

11. STANDARDS ON AUDITING

| A. STANDARDS FOR CLASS ROOM DISCUSSION: | | |
|--|--------|--|
| 1. | SA 250 | Consideration of Laws and Regulations in an audit of financial statements |
| 2. | SA 260 | Communication with Those charged with governance |
| 3. | SA 265 | Communicating deficiencies in internal control with those charged with governance and management |
| 4. | SA 501 | Audit Evidence - Specific Considerations for Selected Items |
| 5. | SA 505 | External Confirmations |
| 6. | SA 510 | Initial Audit Engagements - Opening Balances |
| 7. | SA 540 | Auditing Accounting Estimates, Including Fair Value Accounting Estimates and Related Disclosures |
| 8. | SA 560 | Subsequent Events |
| 9. | SA 570 | Going Concern |
| 10. | SA 580 | Written Representations |
| 11. | SA 620 | Using the Work of an Auditor's Expert |
| B. STANDARDS ALREADY COVERED AS PART OF VARIOUS CHAPTERS: | | |
| 12. | SA 200 | Overall Objectives of an Independent auditor and conduct of an audit in accordance with standards on auditing (Chapter - 2 - Nature of Auditing) |
| 13. | SA 210 | Agreeing the terms of audit engagement (Chapter - 2 - Nature of Auditing) |
| 14. | SA 230 | Audit Documentation (Chapter - 4 - Audit Documentation) |
| 15. | SA 240 | Auditors responsibility relating to fraud in an audit of financial statements (Chapter - 9 - Fraud reporting) |
| 16. | SA 299 | Responsibility of Joint auditor's (Chapter - 5 - Company auditors) |
| 17. | SA 300 | Planning an audit of financial statements (Chapter - 3 - Audit Strategy) |
| 18. | SA 315 | Identifying and assessing risk of material misstatement through understanding the entity and its environment. (Chapter - 8 - Risk assessment) |
| 19. | SA 500 | Audit Evidence (Chapter - 4 - Audit Documentation) |
| 20. | SA 600 | Using the Work of Another Auditor (Chapter - 6 - Audit Reporting) |
| 21. | SA 610 | Using the Work of Internal Auditors (Chapter - 6 - Audit Reporting) |
| 22. | SA 700 | Forming an Opinion and Reporting on Financial Statements (Chapter - 6 - Audit Reporting) |
| 23. | SA 701 | Communicating Key Audit Matters in the Independent Auditor's Report (Chapter - 6 - Audit Reporting) |
| 24. | SA 705 | Modifications to the Opinion in the Independent Auditor's Report (Chapter - 6 - Audit Reporting) |
| 25. | SA 706 | Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report (Chapter - 6 - Audit Reporting) |
| C. STANDARDS FOR SELF STUDY: | | |
| 26. | SA 320 | Materiality in planning and performing an audit |
| 27. | SA 330 | The Auditor's Responses to Assessed Risks |
| 28. | SA 520 | Analytical Procedures |
| 29. | SA 530 | Audit Sampling |
| 30. | SA 550 | Related Parties |
| D. ADVANCED STANDARDS (WILL BE GIVEN LATER) | | |
| 31. | SA 220 | Quality Control for an audit of Financial statements |
| 32. | SA 402 | Audit Considerations Relating to an Entity Using a Service Organisation |
| 33. | SA 450 | Evaluation of Misstatements identified During the Audit |
| 34. | SA 710 | Comparative Information - Corresponding Figures and Comparative Financial Statements |
| 35. | SA 720 | The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Statements |

SA 200: OVERALL OBJECTIVES OF THE INDEPENDENT AUDITOR AND THE CONDUCT OF AN AUDIT IN ACCORDANCE WITH STANDARDS ON AUDITING (ON OR AFTER APRIL 1, 2010)

- A. **OVERALL OBJECTIVES OF INDEPENDENT AUDITOR:** Refer Chapter - 1 (Fundamentals to auditing)
- B. **DEFINITIONS:**
- MISSTATEMENT:** Refer Chapter - 1 (Fundamentals to auditing)
 - FINANCIAL STATEMENTS:** Refer Chapter - 1 (Fundamentals to auditing)
 - APPLICABLE FRFW:** Refer Chapter - 1 (Fundamentals to auditing)
 - PROFESSIONAL SKEPTICISM:** Refer Chapter - 2 (Nature of Auditing)
 - PROFESSIONAL JUDGMENT:** Refer Chapter - 2 (Nature of Auditing)
 - SUFFICIENT AND APPROPRIATE EVIDENCE:** Refer Chapter - 4 (Audit Documentation and Evidence)
 - AUDIT RISK:** Refer Chapter - 8 (Risk assessment and internal control)
 - PREMISE:** Refer Chapter - 2 (Nature of Auditing)
- C. **COMPLYING WITH SA'S RELEVANT TO AUDIT:**
- The auditor shall comply with all SAs relevant to the audit. An SA is relevant to the audit if the circumstances addressed by the SA exist.
 - The auditor shall have an understanding of the entire text of an SA, including its application and other explanatory material, to understand its objectives and to apply its requirements properly.
 - The auditor shall not represent compliance with SAs in the auditor's report unless the auditor has complied with the requirements of this SA and all other SAs relevant to the audit.

RELEVANT QUESTION:

| | |
|--|--|
| 1. The auditor shall comply with standards on auditing while discharging audit functions. Comment. | |
| A. Write Point - C and also write provision of companies act, 2013 (Sec. 143(9)). | |

SA 210 (REVISED): AGREEING THE TERMS OF AUDIT ENGAGEMENTS (ON OR AFTER APRIL 1, 2010)

- A. **OBJECTIVE OF THE AUDITOR:**
- The objective of the auditor is to accept or continue an audit engagement only when the terms of audit have been agreed through:
- Establishing whether the preconditions for an audit are present; and
 - Confirming that there is a common understanding between the auditor and management of the terms of the audit engagement. (Mutual consent)
- B. **PRECONDITIONS FOR AN AUDIT:** Refer Chapter - 2 (Nature of Auditing)
- C. **LIMITATION ON SCOPE PRIOR TO AUDIT ENGAGEMENT ACCEPTANCE:** Refer Chapter - 2 (Nature of Auditing)
- D. **NON ACCEPTANCE OF AUDIT ENGAGEMENT:**
- The auditor shall not accept the proposed audit engagement:
- If the auditor has determined that the financial reporting framework to be applied in the preparation of the financial statements is unacceptable or
 - If the agreement of management has not been obtained.

- E. **FORM AND CONTENTS OF THE AUDIT ENGAGEMENT:** Refer Chapter - 2 (Nature of Auditing)
- F. **ISSUANCE OF ENGAGEMENT LETTER DURING RECURRING AUDITS:** Refer Chapter - 2 (Nature of Auditing)
- G. **CHANGES IN THE TERMS OF THE AUDIT ENGAGEMENT:** Refer Chapter - 2 (Nature of Auditing)

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

- A. **NATURE AND PURPOSES OF AUDIT DOCUMENTATION:** Refer Chapter - 4 (Audit Documentation and Evidence) (Q.No. 8)
- B. **OBJECTIVE OF THE AUDITOR:**
The objective of the auditor is to prepare documentation that provides:
- A sufficient and appropriate record of the basis for the auditor's report; and
 - Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.
- C. **DEFINITIONS OF AUDIT DOCUMENTATION:** Refer Chapter - 4 (Audit Documentation and Evidence) (Q No. 8)
- D. **TIMELY DOCUMENTATION OF AUDIT DOCUMENTATION:**
- Preparing sufficient and appropriate audit documentation on a timely basis helps to enhance the quality of the audit and facilitates the effective review and evaluation of the audit evidence obtained and conclusions reached before the auditor's report is finalised.
 - Documentation prepared after the completion of audit is likely to be less accurate than documentation prepared at the time such work is performed
- E. **FORM, CONTENT AND EXTENT OF AUDIT DOCUMENTATION:** Refer Chapter - 4 (Audit Documentation and Evidence) (Q No. 9).
- F. **ASSEMBLY OF THE FINAL AUDIT FILE**
- The auditor shall assemble the audit documentation in an audit file on a timely basis and complete the administrative process of assembling of final audit file within 60 days from the date of auditors report.
 - After the assembly of the final audit file has been completed, the auditor shall not delete or discard audit documentation of any nature before the end of its retention period.
 - Where the auditor finds it necessary to modify existing audit documentation or add new audit documentation after the assembly of the final audit file has been completed, the auditor shall document:
 - The specific reasons for making them; and
 - When and by whom they were made and reviewed.
- G. **MATTERS ARISING AFTER THE DATE OF THE AUDITOR'S REPORT:**
If the auditor performs new or additional audit procedures or draws new conclusions after the date of the auditor's report,
The auditor shall 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.

