SEP 25 / JAN 26

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Let me tell you a kutty story...

CA INTERMEDIATE

AUDITING & ETHICS

CONCEPT BOOK

CA CPA Nivedha Shankar

DO IT

FOR YOUR FUTURE SELF

PREFACE

Dear Readers,

I extend my heartfelt gratitude to each of you for choosing this material as a part of your preparation journey. With utmost dedication, I've endeavoured to distill complex subject matter into concise notes, tailored to facilitate easy comprehension and swift revision, particularly on the previous day of examinations.

"**Where numbers speak louder than words - Welcome to the CA classroom**." It's a place where discipline meets determination, and where students learn not just to pass exams, but to uphold integrity, accuracy, and excellence in every calculation they make."

It's imperative to acknowledge that this material draws inspiration ONLY from the Study material issued by ICAI. I strongly recommend watching classes before reading into the text, as they provide depth to the topics covered herein.

Audit can seem overwhelming due to its vastness and theoretical nature. However, this material simplifies it for you. By breaking down complex concepts, it aims to make audit easier to understand and remember. With this resource, you'll gain confidence and clarity to tackle any audit-related challenge.

Furthermore, mastering audit isn't just for exams—it's essential for your career as a Chartered Accountant. As future auditors, what you learn here will directly apply to your role in ensuring financial integrity in businesses. So, studying audit isn't just about passing exams; it is It's imperative to acknowledge that this material draws inspiration ONLY from the Study material issued by ICAI. I strongly recommend watching classes before reading into the text, as they provide depth to the topics covered herein.

about preparing for your future as a trusted professional.

I extend my sincerest wishes to all aspirants embarking on this journey. May your diligence and dedication pave the way for success.

Warm regards,

CA Nivedha Shankar

EDITION -V3.0 IN THE MONTH MARCH, 2025

ACKNOWLEDGEMENT

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I would also like to Thank my Family members Mr. Sankaranarayanan, Mrs. Radha, Mr. Balasubramanian (Late), Mrs. Jayalakshmi, Mr. Shankar, Mrs. Gomathi Shankar, Mr. Karthik Manikonda, Mrs Vasantha Rani, Mr Rajesh Babu, Mrs Bharathi, Mr Ramesh Babu, and Master Rishen Dheera for their continuous support which helped me overcome challenges and strive for excellence.

I would also like to thank Keerthi sree Challah, Varun Teja who have helped in giving valuable suggestions to bring the material to its current standing.

Regards,

CA Nivedha Shankar

Important Note for Those appearing in 2024 CA inter exams

This material comprises concise notes designed to aid your understanding of the subject. In addition to these notes, summaries will be provided during class sessions. I highly recommend integrating both resources into your study routine, along with the question booklet provided, to ensure comprehensive preparation. By assimilating all three components together, you will gain a holistic understanding of the subject matter, equipping you with the knowledge and skills necessary for success in your examinations.

For any doubts call or WhatsApp faculty on +91 9884 413960.

