

1. MEANING AND DEFINITION OF AUDITING

"An audit is **independent examination** of financial information of **any entity**, whether profit oriented or not, and irrespective of its size or legal form, when such an examination is conducted with a view to **expressing an opinion** thereon."

➡ 1.1 ANALYSIS OF DEFINITION

Auditing provides assurance. Its basic nature lies in providing assurance to users - providing confidence to users of financial statements. Such an assurance lends credibility to financial statements. Audited financial statements provide confidence to users that financial information reflected in financial statements can be relied upon.

The Auditor conducting Audit should take care to ensure that financial statements would not mislead anybody.

In doing so, he has to see that financial statements would not mislead anybody by ensuring that: -

- the accounts have been drawn up with reference to entries in the books of account;
- the entries in the books of account are adequately supported by sufficient and appropriate evidence;
- none of the entries in the books of account has been omitted in the process of compilation;
- the information conveyed by the statements is clear and unambiguous;
- the financial statement amounts are properly classified, described and disclosed in conformity with accounting standards;
- the statement of accounts presents a true and fair picture of the operational results and of the assets and liabilities.

2. QUALITIES OF AN AUDITOR

An auditor is concerned with the reporting on financial matters of business and other institutions. Financial matters inherently are to be set with the problems of human fallibility; errors and frauds are frequent.

Tact, caution, firmness, good temper, integrity, discretion, industry, judgement, patience, clear headedness and reliability are some of qualities which an auditor should have. In short, all those personal qualities that go to make a good businessman contribute to the making of a good auditor.

In addition, he must have the shine of culture for attaining a great height. He must have the highest degree of integrity backed by adequate independence.

The auditor, who holds a position of trust, must have the basic human qualities apart from the technical requirement of professional training and education. He is called upon constantly to critically review financial statements and it is obviously useless for him to attempt that task unless his own knowledge is that of an expert.

An exhaustive knowledge of accounting in all its branches is the sine qua non of the practice of auditing. He must know thoroughly all accounting principles and techniques.

3. SA 200 OVERALL OBJECTIVES OF THE INDEPENDENT AUDITOR AND CONDUCT OF THE AUDIT IN ACCORDANCE WITH Sa's

- | | |
|-----------------------------------|--------------------------------------------------|
| a) Overall Objective of Auditor | d) Reasonable Assurance |
| b) Scope of Audit | e) Inherent Limitations of Audit |
| c) Aspects to be covered in Audit | f) Auditor Requirement/Responsibility of Auditor |



➡ 3.1 OVERALL OBJECTIVES OF THE AUDITOR

As per **SA-200** "Overall Objectives of the Independent Auditor", in conducting an audit of financial statements, the overall objectives of the auditor are:

- To obtain **reasonable assurance** about whether the F. S. as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the F.S. are prepared, in all material respects, in accordance with an applicable FRF, and
- To **report** on the F.S. and communicate as required by the SAs, in accordance with the auditor's findings.

In all cases when reasonable assurance cannot be obtained and a qualified opinion in the auditor's report is insufficient, the SAs require that the auditor disclaim an opinion or withdraw from the engagement.

IMP Notes : The user, however, should not assume that the auditor's opinion is an assurance as to the future viability of the enterprise or the efficiency or effectiveness with which management has conducted the affairs of the enterprise.

➡ 3.2 SCOPE OF AUDIT - WHAT IT INCLUDES"

Scope refers to range or reach of something. The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. Users of financial statements may be shareholders, employees, customers, government and regulatory authorities, bankers etc. Enhancing of degree of confidence is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework.

The following points are included in scope of audit of financial statements: -

(1) Coverage of all aspects of entity

Audit of financial statements should be organized adequately to cover all aspects of the entity relevant to the financial statements being audited.

(2) Reliability & sufficiency of financial information

The auditor should be reasonably satisfied that information contained in underlying accounting records and other source data (like bills, vouchers, documents etc.) is reliable and sufficient basis for preparation of financial statements.

The auditor makes a judgment of reliability and sufficiency of financial information by studying & assessing of accounting systems & internal controls and by carrying out appropriate tests, enquiries and procedures.

(3) Proper disclosure of financial information

The **management responsible for preparation** & presentation of financial statements makes many judgments .

The auditor should also decide whether relevant **information is properly disclosed** in the financial statements. He should also keep in mind applicable statutory requirements in this regard. It is done by ensuring that financial statements properly summarize transactions & events & by considering judgments made by management in preparation of financial statements.

For example, choosing method of charging depreciation on fixed assets or choosing appropriate method for valuation of inventories.

The auditor evaluates **selection and consistent application of accounting policies** by management; whether such a selection is proper & whether chosen policy has been applied consistently on a period-to-period basis.

Understand that financial statements of an entity are prepared on historical financial information basis. "Historical financial information" means information expressed in financial terms in relation to a particular entity, derived primarily from that entity's accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

For example, when purchases and sales are reflected in financial statements of an entity, these are examples of historical financial information. These are about transactions which have occurred in past.



➡ 3.3 SCOPE OF AUDIT - WHAT IT DOES NOT INCLUDE?

Auditor is not expected to perform duties which fall outside domain of his competence. For example, physical condition of certain assets like that of sophisticated machinery cannot be determined by him. Similarly, it is not expected from an auditor to determine suitability and life of civil structures like buildings. These require different skillsets which may be performed by qualified engineers in their respective fields.

An auditor is not an expert in authentication of documents. The genuineness of documents cannot be authenticated by him because he is not an expert in this field.

An audit is not an official investigation into alleged wrong doing. He does not have any specific legal powers of search or recording statements of witness on oath which may be necessary for carrying out an official investigation.

Audit is distinct from investigation. Investigation is a critical examination of the accounts with a special purpose. For example, if fraud is suspected and it is specifically called upon to check the accounts whether fraud really exists, it takes character of investigation.

The objective of audit, on the other hand, as has already been discussed, is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion.

Therefore, audit is never started with a pre-conceived notion about state of affairs; about wrong-doing some wrong having been committed. The auditor seeks to report what he finds in normal course of examination of accounts. However, it is quite possible that sometimes investigation results from the prima facie findings of the auditor. It may happen that auditor has given some findings of serious concern. Such finding may prompt for calling an investigation.

The scope of audit is general and broad whereas scope of investigation is specific and narrow.

➡ 3.4 REASONABLE ASSURANCE W.R.T MISSTATEMENT

- Auditor is required to obtain **reasonable assurance** as to whether the financial statements are free from material misstatements
- Reasonable assurance is to be distinguished from absolute assurance. Absolute assurance is a complete assurance or a guarantee that financial statements are free from material misstatements. It is a high-level of assurance but it is not complete assurance.
- Thus, auditor obtains sufficient and appropriate audit evidence to reduce audit risk to an acceptable low level.
- However, reasonable assurance is not absolute assurance. This is due to inherent limitations of an audit.

➡ 3.5 INHERENT LIMITATIONS OF AUDIT

As per SA 200 "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing",

The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit. The inherent limitations of an audit arise from:

(1) Nature of financial reporting

Preparation of financial statements involves making many judgments by management. These judgments may involve subjective decisions or a degree of uncertainty. Therefore, auditor may not be able to obtain absolute assurance that financial statements are free from material misstatements due to frauds or errors.

Responsibility of preparation of F.S and design of Internal control- One of the premises for conducting an audit is that management acknowledges its responsibility of preparation of financial statements in accordance with applicable FRF & for devising suitable internal controls. However, such controls may not have operated to produce reliable financial information due to their own limitations.

(2) Nature of Audit procedures

Practical Limitation due to Sampling- The auditor carries out his work by obtaining audit evidence through performance of audit procedures. However, there are practical & legal limitations on ability of auditor to obtain audit evidence. For example, an auditor does not test all transactions and balances. He forms his opinion only by testing samples.

Legal Limitation - Management may not provide complete information as requested by auditor. There is no way



by which auditor can force management to provide complete information. In case he is not provided with required information, he can only report.

Fraud by Management - The management may consist of dishonest people & may be, itself, involved in fraud. It may be engaged in concealing fraud by designing sophisticated and carefully organized schemes which may be hard to detect by the auditor. It may produce fabricated documents to lead him to believe that audit evidence is valid.

Related Party Transaction (SA 550) - It is quite possible that entity may have entered into some transactions with related parties. Such transactions may be only paper transactions and may not have actually occurred. The auditor may not be aware of such related party relationships or audit procedures may not be able to detect probable wrong doings in such transactions.

(3) Not in nature of investigation

As already discussed, audit is not an official investigation. Hence, auditor cannot obtain absolute assurance that financial statements are free from material misstatements due to frauds or errors.

(4) Timeliness of financial reporting & decrease in relevance of information over time

The relevance of information decreases over time & auditor cannot verify each and every matter. Therefore, a balance has to be struck between reliability of information and cost of obtaining it.

For example, an auditor who is conducting audit of a company since last two years. During these two years, he has sought detailed information from management of company regarding various matters. During his third- year, he chooses to rely upon some information obtained as part of audit procedures of second year. However, it could be possible that something new has happened & that information is not relevant.

(5) Future events- Detail Discussion in SA 560

Future events or conditions may affect an entity adversely. Adverse events may seriously affect ability of an entity to continue its business. The business may cease to exist in future due to change in market conditions, emergence of new business models or products or due to onset of some adverse events.

4. Ethical Requirements Relating to an Audit of F.S.

The term "Ethics" means moral principles which govern a person's behaviour or his conducting of an activity. Ethics is something which comes from an individual intrinsically. Ethics is the science of morals in human conduct.

Need for Professional Ethics: Society in general, governments, clients, taxing authorities, employees, investors, the business and financial community in particular, have reposed **tremendous trust** in services rendered by Chartered Accountants.

The purpose of assurance engagements is to **enhance confidence** of the intended users. Therefore, users need to trust the person who is providing such services. Professional ethics seek to **protect the interests of the profession** as a whole and act as a shield that enables us to command respect.

Any **deviation from the ethical responsibilities brings the disciplinary mechanism** into action which may result into fines, suspension of membership, removal from membership or other disciplinary actions.

Principle based approach Vs Rule based approach (Ethical or legal): The essence of principles-based approach is that it requires compliance with spirit of ethics. It requires accountants to exercise professional judgment based upon their professional knowledge, skill and expertise.

However, rules-based approach to ethics strictly follows clearly established rules. It may lead to a narrow outlook and spirit of ethics may be overlooked while strictly adhering to rules. Rules- based approach is somewhat rigid as it may not be possible to deal with every practical situation relying upon rules.

The auditor shall comply with relevant ethical requirements, including independence. Relevant ethical requirements ordinarily comprise the Code of Ethics issued by the ICAI. The fundamental principles are:

1. Integrity

Integrity requires auditor to be straight forward and honest in all professional and business relationships. It implied fair dealing and truthfulness. It effectively means that he shall not be associated with reports, returns, communications or other information which he believes contains a materially false or misleading statements; contains statements or information provided recklessly or omits required information where such omission could be misleading.



2. Objectivity;

The principle of objectivity requires an auditor **not to compromise professional judgment** because of bias, conflict of interest or undue influence of others.

3. Professional competence and due care

It requires that auditor attains and maintains professional knowledge and skill at the level required to render competent professional service based on current technical and professional standards and legislation and also to act diligently and in accordance with technical and professional standards. Diligence includes responsibility to act carefully, thoroughly and on a timely basis in accordance with requirements of and assignment.

4. Confidentiality

Confidentiality principle requires a professional accountant to respect the confidentiality of information acquired as a result of professional or business relationships. Confidentiality serves the public interest because it facilitates the free flow of information from the professional accountant's client or employing organization to the accountant with the understanding that the information will not be disclosed to a third party.

However, such confidential information may be disclosed, for example, when it is required by law, when it is permitted by law and is authorised by the client or employer or there is a professional duty or right to disclose when not prohibited by law.

5. Professional behaviour

It requires an accountant to **comply with relevant laws and regulations** and avoid any conduct that the accountant knows or should know might discredit the profession. A professional accountant **shall not** knowingly engage in any employment, occupation or activity that **impairs or might impair** the integrity, objectivity or good reputation of the profession, and as a result would be incompatible with the fundamental principles.

6. Independence - Refer detail concept given at the end of this chapter.

5. Professional Skepticism

Professional skepticism refers to 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.

Professional Skepticism Requirement and Auditor Expectation.

1. The auditor shall plan & perform an audit with professional skepticism.

2. It Reduces risk of:

- ▲ Overlooking unusual circumstances.
- ▲ Over generalizing when drawing conclusions from audit observations.
- ▲ Using inappropriate assumptions in determining N, T, E of audit procedures & evaluating the results thereof.

3. Professional skepticism includes being alert to:

- ▲ Contradictory audit evidence.
- ▲ Questions on reliability of documents.
- ▲ Conditions indicating possible frauds.
- ▲ Circumstances suggesting need for audit procedures in addition to those suggested in SA's.

Professional skepticism is necessary to the **critical assessment of audit evidence**. It also includes consideration of the **sufficiency and appropriateness of audit evidence** obtained in the light of the circumstances, for example in the case where fraud risk factors exist and a single document, of a nature that is susceptible to fraud, is the sole supporting evidence for a material financial statement amount.

The auditor may accept records and documents as genuine unless the auditor has reason to believe the contrary. Nevertheless, the auditor is required to consider the **reliability of information** to be used as audit evidence. In cases of **doubt about the reliability of information or indications of possible fraud**, the SAs require that the auditor investigate further and determine what modifications or additions to audit procedures are necessary to resolve the matter.

The auditor cannot be expected to disregard past experience of the honesty and integrity of the entity's management and those charged with governance. Nevertheless, a belief that management and those charged with governance are honest and have integrity does not relieve the auditor of the need to maintain professional skepticism.



6. PROFESSIONAL JUDGMENT

Meaning:

- The application of relevant training, knowledge and experience,
- Within the context provided by auditing, accounting & ethical standards,
- In making informed decisions about the courses of action.
- That are appropriate in the circumstances of the audit engagement.

Requirements:

- A. The auditor shall exercise professional judgment in planning and performing an audit of financial statements.
- B. Its exercise depends on facts & circumstances known to the auditor.
- C. Professional Judgment is to be exercised throughout the audit and to be appropriately documented.
- D. **Professional Judgment is important when deciding about:**
 - Materiality & audit risk.
 - NTE of audit procedures.
 - Evaluating sufficiency & appropriateness of audit procedures.
 - Evaluating management judgment in applying applicable FRF.
 - Drawing conclusions based on audit evidence.

7. ADVANTAGES OF AUDIT OF FINANCIAL STATEMENTS

- a) Audited accounts provide **high quality information**. It gives confidence to users that information on which they are relying is qualitative and it is the outcome of an exercise carried out by following Auditing Standards recognized globally.
- b) **Shareholder interest is safeguarded by an audit**. In case of companies, shareholders may or may not be involved in daily affairs of the company. The financial statements are prepared by management. As shareholders are owners of the company, they need an independent mechanism so that financial information is qualitative and reliable.
- c) An audit acts as a **moral check on employees** from committing frauds for the fear of being discovered by audit.
- d) Audited financial statements are **helpful to government authorities** for determining tax liabilities.
- e) Audited financial statements can be **relied upon by lenders**, bankers for making their credit decisions i.e. whether to lend or not to lend to a particular entity.
- f) An audit may also **detect fraud** or error or both.
- g) An audit **reviews existence and operations of various controls** operating in any entity. Hence, it is useful at pointing out deficiencies.

8. SA 220 QUALITY CONTROL FOR AN AUDIT OF FINANCIAL STATEMENTS

ELEMENTS OF A SYSTEM OF QUALITY CONTROL

As per SQC 1 "Quality Control for Firms that perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements", the firm's system of quality control should include policies and procedures addressing each of the following elements:



Acceptance and continuance of client relationships and audit engagements

1. The engagements partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationship and audit engagements have been followed.
2. If the engagement partner obtains information that would have caused the firm to decline the audit engagement had that information been available earlier, the engagement partner shall communicate that information promptly to the firm, so that the firm and the engagement partner can take the necessary action.

A firm before accepting an engagement should acquire vital information about client. Such an information should help firm to decide about:-

- ▲ The integrity of the principal owners, key management and TCWG of the entity;
- ▲ Competency of engagement team to perform the audit engagement and availability of necessary capabilities, including time and resources;
- ▲ Compliance with relevant ethical requirements by firm and the engagement team; and
- ▲ Significant matters that have arisen during the current or previous audit engagement, and their implications for continuing the relationship.

With regard to the integrity of a client, matters that the firm considers include,

For example:

- The identity & business reputation of client's principal owners, key management, related parties & TCWG.
- The nature of client's operations, including its business practices.
- Information concerning attitude of client's principal owners, key management & TCWG towards such matters as aggressive interpretation of accounting standards & internal control environment.
- Whether client is aggressively concerned with maintaining the firm's fees as low as possible.
- Indications of an inappropriate limitation in the scope of work.
- Indications that the client might be involved in money laundering or other criminal activities.
- The reasons for the proposed appointment of the firm and non-reappointment of the previous firm.

If there is any conflict of interest between the firm & client, it should be properly resolved before accepting the engagement.

Human resources

The firm should establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the capabilities, competence, and commitment to ethical principles necessary to perform its engagements in accordance with professional standards and regulatory and legal requirements, and to enable the firm or engagement partners to issue reports that are appropriate in the circumstances.

Such policies and procedures address the following personnel issues:


- Recruitment;
- Performance evaluation;
- Capabilities;
- Competence
- Career development;
- Promotion;
- Compensation; and
- Estimation of personnel needs.

Addressing these issues enables the firm to ascertain the number and characteristics of the individuals required for the firm's engagements. The firm's recruitment processes include procedures that help the firm select individuals of integrity as well as the capacity to develop the capabilities and competence necessary to perform the firm's work.



Assignment of engagement teams	<p>The engagement partner shall be satisfied that the engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to:</p> <ol style="list-style-type: none"> 1. Perform the audit engagement in accordance with professional standards & regulatory & legal requirements,& 2. Enable an auditor's report that is appropriate in the circumstances to be issued. 	
Independence	<p>The engagement partner shall form a conclusion on compliance with independence requirements. In doing so, the engagement partner shall:</p> <ol style="list-style-type: none"> 1 Obtain relevant information to identify circumstances and relationship that create threats to independence; 2 Evaluate information on identified breaches, of the firm's independence policies and procedures; and 3 Take appropriate action to eliminate such threats or reduce them to an acceptable level or to withdraw from the audit engagement. 	
Relevant ethical requirements Note – Covered in SA 200	<ol style="list-style-type: none"> 1 Throughout the audit engagement, the engagement partner shall remain alert, for non-compliance with relevant ethical requirements by members of the engagement team. 2 If matters come to the engagement partner's attention that indicate that members of the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. 	
Leadership, responsibilities for quality on audits	<p>As per SA 220 "Quality Control for an Audit of Financial Statements" the engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned.</p> <p>As a part of this responsibility Engagement Partner should emphasize the following to the engagement Team (ET):</p> <ul style="list-style-type: none"> • Compliance with professional Standards and legal requirements. • Compliance with firm's Quality Control Policies. • Issuance of appropriate audit report. • Ability to raise concerns without fear. • Quality is essential & indispensable in engagement performance. <p>Meaning of Engagement partner: The partner or other person in the firm who is a member of the Institute of Chartered Accountants of India and is in full time practice and is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.</p>	
Engagement performance	Direction, supervision & performance	<p>The engagement partner shall take responsibility for:</p> <ul style="list-style-type: none"> • The direction, supervision and performance of the audit engagement in compliance with professional standards & regulatory and legal requirements, and • The auditor's report being appropriate in the circumstances.
	Reviews	<ul style="list-style-type: none"> • The engagement partner shall take responsibility for reviews being performed in accordance with the firm's review policies and procedures. • On or before the date of the auditor's report, the engagement partner shall, be satisfied that sufficient appropriate audit evidence has been obtained to support the conclusions and the auditor's report.
	Consultation	<p>The engagement partner shall:</p> <ul style="list-style-type: none"> • Take responsibility for the engagement team undertaking appropriate consultation of difficult matters;



	<ul style="list-style-type: none"> • Be satisfied that engagement team have undertaken consultation both within the engagement team & between the engagement team and others; • Be satisfied that the nature and scope of and conclusions resulting from, such consultations are agreed with the party consulted; and • Determine that conclusions resulting from such consultations have been implemented.
Policy and Procedure for Engagement Performance	<p>Through its policies and procedures, the firm seeks to establish consistency in the quality of engagement performance. This is often accomplished through written or electronic manuals, software tools or other forms of standardized documentation, and industry or subject matter-specific guidance materials.</p> <p>Matters addressed include the following:</p> <ul style="list-style-type: none"> • How engagement teams are briefed on the engagement to obtain an understanding of the objectives of their work. • Processes for complying with applicable engagement standards. • Processes of engagement supervision, staff training and coaching. • Methods of reviewing the work performed, the significant judgments made and the form of report being issued. • Appropriate documentation of the work performed and of the timing and extent of the review. • Processes to keep all policies and procedures current.
Monitoring 9)	<ul style="list-style-type: none"> • The firm should establish policies and procedures designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, operating effectively and complied with in practice. • Such policies and procedures should include an ongoing consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements. • The purpose of monitoring compliance with quality control policies and procedures is to provide an evaluation of: <ul style="list-style-type: none"> o Adherence to professional standards and regulatory and legal requirements; o Whether the quality control system has been appropriately designed and effectively implemented; and o Whether the firm's quality control policies and procedures have been appropriately applied, so that reports that are issued by the firm or engagement partners are appropriate in the circumstances. • Follow-up by appropriate firm personnel so that necessary modifications are promptly made to the quality control policies and procedures. 
Engagement quality control review	<ol style="list-style-type: none"> 1. For audits of financial statements of listed entities and those other audit engagements for which the engagement quality control review is required, the engagement partner shall: <ol style="list-style-type: none"> a) Determine that an engagement quality control reviewer has been appointed, b) Discuss significant matters with the engagement quality control reviewer, and c) Not date the auditor report until the completion of the engagement quality control review, 2. The engagement quality control reviewer shall evaluate the following: <ol style="list-style-type: none"> (a) Discussion of significant matters with the engagement partner (b) Review of the financial statements and the proposed auditor's report (c) Review of selected audit documentation and



	<p>(d) Conclusions reached in formulating the auditor's report and consideration of whether the proposed auditor's report is appropriate.</p> <p>3. For audits of financial statements of listed entities, the engagement quality control reviewer shall also consider the following:</p> <p>(a) The engagement team's evaluation of the firm's independence</p> <p>(b) Whether appropriate consultations have taken place & the conclusions arising from those consultations</p> <p>(c) Whether audit documentation selected for reviews reflects the work performed and supports the conclusions reached</p>
Differences of opinion	If differences of opinion arise within the engagement team with those consulted or between the engagement partner and the engagement quality control reviewer, the engagement team shall follow the firm's policies and procedures for dealing with and resolving differences of opinion.
Documentation	<p>1. The auditors shall document:</p> <p>a) Issues identified with respect to compliance with relevant ethical requirement & how they were resolved</p> <p>b) Conclusions on compliance with independence requirements</p> <p>c) Conclusions reached regarding the acceptance and continuance of client relationships and audit engagements</p> <p>d) The consultations undertaken during the course of the audit engagement</p> <p>2. The engagement quality control reviewer shall document, for the audit engagement reviewed that,</p> <p>a) The procedures for engagement quality control review have been performed</p> <p>b) The engagement quality control review has been completed on or before the date of the auditors reports and</p> <p>c) The reviewer is not aware of any unresolved matters.</p>

9. INDEPENDENCE OF AUDITORS

➡ 9.1 MEANING OF INDEPENDENCE

- ❖ To define "independence" precisely is not possible since independence is a state of mind and personal character.
- ❖ According to the Guidance Note of the ICAI on "Independence of Auditors" independence implies that the judgment of a person is not subordinate to the wishes or directions of another person who might have engaged him.
- ❖ It stipulates that the independence is a condition of mind and personal character and should not be confused with the visible standards of independence.

➡ 9.2 INDEPENDENCE IS:

- (a) **Independence of mind** - the state of mind that permits the provision of an opinion without being affected by influences allowing an individual to act with integrity, and exercise objectivity and professional skepticism; and
- (b) **Independence in appearance** - the avoidance of facts and circumstances that are so significant that a third party would reasonably conclude an auditor's integrity, objectivity or professional skepticism had been compromised."

Independence of the auditor has not only to exist in fact, but also appear to so exist to all reasonable persons.

- ❖ The auditor has to conduct himself in such a way that no reasonable person, can doubt his objectivity and integrity. In fact, the word independent as a prefix in audit proposition in itself enshrines the concept of independence of an auditor and it is thus, considered fundamental concept in the theory of auditing.
- ❖ The relationship between the auditor and the client should be such that firstly, he himself is satisfied about his client and then it is understood by others that the independence of the auditor is not affected.



➡ 9.3 REQUIREMENTS OF LAW ENSURING INDEPENDENCE

Law also makes an attempt to ensure auditor's independence. For instance:

- ❖ The Companies Act, 2013 contains specific provisions to ensure the independence of the auditor e.g.
 - ✓ the right of access given to the auditor to the books of account and other documents,
 - ✓ provisions disqualifying certain persons to act as auditor,
 - ✓ Provisions relating to appointment, removal, etc. are to ensure the independence of the auditor.
- ❖ Various provisions in the Schedules to the Chartered Accountants' Act, 1949 on misconduct are also an attempt to protect the independence of the auditor and to keep the professional competence.

➡ 9.4 THREATS TO INDEPENDENCE

1. **Self-interest threats-** It may occur as a result of the financial or other interests of a professional accountant or of a relative. Examples are:
 - ❖ Direct or indirect financial interest in a client,
 - ❖ Loan or guarantee to or from the concerned client,
 - ❖ Undue dependence on a client's fees,
 - ❖ Close business relationship with an audit client,
 - ❖ Potential employment with the client, and
 - ❖ Contingent fees for the audit engagement
2. **Self-review threats-** It may occur when a previous judgment needs to be re- evaluated by the professional accountant responsible for that judgment. Instances where such threats may arise are:
 - ❖ when an auditor having recently been a director or senior officer of the company, and
 - ❖ when auditors perform services that are themselves subject matters of audit.
3. **Advocacy threats-** It may occur when a professional accountant promotes a position or opinion to the point that subsequent objectivity may be compromised. For example, an auditor dealing with shares or securities of the audited company, or becomes the client's advocate in litigation and third-party disputes.
4. **Familiarity threats-** are self-evident, and occur when auditors form relationships with the client where they end up being too sympathetic to the client's interests. This can occur in many ways:
 - Close relative of the audit team working in a senior position in the client company,
 - Former partner of the audit firm being a director or senior employee of the client,
 - Long association between specific auditors and their specific client counterparts, and
 - Acceptance of significant gifts or hospitality from the client company, its directors or employees.
5. **Intimidation threats-** which occur when auditors are deterred from acting objectively with an adequate degree of professional skepticism. Basically, these could happen because of threat of replacement over disagreements with the application of accounting principles, or pressure to disproportionately reduce work in response to reduced audit fees.

➡ 9.5 SAFEGUARDS TO INDEPENDENCE

The Chartered Accountant has a responsibility to remain independent by taking into account the context in which they practice, the threats to independence and the safeguards available to eliminate the threats.

The following are the guiding principles in this regard: -

1. Auditors should always be and appears to be independent of the entities that they are auditing.
2. Auditor should abide himself with the key fundamental principles are integrity, objectivity and professional skepticism.
3. Auditor should consider threats to independence before accepting any audit assignment.
4. In case of existence of any threats to independence, auditor should not accept the engagement or put in place safeguards that eliminate them. If necessary safeguards cannot be put in place due to circumstances, auditor should withdraw.
5. If the auditor is unable to fully implement credible and adequate safeguards, then he must not accept the work.



10. SA 210 – AGREEING THE TERMS OF AUDIT ENGAGEMENT

➡ 10.1 WHAT IS AN ENGAGEMENT?

Engagement means an arrangement to do something. In the context of auditing, it means a formal agreement between auditor and client under which auditor agrees to provide auditing services. It takes the shape of engagement letter.

➡ 10.2 OBJECTIVE OF AUDITOR

The objective of the auditor is to **accept or continue** an audit engagement only when the basis upon which it is to be performed has been agreed, through:

- Establishing whether the **preconditions for an audit** are present; &
- Confirming that there is a **common understanding** between the auditor and management & TCWG, of the terms of the audit engagement.

➡ 10.3 PRECONDITIONS FOR AN AUDIT

The use by management of an acceptable FRF in the preparation of the financial statements & the agreement of management &, where appropriate, TCWG to the premise on which an audit is conducted. In order to establish whether the preconditions for an audit are present, the auditor shall:

- 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:
 - Access to all relevant information such as records, documentation and other matters;
 - Additional information that the auditor may request from management for the purpose of the audit and
 - Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

➡ 10.4 WHAT HAPPENS IF PRECONDITIONS FOR AN AUDIT ARE NOT PRESENT?

If the preconditions for an audit are not present, the auditor shall discuss the matter with management. Unless required by law or regulation to do so, 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 is not obtained on matters relating to understanding of responsibility of management on preparation of financial statements, internal controls for preparation of financial statements, providing access to all information to auditor and unrestricted access to persons within the entity.

➡ 10.5 LIMITATION ON SCOPE PRIOR TO AUDIT ENGAGEMENT ACCEPTANCE

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

➡ 10.6 OTHER FACTORS AFFECTING AUDIT ENGAGEMENT ACCEPTANCE

If the preconditions for an audit are not present, the auditor shall discuss the matter with management. The auditor shall not accept the proposed audit engagement:

- If the auditor has determined that the FRF to be applied in the preparation of the F.S. is unacceptable, or
- If the management does not agree with its responsibilities prescribed above.



➡ 10.7 AGREEMENT ON AUDIT ENGAGEMENT TERMS

- 1) The auditor shall agree the terms of the audit engagement with management or TCWG, as appropriate.
- 2) **The audit engagement letter is sent by auditor to his client. The agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include:**
 - The objective and scope of the audit of the F.S.;
 - The responsibilities of the auditor;
 - The responsibilities of management;
 - Identification of the applicable FRF for the preparation of the F.S. &
 - Reference to the expected form and content of any reports to be issued by the auditor & a statement that there may be circumstances in which a report may differ from its expected form and content.
- 3) If law or regulation prescribes in sufficient detail the terms of the audit engagement referred above, the auditor need not record them in a written agreement, except for the fact that such law or regulation applies and that management acknowledges and understands its responsibilities.

➡ 10.8 RECURRING AUDITS

In case of recurring audits, the auditor shall assess whether circumstances require revision in terms of the audit engagement and whether there is a need to remind the entity of the existing terms of the audit engagement. 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, legal or regulatory requirements or changes in other reporting requirements

➡ 10.9 ACCEPTANCE OF A CHANGE IN THE TERMS OF THE AUDIT ENGAGEMENT:

a) Request from Entity to change the Terms of Audit Engagement-When Reasonable Justification Exists?

A request from the entity for the auditor to change the terms of the audit engagement may result from a **change in circumstances** affecting the need for the service,

A misunderstanding as to the nature of an audit as originally requested or a restriction on the scope of the audit engagement, whether imposed by management or caused by other circumstances.

The auditor considers the justification given for the request, particularly the implications of a restriction on the scope of the audit engagement. A change may not be considered reasonable if it appears that change relates to information that is incorrect, incomplete or otherwise unsatisfactory.

An example might be where the auditor is unable to obtain sufficient appropriate audit evidence regarding receivables and the entity asks for the audit engagement to be changed to a review engagement to avoid a qualified opinion or a disclaimer of opinion.

b) What should auditor consider before agreeing to change the audit engagement to the engagement providing lower level of assurance?

If, prior to completing the audit engagement, the auditor is requested to change the audit engagement to an engagement that conveys a lower level of assurance, the auditor shall determine whether there is reasonable justification for doing so.

Before agreeing to change an audit engagement to a review or a related service, an auditor who was engaged to perform an audit in accordance with SAs may also need to assess any legal or contractual implications of the change.

If the auditor concludes that there is reasonable justification to change the audit engagement to a review or a related service, the audit work performed to the date of change may be relevant to the changed engagement. In order to avoid confusing the reader, the report on the related service would not include reference to:



(a) The original audit engagement or

(b) Any procedures that may have been performed in the original audit engagement, except where the audit engagement is changed to an engagement to undertake agreed-upon procedures and thus reference to the procedures performed is a normal part of the report.

If the terms of the audit engagement are changed, the auditor and management shall agree on and record the new terms of the engagement in an engagement letter or other suitable form of written agreement.

c) Recourse available to auditor in situation of non-agreement to a change in terms of engagement and lack of permission from management to continue original audit engagement

If the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted by management to continue the original audit engagement, the auditor shall:

(a) Withdraw from the audit engagement where possible under applicable law or regulation and

(b) Determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators.

11. AUDITING AND ASSURANCE STANDARDS BOARD

Objectives and functions of the auditing and assurance standards board

- i. To review the existing and emerging auditing practices worldwide.
- ii. To formulate Engagement Standards, Standards on Quality Control and Statements on Auditing.
- iii. To review and revise the existing Standards and Statements on Auditing.
- iv. To develop Guidance Notes on issues arising out of any Standard, auditing issues pertaining to any specific industry and revise.
- v. To review and revise the existing Guidance Notes
- vi. To formulate General Clarifications, where necessary, on issues arising from Standards.
- vii. To formulate and issue Technical Guides, Practice Manuals, Studies and other papers.

Composition

Apart from amongst the elected members of the Council of the ICAI the following are also represented on AASB:

- i. Eminent members of the profession.
- ii. One special invitee from each three regulatory bodies SEBI RBI and IRDA
- iii. One special invitee from the Indian Institute(s) of Management,
- iv. One special invitee from a prominent Industry association.
- v. One special invitee representing public interest.

Term of the members

- a. The term of the Chairman of the Board is 3 years or his term of council whichever less.
- b. The Council of the ICAI may fill any vacancy in the office of the Chairman and the Chairman so appointed holds office for the unexpired term of the Council.
- c. The term of other members of the Board and the special invitees is one year.

12. WHAT IS AN ENGAGEMENT?

Engagement means an arrangement to do something. In the context of auditing, it means a formal agreement between auditor and client under which auditor agrees to provide auditing services. It takes the shape of engagement letter.

13. MEANING OF ASSURANCE ENGAGEMENT

"Assurance engagement" means an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria.



It means that the practitioner gives an opinion about specific information due to which users of information are able to make confident decisions knowing well that chance of information being incorrect is diminished.

Elements of an Assurance Engagement	<p>Following elements comprise an assurance engagement: -</p> <ol style="list-style-type: none"> 1 A three party relationship involving a practitioner, a responsible party, and intended users An assurance engagement involves abovesaid three parties. A practitioner is a person who provides the assurance. The term practitioner is broader than auditor. Audit is related to historical information whereas practitioner may provide assurance not necessarily related to historical financial information. A responsible party is the party responsible for preparation of subject matter. Intended users are the persons for whom an assurance report is prepared. These persons may use the report in making decisions. 2. An appropriate subject matter It refers to the information to be examined by the practitioner. For example, financial information contained in financial statements while conducting audit of financial statements. 3. Suitable criteria These refer to benchmarks used to evaluate the subject matter like standards, guidance, laws, rules and regulations. 4. Sufficient appropriate evidence 5. A written assurance report in appropriate form A written report is provided containing conclusion that conveys the assurance about the subject matter. A written assurance report is the outcome of an assurance engagement.
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Checkbox	Elements of an assurance engagement
✓	Three Party relationship
✓	An appropriate subject matter
✓	Suitable Criteria
✓	Sufficient appropriate evidence
✓	Written assurance report in appropriate form

Meaning of Review; Audit Vs. Review	<p>We have learnt that audit is a reasonable assurance engagement. It provides reasonable assurance. However, review is a limited assurance engagement. It provides lower level of assurance than audit. Further, review involves fewer procedures and gathers sufficient appropriate evidence on the basis of which limited conclusions can be drawn up. However, both "audit" and "review" are related to financial statements prepared on the basis of historical financial information.</p>
Types of Assurance Engagements- Reasonable assurance engagement vs. Limited assurance engagement	<p>As already discussed, assurance engagements provide assurance to users. The difference is of degree. Reasonable assurance engagement like audit provides reasonable assurance which is a high level of assurance. Limited assurance engagement like review provides lower level of assurance than audit. It is only a moderate level of assurance.</p>



Reasonable assurance engagement	Limited assurance engagement
Reasonable assurance engagement provides high level of assurance.	Limited assurance engagement provides lower level of assurance than reasonable assurance engagement
It performs elaborate and extensive procedures to obtain sufficient appropriate evidence.	It performs fewer procedures as compared to reasonable assurance engagement.
It draws reasonable conclusions on the basis of sufficient appropriate evidence.	It involves obtaining sufficient appropriate evidence to draw limited conclusions.
Example of reasonable assurance engagement is an audit engagement.	Example of limited assurance engagement is review engagement.

Besides reasonable assurance engagements and limited assurance engagements, there is another kind of assurance which is related to matters other than historical financial information. Such an assurance may relate to prospective financial information and not to historical financial information. It may relate to providing assurance on internal controls in an entity.

"Prospective financial information" means financial information based on assumptions about events that may occur in the future and possible actions by an entity. It can be in the form of a forecast or projection or combination of both.

It is to be noted that in such type of assurance engagements, examination is not of historical financial information.

Here, it is important to note the difference between **"Historical financial information"** and **"Prospective financial information."** The former relates to information expressed in financial terms of an entity about economic events, conditions or circumstances occurring in past periods. The latter relates to financial information based on assumptions about occurrence of future events and possible actions by an entity.

Therefore, historical financial information is rooted in past events which have already occurred whereas prospective financial information is related to future events.

In assurance reports involving prospective financial information, the practitioner obtains sufficient appropriate evidence to the effect that management's assumptions on which the prospective financial information is based are not unreasonable, the prospective financial information is properly prepared on the basis of the assumptions and it is properly presented and all material assumptions are adequately disclosed.

Prospective financial information relates to future events. While evidence may be available to support the assumptions on which the prospective financial information is based, such evidence is itself generally future- oriented. The auditor is, therefore, not in a position to express an opinion as to whether the results shown in the prospective financial information will be achieved.

Therefore, in such assurance engagements, practitioner provides a report assuring that nothing has come to practitioner's attention to suggest that these assumptions do not provide a reasonable basis for the projection.

Hence, such type of assurance engagement provides only a "moderate" level of assurance.

Examples of assurance engagements

Checkbox	Example of engagement assurance	Type of assurance engagement
✓	Audit of statements financial	Reasonable assurance engagement
✓	Review of statements financial	Limited assurance engagement
✓	Examination of Prospective financial information	Provides assurance regarding reasonability of assumptions forming basis of projections and related matters
✓	Report on controls operating at an organization	Provides assurance regarding design and operation of controls



14. ENGAGEMENT AND QUALITY CONTROL STANDARDS: AN OVERVIEW

Engagement Standards	<p>The following Standards issued under authority of ICAI Council are collectively known as Engagement Standards:-</p> <ol style="list-style-type: none"> 1. Standards on auditing (SAs) which apply in audit of historical financial information. 2. Standards on review engagements (SREs) which apply in review of historical financial information. 3. Standards on Assurance engagements (SAEs) which apply in assurance engagements other than audits and review of historical financial information. 4. Standards on Related Services (SRSs) which apply in agreed upon procedures to information, compilation engagements and other related service engagements. <p>The purpose of issue of these standards is to establish high quality standards and guidance in the areas of financial statement audits and in other types of assurance services.</p>
Standards on Auditing	<p>Standards on Auditing apply in the context of an audit of financial statements by an independent auditor. It is important to remember that Standards on Auditing apply in audit of historical information. These establish high quality benchmarks and are followed by auditors in conducting audit of financial statements.</p> <p>Standards on Auditing have been issued on wide spectrum of issues in the field of auditing ranging from overall objectives of independent auditor, audit documentation, planning an audit of financial statements, identifying and assessing risk of material misstatement, audit sampling, audit evidence and forming an opinion and reporting on financial statements. These cover all significant aspects of audit of financial statements.</p> <p>Some examples of Standards on Auditing are:-</p> <ul style="list-style-type: none"> • SA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in accordance with Standards on Auditing • SA 230 Audit Documentation • SA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment • SA 500 Audit Evidence • Revised SA 700 Forming an Opinion and Reporting on Financial Statements
Standards on Review Engagements	<p>Standards on review engagements apply in the context of review of financial statements. We have already understood that review is a limited assurance engagement and it provides assurance which is lower than that provided by audit. It is due to the fact that review involves fewer procedures as compared to audit. Since a review also provides assurance to users, it also involves obtaining sufficient appropriate evidence. For example, when an auditor performs review of interim financial information of an entity.</p> <p>Examples of Standards on Review engagements are:</p> <ul style="list-style-type: none"> • SRE 2400 (Revised) Engagements to Review Historical Financial Statements • SRE 2410 Review of Interim Financial Information Performed by the Independent Auditor of the Entity <p>It is to be noted that both Standards on auditing and Standards on review engagements apply to engagements involving historical financial information.</p>
Standards on Assurance Engagements	<p>There is another set of standards which apply in assurance engagements dealing with subject matters other than historical financial information. Such assurance engagements do not include "audit" or "review" of historical financial information. These standards are known as Standards on Assurance Engagements. For example, an assurance engagement relating to examination of prospective financial information.</p> <p>It is to be noted that in such type of assurance engagements, examination is not of historical</p>



	<p>financial information or engagement may relate to providing assurance regarding non-financial matters like design and operation of internal control in an entity.</p> <p>Examples of Standards on Assurance Engagements are:</p> <ul style="list-style-type: none"> • SAE 3400 The Examination of Prospective Financial Information • SAE 3420 Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus
Standards on Related Services	<p>Lastly, there are standards on related services. These standards apply in engagements to perform agreed-upon procedures regarding financial information.</p> <p>For example, an engagement to perform agreed-upon procedures may require the auditor to perform certain procedures concerning individual items of financial data, say, accounts payable, accounts receivable, purchases from related parties and sales and profits of a segment of an entity, or a financial statement, say, a balance sheet or even a complete set of financial statements.</p> <p>An engagement in which practitioner may be called upon to assist management with the preparation and presentation of historical financial information without obtaining assurance on that information. Such type of compilation engagements fall in the category of related services and practitioner issues a report clearly stating that it is not an assurance engagement and no opinion is being expressed.</p> <p>These types of services are called related services and standards have been issued to deal with practitioner's responsibilities in this regard.</p> <p>Examples of Standards on related services are:</p> <ul style="list-style-type: none"> • SRS 4400 Engagements to perform agreed-upon procedures regarding financial information • SRS 4410 (Revised) Compilation engagements <p>It is to be clearly understood that all the above standards i.e., Standards on Auditing (SAs), Standards on Review Engagements (SREs), Standards on Assurance Engagements (SAEs) and Standards on related services (SRSs) are collectively known as the Engagement Standards.</p> <p>Engagement Standards issued under the authority of Council of ICAI deal with responsibilities of auditor/practitioner</p>
Standards on Quality Control	<p>Standards on Quality Control (SQC) have been issued to establish standards and provide guidance regarding a firm's responsibilities for its system of quality control for the conduct of audit and review of historical financial information and for other assurance and related service engagements.</p> <p>SQC 1 has been issued in this regard. It requires auditors/practitioners to establish system of quality control so that firm and its personnel comply with professional standards and regulatory & legal requirements and reports issued are appropriate.</p> <p>Its basic objective is that while rendering services, to which engagement standards apply, there should be a system of quality control with in firms to ensure complying with professional standards/legal requirements. System of quality control ensures issuing of appropriate reports in the circumstances.</p> <p>Further, it is also to be remembered that Standards on Quality Control (SQC) are to be applied for all services covered by Engagement Standards.</p>
Why are Standards needed?	<ul style="list-style-type: none"> • Standards ensure carrying out of audit against established benchmarks at par with global practices. • Standards improve quality of financial reporting thereby helping users to make diligent decisions. • Standards promote uniformity as audit of financial statements is carried out following these Standards.



	<ul style="list-style-type: none"> Standards equip professional accountants with professional knowledge and skill. Standards ensure audit quality 										
Duties in relation to Engagement and Quality Control Standards	<p>It is the duty of professional accountants to see that Standards are followed in engagements undertaken by them. Ordinarily, these are to be followed by professional accountants. However, a situation may arise when a specific procedure as required in Standards would be ineffective in a particular engagement. In such a case, he is required to document how alternative procedures performed achieve the purpose of required procedure. Also, reason for departure has also to be documented unless it is clear. Further, his report should draw attention to such departures. It is also to be noted that a mere disclosure in the report does not absolve a professional accountant from complying with applicable Standards.</p> <table> <tr> <th>Checkbox</th><th>Example of engagement assurance</th></tr> <tr> <td>✓</td><td>Standards on auditing (SAs) apply in audit of historical financial information.</td></tr> <tr> <td>✓</td><td>Standards on review engagements (SREs) apply in review of historical financial information.</td></tr> <tr> <td>✓</td><td>Standards on assurance engagements (SAEs) apply in engagements dealing in matters other than historical financial information.</td></tr> <tr> <td>✓</td><td>Standards on related services (SRSs) apply in engagements to perform agreed-upon procedures regarding financial information and other services like assisting management in preparation and presentation of financial statements.</td></tr> </table>	Checkbox	Example of engagement assurance	✓	Standards on auditing (SAs) apply in audit of historical financial information.	✓	Standards on review engagements (SREs) apply in review of historical financial information.	✓	Standards on assurance engagements (SAEs) apply in engagements dealing in matters other than historical financial information.	✓	Standards on related services (SRSs) apply in engagements to perform agreed-upon procedures regarding financial information and other services like assisting management in preparation and presentation of financial statements.
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SA - 260 COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE

The role of communication	<p>Effective two-way communication is important in assisting:</p> <ol style="list-style-type: none"> The auditor and in understanding matters related to the audit in context, and in developing a constructive working relationship, while maintaining the auditor's independence and objectivity The auditor in obtaining from TCWG information relevant to the audit. For example, TCWG may assist the auditor in understanding the entity and its environment, and TCWG in fulfilling their responsibility to oversee the financial reporting process, thereby reducing the risks of material misstatement of the financial statements. <p>Although the auditor is responsible for communicating matters required by this SA, management also has a responsibility to communicate matters of governance interest to those charged with governance. Communication by the auditor does not relieve management of this responsibility.</p> <p>Similarly, communication by management with TCWG of matters that the auditor is required to communicate does not relieve the auditor of the responsibility to also communicate them. Communication of these matters by management may, however, affect the form or timing of the auditor's communication with those charged with governance.</p> <p>Clear communication of specific matters required to be communicated by SAs is an integral part of every audit. SAs do not, however, require the auditor to perform procedures specifically to identify any other matters to communicate with those charged with governance.</p>
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	Law or regulation may restrict the auditor's communication of certain matters with those charged with governance. For example, laws or regulations may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act.
Objectives	<p>The objectives of the auditor are:</p> <ol style="list-style-type: none"> To communicate clearly with TCWG the responsibilities of the auditor in relation to the financial statement audit, and an overview of the planned scope and timing of the audit; To obtain from TCWG information relevant to the audit; To provide TCWG with timely observations arising from the audit that are significant and relevant to their responsibility to oversee the financial reporting process; and To promote effective two-way communication between the auditor and TCWG
MATTERS TO BE COMMUNICATED	
The auditor's responsibilities in relation to the financial statement audit	<ol style="list-style-type: none"> 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 The audit of the financial statements does not relieve management or TCWG of their responsibilities.
The auditor's responsibilities in relation to the financial statement audit	The auditor shall communicate with TCWG an overview of the planned scope and timing of the audit, which includes communicating about the significant risks identified by the auditor.
Significant findings from the audit auditor independence	<p>The auditor shall communicate with those charged with governance:</p> <p>(a) The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures. When applicable, the auditor shall explain to TCWG why the auditor considers a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be most appropriate to the particular circumstances of the entity;</p> <p>(b) Significant difficulties encountered during the audit may include such matters as:</p> <ul style="list-style-type: none"> Significant delays by management, the unavailability of entity personnel, or unwillingness by management to provide information necessary for the auditor to perform the auditor's procedures. An unreasonably brief time within which to complete the audit. Extensive unexpected effort required to obtain sufficient appropriate audit evidence. The unavailability of expected information. Restrictions imposed on the auditor by management. Management's unwillingness to make or extend its assessment of the entity's ability to continue as a going concern when requested. In some circumstances, such difficulties may constitute a scope limitation that leads to a modification of the auditor's opinion.) <p>(c) Significant Matters Discussed, or Subject to Correspondence with Management.</p> <p>(d) Unless all of TCWG are involved in managing the entity:</p> <ul style="list-style-type: none"> Significant matters arising during the audit that were discussed, or subject to correspondence, with management; and Written representations the auditor is requesting;



	<p>(e) Circumstances that affect the form & content of the auditor's report, if any;&</p> <p>(f) Any other significant matters arising during the audit that, in the auditor's professional judgment, are relevant to the oversight of the financial reporting process.</p>
Auditor independence	<p>In the case of listed entities, the auditor shall communicate with TCWG, a statement that the engagement team and others in the firm, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence; and</p> <ul style="list-style-type: none"> • All relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgment, may reasonably be thought to bear on independence. This shall include total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity; and • The related safeguards that have been applied to eliminate identified threats to independence or reduce them to a acceptable level.

THE COMMUNICATION PROCESS

Establishing the communication process	The auditor shall communicate with TCWG the form, timing and expected general content of communications.
Forms of communication	The auditor shall communicate in writing with TCWG regarding significant findings from the audit if, in the auditor's professional judgment, oral communication would not be adequate. Written communications need not include all matters that arose during the course of the audit. The auditor shall communicate in writing with TCWG regarding auditor independence when required.
Timing of communications	The auditor shall communicate with TCWG on a timely basis.
Adequacy of the communication process	The auditor shall evaluate whether the two-way communication between the auditor and TCWG has been adequate for the purpose of the audit. If it has not, the auditor shall evaluate the effect, if any, on the auditor's assessment of the risks of material misstatement and ability to obtain sufficient appropriate audit evidence, and shall take appropriate action.
Documentation	<p>Where matters required by this SA to be communicated are communicated orally, the auditor shall include them in the audit documentation, and when and to whom they were communicated. Where matters have been communicated in writing, the auditor shall retain a copy of the communication.</p> <p>Various factors affecting mode of communication are:</p> <ul style="list-style-type: none"> ➤ Whether a discussion of the matter will be included in the auditor's report e.g.KAM. ➤ Whether management has previously communicated the matter. ➤ The size, operating structure, control environment, and legal structure of the entity. ➤ In the case of an audit of special purpose F.S., whether the auditor also audits the entity's general purpose F.S. ➤ Legal requirements. In some jurisdictions, a written communication with TCWG is required in a prescribed form by local law. ➤ The expectations of TCWG, including arrangements made for periodic meetings or communications with the auditor. ➤ The amount of ongoing contact and dialogue the auditor has with TCWG. ➤ Whether there have been significant changes in the membership of a governing body.



Consideration of SA-701 which is applicable

SA 701 deals with the auditor's responsibility to communicate key audit matters in the auditor's report. That SA acknowledges that, when SA 701 applies, matters communicated to TCWG may be determined to be key audit matters, requiring inclusion in the audit report in accordance with SA 701.

SA - 299 JOINT AUDIT OF FINANCIAL STATEMENTS

INTRODUCTION

Objectives	<p>The objectives of this Standard are:</p> <ul style="list-style-type: none">a. To lay down broad principles for the joint auditors in conducting the joint audit.b. To provide a uniform approach to the process of joint audit.c. To identify the distinct areas of work and coverage thereof by each joint auditor.d. To identify individual responsibility and joint responsibility of the joint auditors in relation to audit.
Advantages of Joint Audit	<p>The practice of appointing Chartered Accountants as joint auditors is quite widespread in big companies and corporations. Joint audit basically implies pooling together the resources and expertise of more than one firm of auditors to render an expert job in a given time period which may be difficult to accomplish acting individually. It essentially involves sharing of the total work. This is by itself a great advantage. In specific terms the advantages that flow may be the following:</p> <ul style="list-style-type: none">a. Sharing of expertise.b. Advantage of mutual consultation.c. Lower workload.d. Better quality of performance.e. Improved service to the client.f. Displacement of the auditor of the company taken over in a takeover often obviated.g. In respect of multi-national companies, the work can be spread using the expertise of the local firms which are in a better position to deal with detailed work and the local laws and regulations.h. Lower staff development costs.i. Lower costs to carry out the work.j. A sense of healthy competition towards a better performance
Definition of 'Joint Audit' and 'Joint Auditors'	<p>A joint audit is an audit of financial statements of an entity by two or more auditors appointed with the objective of issuing the audit report. Such auditors are described as joint auditors.</p>
Requirements	
Audit Planning, Risk Assessment and Allocation of Work	<p>The engagement partner and other key members of the engagement team from each of the joint auditors shall be involved in planning the audit. The joint auditors shall jointly establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan.</p> <p>Prior to the commencement of the audit, the joint auditors shall discuss and develop a joint audit plan. In developing the joint audit plan, the joint auditors shall:</p> <ul style="list-style-type: none">a. Identify division of audit areas and common audit areas amongst the joint auditors that define the scope of the work of each joint auditor;b. Ascertain the reporting objectives of the engagement to plan the timing of the audit and the



	<p>nature of the communications required;</p> <ol style="list-style-type: none"> Consider and communicate among all joint auditors the factors that, in their professional judgment, are significant in directing the engagement team's efforts; Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other or similar engagements performed earlier by the respective engagement partner(s) for the entity is relevant. Ascertain the nature, timing and extent of resources necessary to perform the engagement. <p>Where joint auditors are appointed, they should, by mutual discussion, divide the audit work among themselves. The division of work would usually be in terms of audit of identifiable units or specified areas. In some cases, due to the nature of the business of the entity under audit, such a division of work may not be possible. In such situations, the division of work may be with reference to items of assets or liabilities or income or expenditure. Certain areas of work, owing to their importance or owing to the nature of the work involved, would often not be divided and would be covered by all the joint auditors.</p> <p>At this stage, risks of material misstatement need to be considered and assessed by each of the joint auditors and shall be communicated to other joint auditors, and documented, whether pertaining to the overall financial statements level or to the area of allocation among the other joint auditors.</p> <p>The joint auditors shall discuss and document the NTE of the audit procedures for common and specific allotted areas of audit to be performed by each of the joint auditors and the same shall be communicated to those charged with governance.</p> <p>The joint auditors shall obtain common engagement letter and common management representation letter.</p> <p>After identification and allocation of work among the joint auditors, the work allocation document shall be signed by all the joint auditors and the same shall be communicated to those charged with governance of the entity.</p>
<p>Responsibility and Co-ordination among Joint Auditors</p>	<p>In respect of audit work divided among the joint auditors, each joint auditor shall be responsible only for the work allocated to such joint auditor including proper execution of the audit procedures.</p> <p>All the joint auditors shall be jointly and severally responsible for :</p> <ol style="list-style-type: none"> The audit work which is not divided among the joint auditors and is carried out by all joint auditors; Decisions taken by all the joint auditors under audit planning in respect of common audit areas concerning the nature, timing and extent of the audit procedures to be performed by each of the joint auditors. Matters which are brought to the notice of the joint auditors by any one of them and on which there is an agreement among the joint auditors; Examining that the financial statements of the entity comply with the requirements of the relevant statutes; Presentation and disclosure of the financial statements as required by the applicable financial reporting framework; Ensuring that the audit report complies with the requirements of the relevant statutes, the applicable Standards on Auditing and the other relevant pronouncements issued by ICAI. <p>Where, in the course of the audit, a joint auditor comes across matters which are relevant to the areas of responsibility of other joint auditors and which deserve their attention, or which require disclosure or require discussion with, or application of judgment by other joint auditors, the said joint auditor shall communicate the same to all the other joint auditors in writing prior to the completion of the audit.</p> <p>It shall be the responsibility of each joint auditor to determine the nature, timing and extent of audit procedures to be applied in relation to the areas of work allocated to said joint auditor. It is the individual responsibility of each joint auditor to study and evaluate</p>



	the prevailing system of internal control and assessment of risk relating to the areas of work allocated to said joint auditor.
Audit Conclusion and Reporting	<p>The joint auditors are required to issue common audit report, however, where the joint auditors are in disagreement with regard to the opinion or any matters to be covered by the audit report, they shall express their opinion in a separate audit report.</p> <p>A joint auditor is not bound by the views of the majority of the joint auditors regarding the opinion or matters to be covered in the audit report and shall express opinion formed by the said joint auditor in separate audit report in case of disagreement. In such circumstances, the audit report(s) issued by the joint auditor(s) shall make a reference to the separate audit report(s) issued by the other joint auditor(s).</p> <p>Further, separate audit report shall also make reference to the audit report issued by other joint auditors. Such reference shall be made under the heading "Other Matter Paragraph" as per Revised SA 706, "Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report".</p> <p>Each joint auditor is entitled to assume that:</p> <ol style="list-style-type: none"> The other joint auditors have carried out their part of the audit work and the work has actually been performed in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. It is not necessary for a joint auditor to review the work performed by other joint auditors or perform any tests in order to ascertain whether the work has actually been performed in such a manner. The other joint auditors have brought to said joint auditor's notice any departure from applicable financial reporting framework or significant observations that are relevant to their responsibilities noticed in the course of the audit. <p>Where financial statements of a division/branch are audited by one of the joint auditors, the other joint auditors are entitled to proceed on the basis that such financial statements comply with all the legal and regulatory requirements and present a true and fair view of the state of affairs and of the results of operations of the division/branch concerned.</p> <p>Before finalizing their audit report, the joint auditors shall discuss and communicate with each other their respective conclusions that would form the content of the audit report.</p>
Communication with Those Charged with Governance	<p>When the joint auditors expect to modify the opinion in the auditor's report, the joint auditors shall communicate with those charged with governance the circumstances that led to the expected modification and the proposed wording of the modification to ensure compliance with Revised SA 705, "Modifications to the Opinion in the Independent Auditor's Report".</p> <p>If the joint auditors expect to include an Emphasis of Matter or an Other Matter paragraph in the auditor's report, the joint auditors shall communicate with those charged with governance regarding this expectation and the proposed wording of this paragraph to ensure compliance with Revised SA 706, "Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report".</p>



STUDENT NOTES