RELEVANT QUESTIONS:

| | |
|--|------------|
| <p>1. Judging the significance of a matter requires an objective analysis of the facts and circumstances. Documentation of the professional judgments made, where significant, serves to explain the auditor's conclusions and to reinforce the quality of the judgment. Explain with the help of examples.</p> <p>A. Write Answer to Q No. 14 of Chapter - 4 Audit Documentation.</p> | RTP M19(N) |
|--|------------|

| | |
|---|--|
| 2. Write about assembly of final audit file in light of SA 230. A. Write Point - F | |
| 3. What are the matters the auditor shall document if any matters arising after the date of auditors report? A. Write Point - G. | |

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

A. OBJECTIVES OF THE AUDITOR:

The objectives of the auditor are:

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

B. MANAGEMENT REPRESENTATIONS:

The auditor shall obtain written representations from management and, where applicable, those charged with governance that:

- a) They acknowledge their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud;
- b) They have disclosed to the auditor their knowledge of fraud or suspected fraud affecting the entity involving:
 - i) Management;
 - ii) Employees who have significant roles in internal control; or
 - iii) Others, where the fraud could have a material effect on the financial statements; and

C. COMMUNICATIONS TO MANAGEMENT AND WITH THOSE CHARGED WITH GOVERNANCE:

If the auditor has identified or suspect's fraud involving:

- a) Management;
- b) Employees who have significant roles in internal control; or
- c) Others where the fraud results in a material misstatement in the financial statements.

The auditor shall communicate these matters to those charged with governance on a timely basis. If the auditor suspects fraud involving management, the auditor shall communicate these suspicions to those charged with governance and discuss with them the nature, timing and extent of audit procedures necessary to complete the audit.

D. COMMUNICATIONS TO REGULATORY AND ENFORCEMENT AUTHORITIES:

Further he shall communicate such fraud details to regulatory authorities if such communication is required as per applicable financial reporting framework. (E.g., 143(12) of companies act)

RELEVANT QUESTION:

| | |
|---|--|
| 1. Auditor shall communicate the identified or suspected fraud to management and regulatory authorities. Comment in light of SA 240. A. Write Point - C & D. | |
|---|--|

**SA 250 (REVISED) THE AUDITOR'S RESPONSIBILITIES RELATING TO LAWS AND REGULATIONS
IN AN AUDIT OF FINANCIAL STATEMENTS (W.E.F.1ST APRIL 2009)**

A. RESPONSIBILITY OF MANAGEMENT FOR COMPLIANCE WITH LAWS AND REGULATIONS:

It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations.

B. RESPONSIBILITY OF THE AUDITOR:

a) The auditor is not responsible for preventing non-compliance and cannot be expected to detect all non-compliance with all laws and regulations.

b) Further This standards divides the responsibility of auditor in relation to Consideration of laws and regulations into two types:

Type 1 - Those laws and regulations which have a direct effect on the determination of material amounts and disclosures in the financial statements.

Type 2 - Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to continue its business, or to avoid material penalties and therefore non-compliance with such laws and regulations may have a material impact on the financial statements.

C. OBJECTIVES OF THE AUDITOR:

The objectives of the auditor are:

a) To obtain sufficient appropriate audit evidence regarding compliance with Type 1 laws and regulations;

b) To perform Limited audit procedures to help identify instances of non-compliance with Type 2; and

c) To report appropriately to identified non-compliance with laws and regulations

D. DEFINITION OF NON COMPLIANCE

a) Acts of omission or commission by the entity, either intentional or unintentional, which are contrary to the prevailing laws or regulations.

b) Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees.

c) Non-compliance does not include personal misconduct (unrelated to the business activities of the entity) by those charged with governance, management or employees of the entity.

E. LIMITED AUDIT PROCEDURES FOR TYPE - 2 LAWS AND REGULATIONS:

The auditor shall perform the following Limited audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements:

a) Inquiring of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations; and

b) Inquiring and Inspecting correspondence, if any, with the relevant licensing or regulatory authorities.

c) Inquiring Entity's Legal counsel to know the details of pending litigations and resultantly estimate the possible non compliances.

F. INDICATIONS OF NON-COMPLIANCE WITH LAWS AND REGULATIONS:

The following are few indicators of Non compliances with various laws and regulation. This list is only illustrative and not exhaustive.

Further an indicator doesn't mean that there is a severe Non-compliance. It only provides the auditor the guidance to identify non compliances if any exists.

- i) Investigations by regulatory organisations and government departments.
- ii) Payment of fines or penalties.
- iii) Payments for unspecified services or loans to consultants, related parties, employees or government employees.
- iv) Purchasing at prices significantly above or below market price.
- v) Unusual payments in cash or payments in form of bearer cheques,
- vi) Unusual payments towards legal and retainership fees.
- vii) Unusual transactions with companies registered in tax havens.
- viii) Unauthorised transactions or improperly recorded transactions.
- ix) Adverse media comment.

G. REPORTING NON-COMPLIANCE TO THOSE CHARGED WITH GOVERNANCE:

If the auditor suspects that management or those charged with governance are involved in non-compliance, the auditor shall communicate the matter to the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board.

H. REPORTING NON-COMPLIANCE IN THE AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS:

- a) If the auditor concludes that the non-compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements, the auditor shall express a qualified or adverse opinion on the financial statements.
- b) If the auditor is unable to obtain sufficient appropriate audit evidence to evaluate whether non-compliance that may be material to the financial statements has, or is likely to have, occurred, the auditor shall express a qualified opinion or disclaim an opinion on the financial statements.

RELEVANT QUESTIONS:

| | |
|---|--|
| 1. With reference of SA 250, give some examples or matters indicating to the auditor about non-compliance of laws & regulations by management. A. Write Point - F. | RTP N18(O) MTP N18(O) MTP M18(N) |
| 2. Write about reporting of non-compliance identified by the auditor during the course of audit. A. Write Point - G and H. | |

SA 260 (REVISED): COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE (W.E.F. 1ST APRIL 2009)

A. OBJECTIVES OF THE AUDITOR:

The objectives of the auditor are:

- a) To communicate clearly with those charged with governance the responsibilities of the auditor in relation to the financial statement audit, and an overview of the planned scope and timing of the audit;
- b) To obtain from those charged with governance information relevant to the audit;
- c) To provide those charged with governance with timely observations arising from the audit that are significant and relevant to their responsibility to oversee the financial reporting process; and
- d) To promote effective two-way communication between the auditor and those charged with governance

B. DEFINITIONS:

THOSE CHARGED WITH GOVERNANCE:

- a) The person(s) or organization(s) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process.

- b) For some entities, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

MANAGEMENT:

The person's with executive responsibility for the conduct of the entity's operations.

For some entities, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.

C. MATTERS TO BE COMMUNICATED:

a) THE AUDITOR'S RESPONSIBILITIES:

The auditor shall communicate with those charged with governance the responsibilities of the auditor in relation to the financial statement audit, including that:

- i) The auditor is responsible for forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance; and
- ii) The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.

b) SIGNIFICANT FINDINGS FROM THE AUDIT:

The auditor shall communicate with those charged with governance:

1. The auditor's views about significant qualitative aspects of the entity's accounting practices.
2. **SIGNIFICANT DIFFICULTIES** encountered during the audit such as;
 - i) Significant delays by management to provide information necessary for the auditor to perform the auditor's procedures.
 - ii) An unreasonably brief time within which to complete the audit.
 - iii) Extensive unexpected effort required to obtain sufficient appropriate audit evidence.
 - iv) The unavailability of expected information.
 - v) Restrictions imposed on the auditor by management.
 - vi) Management's unwillingness to make or extend its assessment of the entity's ability to continue as a going concern when requested.
3. Circumstances that affect the form and content of the auditor's report, if any; and
4. Any other significant matters arising during the audit.

D. THE COMMUNICATION PROCESS:

- a) The auditor shall communicate in writing with those charged with governance regarding significant findings from the audit if, in the auditor's professional judgment, oral communication would not be adequate.
- b) The auditor shall communicate with those charged with governance on a timely basis.
- c) Further if any matter is communicated orally then the auditor shall document the matters communicated (When and To Whom).

RELEVANT QUESTIONS:

| | |
|--|-------------------------|
| 1. State the significant difficulties encountered during audit with reference to SA-260: Communication with Those Charged With Governance. | RTP M18 (O) |
| A. Write Point - C(b)(2) including sub points (i - vi) | RTP M17, MTP M18 (O) |
| 2. What are that significant findings that the auditor shall communicate with those charged with governance and management. | |
| A. Write Point - C (b). | |

SA 265 COMMUNICATING DEFICIENCIES IN INTERNAL CONTROL TO THOSE CHARGED WITH GOVERNANCE AND MANAGEMENT (ON OR AFTER APRIL 1, 2010)

A. DEFINITION:

1. DEFICIENCY IN INTERNAL CONTROL:

This exists when:

- i) A control is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements on a timely basis; (Weakness in control) or
- ii) A control necessary to prevent, or detect and correct, misstatements in the financial statements on a timely basis is missing. (Absence of Control).

2. SIGNIFICANT DEFICIENCY:

A deficiency or combination of deficiencies in internal control that, in the auditor’s professional judgment, is of sufficient importance to merit the attention of those charged with governance.

B. REQUIREMENTS:

The auditor shall also communicate to management at an appropriate level of responsibility on a timely basis:

- i) In writing, significant deficiencies in internal control that the auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances; and
- ii) Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties and that, in the auditor’s professional judgment, are of sufficient importance to merit management’s attention.

C. COMMUNICATION SHALL INCLUDE (LETTER OF WEAKNESS)

The auditor shall include the following aspects while communicating significant deficiencies:

- a) A description of the deficiencies and an explanation of their potential effects; and
- b) Sufficient information to enable those charged with governance and management to understand the context of the communication. In particular, the auditor shall explain that:
 - i) The purpose of the audit to express an opinion on the financial statements;
 - ii) The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control; and
 - iii) The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance.
 - iv) The deficiencies identified are not exhaustive but illustrative only based on test check.

RELEVANT QUESTIONS:

| | |
|--|--------------------|
| <p>1. During the course of audit of an entity, the auditor ascertains that the internal control system is not effective and rather weak with certain lapses. Give in detail the communication in this regard the auditor will have with the management.</p> <p>A. Write Point - A and C.</p> | <p>M18(O) - 6M</p> |
| <p>2. Write about communicating deficiencies in internal control.</p> <p>A. Write Point - A and C.</p> | <p>N16 - 4M</p> |

SA 300 (REVISED) PLANNING AN AUDIT OF FINANCIAL STATEMENTS (ON OR AFTER 1ST APRIL 2008)

A. **INVOLVEMENT OF KEY ENGAGEMENT MEMBERS:** Refer Chapter - 3 (Audit Strategy, Planning and Programme) (Q No. 6)

B. **PRELIMINARY ENGAGEMENT ACTIVITIES:**

The auditor shall undertake the following activities at the beginning of the current audit engagement:

1. Performing procedures required by SA 220, "Quality Control for an Audit of Financial Statements" regarding the continuance of the client relationship and the specific audit engagement;
2. Evaluating compliance with ethical requirements, including independence, as required by SA 220;
3. Establishing an understanding of the terms of the engagement, as required by SA 210 and
4. Communicating with the predecessor auditor, if applicable.

C. **PLANNING ACTIVITIES:** Refer Chapter - 3 (Audit Strategy, Planning and Programme) (Q No. 3)

D. **ADDITIONAL CONSIDERATION IN CASE OF INITIAL AUDIT ENGAGEMENT:**

The Auditor shall undertake the following to start an initial audit -

1. Perform the procedures as laid down under SA 220 regarding acceptance and continuance of client relationship.
2. Communicating with the predecessor auditor, if applicable.

Note: The above two points are already covered as part of Point - B (1 & 4)

RELEVANT QUESTION:

| | |
|--|--|
| 1. Write about Preliminary engagement activities in light of SA 300. | |
| A. Write Point - B. | |

SA 315 IDENTIFYING AND ASSESSING THE RISKS OF MATERIAL MISSTATEMENT THROUGH UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT

A. **OBJECTIVE:** Refer Chapter - 8 (Risk assessment) (Q No. 2)

B. **DEFINITIONS:**

1. **ASSERTION:** Representations made by management w.r.t transactions or balances or disclosures in the financial statements which are used by the auditor to consider the different types of potential misstatements that may occur.
2. **SIGNIFICANT RISK:** An identified and assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration.

C. **RISK ASSESSMENT PROCEDURE AND RELATED ACTIVITIES:** Refer Chapter - 8 (Risk assessment) (Q No. 2)

D. **UNDERSTANDING OF ENTITY AND ITS ENVIRONMENT:** Refer Chapter - 3 (Audit Strategy) (Q No. 4)

E. **ENTITY'S INTERNAL CONTROL:** Refer Chapter - 8 (Risk assessment) (Q No. 5,6,7,8 and 12)

F. **IDENTIFYING AND ASSESSING RISK OF MMS:** Refer Chapter - 8 (Risk assessment) (Q No. 3)

G. **SIGNIFICANT RISKS:**

It refers to those risks of material misstatements which in the auditors professional judgement that requires special attention.

The following are the factors that influence auditor's judgments to identify significant risks:

- a) Whether the risk is a risk of fraud;
- b) Whether the risk is related to recent significant economic, accounting, or other developments like changes in regulatory environment, etc., and, therefore, requires specific attention;

- c) Whether the risk involves significant transactions with related parties;
- d) The degree of uncertainty in management assessment of various judgements like accounting estimates and selection of accounting policies ; and
- e) Whether there exist any unusual, exceptional, non-recurring and extraordinary transactions in the entity pertaining to the financial statements under audit.

H. DOCUMENTATION RELATED TO RISK ASSESSMENT:

The auditor shall document:

- a) The discussion among the engagement team and the significant decisions reached;
- b) Key elements of the understanding obtained regarding various aspects of the entity and its environment;
- c) The sources of information from which the understanding was obtained; and the risk assessment procedures performed;
- d) The identified and assessed risks of material misstatement at the financial statement level and at the assertion level.

RELEVANT QUESTIONS:

| | |
|---|---|
| <p>1. The auditor may exercise his judgement to identify which risks are significant risks. Explain the above in context of SA-315. A. Write Point - G.</p> | <p>RTP N18 (O) RTP M17, MTP N17</p> |
| <p>2. As part of the risk assessment, the auditor shall determine whether any of the risks identified are, in the auditor’s judgment, a significant risk. In exercising judgment as to which risks are significant risks, state the factors which shall be considered by the auditor. Explain the above in context of SA-315. A. Write Point - G.</p> | <p>RTP M18 (N&O)</p> |

SA 500 (REVISED) AUDIT EVIDENCE (W.E.F. APRIL 1, 2009)

A. OBJECTIVE OF THE AUDITOR:

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

B. DEFINITIONS:

1. ACCOUNTING RECORDS:

The records of initial accounting entries and supporting records, such as checks and records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers, journal entries and other adjustments to the financial statements that are not reflected in journal entries; and records such as work sheets and spread sheets supporting cost allocations, computations, reconciliations and disclosures

2. APPROPRIATENESS: Refer Chapter - 4 (Audit Documentation) (Q No. 3)

3. AUDIT EVIDENCE: Refer Chapter - 4 (Audit Documentation) (Q No. 3)

4. SUFFICIENCY: Refer Chapter - 4 (Audit Documentation) (Q No. 3)

5. MANAGEMENT’S EXPERT:

An individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity (management) to assist the entity in preparing the financial statements.

C. INFORMATION TO BE USED AS AUDIT EVIDENCE:

- 1. **PROVIDED BY MANAGEMENT EXPERTS:** When information to be used as audit evidence has been prepared using the work of a management’s expert, the auditor shall:

- a) Evaluate the competence, capabilities and objectivity of that expert;
 - b) Obtain an understanding of the work of that expert; and
 - c) Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion.
2. **PROVIDED BY MANAGEMENT:** When using information produced by the entity, the auditor shall evaluate whether the information is sufficiently reliable for the auditor's purposes:
- a) Obtaining audit evidence about the accuracy and completeness of the information; and
 - b) Evaluating whether the information is sufficiently precise and detailed for the auditor's purposes.
4. **INCONSISTENCY IN, OR DOUBTS OVER RELIABILITY OF AUDIT EVIDENCE:**
- a) Audit evidence obtained from one source is inconsistent with that obtained from another; or
 - b) The auditor has doubts over the reliability of information to be used as audit evidence, the auditor shall determine what modifications or additions to audit procedures are necessary to resolve the matter.
 - c) Further if the auditor ultimately concludes that there is No sufficient appropriate evidence then he shall modify the opinion as per SA 705.

RELEVANT QUESTIONS:

| | |
|---|-------------------------|
| <p>1. The quantity of audit evidence needed is affected by the auditor's assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence, however, may not compensate for its poor quality. Analyse and Explain stating clearly the factors affecting the auditor's judgement as to sufficiency of audit evidence.</p> <p>A. Write Point - B (2&4)</p> | RTP M19 (N) |
| <p>2. Most of the auditor's work in forming the auditor's opinion consists of obtaining and evaluating audit evidence. Explain</p> <p>A. Refer Q. No. 7 of Chapter - 4 - Audit Documentation.</p> | RTP N18 (N) |
| <p>3. "The nature and timing of the audit procedures to be used may be affected by the fact that some of the accounting data and other information may be available only in electronic form or only at certain points or periods in time". Explain.</p> <p>A.</p> <ol style="list-style-type: none"> 1. The nature and timing of the audit procedures to be used <u>may be affected by the fact</u> that some of the accounting data and other information may be available <u>only in electronic form or only at certain points or periods in time</u>. For example, source documents, such as purchase orders and invoices, may exist only in electronic form when an <u>entity uses electronic commerce</u>, or may be discarded after scanning when an entity uses image processing systems to facilitate storage and reference. 2. Certain electronic information <u>may not be retrievable after a specified period of time</u>, for example, if files are changed and if backup files do not exist. Accordingly, the auditor may find it necessary <u>as a result of an entity's data retention policies to request retention of some information for the auditor's review or to perform audit procedures at a time when the information is available</u>. | RTP M18 (O), RTP M17 |

SA 501 (Revised) AUDIT EVIDENCE - SPECIFIC CONSIDERATIONS FOR SELECTED ITEMS**A. OBJECTIVE OF THE AUDITOR:**

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

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

B. EXISTENCE AND CONDITION OF INVENTORY:**1. ATTEND MANAGEMENT INVENTORY COUNTING:**

- a) The auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of inventory as at year end i.e., Date of financial statements by:
- i) Attendance at physical inventory counting performed by management to:
 - Evaluate management's process of physical inventory counting;
 - Inspect the inventory; and
 - Perform test counts; and
 - ii) Reconcile the physical inventory with the inventory records to identify any discrepancies.
- b) If inventory counting is carried at other than balance sheet date then the auditor shall identify the changes occurred between balance sheet date and count date and shall ensure whether the changes are properly recorded.

2. PHYSICAL INSPECTION BY AUDITOR DIRECTLY:

- a) If the auditor is unable to attend physical inventory counting by management due to unforeseen circumstances, the auditor shall make or observe some physical counts on an alternative date, and perform audit procedures on intervening transactions.

3. PHYSICAL INSPECTION IMPRACTICABILITY:

- a) If attendance at physical inventory counting is impracticable, the auditor shall perform alternative audit procedures to obtain sufficient appropriate audit evidence regarding the existence and condition of inventory.
- b) The alternative procedure includes inspection of documentation of subsequent sale of specific items of inventory purchased on or before balance sheet date. This will ensure the auditor to confirm about existence and condition of inventory as on reporting date.
- c) If alternative procedures are not possible to do so, the auditor shall modify the opinion in the auditor's report in accordance with SA 705.

4. INVENTORY IN THE CUSTODY OF THIRD PARTY:

- a) When inventory under the custody and control of a third party the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of that inventory by performing one or both of the following:
- b) Request confirmation from the third party as to the quantities and condition of inventory held on behalf of the entity. (SA 505)
- c) If there exists doubts as to reliability of confirmation provided by third parties then the auditor may perform the below procedures:
- i) Attending or arranging another auditor for physical count procedures of third parties, if practicable.
 - ii) Obtaining another auditor report on adequacy of third party count procedures.
 - iii) Inspecting documentation regarding inventory held by third party eg: warehouse receipts.
 - iv) Requesting confirmation from other parties where the inventory is pledged as collateral.

C. LITIGATION AND CLAIMS:

The auditor shall design and perform audit procedures in order to identify litigation and claims involving the entity which may give rise to a risk of material misstatement, including:

- a) Inquiry of management and, where applicable, others within the entity, including in-house legal counsel;
- b) Reviewing minutes of meetings of those charged with governance and correspondence between the entity and its external legal counsel; and

- c) Reviewing legal expense accounts.
- d) If the auditor assesses a risk of material misstatement regarding litigation or claims that have been identified, or when audit procedures performed indicate that other material litigation or claims may exist, the auditor shall, in addition to the procedures required by other SAs, seek direct communication with the entity's external legal counsel.
- e) The auditor shall do so through a letter of inquiry, prepared by management and sent by the auditor, requesting the entity's external legal counsel to communicate directly with the auditor.
- f) If management refuses to give the auditor permission to communicate or meet with the entity's external legal counsel, or the entity's external legal counsel refuses to respond appropriately to the letter of inquiry, or is prohibited from responding; and
- g) If the auditor is unable to obtain sufficient appropriate audit evidence by performing alternative audit procedures then the auditor shall modify the opinion in the auditor's report in accordance with SA 705.

h) WRITTEN REPRESENTATIONS:

The auditor shall request management and, where appropriate, those charged with governance to provide written representations that all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to the auditor and appropriately accounted for and disclosed in accordance with the applicable financial reporting framework.

D. SEGMENT INFORMATION:

The auditor shall obtain sufficient appropriate audit evidence regarding the presentation and disclosure of segment information in accordance with the applicable financial reporting framework by:

- a) Obtaining an understanding of the methods used by management in determining segment information, and:
 - i) Evaluating whether such methods are likely to result in disclosure in accordance with the applicable financial reporting framework; and
 - ii) Where appropriate, testing the application of such methods; and
- b) Performing analytical procedures or other audit procedures appropriate in the circumstances.

RELEVANT QUESTIONS:

| | |
|---|--|
| 1. Paramount Exports Ltd is a manufacturer exporter having its own production capacity and also gets the job work done through various job workers. The auditor of Paramount Exports Ltd. Considers that inventory held with job workers is material to the financial statements. Suggest audit procedures in the given case? A. Write Point - B (4) - a and b. | NEW SM |
| 2. Pride India Ltd is a manufacturer of various FMCG (fast moving consumable goods) range of products. The company is having several cases of litigation pending in courts. The auditor wanted to identify litigation and claims resulting to risk of material misstatements. Suggest the auditor w.r.t SA 501. A. Write Point - C (a, b and c). | NEW SM |
| 3. ABC Ltd is engaged in manufacturing of different type of yarns. On-going through its financial statements for the past years, it is observed that inventory is material to the financial statements. You as an auditor of the company wanted to obtain sufficient appropriate audit evidence regarding the existence and condition of the inventory as appearing in the financial statements. Discuss, how would you proceed as an auditor. A. Write Point - B (1). | MTP M19(N) MTP N18(N) MTP M18(N) |
| 4. Briefly mention the matters that are relevant in planning attendance at physical inventory counting? A. The auditor shall consider the following: <ol style="list-style-type: none"> 1. Nature of Inventory 2. Stages of completion of WIP | N18 (N) - 5M |

- | | |
|---|--|
| <ol style="list-style-type: none"> 3. Internal Controls related to Inventory 4. Whether adequate instructions are given for physical inventory counting 5. Timing of physical inventory counting 6. Whether the entity is maintaining perpetual inventory system 7. Whether assistance of auditors expert is needed 8. The location at which inventory is held and related risks. | |
|---|--|

SA 505 (REVISED) EXTERNAL CONFIRMATION (ON OR AFTER APRIL 1, 2010)

A. DEFINITIONS:

1. EXTERNAL CONFIRMATION:

Audit evidence obtained as a direct written response to the auditor from a third party (AKA the confirming party), in paper form, or by electronic or other medium.

2. POSITIVE CONFIRMATION REQUEST:

A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information.

3. NEGATIVE CONFIRMATION REQUEST:

A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.

4. EXCEPTION:

A response indicates a difference between information requested to be confirmed, or contained in the entity's records, and information provided by the confirming party.

B. EXTERNAL CONFIRMATION PROCEDURES:

When using external confirmation procedures, the auditor shall maintain control over external confirmation requests, including:

1. Determining the information to be confirmed or requested;
2. Selecting the appropriate confirming party;
3. Designing the confirmation requests which may be positive pattern or negative pattern and
4. Sending the requests, including follow-up requests when applicable, to the confirming party.
5. Following are examples of situations or areas where external confirmations may be useful-
 - a) Bank balances and other information from bankers
 - b) Account receivables balances
 - c) Inventory held by third parties
 - d) Account payable balances.
6. External confirmation procedures frequently are performed to confirm or request information regarding account balances and their elements.
7. They may also be used:
 - a) To confirm terms of agreements.
 - b) Contracts, or
 - c) Transactions between an entity and other parties, or
 - d) To confirm the absence of certain conditions, such as a "side agreement".
 - e) Property title deeds held by financiers as security.
 - f) Amounts due to lenders.
8. Therefore external confirmation can be obtained not only for account balances at yearend but also for above details.

C. MANAGEMENT'S REFUSAL TO ALLOW THE AUDITOR TO SEND A CONFIRMATION REQUEST:

If management refuses to allow the auditor to send a confirmation request, the auditor shall:

- Inquire as to management's reasons for the refusal, and seek audit evidence as to their validity and reasonableness;
- Evaluate the implications of management's refusal on the auditor's assessment of the relevant risks of material misstatement, including the risk of fraud, and on the nature, timing and extent of other audit procedures; and
- Perform alternative audit procedures designed to obtain relevant and reliable audit evidence.
- If the auditor concludes that management's refusal to allow the auditor to send a confirmation request is unreasonable, or the auditor is unable to obtain relevant and reliable audit evidence from alternative audit procedures, the auditor shall communicate with those charged with governance in accordance with SA 260.
- The auditor also shall determine the implications for the audit and the auditor's opinion in accordance with SA 705.

D. NEGATIVE CONFIRMATIONS:

In the following situations the auditor can use negative confirmation procedure:

- The auditor has assessed the risk of material misstatement as low;
- The population of items subject to negative confirmation procedures comprises a large number of small, homogeneous, account balances, transactions or conditions;
- A very low exception rate is expected; and
- Very low chances of non-response from third party.