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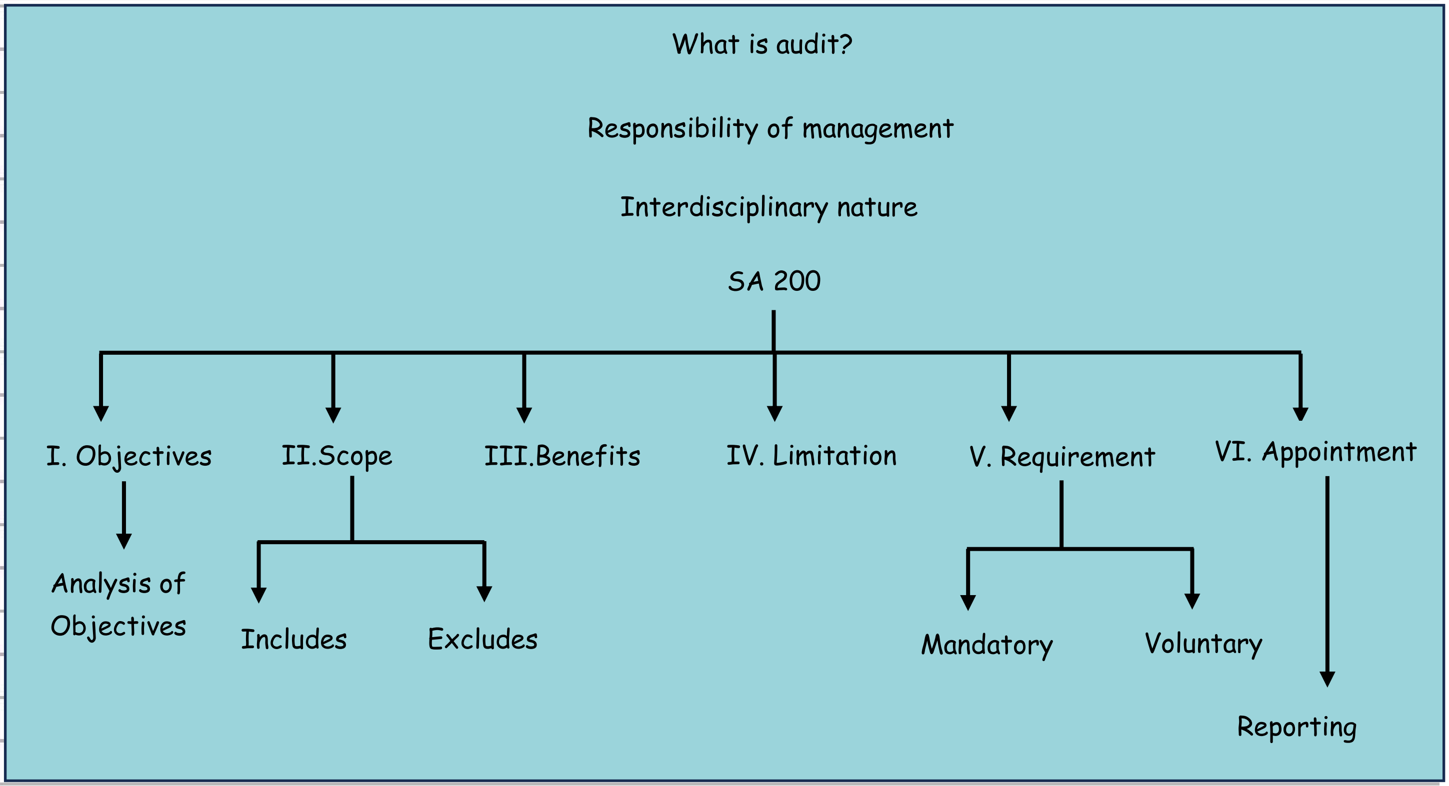
NATURE OBJECTIVE & SCOPE OF AUDIT



What is Audit?

"An audit is an **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".

In doing so, he has to see that the **financial statements would not mislead anybody by ensuring** that: *[Q: How auditor ensures that the FS doesn't mislead?]*

a) The accounts have been drawn up with **reference to entries in the books of accounts.**

b) The entries in the BoA are adequately supported by sufficient and appropriate **evidence**.

c) None of the entries in the BoA have been **omitted** in the process of compilation.

d) The information conveyed by the statement is **clear and unambiguous.**

e) The Financial Statement amounts are properly **classified, described, and disclosed** in conformity with accounting standards.

f) The statement of accounts present a **true and fair picture** of the operational results and of the assets and liabilities.

Responsibility of Management of Entity: Preparation & presentation of Financial Statements. The Auditor expresses an opinion on Financial Statement by means of written Audit Report.

Interdisciplinary nature of auditing- Relationship with diverse subjects

Accounting	Auditing reviews the FS which is nothing but a result of the overall accounting process.
Law	An auditor should have a good knowledge of business laws affecting the entity
Economics	Auditor is required to be familiar with the overall economic environment of the client
Behavioural Science	Knowledge of human behaviour is essential for an auditor to effectively discharge his duties
Statistics & Mathematics	Auditor is also expected to have the knowledge of statistical sampling for meaningful conclusions and mathematics for verification of inventories
Data Processing	EDP Auditing in itself is developing as a discipline in itself.
Financial Management	Auditor is expected to have various knowledge about various financial techniques, funds flow, ratio analysis, capital budgetting etc
Production	Good auditor is one who understands the client and his business functions such as production, cost system, marketting etc.

SA 200: "Overall Objectives of the Independent Auditor and the conduct of an audit in accordance with the standards on auditing"

I. OBJECTIVES

a) To obtain **reasonable assurance** about whether the Financial Statements (FS) 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 FS are prepared, in all material aspects, **in accordance** with an **Applicable Financial Reporting Framework (AFRF)**, and

b) **To report** on the FS and **communicate** as required by the SAs, in accordance with the auditor's findings.

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ANALYSIS OF THE OBJECTIVES

a) Obtain RA about whether the FS as a whole are free from MM whether due to fraud or error.
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. However, reasonable assurance is not a complete guarantee. Although it is a high-level of assurance but it is not complete assurance.

Audit is carried out by the auditor with professional competence and skills in accordance with SA. Audit procedures are applied in accordance with SAs, audit evidence is obtained and evaluated. On basis of that, conclusions are drawn and opinion is formed. It leads to high level of assurance which is called as RA but it is not absolute assurance.

b) Misstatements in FS can occur due to fraud or error or both. The auditor seeks to obtain RA whether FS as a whole are free from MM caused by fraud or error. He must see effect of misstatements on FS as whole, in totality.

c) Obtaining RA that FS as a whole are free from material misstatements enables the auditor to express an opinion on whether the FS are prepared, in all material respects, in accordance with an AFRF

d) The opinion is reported and communicated in accordance with audit findings through a written report as required by Standards on Auditing.

"Historical financial information" means information expressed in financial terms
- of 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.

Applicable Financial Reporting Framework: A framework adopted in the preparation and presentation of the FS that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation. Eg: In case of companies in India, FRF is provided under Schedule III of Companies Act,2013.

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What is Applicable Financial Reporting Framework for Companies in India?__________________________

II. SCOPE OF AUDIT

Includes:	Does not include:
Coverage of all aspects	Responsibility of Preparation & presentation of FS
Reliability & Sufficiency of Financial information	Duties outside scope of competence (Physical condition of assets, Suitability & life of civil structures)
Proper disclosure of financial information	Expertise in authentication of documents (Genuineness)
Expression of an opinion on FS	Investigation

III. BENEFITS OF AUDIT - WHY IS AUDIT NEEDED?

- 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.
- In case of companies, **shareholders** may or may not be involved in daily affairs of the company. The financial statements are prepared by management consisting of directors. As shareholders are owners of the company, they need an independent mechanism so that financial information is qualitative and reliable.
- An audit acts as a moral check on **employees** from committing frauds for the fear of being discovered by audit.
- Audited financial statements are helpful to **government authorities** for determining tax liabilities.
- 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.
- An audit may also **detect fraud or error** or both.
- An audit **reviews existence and operations** of various **controls** operating in any entity. Hence, it is useful at pointing out deficiencies.

IV. INHERENT LIMITATIONS OF AUDIT

The auditor is not expected to, and cannot, reduce audit risk to zero because there are inherent limitations of an audit. The inherent limitations of an audit arise from:

i) **The Nature of Financial Reporting:** The preparation of financial statements involves judgment 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.

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Management acknowledges its responsibility of preparation of financial statements in accordance with applicable financial reporting framework and for devising suitable internal controls. However, such controls may not have operated to produce reliable financial information due to their own limitations.

Eg: Management has devised a control that all purchase bills should reflect stamp and signatures of an authorized person in "Goods Receiving Section" of the company stating the date and time of receiving goods in premises. It is an example of internal control devised by the company to ensure that only those purchase bills are produced for payment for which goods have been actually received. Now, what happens if concerned accountant and authorised person in "Goods Receiving Section" collude. It is a case of overriding of internal controls devised by the company due to collusion between two persons. Such a probable collusion is one of limitations of internal controls itself.

ii) **Nature of Audit Procedures:** There are *practical and legal* limitations on ability of auditor to obtain audit evidence.

Practical limitation: 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 as may be requested by auditor. In case he is not provided with required information, he can only report.

iii) **Not in the nature of Investigation:** An audit is **not an official investigation** into alleged wrongdoing

iv) **Timeliness of financial reporting**:

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

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 stint, 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 and that information is not relevant. So, the information being relied upon by auditor is not timely and may have lost its reliability.

v) **Future events**: 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

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V. AUDIT REQUIREMENTS (MANDATORY OR VOLUNTARY)

Audit is **not** mandatory for **ALL**.

Under Law [mandatory] for the following:

a) **Companies** governed by Companies Act, 2013

b) **Banking companies** governed by Banking Regulation Act, 1949

c) Other stat bodies **required by regulators or Specific Act**

d) (Electricity Companies ______, Cooperative Societies ______, Public and Charitable Trust, Corporations set up under an act of Parliament or state legislature ______, Specified entities under various sections of the IT Act ______)

VOLUNTARY AUDITS:

a) Audit of proprietary entities, Partnership firms, HUF etc

b) **Internal rules** may require audit.

c) Sanction of **grants, loans** may require audit.

VI. APPOINTMENT OF AUDITOR

An auditor is appointed by the owners /constitutional /govt authorities in accordance with applicable laws and regulations. The audit report is submitted to the person making the appointment.

Company	Government Company	Firm
• Shareholders in AGM	• CAG	• Partners

BASICS BEFORE SA 210

I. What is Engagement?

II. What is Assurance Engagement?

III. Elements of Assurance Engagements?

IV. Types of Assurance Engagements?

V. Examples of Assurance Engagements?

VI. Prospective Financial Information

VII. Difference between Historical & Prospective Financial Information

VIII. Why are standards needed?

IX. Duties in relation to Engagement & Quality Control standards:

X. Qualities of Auditor

I. WHAT IS 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.

II. WHAT IS ASSURANCE ENGAGEMENT?

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

III.Elements of Assurance engagements:	
Three party Relationship	Practitioner, Responsible party & intended users
An appropriate subject matter	Fi in FS
Suitable criteria	Benchmarks (standards, guidelines, law, rules & regulation)
Sufficient appropriate evidence	Qty & Quality
Written assurance report in appropriate form	Outcome/ conclusion

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IV. TYPES OF ASSURANCE ENGAGEMENTS?

Reasonable Assurance Eng	Limited Assurance Eng
High level of assurance	Lower levels of assurance compared to RAE
Elaborate & extensive procedures to obtain sufficient and appropriate evidence	Fewer procedures as compared to RAE
Draws reasonable conclusions	Draws limited conclusions
Eg. Audit engagement	Eg. Review engagement

Assurance engagements dealing with matters other than historical financial information. Provides only a "Moderate level of assurance". Examination of prospective FI (Like forecast) or assurance regarding operation of controls.

V. EXAMPLES OF ASSURANCE ENGAGEMENTS?

Audit of FS	Reasonable Assurance engagement
Review of FS	Limited Assurance Engagement
Examination of PFI	Provides assurance regrading reasonability of assumptions forming basis of projections
Reports on controls operating at organisation	Provides assurance regarding design & operation of controls

VI. PROSPECTIVE FINANCIAL INFORMATION

Prospective FI means FI based on assumptions about events that may occur in future and possible actions by entity. Can be in form of a forecast or projection or combo of both.

- Practitioner may obtain SAAE to effect that:

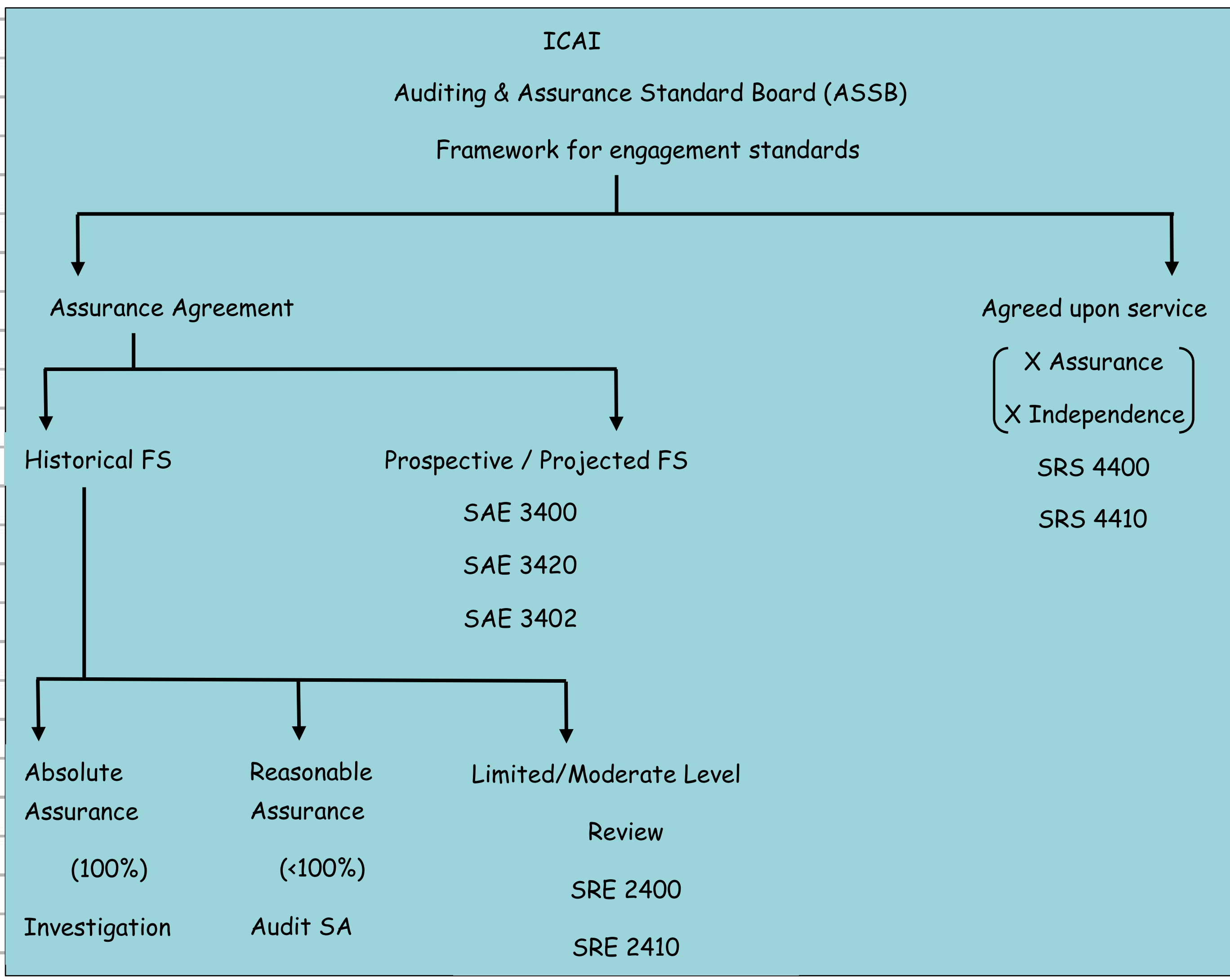
- Management's assumptions on which PFI is based are not unreasonable
- PFI is properly prepared on the basis of assumptions.
- Its properly presented & all material aspects are properly disclosed.

- PFI relates to future events. While evidence may be available to support assumptions on which PFI is based, such evidence is itself generally future oriented.

- Auditor is not in a position to express an opinion as to whether results shown in the PFI will be achieved. