consultations are documented and implemented.
2.7	**Monitoring**
	• The firm should establish policies and procedures designed to provide it with reasonable assurance that the policies and procedures related to the system of QC is adequate, relevant, operating effectively and complied with in practice. This will includes ongoing evaluation of firms system of QC including a periodic inspection of completed engagements. • The firm should evaluate the effect of deficiencies noted as a result of monitoring process and should determine whether they are either: • Instances, that may not indicate insufficiency of firm Q.C • Systematic, repetitive or other significant deficiencies requiring prompt corrective action. • Firm should also communicate to relevant engagement partner, deficiencies noted and recommendations for appropriate remedial action.

- The Firm should also ensure proper dealing with complaints & Allegations about non-compliance with legal or Professional standards & firm's system of Q.C.

3. Difference of Opinion

The firm should establish policies and procedures to resolve difference of opinion within engagement Team, with those consulted & engagement partner & engagement QC reviewer. Conclusions reached should also be documented and implemented. The report should not be issued until the matter is resolved.

4. Engagement Q.C. Review

- For audits of the financial statements of listed entities, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required,
- the engagement partner shall:
  - ◊ Determine that an engagement quality control reviewer has been appointed;
  - ◊ Discuss the significant matters arising during the audit engagement, with the engagement quality control reviewer;
- The engagement quality control reviewer shall perform an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor's report. This evaluation shall involve:
  - ◊ Discussion of significant matters with the engagement partner;
  - ◊ Review of the financial statements and the proposed auditor's report;
  - ◊ Evaluation of the conclusions reached in formulating the auditor's report, and consideration of whether the proposed auditor's report is appropriate.
- For Engagement of Q.C. Review, the firm should establish policies and procedures setting out:
  - ◊ NTE of an engagement quality control review.
  - ◊ Criteria for the eligibility of engagement quality control reviewer; and
  - ◊ Documentation requirements for an engagement quality control review.

5. Completion of assembly of Final Engagement Files

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

6. Confidentiality, safe custody etc. of Engagement Documentation

The firm should establish policies and procedures designed to ensure the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation. This engagement documentation should also to be retained for sufficient period. (At least for 7 years)

7. Documentation

The firm should establish policies and procedures requiring appropriate documentation to provide evidence of the operation of each element of its system of Q.C.

SA 200 — OVERALL OBJECTIVES OF THE INDEPENDENT AUDITOR AND THE CONDUCT OF AN AUDIT IN ACCORDANCE WITH STANDARDS ON AUDITING (W.E.F. 1ST APRIL' 2010)

1. Overall objectives of the Independent Auditor [M93]

While auditing the financial statements, the overall objectives of the auditor are:

- To obtain reasonable assurance about whether the financial statements are free from material misstatements thereby enabling the auditor to express an opinion on whether financial statement are prepared as per applicable financial reporting framework; and

	• To report on financial statements and communicate as required by the SAs, in accordance with the auditor's findings. • If reasonable assurance cannot be obtained and qualified opinion is insufficient then he should either disclaim the opinion or **withdraw** from engagement, where withdrawal is legally permitted.
2.	**Definitions**
2.1	**Applicable Financial Reporting Framework**
	means, framework/law/regulations followed by the management in preparation of financial statements. (Example: Schedule III of the Co. Act, 2013, Accounting Standards etc.)
2.2	**Audit Evidence**
	Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based.
2.3	**Professional Judgment**
	The applicable of relevant training, knowledge and experience in taking appropriate decisions during audit engagement.
2.4	**Professional Skepticism**
	An attitude that includes a questioning mind being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.
2.5	**Risk of Material Misstatement**
	Risk that financial statements are misstated prior to audit. It consists of two components: Inherent risk and control Risk.
2.6	**Misstatement**
	A difference between the amounts, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Misstatement can arise from error or fraud.
3.	**Reasonable Assurance**
	Auditor is required to obtain reasonable assurance as to whether the financial statements are free from material misstatements. However, reasonable assurance is not absolute assurance. This is due to inherent limitations of an audit. Thus, auditor obtains sufficient and appropriate audit evidence to reduce audit risk to an acceptable low level.
4.	**Inherent limitations of an Audit [M89 M11]**
	Auditor cannot obtain absolute assurance. (Cannot reduce audit risk to Zero). This is due to inherent limitations of an audit due to which auditor obtains persuasive evidence rather than conclusive. It arises from:
4.1	**Nature of Financial Reporting**
	• Preparation of financial statement involves judgment by mgt. For Example, accounting estimates. Moreover, auditor has to consider whether these estimates appear to be reasonable. • There may be subjective decisions. • Evidences w.r.t. such items can only be persuasive.
4.2	**Nature of Audit Procedures**
	• Mgt. or others may not provide complete information. • Moreover frauds may involve carefully designed schemes to conceal it. Thus auditor may not detect them.
4.3	**Limitations w.r.t. Time and Cost**
	• Users expect that the auditor will form an opinion on financial statements within reasonable time and cost. • Thus auditor resorts to test procedures (not 100% checking).

- Moreover, he directs more efforts to risky areas.

Due to aforesaid inherent limitations, there is unavoidable risk that some material mis-statement may remain undetected.

5. Requirements/ Responsibilities of the Auditor

5.1 Ethical Requirements

The auditor is subject to following relevant ethical requirements including independence.

- Integrity
- Objectivity
- Professional competence and due care
- Confidentiality and
- Professional behavior
- He is also required to comply with code of ethics issued by ICAI.

5.2 Professional Skepticism

The Auditor shall plan and perform an audit with professional skepticism recognising that the circumstances may exist, that causes the financial statements to be materially mis-stated. He should

recognize the conditions indicating possible misstatements. It includes being alert to, for example:-

- Contradictory evidence
- Conditions indicating possible frauds
- Conditions questioning reliability

Moreover, it requires critical assessment of audit evidence gathered. By maintaining professional skepticism, overall risk can be reduced.

5.3 Professional Judgment

The Auditor shall exercise professional judgement in planning and performing an audit of financial statements. Professional judgement depends on facts & circumstances known to the auditor. Professional judgement should also be exercised throughout the Audit. Professional judgement is necessary regarding decisions about:-

- Materiality
- Audit risk
- NTE of audit Procedure
- Sufficiency & appropriateness of audit evidence
- Drawing of conclusions based on the audit evidence obtained.

6. Sufficient & appropriate Audit Evidence and Audit Risk

To obtain reasonable assurance, the auditor shall obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor's opinion. Sufficiency is the measure of quantity of audit evidence whereas appropriateness is the measure of quality of audit evidence.

7. Conduct of an Audit in Accordance with SAs

The auditor shall comply with all SAs relevant to the audit. An SA is relevant to the audit when the SA is in effect and the circumstances addressed by the SA exist. The auditor should have an understanding of the entire text of an SA to apply it properly. He should represent compliance with SAs in auditor's report only if he has complied with requirements of all relevant SAs. If he fails to achieve an objective in relevant SAs, in that case, he should consider the need to modify the audit report, or withdraw from the engagement. It is a significant matter requiring documentation as well.

No.	Question Bank	Exam	Marks	Refer Point
1	What are the overall objectives of the Auditor under SA 200?	M93	4	1
2	Discuss the inherent limitations of an audit.	M89 M11	4	4
3	"An auditor is responsible for expressing his opinion on financial statements in statutory audit". Comment.	M95	4	
Ans	• The primary objective of audit is to enable the auditor to express his opinion on the financial statements prepared within the framework of recognized accounting policies and relevant statutory requirements. • The opinion that he expresses should be of the "true and fair" view of the financial position and the operational results reflected in the financial statements. • As per SA 200, auditor can express his opinion on the financial statements only after obtaining reasonable assurance. To obtain reasonable assurance, the auditor shall obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor's opinion.			
4	Enumerate (in brief) the basic principles governing an audit.	N03 N05 N06 PM	4	
Ans	**Basic Principles Governing an Audit:** SA 200 on "Overall objectives of an Independent Auditor and the conduct of an audit in accordance with SAs" issued by the ICAI describes the basic principles which govern the auditor's professional responsibilities and which should be complied with whenever an audit of financial information of any entity is carried out. The basic principles as stated are as under: • **Integrity, Objectivity and Independence:** The auditor should be honest, straightforward and sincere in his approach to his professional work. He must be fair and must not allow prejudice or bias to override his objectivity. He should maintain an impartial attitude and both be and appear to be free of any interest which might be regarded, whatever its actual effect, as being incompatible with integrity and objectivity. • **Confidentiality:** The auditor should respect the confidentiality of information acquired in the course of his work and should not disclose any such information to a third party without specific authority or unless there is a legal or professional duty to disclose. • **Skills and Competence:** The audit should be performed and the report should be prepared with due professional care by persons who have adequate training, experience and competence in auditing. • **Work Performed by Others:** When the auditor delegates work to assistants or uses work performed by other auditors and experts, he will be entitled to rely on work performed by others provided he exercise adequate skill and care and is not aware of any reasons to believe that he should not have so relied. The auditor should carefully direct supervise and review work delegated to assistants and obtains reasonable assurance that work performed by other auditors or experts is adequate for his purpose since he will continue to be responsible for forming and expressing his opinion on the financial information. • **Documentation:** The auditor should document matters which are important in providing evidence that the audit was carried in accordance with the basic principles. • **Planning:** Planning enables the auditor to conduct an effective audit in an efficient and timely manner. Primarily, planning should be based on the knowledge of the client's business. Plans should be further developed and revised as necessary during the course of the audit. • **Audit Evidence:** The auditor should obtain sufficient appropriate audit evidence through the performance of compliance and substantive procedures to enable him to draw reasonable conclusions there from on which to base his opinion on the financial information. • **Accounting System and Internal Control:** The auditor should reasonably assure himself that the			

<table>
<tr><td>Ans</td><td colspan="4">accounting system is adequate and that all the accounting information which should be recorded has in fact been recorded and internal controls normally contribute to such assurance.

• Audit Conclusion and Reporting: The auditor should review and assess the conclusions drawn from the audit evidence obtained and from his knowledge of business of the entity as the basis for the expression of his opinion on the financial information. This review and assessment involves forming an overall conclusion as to whether:

◊ the financial information has been prepared using acceptable accounting policies which have been consistently applied,

◊ the financial information complies with relevant regulations and statutory requirements,

◊ There is an adequate disclosure of all material matter relevance to the proper presentation of the financial information, subject to statutory requirements, where applicable.</td></tr>
<tr><td>5</td><td>"The auditors need not review accounting policies unless there is a change in the basis of accounting ''.</td><td>M00 M08 PM</td><td>8</td><td></td></tr>
<tr><td>Ans</td><td colspan="4">The auditor while conducting an audit should critically examine the accounting policies adopted by the client and test them for conformity with the accounting standards and recommendations of the Institute. The Companies Act, 2013 as well as many other statutes requires that the financial statements of an enterprise should give a true and fair view of its financial position and working results. This requirement is implicit even in the absence of a specific statutory provision to this effect. However, what constitutes

a 'true and fair' view has not been defined either in the Companies Act, 2013 or in any other statute. The pronouncements of the Institute seek to describe the accounting principles and the methods of applying these principles in the preparation and presentation of financial statements so that they give a true and fair view. The 'Preface to the Statements of Accounting Standards' issued by the Institute in 1979 states as under:

"While discharging their attest function, it will be the duty of the members of the Institute to ensure that the Accounting Standards are implemented in the presentation of financial statements covered by their audit reports. In the event of any deviation from the Standards, it will be also their duty to make adequate disclosures in their reports so that the users of such statements may be aware of such deviations."

In cases where no pronouncement of the Institute exists, the auditor should examine the acceptability of the said accounting policy. The view presented in the financial statements of an enterprise of its state of affairs and of the profit or loss can be significantly affected by the accounting policies followed in the preparation and presentation of the financial statements. The accounting policies followed vary from enterprise to enterprise. Disclosure of significant accounting policies followed is necessary if the view presented is to be properly appreciated. It is also quite clear that there is no single list of accounting policies which are applicable to all circumstances. The differing circumstances in which enterprises operate in a situation of diverse and complex economic activity make alternative accounting principles and methods of applying those principles acceptable. The choice of the appropriate accounting principles and the methods of applying those principles in the specific circumstances of each enterprise calls for considerable judgement by the management of the enterprise. The auditor is further required to determine whether the relevant information is properly disclosed in the financial statements by considering the judgements that management has made in preparing the financial statements; accordingly, the auditor assesses the selection and consistent application of accounting policies, the manner in which the information has been classified, and the adequacy of disclosure.

Thus, the auditor should determine himself as to whether or not the said treatment is consistent with the basic principles of accounting. Therefore, it would not be correct to state that the auditor need not review the accounting policies unless there is a change in the basis of accounting.</td></tr>
<tr><td>6</td><td>Explain briefly duties and responsibilities of an auditor in case of material misstatement resulting from Management Fraud.</td><td>N09 PM</td><td>6</td><td></td></tr>
<tr><td>Ans</td><td colspan="4">Misstatement in the financial statements can arise from fraud or error. The term fraud refers to an 'Intentional Act' by one more individuals including management and TCWG. The primary responsibility for the prevention and detection of fraud rests with CWG and the management of the entity.</td></tr>
</table>

Ans

"SA 200A" indicates that an audit conducted in accordance with the "SA" is designed to provide a reasonable assurance, that the FS taken as a whole are free from any material misstatement, whether caused by error or fraud. Owing to the inherent limitations of an audit, there is some unavoidable risk, that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with the "SA" generally accepted in India. An audit does not guarantee that all material misstatement will be detected.

Certain levels of management may be in a position to override the control procedures designed to prevent similar frauds by other employees. The auditor's opinion on the FS is based on the concept of obtaining reasonable assurance. Hence, the auditor does not guarantee that material misstatements will be detected.

SA 210 | AGREEING THE TERMS OF AUDIT ENGAGEMENTS (W.E.F. 1ST APRIL' 2010)

1. Introduction

This SA is applicable to engagement relating to (a) audit of financial statements; and (b) other services like management consultancy, tax, accountancy etc. The clients and the auditor should agree on the terms of engagement by way of audit engagement letter, to avoid any misunderstanding. Auditor should send audit engagement letter preferably before commencement of engagement.

2. Preconditions for an Audit

Before accepting an audit engagement, auditor is required to ensure existence of preconditions. Accordingly, Pre-conditions to be examined are:

- Determine whether the financial reporting framework to be applied in the preparation of the financial statements is acceptable; and
- Obtain the agreement of management that it acknowledges and understands its responsibilities for followings:
  - ◊ The preparation of the F.S. in accordance with the applicable FRF.
  - ◊ Exercising necessary internal control to enable the preparation of F.S. that are free from material misstatement, whether due to fraud or error.
  - ◊ To provide the auditor with (a) Access to all relevant information such as records, documentation and other matters; (b) Additional information that the auditor may request from management for the purpose of the audit; and (c) Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

3. Limitation on Scope prior to Audit Engagement Acceptance

If management or TCWG impose a limitation on the scope of the auditor's work, and auditor believes that such limitation will result in the auditor disclaiming an opinion on the FSs, the auditor should not accept such a limited engagement as audit engagement, unless required by law or regulation to do so.

4. Principal contents of Audit Engagement Letter

4.1 Following are the mandatory items to be included in Audit Engagement Letter

- The Objective and scope of the audit
- The responsibilities of the auditor
- The responsibilities of the management
- Identification of the applicable financial reporting framework for the preparation of the financial statements
- Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

4.2 Followings items are optional to be included in Audit Engagement Letter, wherever relevant

- The fact that because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with SAs.
- The expectation that management will provide written representations.
- The agreement of management to make available to the auditor draft financial statements and any accompanying other information till time to allow the auditor to complete the audit in accordance with the proposed timetable.
- The agreement of management to inform the auditor of facts that may affect the financial statements, of which management may become aware during the period from the date of the auditor's report to the date the financial statements are issued.
- The basis on which fees are computed and any billing arrangements.
- A request for management to acknowledge receipt of the audit engagement letter and to agree to the terms of the engagement outlined therein.
- The fact that the audit process may be subjected to a peer review under the Chartered Accountants Act, 1949.
- Arrangements concerning the involvement of other auditors and experts in some aspects of the audit.
- Arrangements concerning the involvement of internal auditors and other staff of the entity.
- Any restriction of the auditor's liability when such possibility exists.
- A reference to any further agreements between the auditor and the entity.
- Any obligations to provide audit working papers to other parties.

5. Recurring Audits [M13]

The auditor may decide not to send a new audit engagement letter or other written agreement each period. However, the following factors may make it appropriate to revise the terms of the audit engagement or to remind the entity of existing terms:

- Any indication that the entity misunderstands the objective and scope of the audit.
- Any revised or special terms of the audit engagement.
- A recent change of senior management.
- A significant change in ownership.
- A significant change in nature or size of the entity's business.
- A change in legal or regulatory requirements.
- A change in the financial reporting framework adopted in the preparation of the financial statements.
- A change in other reporting requirements.

6. Acceptance of change in Engagement Terms

- The auditor should not agree to a change in the terms of the audit engagement, where there is no reasonable justification for doing so.
- Before agreeing, to change, he should also consider, any legal or contractual implications of the change.
- If the auditor is not agree with changed terms of the audit engagement & client doesn't permit him to continue with original audit engagement, then the auditor should Withdraw from the audit engagement and consider any obligation to report the circumstances to other parties such as those charged with governance, owners or regulators.

7. Additional Consideration

7.1 Financial Reporting Standards (FRS) Supplemented by Law or Regulation

If FRS established by an authorized or recognized standards setting organization are supplemented by law or regulation, the auditor should determine whether there are any conflicts between the FRS and the additional requirements. If such conflicts exist, the auditor should discuss with management the nature of the additional requirements and shall agree whether:

- The additional requirements can be met through additional disclosures in the financial statements; or
- The description of the applicable financial reporting framework in the financial statements can be amended accordingly.

If neither of the above actions is possible, the auditor should determine whether it will be necessary to modify the auditor's opinion in accordance with SA 705 (Revised).

7.2 Financial Reporting Framework prescribed by Law or Regulation

If the auditor has determined that the financial reporting framework prescribed by law or regulation would be unacceptable but for the fact that it is prescribed by law or regulation. Auditor shall accept the audit engagement only if the following conditions are present:

- Management agrees to provide additional disclosures in the financial statements required to avoid the financial statements being misleading, and
- It is recognized in the terms of the audit engagement that:
  - ◊ The auditor's report on the financial statements will incorporate an Emphasis of Matter paragraph, drawing users' attention to the additional disclosures, in accordance with SA 706(Revised), and
  - ◊ Unless the auditor is required by law or regulation to express the auditor's opinion on the financial statements by using the phrases "present fairly, in all material respects", or "give a true and fair view" in accordance with the applicable financial reporting framework, the auditor's opinion on the financial statements will not include such phrases. If the conditions outlined above are not present and the auditor is required by law or regulation to undertake the audit engagement, the auditor shall:
- Evaluate the effect of the misleading nature of the financial statements on the auditor's report; and
- Include appropriate reference to this matter in the terms of the audit engagement.

7.3. Auditor's Report Prescribed by Law or Regulation

Some times, the law or regulation applicable to the entity prescribed the layout or wording of the auditor's report in a form or in terms that are significantly differ from the requirement of SAs. In these circumstances, the auditor should evaluate:

- Whether, users might misunderstand the assurance obtained from the audit of the financial statements and, if so,
- Whether, additional explanation in the auditor's report can mitigate possible misunderstanding.

If the auditor concludes that additional explanation in the auditor's report can't mitigate possible misunderstanding, the auditor should not accept the audit engagement, unless required by law or regulation to do so.

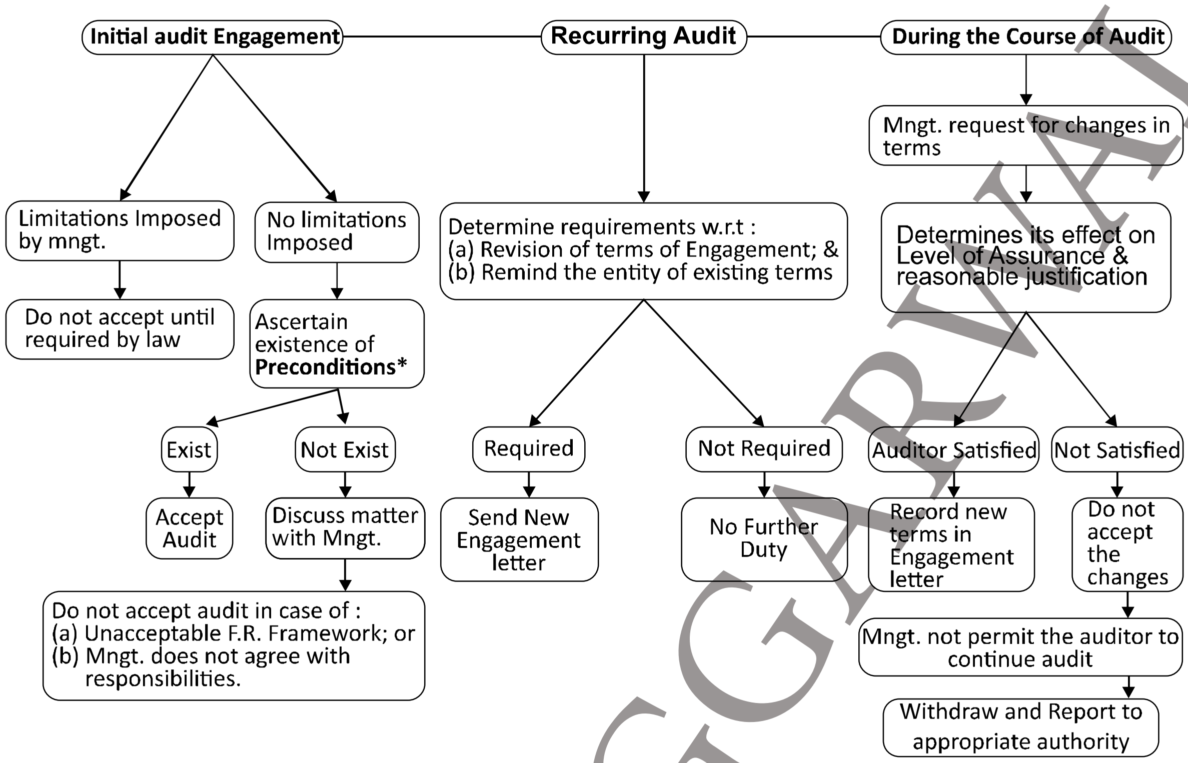
An audit conducted in accordance with law or regulation does not comply with SAs. Accordingly, the auditor should not include any reference within the auditor's report to the audit having been conducted in accordance with SAs.

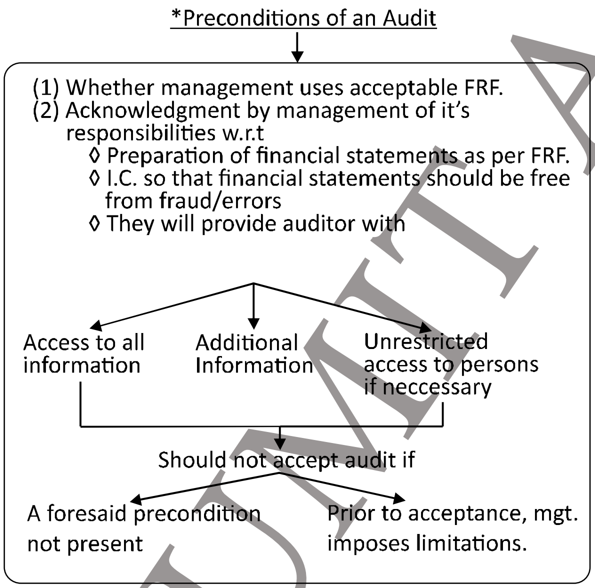
8. GENERAL CLARIFICATION (GC) – AASB/2/2004 ON SA 210

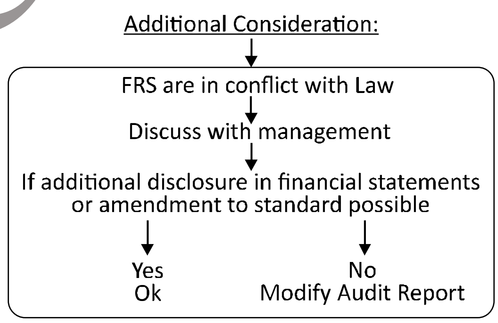
- Whether it is necessary that the engagement letter issued by the auditor should be acknowledged by addressee and returned to the auditor to indicate that the client's understanding of the terms of the engagement is in accordance with SA 210.

	• As prescribed in SA 210, 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 ICAI,*** 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 u/s 143 of the Companies Act, 2013, audit of public sector banks, etc. In such cases, it is not necessary that the engagement letter sent by the auditor in accordance SA 210 is acknowledged by the addressee and returned to 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. In such cases, the auditor should take necessary steps to resolve the issues. • 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 that (a) 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 sending the audit engagement letter.
9.	**Format of Audit Engagement Letter [N07]:** Refer Chapter 23

Summary SA 210







No.	Question Bank	Exam	Marks	Refer Point
1	R & Co, a firm of Chartered Accountants have not revised the terms of engagements and obtained confirmation from the clients, for last 5 years despite changes in business and professional environment. Please elucidate the circumstances that may warrant the revision in terms of engagement.	M13 PM	4	5
2	M/s. PQR & Company, Chartered Accountants have been appointed Statutory Auditors of a listed Company for the year ended 31st March, 2008. Draft an appropriate engagement letter to be sent to the Board of Directors for the same.	N07 PM	8	9

SA 220 QUALITY CONTROL FOR AN AUDIT OF FINANCIAL STATEMENTS (W.E.F. 1ST APRIL' 2010)

1. Objective

The objective of the auditor is to implement quality control procedures at the engagement level that provide the auditor with reasonable assurance that:

- The audit complies with professional standards and regulatory and legal requirement; and
- The auditor's report issued is appropriate in the circumstances.

2. Responsibility of the Engagement Partner

To ensure quality control for an audit of financial statements for particular audit engagement, the engagement partner should follow the following requirements:

- **Leadership Responsibilities:** The engagement partner should take responsibility for the overall quality on each audit engagement to which that partner is assigned.
- **Ethical Requirement:** Member of the engagement team should comply with relevant ethical requirements.
- **Independence:** The engagement partner should form a conclusion on compliance with independence requirements.
- **Acceptance and Continuation of Client Relationship and Audit Engagement:** The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationship and audit engagements have been followed.
- **Assignment of Engagement Teams:** The engagement partner should satisfied himself that engagement team have the appropriate competence and capabilities to
  - ◊ Perform the audit engagement in accordance with professional standards and regulatory and legal requirements, and
  - ◊ Enable an auditor's report that is appropriate in the circumstances to be issued.
- **Engagement Performance:** The engagement partner should take responsibility for the direction, supervision and performance of the audit engagement team and should satisfy that sufficient appropriate audit evidence has been obtained to support the conclusions and the auditor's report.
- **Consultation:** The engagement partner should take responsibility for the engagement team that they are taking appropriate consultation for difficult matters.
- **Difference of Opinion:** If difference of opinion arises, the engagement team should follow the firm's policies and procedures for dealing with and resolving differences of opinion.

3. Engagement Quality Control Review

For audits of financial statements of listed entities and those other audit engagement for which the engagement quality control reviews is enquired, the engagement partner should:

- Determine that an engagement quality control reviewer has been appointed; and
- Discuss significant matters arising during audit engaement with the engagement quality control reviewer.

The Engagement Quality Control Reviewer should evaluate the following:

- Discussion of significant matters with the engagement partner.
- Review of the financial statements and the proposed auditor's report.
- Review of selected audit documentation; and
- Conclusion reached in formulating the auditor's report and consideration of whether the proposed auditor's report is appropriate.

4.	**Monitoring**
	An effective system of quality control includes a monitoring process designed to provide the firm with reasonable assurance that its policies and procedures relating to the system of quality control are relevant, adequate and operating effectively.
5.	**Documentation**
5.1	**The Auditor shall document**
	• Issue identified w.r.t. compliance with relevant ethical requirements and how they were resolved. • Conclusions on compliance with independence requirements that apply to the audit engagement, and any relevant discussions with the firm that support these conclusions. • Conclusions reached regarding the acceptance and continuance of client relationships and audit engagements. • The nature and scope of, audit conclusions resulting from, consultations undertaken during the course of the audit engagement.
5.2	**The Engagement Quality Control Reviewer shall document, for the Audit Engagement reviewed that**
	• The procedures for engagement quality control review have been performed. • The engagement quality control review has been completed on or before the date of the auditor's reports. • The reviewer is not aware of any unresolved matters.

SA 230 AUDIT DOCUMENTATION (W.E.F. 1ST APRIL' 2009)

1.	**Scope of this SA**
	This SA deal with auditor's responsibility to prepare audit documentation for an audit of financial statements. The specific documentation requirements of other SAs do not limit the application of this SA. Laws or regulations may establish additional documentation requirements.
2.	**Nature and Purpose of Audit Documentation**
	Audit documentation refers to the working papers prepared or obtained and retained by the auditors for his audit work. Audit documentation serves the following purpose: • Evidence that support the auditor opinion in his audit report; and • Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements. **Audit documentation serves a number of additional purposes including the following:** • Assisting the engagement team to plan and perform the audit. • Assisting members of the engagement team responsible for supervision to direct and supervise the audit work. • Enabling the engagement team to be accountable for its work. • Retaining a record of matters of continuing significance to future audits. • Enabling the conduct of quality control reviews and inspections in accordance with SQC 1. • Enabling the conduct of external inspection in accordance with applicable legal, regulatory or other requirements.
3.	**Experienced Auditor**
	An individual (whether internal or external to the firm) who has practical audit experience, and a reasonable understanding of:

- Audit processes
- SAs and applicable legal and regulatory requirements
- The business environment in which the entity operates; and
- Auditing and financial reporting issues relevant to the entity's industry.

4. Form, Content and Extent of Audit Documentation

The auditor should prepare audit documentation that is sufficient to enable an experienced auditor having no previous connection with the audit to understand:-

- The nature, timing and extent of the audit procedures performed to comply with the SA, and applicable legal and regulatory requirements.
- The results of the audit procedures performed, and the audit evidence obtained; and
- Significant matters arising during the audit and the conclusions reached thereon and significant professional judgments made in reaching those conclusion.

If the auditor identified information that is inconsistent with the auditor's final conclusion regarding significant matter, the auditor should document how the auditor addressed the inconsistency.

The auditor should document discussions of significant matters with management, including the nature of discussion and when and with whom the discussions took place.

5. Factor Governing Form & Content of Working Papers

The form, content and Extent of audit documentation depend on factors such as:-

- The size and complexity of the entity.
- The nature of the audit procedure to be performed.
- The identified risk of material misstatement.
- The significance of the audit evidence obtained.
- The nature and extent of exceptions identified.
- The audit methodology and tool used.

6. Departure from a Relevant Requirement

If, in exceptional circumstances, the auditor departs from a relevant requirement in a SA, the auditor should document the reasons for the departure and alternative procedures performed.

7. Matters Arising after the Date of the Auditor's Report

If, it exceptional circumstances, the auditor performs new or additional audit procedures or draws new conclusions after the date of the auditor's report, the auditor should document:

- The circumstances encountered.
- The new or additional audit procedures performed, audit evidence obtained, and conclusions reached, and their effect on the auditor's report; and
- When and by whom the resulting changes to audit documentation were made and reviewed.

8. Assembly of the Final Audit File

- The auditor should assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report. (SQC -1: Time limit 60 days after the date of the auditor's report)
- After the assembly, the auditor should not delete audit documentation of any nature before the end of its retention period. (SQC-1 : minimum 7 years)
- In exceptional circumstances, if the auditor finds it is necessary to modify existing audit documentation or add new documentation after the assembly of the final audit file, the auditor should document, the (a) specific reasons for making such modification/addition; and (b) when and by whom they were made and reviewed.

No.	Question Bank	Exam	Marks	Refer Point
1	As an auditor how would you deal with the following: The statutory auditor of the holding company demands for the working paper of the auditors of the subsidiary company, of which you are the auditor?	Case Study		
Ans	As per SA 230, "Audit Documentation" working papers are the property of the auditor. The auditor may, at his discretion, make portion of or extracts of his working papers available to his client. SA 600 "Using the Work of Another Auditors" also states that an auditor should respect the confidentiality of information acquired during the course of his audit work and should not disclose such information unless there is a legal or professional duty to disclose. As per ICAI Guidelines, statutory auditor of an enterprise do not have right of access to the audit working papers of the branch auditor. An auditor can rely on the work of another auditor, without having any right of access to the audit working papers of other auditor. **Conclusion:** Statutory auditor of Holding company cannot have access to audit working papers of the subsidiary company's auditor. He can however, asks the auditor to answer certain questions about the manner in which the audit is conducted and certain other clarifications regarding audit.			
2	Mr. A, a practising Chartered Accountant, has been appointed as an auditor of True Pvt. Ltd. What factors would influence the amount of working papers required to be maintained for the purpose of his audit ?	N15	5	5

SA 240 — THE AUDITOR'S RESPONSIBILITIES RELATING TO FRAUD IN AN AUDIT OF FINANCIAL STATEMENTS (W.E.F. 1ST APRIL' 2009)

1.	**Characteristics of Fraud**
	Misstatement in the financial statements can arise from either fraud (intentional) or error (unintentional). Fraud refers to intentional misrepresentation of financial information by one or more individuals among employees, management those charged with governance, or third parties. The auditor is concerned with fraud that causes a material misstatement in the financial statements.
2.	**Responsibility for the Prevention and Detection of Fraud**
	The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance and for this purpose they should implement and continuously operate an adequate system of internal control which may reduce the opportunities for fraud to take place.
3.	**Auditor's Responsibilities relating to fraud in an audit of Financial Statements [N09]**
	• An auditor is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free material misstatement, whether caused by fraud or error. • When obtaining reasonable assurance, the auditor is responsible for maintaining an attitude of professional skepticism throughout the audit. • As described in SA 200, due to the inherent limitation of an audit, there is an unavoidable risk that some material misstatement of the financial statements will not be detected, even though the audit is properly planned and performed in accordance with the SAs. • The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error. This is because fraud may involve sophisticated and carefully organized schemes designed to conceal it. • It is difficult for the auditor to determine whether misstatements in judgment areas such as accounting estimates are caused by fraud or error. • The risk of the auditor not detecting a material misstatement resulting from management fraud is

greater than for employee fraud because management can easily manipulate accounting records.

- If conditions cause the auditor to believe that a document may not be authentic or that terms in document have been modified, the auditor shall investigate further.
- Where responses to inquiries of management or TCWG are inconsistent, the auditor shall investigate the inconsistencies.

4. Objectives:

The objectives of the auditor are

- To identify and assess the risks of material misstatement in the financial statements due to fraud.
- To obtain sufficient appropriate audit evidence about the assessed risks of material misstatement due to fraud. and
- To respond appropriately to identified or suspected fraud.

5. Professional Skepticism

Professional skepticism means an approach that would ensure that if something is wrong, it is detected. This attitude of auditor helps him in identifying and evaluating

- Matter that increase the risk of material misstatements resulting from fraud or error,
- Circumstances that make the auditor to suspect material misstatements, and The question of managements' representations reliability. The auditor is entitled to accept the records and documents as genuine unless, there is some evidence to the contrary.

6. Discussion with the Audit Team

The auditor must discuss with the other members of the audit team regarding the possibility and suspicion of material misstatement in the financial statement resulting from fraud or error. This discussion should occur notwithstanding the engagement team member's beliefs that management and those charged with governance are honest and have integrity.

7. Risk Assessment Procedures and Related Activities

When performing risk assessment procedures and related activities to obtain an understanding of the entity and its environment, including the entity's internal control, required by SA 315, the auditor should perform the following procedures to obtain information for use in identifying the risks of material misstatement due to fraud:

7.1 Enquiring Management and Others within the Entity

The auditor should enquire the management on the following matters:

- Management understands regarding the accounting and internal control systems to prevent and detect error.
- Awareness of any known fraud by the management.
- Management's process for identifying & responding to the risks of fraud in the entity, including any specific risks of fraud.
- Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to employees regarding its views on business practices and ethical behavior.
- For those entities that have an internal audit function, the auditor should make inquiries of internal auditor.

7.2 Enquiring Those Charged with Governance

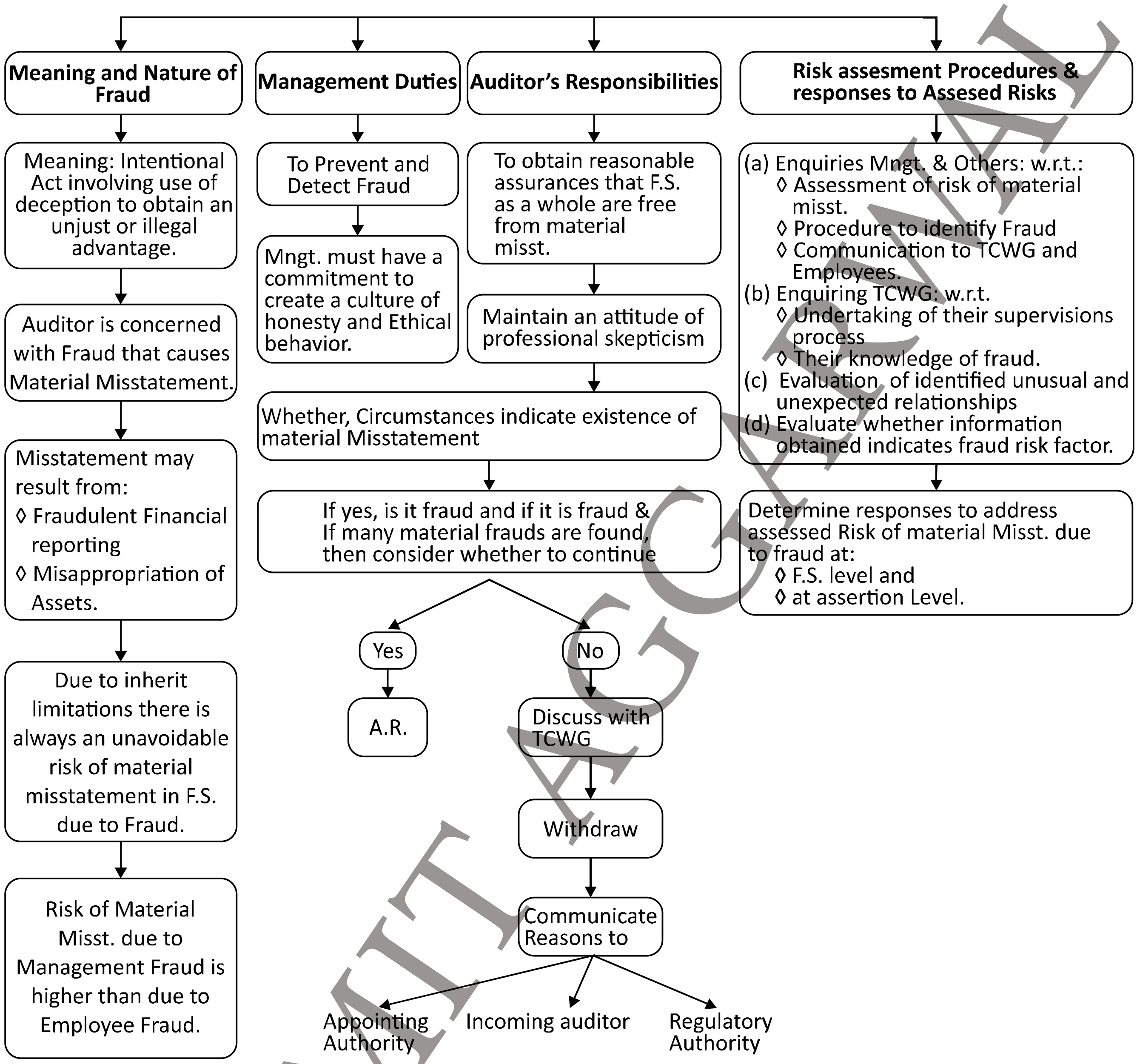
- He should obtain an understanding of how they supervise management's processes.
- The auditor shall ask whether they have knowledge of any fraud affecting the entity.

7.3 Unusual or Unexpected Relationships Identified

	The auditor should evaluate whether unusual or unexpected relationships identified in performing analytical procedures, may indicate risks for material misstatement due to fraud.
7.4	**Other Information**
	The auditor should consider whether other information obtained by the auditor indicates risks of material misstatement due to fraud.
8.	**Evaluation of Fraud Risk Factors**
	The auditor should evaluate whether the information obtained from the other risk assessment procedures and related activities performed indicates that one or more fraud risk factors are present. However, fraud risk factors may not necessarily indicate the existence of fraud.
9.	**Identification and Assessment of the Risks of Material Misstatement Due to Fraud**
	• In accordance with SA 315, the auditor should identify and assess the risks of material misstatement due to fraud at the financial statement level, and at the assertion level for classes of transactions, account balances and disclosures. • The auditor should, based on a presumption that there are risks of fraud in revenue recognize, evaluate which types of revenue, revenue transactions or assertions give rise to such risks. • The auditor should treat those assessed risks due to fraud as significant risks and accordingly, to the extent not already done so, the auditor should obtain an understanding of the entity's related controls, including control activities, relevant to such risks.
10.	**Auditor Response**
10.1	**Responses to the Assessed Risks of Material Misstatement Due to Fraud**
	• In accordance with SA 330, the auditor should determine overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level. In determining overall responses, the auditor should: • Assign and supervise audit team as per their capability; • Evaluate whether accounting policies adopted by the entity, indicate fraudulent financial reporting, resulting from management's effort to manage earnings; and • Incorporate surprise element in the selection of the nature, timing and extent of audit procedures.
10.2	**Responses to Assessed Risks of Material Misstatement Due to Fraud at the Assertion Level**
	The auditor should design and perform further audit procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement due to fraud at the assertion level.
10.3.	**Responses to Risks Related to Management Override of Controls**
	Management is in a unique position to perpetrate fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls. The auditor should design and perform audit procedures in the area relating to (a) Journal Entries (b) Accounting Estimates, and (c) Unusual transactions. The auditor should also determine whether the auditor needs to perform extra audit procedures.
11.	**Evaluation of Audit Evidence**
	• The auditor should evaluate whether analytical procedures are consistent with the auditor's understanding of the entity and its environment. • When the auditor identifies a misstatement, the auditor should evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the auditor should evaluate the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management representations. • If the auditor identifies a misstatement, and the auditor has reason to believe that it is or may be the result of fraud and that management is involved, the auditor should re-evaluate the assessment of the risks of material misstatement due to fraud and its resulting impact on the NTE of audit procedures.

	• When the auditor confirms that, or is unable to conclude whether, the financial statements are materially misstated as a result of fraud; the auditor should evaluate the implications for the audit.
12	**Auditor Unable to Continue the Engagement [N06]**
	If, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounter exceptional circumstances that bring into question the auditor's ability to continue performing the audit, the auditor shall: • Determine the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities. • Consider whether, it is appropriate to withdraw from the engagement, where withdrawal from the engagement is legally permitted; and • If the auditor withdraws: ◊ Discuss with the appropriated level of management and those charged with governance, the auditor's withdrawal from the engagement and the reasons for the same; and ◊ Determine whether there is a professional or legal requirement to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities, the auditor's withdrawal from the engagement and the reasons for the same.
13	**Management Representations**
	The auditor should obtain a management representation that: • They acknowledge their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud. • They have disclosed to the auditor the result of its assessment of the risk of fraud. • They have disclosed to the auditor their knowledge of fraud or suspected fraud affecting the entity involving (a) Management; (b) Employees who have significant roles in internal control; or (c) Others; and • They have disclosed to the auditor, its knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.
14.	**Communications to Management and TCWG**
	If the auditor has identified a fraud or has indication of fraud, the auditor should communicate these matters to the appropriate level of management on a timely basis. He should also communicate with TCWG, any other matters related to fraud that are, in the auditor's judgment, relevant to their responsibilities.
15.	**Communications to Regulatory and Enforcement Authorities**
	As per SA 200, the auditor should not disclose the client's information to anybody without the client's permission or under any regulatory requirement. But in certain circumstances, the statute, the law or courts may override the duty of confidentiality.
16.	**Documentations**
	The auditor should document the following in his working papers: • The risk factors identified at present. • The auditor response to those risk factors. • Inquiring of management regarding the risk of fraud in the entity. • Entity programme for prevention or detection of fraud.

Summary SA 240



No.	Question Bank	Exam	Marks	Refer Point
1	Explain briefly duties and responsibilities of an auditor in case of material misstatement resulting from Management Fraud.	N09 PM	6	3
2	As a Statutory Auditor, how would you deal with a misstatement resulting from fraud or suspected fraud during the audit and conclude that it is not possible to continue the performance of audit.	N06 PM	5	12
3	The teeming and lading fraud was detected and the amount involved was subsequently deposited by the Executive Director of the company and, therefore, need not be reported upon.	N99	4	
4	The Managing Director of 'the Company has committed a "Teeming and Lading" Fraud. The amount involved has been however subsequently after the year end deposited in the company.	N99 M05 PM	4	

Ans	• The Managing Director of the company has committed a "Teeming and Lading" fraud. The fact that the amount involved has been subsequently deposited after the year end is not important because the auditor is required to perform his responsibilities as laid down in SA 240, "The Auditor's responsibilities relating to Fraud in an Audit of Financial Statements". • First of all, as per SA 240, the auditor needs to perform procedures whether the financial statements are materially misstated. Because an instance of fraud cannot be considered as an isolated occurrence and it becomes important for the auditor to perform audit procedures and revise the audit risk assessment. • Secondly, the auditor needs to consider the impact of fraud on financial statements and its disclosure in the audit report. • Thirdly, the auditor should communicate the matter to the Chairman and Board of Directors. • Finally, in view of the fact that the fraud has been committed at the highest level of management, it affects the reliability of audit evidence previously obtained since there is a genuine doubt about representations of management. Finally, the auditor shall have to report under CARO, 2003 indicating the nature and amount involved in respect of fraud noticed during the year.			
5	While conducting statutory Audit of ABC Ltd., you come across IOUs amounting to Rs. 2 crores as against a cash balance shown in books of Rs. 2.10 crores. You also observe that despite similar high balances throughout the year, small amounts of Rs. 50,000 are withdrawn from the bank to meet day-today expenses.	J09 PM	5	
Ans	• According to SA 240, "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements" when, the auditor comes across such circumstances indicating the possible misstatements resulting from the fraud, then the auditor needs to consider the impact of fraud on financial statements and its disclosure in the audit report. In this case, the circumstances indicate that the possible misstatement in financial statements is due to fraud and error and the auditor must investigate further to consider effect on financial statements. • The Guidance Note on Audit of Cash and Bank balances also mentions that if the entity is maintaining an unduly large balance of cash, he should carry out surprise verification of cash more frequently to ascertain whether it agrees. If cash in hand is not in agreement with the book balance, he should seek explanations and if the same are not satisfactory should state the said fact appropriately in his Audit Report.			
6	In the course of audit of A Ltd. you suspect that the management has indulged in fraudulent financial reporting. State the possible source of such fraudulent financial reporting.	M12 PM	6	
Ans	As per SA 240, "The Auditor's responsibilities relating to Fraud in an Audit of Financial Statements", fraudulent financial reporting involves intentional misstatements or omissions of amounts or disclosures in financial statements to deceive financial statement users. It may be accomplished by manipulation, falsification, or alteration of accounting records or supporting documents from which the financial statements are prepared. or Misrepresentation in, or intentional omission from, the financial statements of events, transactions or other significant information or intentional misstatements involve intentional misapplication of accounting principles relating to measurement, recognition, classification, presentation, or disclosure etc. It often involves management override of controls, misappropriation of assets etc, that otherwise may appear to be operating effectively. Fraud can be committed by management overriding controls using such techniques as: • Recording fictitious journal entries, particularly close to the end of an accounting period, to manipulate operating results or achieve other objectives. • Inappropriately adjusting assumptions and changing judgments used to estimate account balances. • Omitting, advancing or delaying recognition in the financial statements of events and transactions that have occurred during the reporting period. • Concealing, or not disclosing, facts that could affect the amounts recorded in the financial statements.			

	• Engaging in complex transactions that are structured to misrepresent the financial position or financial performance of the entity. • Altering records and terms related to significant and unusual transactions. • Embezzling receipts (for example, misappropriating collections on accounts receivable or diverting receipts in respect of written-off accounts to personal bank accounts). • Stealing physical assets or intellectual property (for example, stealing inventory for personal use or for sale, stealing scrap for resale, colluding with a competitor by disclosing technological data in return for payment). • Causing an entity to pay for goods and services not received (for example, payments to fictitious vendors, kickbacks paid by vendors to the entity's purchasing agents in return for inflating prices, payments to fictitious employees). • Using an entity's assets for personal use (for example, using the entity's assets as collateral for a personal loan or a loan to a related party).			
7	M/s Honest Limited has entered into a transaction on 5th March, 2013, near year-end, whereby it has agreed to pay Rs. 5 lakhs per month to Mr. Y as annual retainer-ship fee for "engineering consultation". No amount was actually paid, but Rs. 60 lakhs is provided in books of account as on March 31, 2013. Your inquiry elicits a response that need-based consultation was obtained round the year, but there is no documentary or other evidence of receipt of the service. As the auditor of M/s Honest Limited, what would be your approach?	N13 PM	5	
Ans	As per SA 240 on "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", fraud can be committed by management overriding controls using techniques such as recording fictitious journal entries, particularly close to the end of an accounting period, to manipulate operating results or to achieve other objectives. Keeping in view the above, it is clear that Company has passed fictitious journal entries close to the end of an accounting period to manipulate the operating results. Also Auditor's enquiry elicited a response that need-based consultation was obtained round the year, but there is no documentary or other evidence of receipt of the service, is not acceptable. Accordingly, the auditor would adopt the following approach: If, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit, the auditor should: • Determine the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the auditor appointment or, in some cases, to regulatory authorities; • Consider whether it is appropriate to withdraw from the engagement, where withdrawal is legally permitted; and • If the auditor withdraws: ◊ Discuss with the appropriate level of management and TCWG, the auditor's withdrawal from the engagement and the reasons for the withdrawal; and ◊ Determine whether there is a professional or legal requirement to report to the person(s) who made the auditor appointment or, in some cases, to regulatory authorities, the auditor's withdrawal from the engagement and the reasons for the withdrawal.			
8	In the course of audit of K Ltd., its auditor Mr. 'N' observed that there was a special audit conducted at the instance of the management on a possible suspicion of a fraud and requested for a copy of the report to enable him to report on the fraud aspects. Despite many reminders it was not provided. In absence of the special audit report, Mr. 'N' insisted that he be provided with at least a written representation in respect of fraud on/by the company. For this request also, the management remained silent. Please guide Mr. 'N'.	M14 PM	5	

Ans	**Auditors Responsibilities Relating to Fraud** • As per SA 240, “The Auditor’s Responsibilities relating to Fraud in an Audit of FS”, the primary responsibility for the prevention and detection of fraud rests with both TCWG and management. In addition an auditor conducting an audit in accordance with SAs is responsible for obtaining reasonable assurance that the FS taken as a whole are free from material misstatement, whether caused by fraud or error. • As per SA 580, “Written Representations (WR)”, If management does not provide one or more of the requested WR, the auditor shall discuss the matter with management; re-evaluate the integrity of management and evaluate the effect that this may have on the reliability of representations (oral or written) and audit evidence in general; and take appropriate actions, including determining the possible effect on the opinion in the auditor’s report. • The auditor shall disclaim an opinion on the FS if the auditor concludes that there is sufficient doubt about the integrity of management such that the WR are not reliable; or management does not provide the WR. • Further the auditor is also required to report as per Paragraph 4 (xxi) of CARO, 2003, if there is any fraud on or by the company has been noticed or reported during the year. If yes, the nature and the amount involved is to be indicated. • In the given case, in the course of audit of K Ltd., its auditor Mr. N observed that there was a special audit conducted at the instance of the management on a possible suspicion of fraud. Therefore, the auditor requested for special audit report, which was not provided by the management despite of many reminders. Mr. N also insisted for WR in respect of fraud on/by the company. For this request also management remained silent. • Hence, the fact is required to be reported as per Paragraph 4(xxi) of the CARO, 2003 and the auditor should also disclaim an opinion on the FS.			
9	In the books of accounts of M/s ABC Ltd. huge differences are noticed between the control accounts and subsidiary records. The Chief Accountant informs that this is common due to huge volume of business done by the company during the year. As a Statutory Auditor, how would you deal?	PM		
Ans	• The huge differences found between control accounts and subsidiary records in the books of ABC Ltd indicate that there may be material misstatements requiring detailed examination by the auditor to ascertain the cause. • The contention of Chief Accountant cannot be accepted simply because the company has done huge volume of business. • Such a phenomenon indicates that recording of transactions is not being done properly or the accounting system in the company which might have several branches spread over the country fails to capture all transactions in time. • It would also be interesting to see whether it is a recurring phenomenon or such reconciliation could not be done at a subsequent date. • Having regard to all these circumstances, it appears from the facts of the case that these differences indicate the possibility of some kind of material misstatements. • As per SA 240, "The Auditor's Responsibilities relating to Fraud in an Audit of Financial Statements", when the auditor identifies a misstatement, the auditor shall evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the auditor shall evaluate the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management representations, recognizing that an instance of fraud is unlikely to be an isolated occurrence. • When the auditor confirms that, or is unable to conclude whether, the FSs are materially misstated as a result of fraud the auditor shall evaluate the implications for the audit.			

SA 250	CONSIDERATION OF LAWS AND REGULATIONS IN AN AUDIT OF FINANCIAL STATEMENTS (W.E.F. 1ST APRIL' 2009)

1. Scope of this SA

This SA deals with the auditor's responsibility to consider laws and regulations when performing an audit of financial statements. This SA does not apply to other engagements in which the auditor is specifically engaged to test and report on non-compliance of specific laws or regulations.

2. Effect of Laws and Regulation

- The provision of some laws or regulation have a direct impact on the financial statements in that, they determine the reported amounts and disclosures in an entity's financial statements such as tax and labour laws, and
- Other laws or regulation are to be complied with by management but do not have a direct effect on an entity's financial statements such as compliance with environmental regulations etc.
- Some entities operate in heavily regulated industries (such as banks and chemical companies).
- Non-compliance with laws and regulation may result in fines, litigation of other consequences for the entity that may have a material effect on the financial statements.

3. Responsibility of Management for Compliance with Laws and Regulations

It is the responsibility of management to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations. For this purpose management may apply the following procedures:

- Monitoring legal requirements and ensuring that operating procedures are designed to meet these requirements.
- Instituting and operating appropriate systems of internal control.
- Developing, Publishing and following a code of conduct.
- Ensuring employees are properly trained and understand the code of conduct.
- Monitoring compliance with the code of conduct and acting appropriately to discipline employees who fail to comply with it.
- Engaging legal advisors to assist in monitoring legal requirements.
- Maintaining a register of significant laws and regulations with which the entity has to comply within its particular industry and a record of complaints.

4. Responsibility of the Auditor

- The requirements in this SA are designed to assist the auditor in identifying material misstatement of the financial statements due to non-compliance with laws and regulations.
- However, the auditor is not responsible for preventing non compliance and cannot be expected to detect non-compliance with all laws and regulations.
- "The auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether caused by fraud or error." Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements in the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the SAs.
- Sometimes the auditor may be specifically required to report, as part of the audit of the financial statements, on whether the entity complies with certain provisions of laws or regulations.

5. The Auditor's Consideration of Compliance with Laws and Regulations [N14]

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Also Available on amazon.in and flipkart.com

ISBN 81-9305802-X
9788193058022