RELEVANT QUESTIONS:

| | |
|---|---------------------|
| 1. While conducting the audit of Jay Kay Ltd, the auditor K of KLM and Associates, Chartered Accountants observes that there are large number of Trade payables and receivables standing in the books of accounts as on 31 st March. The auditor wanted to send confirmation request to few trade receivables but the management refused the auditor to send confirmation request. How would you as an auditor proceed in this situation? A. Write about Point - 3. | NEW SM |
| 2. What is meant by external confirmation? Mention any four situations where external confirmation may be useful for auditors. A. Write Point - A (1) and B(5). | RTP M17 |
| 3. External confirmation procedures frequently are relevant when addressing assertions associated with account balances and their elements, but need not be restricted to these items. Discuss. A. Write Point - A (1) and B (6,7 and 8). | MTP M18(N) |
| 4. Write a short note on external confirmation as audit procedure? A. Write Point - A (1) and B (1 to 5). | M18(O)-4M N16-4M |

SA 510 (REVISED) INITIAL AUDIT ENGAGEMENTS-OPENING BALANCES (ON OR AFTER APRIL 1, 2010)**A. OBJECTIVE OF THE AUDITOR:**

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

- Opening balances contain misstatements that materially affect the current period's financial statements; and
- Appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are properly accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

B. DEFINITIONS:**INITIAL AUDIT ENGAGEMENT:**

An engagement in which either:

- a) The financial statements for the prior period were not audited; or
- b) The financial statements for the prior period were audited by a predecessor auditor.

OPENING BALANCES:

- a) Those account balances that exist at the beginning of the period.
- b) Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period.
- c) Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

PREDECESSOR AUDITOR:

Predecessor auditor means the auditor from a different audit firm, who audited the financial statements of an entity in the prior period and who has been replaced by the current auditor.

C. AUDIT PROCEDURES FOR AUDIT OF OPENING BALANCES:

The auditor shall obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements by:

- a) Determining whether the prior period's closing balances have been correctly brought forward to the current period or, when appropriate, any adjustments have been disclosed as prior period items in the current year's Statement of Profit and Loss;
- b) Determining whether the opening balances reflect the application of appropriate accounting policies; and
- c) Performing one or more of the following:
 - i) Where the prior year financial statements were audited, referring the copies of the audited financial statements including the other relevant documents relating to the prior period financial statements;
 - ii) Whether audit procedures performed in the current period provide evidence relevant to the opening balances; or
 - iii) Performing specific audit procedures to obtain evidence regarding the opening balances. (Opening Balance verification: Opening TB comparing with Previous year Approved Balance sheet)

D. CONSISTENCY OF ACCOUNTING POLICIES:

The auditor shall obtain sufficient appropriate audit evidence about whether the accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, and whether changes in the accounting policies have been properly accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

E. AUDIT CONCLUSIONS AND REPORTING - OPENING BALANCES:

- a) If the auditor concludes that the opening balances contain a misstatement that materially affects the current period's financial statements, and the effect of the misstatement is not properly accounted for or not adequately presented or disclosed, the auditor shall express a qualified opinion or an adverse opinion, as appropriate, in accordance with SA 705.
- b) If the auditor is unable to obtain sufficient appropriate audit evidence regarding the opening balances, the auditor shall express a qualified opinion or a disclaimer of opinion, as appropriate, in accordance with SA 705.

F. AUDIT CONCLUSIONS AND REPORTING - CONSISTENCY OF ACCOUNTING POLICIES:

If the auditor concludes that:

- a) The current period's accounting policies are not consistently applied in relation to opening balances in accordance with the applicable financial reporting framework; or
- b) Changes in accounting policies is not properly accounted for or not adequately presented or disclosed in accordance with the applicable financial reporting framework.

Then the auditor shall express a qualified opinion or an adverse opinion as appropriate in accordance with SA 705.

G. MODIFICATIONS IN THE PREDECESSOR AUDITOR'S REPORT:

If there exist a modification in the predecessor audit report and the modification is remain relevant and material for the current period under audit then the current auditor shall also modify the opinion in accordance with SA 705.

RELEVANT QUESTIONS:

| | |
|--|------------------------------------|
| 1. Discuss with reference to SA 510, "Initial Audit Engagement - Opening Balances", the procedures the auditor should undertake in respect of opening balances for a new audit engagement. A. Write Point - C. | RTP M19(O) MTP M18(O) M17-5M |
| 2. Auditors of M/s Tender India (P) Ltd. were changed for the accounting year 2016-17. The closing inventory of the company as on 31.03.2016 amounting to Rs.100 lakhs continued as it is and became closing inventory as on 31.03.2017. The auditors of the company propose to exclude from their audit programme the audit of closing inventory of Rs.100 lacs on the understanding that it pertains to the preceding year which was audited by another auditor. A. Write Point - A and the following Points. 1. General principles governing verification of assets require that the auditor should confirm that assets have been correctly valued as on the Balance Sheet date. 2. The contention of the management that the inventory has not undergone any change cannot be accepted. It forms part of normal duties of auditor to ensure that the figures on which he is expressing opinion are correct and properly valued. 3. Moreover, it is also quite likely that the inventory lying might have deteriorated and the same need to be examined. 4. Therefore the auditor is advised not to exclude the audit of closing inventory from his audit programme. | RTP N17 |
| 3. Explain the audit procedure in respect of opening balances for a New Audit Engagements with reference to relevant SA. A. Write Point - C. | MTP N18(O) |
| 4. M/s Pankaj & Associates, chartered accountants have been appointed as an auditor for ABC Limited. CA Pankaj did not apply any audit procedures regarding opening balances. He argued that since financial statements were audited by predecessor auditor therefore he is not required to verify them. Is CA Pankaj correct in his approach? A. Write Point - A and C and conclude that the contention of the auditor not to verify the opening balances is not correct. | N18 (N) - 5M |

SA 540 (REVISED) AUDITING ACCOUNTING ESTIMATES, INCLUDING FAIR VALUE ACCOUNTING ESTIMATES, AND RELATED DISCLOSURES (W.E.F. 1ST APRIL, 2009)

A. OBJECTIVE OF THE AUDITOR UNDER SA - 540:

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

- a) Accounting estimates, including fair value accounting estimates, in the financial statements, whether recognised or disclosed, are reasonable; and
- b) Related disclosures in the financial statements are adequate.

B. DEFINITIONS:

1. ACCOUNTING ESTIMATE:

Accounting estimate is an approximation of a monetary amount in the absence of a precise means of measurement.

2. AUDITOR'S POINT ESTIMATE OR AUDITOR'S RANGE:

The amount, or range of amounts, respectively, derived from audit evidence for use in evaluating management's point estimate.

3. MANAGEMENT'S POINT ESTIMATE:

The amount selected by management for recognition or disclosure in the financial statements as an accounting estimate.

4. ESTIMATION UNCERTAINTY:

It is the susceptibility of an accounting estimate and related disclosures to an inherent lack of precision in its measurement.

5. MANAGEMENT BIAS:

It is a lack of neutrality by management in the preparation and presentation of information.

6. OUTCOME OF AN ACCOUNTING ESTIMATE:

It is the actual monetary amount which results from the resolution of the underlying transaction(s), event(s) or condition(s) addressed by the accounting estimate.

C. RISK ASSESSMENT PROCEDURES AND RELATED ACTIVITIES:

The auditor shall obtain an understanding of the following in order to determine the reasonableness accounting estimates:

- a) The requirements of the applicable financial reporting framework relevant to accounting estimates, including related disclosures.
- b) How management identifies those transactions, events and conditions that may give rise to the need for accounting estimates to be recognised or disclosed in the financial statements.
- c) How management makes the accounting estimates, and an understanding of the data on which they are based, including:
 - i) The methods, including where applicable the model, used in making the accounting estimate;
 - ii) Relevant controls;
 - iii) Whether management has used an expert;
 - iv) The assumptions underlying the accounting estimates.

D. AUDIT PROCEDURE FOR ACCOUNTING ESTIMATES:

Based on the assessed risks of material misstatement, the auditor shall determine:

- a) Whether management has appropriately applied the requirements of the applicable financial reporting framework relevant to the accounting estimate.
- b) Whether the methods for making the accounting estimates are appropriate and have been applied consistently, and whether changes, if any, in accounting estimates or in the method for making them from the prior period are appropriate and
- c) Develop an auditors point estimate or a range to evaluate management's point estimate.
- d) When the auditor uses assumptions or methods that differ from management's, the auditor shall obtain an understanding of management's assumptions or methods sufficient to establish that the auditor's point estimate or range takes into account relevant variables and to evaluate any significant differences from management's point estimate.
- e) Ensure that the assumptions used by auditor, to determine an estimate or range, are reasonable and based on sufficient and appropriate audit evidence.

E. FACTORS EFFECTING ESTIMATION UNCERTAINTY:

The degree of estimation uncertainty associated with an accounting estimate may be influenced by factors such as-

1. The extent to which the accounting estimate depends on judgment.
2. The sensitivity of the accounting estimate to changes in assumptions.
3. The existence of recognised measurement techniques that may mitigate the estimation uncertainty.
4. The length of the forecast period, and the relevance of data drawn from past events to forecast future events.
5. The availability of reliable data from external sources.
6. The extent to which the accounting estimate is based on observable or unobservable inputs.

F. DISCLOSURES RELATED TO ACCOUNTING ESTIMATES:

The auditor shall obtain sufficient appropriate evidence that the accounting estimates adopted are adequately presented and disclosed in financial statements. Further if there is an estimation uncertainty then the same shall also be disclosed as per applicable financial reporting framework.

G. OBTAIN WRITTEN REPRESENTATION:

The auditor shall obtain a written representation from management or TCWG whether they believe the assumptions used for determining accounting estimates chosen by them are reasonable and appropriate.

RELEVANT QUESTIONS:

| | |
|--|------------|
| 1. What are the factors that may influence the degree of estimation uncertainty associated with accounting estimates? A. Write Point - E. | MTP M18(O) |
| 2. Write about audit procedures for accounting estimates. Or Write about audit of accounting estimates. A. Write Point - D. | |

SA 560 (REVISED) SUBSEQUENT EVENTS (W.E.F. 1ST APRIL, 2009)**A. OBJECTIVES:**

The objectives of the auditor are to:

- a) Obtain sufficient appropriate audit evidence about whether events occurring between the date of the financial statements and the date of the auditor's report that require adjustment in the financial statements are appropriately reflected in those financial statements; and
- b) Respond appropriately to facts that become known to the auditor after the date of the auditor's report that may have caused the auditor to amend the auditor's report

B. DEFINITIONS:

1. **SUBSEQUENT EVENTS:** the events occurring between the date of the financial statements and the date of the auditor's report, and facts that become known to the auditor after the date of the auditor's report.
2. **DATE OF THE FINANCIAL STATEMENTS:** The date of the end of the latest period covered by the financial statements.
3. **DATE OF APPROVAL OF THE FINANCIAL STATEMENTS:** The date on which all the statements that comprise the financial statements, including the related notes, have been prepared and those with the recognised authority have asserted that they have taken responsibility for those financial statements.

4. **DATE OF THE AUDITOR'S REPORT:** The date the auditor dates the report on the financial statements in accordance with SA 700.
5. **DATE THE FINANCIAL STATEMENTS ARE ISSUED:** The date that the auditor's report and audited financial statements are made available to third parties.

C. AUDIT PROCEDURE FOR IDENTIFICATION OF SUBSEQUENT EVENTS:

The auditor shall perform the procedures to identify subsequent events which shall include the following:

1. Obtaining an understanding of any management procedures established to ensure that subsequent events are identified.
2. Inquiring of management and those charged with governance as to whether any subsequent events have occurred. Specifically the auditor shall evaluate the following:
 - a) Whether new commitments, borrowings or guarantees have been entered into.
 - b) Whether sales or acquisitions of assets have occurred or are planned.
 - c) Whether any assets have been appropriated by government or destroyed, for example, by fire or flood
 - d) Whether there have been any developments regarding contingencies.
 - e) Whether any unusual accounting adjustments have been made or are Contemplated
 - f) Whether any events have occurred or are likely to occur which will bring into question the appropriateness of accounting policies used in the financial statements as would be the case, for example, if such events call into question the validity of the going concern assumption.
3. Reading minutes of the meetings, of the entity's owners, management and those charged with governance, that have been held after the date of the financial statements.
4. Reading the entity's latest subsequent interim financial statements, if any.

D. CASE- I

FACTS WHICH BECOME KNOWN TO THE AUDITOR AFTER THE DATE OF THE AUDITOR'S REPORT BUT BEFORE THE DATE THE FINANCIAL STATEMENTS ARE ISSUED:

1. Generally the auditor has no obligation to perform any audit procedures regarding the financial statements after the date of the auditor's report.
2. However, when, after the date of the auditor's report but before the date the financial statements are issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of the auditor's report, may have caused the auditor to amend the auditor's report, the auditor shall:
 - a) Discuss the matter with management and those charged with governance.
 - b) Determine whether the financial statements need amendment and, if so,
 - c) Inquire how management intends to address the matter in the financial statements.
3. **IF MANAGEMENT AMENDS THE FINANCIAL STATEMENTS:** the auditor shall:
 - a) Carry out the audit procedures necessary in the circumstances on the amendment.
 - b) Obtain sufficient and appropriate evidence regarding the amendment such subsequent events.
4. **IF MANAGEMENT DOES NOT AMEND THE FINANCIAL STATEMENTS:**
 - a) Where the auditor concludes that the financial statements are not amended and If the auditor's report has not yet been provided to the entity, the auditor shall modify the opinion as required by SA 705 and then provide the auditor's report; or
 - b) If the auditor's report has already been provided to the entity, the auditor shall notify management and those charged with governance not to issue the financial statements to third parties before the necessary amendments have been made.

- c) If the financial statements are nevertheless subsequently issued without the necessary amendments, the auditor shall take appropriate action, to seek to prevent reliance on the auditor's report.

E. CASE - II:

FACTS WHICH BECOME KNOWN TO THE AUDITOR AFTER THE FINANCIAL STATEMENTS HAVE BEEN ISSUED:

1. After the financial statements have been issued, the auditor has no obligation to perform any audit procedures regarding such financial statements.
2. However, when, after the financial statements have been issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of the auditor's report, may have caused the auditor to amend the auditor's report, the auditor shall:
 - a) Discuss the matter with management and, where appropriate, those charged with governance.
 - b) Determine whether the financial statements need amendment and, if so,
 - c) Inquire how management intends to address the matter in the financial statements.

3. IF THE MANAGEMENT AMENDS THE FINANCIAL STATEMENTS: T

The auditor shall:

- a) Carry out the audit procedures necessary in the circumstances on the amendment.
- b) Review the steps taken by management to ensure that anyone in receipt of the previously issued financial statements together with the auditor's report thereon is informed of the situation.
- c) Provide a new auditor's report on the amended financial statements. The report shall include an emphasis of matter or other matter paragraph describing the effect of amendment of financial statements on the earlier issued F/S and earlier issued audit report.

4. IF MANAGEMENT DOES NOT TAKE NECESSARY STEPS:

The auditor shall take appropriate action to seek prevent reliance on the audit report and financial statements that are already issued to third parties.

RELEVANT QUESTIONS:

| | |
|--|--------------------------|
| 1. The auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements have been identified. Explain. A. Write Point - C | RTP M19(N) |
| 2. Inquiry from Management is helpful for Auditor to evaluate subsequent events. Discuss specific enquiries in reference of SA 560, which might have effect on the financial statements. A. Write Point - B(1) and C (2) including sub points (a - f). | RTP N18(O) MTP M19(O) |
| 3. In the context of SA 560 subsequent events, state the specific enquiries on matters by an auditor which may have effect on financial statements. A. Write Point - B(1) and C (2) including sub points (a - f). | N17 - 5M |

SA 570 (REVISED) GOING CONCERN (W.E.F 1ST APRIL, 2009)

A. OBJECTIVE:

The objectives of the auditor are:

- a) To obtain sufficient appropriate audit evidence regarding the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements;

- b) To conclude, based on the audit evidence obtained, whether a material uncertainty exists; and
- c) To report in accordance with this SA.

B. PRELIMINARY ASSESSMENT REGARDING USE OF GOING CONCERN ASSUMPTION BY MANAGEMENT:

The following factors to be considered for preliminary assessment of entity's ability to continue as a going concern:

1. The nature and condition of its business.
2. Effects of external events or conditions such as change in law or regulatory.
3. The information pertaining to operational forecast of foreseeable future.
4. Significant events or transactions that are occurred during the period under review. E.g., fire accident or catastrophe etc.,

C. PERIOD COVERED FOR ASSESSMENT OF ENTITY'S ABILITY TO CONTINUE AS A GOING CONCERN:

1. The assessment period under audit for going concern testing shall be same period as adopted by management.
2. If the management assessment of going concern is less than 12 MONTHS then the auditor shall request management to extend its assessment period to at least twelve months.
3. Further in some cases estimation more than 12 months is also justified and in such a case the assessment shall be made for such extended period.

D. AUDIT PROCEDURE:

The following audit procedures should perform by the auditor if the auditor identifies any circumstances that cast significant doubt on entity's going concern:

1. Whether there is a policy of assessment of risk related to going concern by management.
2. Evaluating management's plans for future actions in relation to its going concern assessment.
3. Whether the entity has prepared a cash flow forecast based on a reliable data.
4. Considering whether any additional information available since the date on which management made its assessment.
5. Requesting written representations from management regarding their plans for future actions and the feasibility of these plans.
6. Further the audit procedures will include:
 - Analysing cash flow, profit and other relevant factors.
 - Analysing the latest interim financial statements.
 - Inquiring the entity's legal counsel regarding existence of any pending litigations and reasonableness of their outcome.
 - Reading the minutes of the meetings of managing committee or shareholders.
 - Performing audit procedures regarding subsequent events that effect entity's going concern.
 - Confirming the existence, terms and adequacy of borrowing facilities if necessary.

E. GOING CONCERN ASSUMPTION IS APPROPRIATE BUT MATERIAL UNCERTAINTY EXIST:

1. FINANCIAL STATEMENTS "ADEQUATELY" DISCLOSES THE FACT:

- a) If the auditor concludes that the financial statements adequately discloses the material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern and management's plans to deal with these events; and
- b) The audit report shall include a separate section under the heading "Material uncertainty related to going concern" and draw the attention of the readers to the specific note point presented or disclosed adequately by management regarding the material uncertainty.
- c) Also the auditor will express an unqualified opinion in this regard as the entity has adequately disclosed about the material uncertainty.

2. FINANCIAL STATEMENTS “DO NOT ADEQUATELY” DISCLOSES THE FACT:

If the auditor concludes that the financial statements are not adequately reflecting the material uncertainty regarding going concern then the auditor shall express a Qualified/Adverse opinion and explain the reasons for modification in the section “Basis for Qualified/Adverse Opinion Paragraph.

F. GOING CONCERN ASSUMPTION IS INAPPROPRIATE:

If the financial statements have been prepared using the going concern basis of accounting but, in the auditor’s judgment, management’s use of the going concern basis of accounting for the preparation of F/S is inappropriate the auditor shall express an adverse opinion.

G. INDICATORS THAT CAST DOUBT ON GOING CONCERN:

The following are examples of events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern. The indicators are classified into three types:

1. FINANCIAL INDICATORS:

- a) Net liability or net current liability position.
- b) Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment;
- c) Indications of withdrawal of financial support by creditors.
- d) Negative operating cash flows indicated by historical or prospective financial statements.
- e) Adverse key financial ratios.
- f) Substantial operating losses or significant deterioration in the value of assets used to generate cash flows.
- g) Arrears or discontinuance of dividends.
- h) Inability to pay creditors on due dates.
- i) Inability to comply with the terms of loan agreements.
- j) Change from credit to cash-on-delivery transactions with suppliers.
- k) Inability to obtain financing for essential new product development or other essential investments.

2. OPERATING INDICATORS:

- a) Management intentions to liquidate the entity or to cease operations.
- b) Loss of key management without replacement.
- c) Loss of a major market, key customer(s), franchise, license, or principal supplier(s).
- d) Labour difficulties.
- e) Shortages of important supplies.
- f) Emergence of a highly successful competitor.

3. OTHER INDICATORS:

- a) Non-compliance with capital or other statutory or regulatory requirements, such as solvency or liquidity requirements for financial institutions.
- b) Pending legal or regulatory proceedings against the entity that may, if successful, result in claims that the entity is unlikely to be able to satisfy.
- c) Changes in law or regulation or government policy expected to adversely affect the entity.
- d) Uninsured or underinsured catastrophes when they occur.

RELEVANT QUESTIONS:

| | |
|--|------------|
| <p>1. On the basis of which assumption the financial statements of a company are prepared. Explain. Also describe the objectives of the auditor regarding going concern.</p> <p>A. First Write fundamental accounting assumptions without detailed explanation and then write Point - A.</p> | RTP M19(N) |
|--|------------|

| | |
|---|------------|
| 2. Operating Conditions that may cast significant doubt on going concern assumption? A. Write Point - G (2). | RTP N18(O) |
|---|------------|

SA 580 (REVISED) WRITTEN REPRESENTATIONS (W.E.F. 1ST APRIL, 2009)

A. DEFINITION OF WRITTEN REPRESENTATION:

A written statement by provided by management to the auditor to confirm certain matters or to support other audit evidence. Written representations in this context do not include financial statements, the assertions therein, or supporting books and records.

B. WRITTEN REPRESENTATIONS AS AUDIT EVIDENCE:

Written representations are necessary information that the auditor requires in connection with the audit of the entity's financial statements. Accordingly, similar to responses to inquiries, written representations are audit evidence.

Although written representations provide necessary audit evidence, they do not provide sufficient appropriate audit evidence on their own

C. OBJECTIVES:

The objectives of the auditor are:

- a) To obtain written representations from management that they believe that they have fulfilled their responsibility for the preparation of the financial statements and for the completeness of the information provided to the auditor;
- b) To support other audit evidence relevant to the financial statements or specific assertions in the financial statements by means of written representations, if determined necessary by the auditor or required by other SAs; and
- c) To respond appropriately to written representations provided by management.

D. DATE OF AND PERIOD COVERED BY WRITTEN REPRESENTATIONS:

The date shall be as near as practicable to, but not later than the date of the auditor's report on the financial statements.

The written representations shall be for all financial statements and period referred to in the auditor's report.

E. DOUBT AS TO THE RELIABILITY OF WRITTEN REPRESENTATIONS:

1. If the auditor has concerns about the competence, integrity of management, the auditor shall determine the effect that may have on the reliability of representations and audit evidence in general.
2. In particular, if written representations are inconsistent with other audit evidence, the auditor shall perform audit procedures to attempt to resolve the matter.
3. If the auditor concludes that the written representations are not reliable, the auditor shall take appropriate actions, including determining the possible effect on the opinion in the auditor's report in accordance with SA 705. (Usually expresses a disclaimer of opinion)

F. WRITTEN REPRESENTATIONS NOT PROVIDED:

If management does not provide one or more of the requested written representations, the auditor shall:

1. Discuss the matter with management;
2. Re-evaluate the integrity of management and evaluate the effect that may have on the reliability of representations; and
3. Take appropriate actions in accordance with SA 705. (Expresses a disclaimer of opinion)

RELEVANT QUESTIONS:

| | |
|---|--|
| 1. What do you mean by "Written Representations"? As an auditor, how you will deal if management does not provide requested written representations? A. Write Point - A and F. | RTP-N18(O) MTP-M19(O) |
| 2. The auditor P of PAR and Co., a firm of Chartered Accountants is conducting audit of AB Industries Ltd. The auditor requests management to provide Banker's certificate in support of Fixed deposits whereas management provides only written representation on the matter. Analyse how would you deal as an auditor. A. Write Point - A and B. | RTP M18(N) RTP-M18(O) MTP-M19(O) |
| 3. The Partner of Vansh and Vaibhav, Chartered Accountants, asked the management to provide statements from the creditors as part of audit evidence and also required written representation from the management but the management did not provide the requested written representations. Discuss how the auditor would proceed. A. Write Point - A and F | MTP N18(O) |
| 4. Write a short note on management representation. A. Write Point - A and B | N16 - 4M |

SA 620 (REVISED) USING THE WORK OF AN AUDITOR'S EXPERT (ON OR AFTER APRIL 1, 2010)**A. OBJECTIVES:**

The objectives of the auditor are:

- To determine whether to use the work of an auditor's expert; and
- If using the work of an auditor's expert to determine whether that work is adequate for the auditor's purposes.

B. DEFINITIONS:**a) AUDITOR'S EXPERT:**

- An individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the auditor to obtaining sufficient appropriate audit evidence.
- An auditor's expert may be either an auditor's internal expert (who is a partner or staff, including temporary staff, of the auditor's firm or a network firm), or an auditor's external expert.
- The auditor expert shall not include engagement team member.
- Factors influencing whether or not to take assistance of auditor expert even though management expert is available:
 - The nature, scope and objectives of the management's expert's work.
 - Whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services. (Employee or Outsider)
 - The extent to which management can exercise control or influence over the work of the management's expert
 - The management's expert's competence and capabilities.
 - Any controls within the entity over the management's expert's work.
- The auditor shall consider various factors while choosing an expert such as his competence, experience or expertise, credibility, previous work handled and such other similar factors.
- The auditor expert shall be independent from the audit client so that such experts report can be used without any doubt as audit evidence.

b) MANAGEMENT'S EXPERT:

An Individual or Organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity for preparation of the financial statements.

C. AGREEMENT WITH THE AUDITOR'S EXPERT:

The auditor shall agree in writing on the following matters with the auditor's expert:

- a) The nature, scope and objectives of that expert's work;
- b) The respective roles and responsibilities of the auditor and that expert;
- c) The nature, timing and extent of communication between the auditor and that expert, including the form of any report to be provided by that expert; and
- d) The need the expert to observe confidentiality requirements.

D. EVALUATING THE ADEQUACY OF THE AUDITOR'S EXPERT'S WORK:

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

1. The relevance and reasonableness of that expert's findings or conclusions, and their consistency with other audit evidence;
2. If that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods in the circumstances; and
3. Whether the source data used by such expert is reliable, complete and relevant.
4. If the auditor determines that the work of the auditor's expert is not adequate for the auditor's purposes, the auditor shall:
 - a) Agree with that expert on the nature and extent of further work to be performed by that expert; or
 - b) Perform further audit procedures as appropriate to the circumstances.

E. REFERENCE TO AUDITORS EXPERT IN THE AUDITORS REPORT:**1. IN CASE OF UNMODIFIED OPINION:**

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

2. IN CASE OF MODIFIED OPINION:

- a) The auditor may make a reference to work of an auditor's expert to make the user understand the nature of modification to auditor's opinion.
- b) The auditor shall indicate in the auditor's report that such reference does not reduce the auditor's responsibility for that opinion.

RELEVANT QUESTIONS:

| | |
|---|-------------|
| <p>1. What are the factors that may influence the auditor's decision on whether to use an auditor's expert, when management has used a management's expert in preparing the financial statements?</p> <p>A. Write Point - B(a)(4)</p> | MTP M18 (O) |
| <p>2. Write about reference to auditor's expert in auditor's report?</p> <p>A. Write Point - B(a)(1) and Point - E.</p> | |

ACADEMIC INTEREST - FOR STUDENT'S SELF STUDY**SA 320 (REVISED) MATERIALITY IN PLANNING AND PERFORMING AN AUDIT (ON OR AFTER APRIL 1, 2010).**

- A. **MATERIALITY IN THE CONEXT OF AUDIT:** Refer Chapter - 3 (Audit Strategy) (Q No.12).
- B. **DEFINITION OF PERFORMANCE MATERIALITY:** Refer Chapter - 3 (Audit Strategy) (Q No.12).
- C. **REVISION OF MATERIALITY:** Refer Chapter - 3 (Audit Strategy) (Q No.13).
- D. **DOCUMENTATION OF MATERIALITY:** Refer Chapter - 3 (Audit Strategy) (Q No.13).

SA 330 (REVISED) THE AUDITOR'S RESPONSES TO ASSESSED RISKS

- A. **OBJECTIVE:** The objective of the auditor is to obtain sufficient appropriate audit evidence about the assessed risks of material misstatement, through designing and implementing appropriate responses to those risks.
- B. **DEFINITIONS:**
 - SUBSTANTIVE PROCEDURES:** Refer Chapter - 4 (Audit Documentation) (Q No. 2)
 - TEST OF CONTROLS:** Refer Chapter - 8 (Risk Assessment).
 - 1. Evaluation of Internal Controls - Q No. 8
 - 2. Test of Controls - Q No. 8
 - 3. Auditors response when deviation from Control is identified - Q No. 13
- C. **TEST OF CONTROLS WHEN SUBTSTIVE PROCEDURES ALONE DO NOT PROVIDE S & A AUDIT EVIDENCE.**
 - 1. Test of controls may be defined as an audit procedure designed to evaluate the operating effectiveness of controls in preventing or detecting and correcting, material misstatements at the assertion level.
 - 2. The auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls when:
 - a) The auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively (i.e., the auditor intends to rely on the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures); or
 - b) Substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level.
 - 3. A higher level of assurance may be sought about the operating effectiveness of controls when the approach adopted consists primarily of tests of controls, in particular where it is not possible or practicable to obtain sufficient appropriate audit evidence only from substantive procedures.
- D. **SUBSTANTIVE PROCEDURES:**
 - 1. The auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure.
 - 2. This requirement reflects the facts that:
 - a) The auditor's assessment of risk is judgmental and so may not identify all risks of material misstatement; and
 - b) There are inherent limitations to internal control, including management override.
 - 3. Depending on the circumstances, the auditor may determine that:
 - a) Performing only substantive analytical procedures will be sufficient to reduce audit risk to an acceptably low level.
 - b) Only tests of details are appropriate.

4. A combination of substantive analytical procedures and tests of details are most responsive to the assessed risks.
5. In designing tests of details, the extent of testing is ordinarily decided in terms of the sample size.

RELEVANT QUESTIONS:

| | |
|--|--------------|
| 1. A higher level of assurance may be sought about the operating effectiveness of controls when the approach adopted consists primarily of tests of controls, in particular where it is not possible or practicable to obtain sufficient appropriate audit evidence only from substantive procedures. Explain. A. Write Point - C | RTP N18(N) |
| 2. Irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure. Analyse and explain. A. Write Point - D | RTP N18(N) |
| 3. A Multinational company wants to appoint you to carry the statutory audit. Discuss with reference to SA 330, the substantive procedures to be performed to assess the risk of material misstatements? A. Write Point - D | N18 (N) - 6M |

SA 520 (REVISED) ANALYTICAL PROCEDURES (ON OR AFTER APRIL 1, 2010)

THE ENTIRE STANDARD IS GIVEN AS A CHAPTER - 13 (ANALYTICAL PROCEDUES)

SA 530 (REVISED) AUDIT SAMPLING (W.E.F. 1ST APRIL, 2009)

THE ENTIRE STANDARD IS GIVEN AS A CHAPTER - 12 (AUDIT SAMPLING)

SA 550 (REVISED) RELATED PARTIES (ON OR AFTER APRIL 1, 2010)

A. **MEANING OF RELATED PARTY:** A party that is either:

1. A related party as defined in the applicable financial reporting framework or
2. Where the applicable financial reporting framework establishes minimal or no related party requirements:
 - a) A person or other entity that has control or significant influence, directly or indirectly through one or more intermediaries, over the reporting entity;⁹
 - b) Another entity over which the reporting entity has control or significant influence, directly or indirectly through one or more intermediaries; or
 - c) Another entity that is under common control with the reporting entity through having:
 - i) Common controlling ownership;
 - ii) Owners who are close family members; or
 - iii) Common key management.

NOTE: Entities that are under common control by a state (i.e., a national, regional or local government) are not considered related unless they engage in significant transactions or share resources to a significant extent with one another.

B. **NATURE OF RELATED PARTY RELATIONSHIPS AND TRANSACTIONS:**

1. Many related party transactions are in the normal course of business. In such circumstances, they may carry no higher risk of material misstatement of the financial statements than similar transactions with unrelated parties.

2. However in some circumstances there exist higher risks of material misstatement:
 - a) Related parties may operate through an extensive and complex range of relationships and structures, with a corresponding increase in the complexity of related party transactions.
 - b) Information systems may be ineffective at identifying or summarising transactions and outstanding balances between an entity and its related parties.
 - c) Related party transactions may not be conducted under normal market terms and conditions; for example, some related party transactions may be conducted without consideration.

C. RESPONSIBILITIES OF THE AUDITOR

1. There are specific accounting and disclosure requirements for related party relationships, transactions and balances to enable users of the financial statements to understand their nature and effects on the financial statements.
2. The auditor has a responsibility to perform audit procedures to identify, assess and respond to the risks of material misstatement arising from the entity's failure to appropriately account for related party relationships, transactions or balances.
3. The auditor needs to obtain an understanding of the entity's related party relationships and transactions sufficient to be able to conclude whether the financial statements, insofar as they are affected by those relationships and transactions:
 - a) Achieve a true and fair presentation ; or
 - b) Are not misleading (for compliance frameworks).

D. IDENTIFICATION OF FRAUD RISK FACTORS:

1. In addition, an understanding of the entity's related party relationships and transactions is relevant to the auditor's evaluation of whether fraud risk factors are present as required by SA 240. This is because fraud may be more easily committed through related parties.
2. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the SAs. In the context of related parties, the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for such reasons as the following:
 - a) Management may be unaware of the existence of all related party relationships.
 - b) Related party relationships may present a greater opportunity for collusion, concealment or manipulation by management.
3. Planning and performing the audit with professional skepticism as required by SA 200 is therefore particularly important in this context, given the potential for undisclosed related party relationships and transactions. The requirements in this SA are designed to assist the auditor in identifying and assessing the risks of material misstatement associated with related party relationships and transactions, and in designing audit procedures to respond to the assessed risks.

RELEVANT QUESTIONS:

| | |
|---|-------------------------|
| <p>1. There are specific accounting and disclosure requirements for related party relationships, transactions and balances to enable users of the financial statements to understand their nature and effects on the financial statements. Analyse and explain stating the responsibility of auditor in this regard.</p> <p>A. Write Point - C.</p> | RTP M19(N) |
| <p>2. What the auditor shall do after identification of significant related party transactions outside the entity's normal course of business.</p> <p>A. As per SA 550 on "Related Parties", for identified significant related party transactions outside the entity's normal course of business, the auditor shall-</p> <ol style="list-style-type: none"> 1. Inspect the <u>underlying contracts or agreements</u>, if any, and evaluate whether: <ol style="list-style-type: none"> a) The <u>business rationale</u> (or lack thereof) of the transactions suggests that | MTP M18(O), M16 - 5M |

- they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets;
- b) The terms of the transactions are consistent with management's explanations; and
 - c) The transactions have been appropriately accounted for and disclosed in accordance with the applicable financial reporting framework; and
2. Obtain audit evidence that the transactions have been appropriately authorized and approved.

Copyrights Reserved
To **MASTER MINDS**, Guntur

THE END

MASTER MINDS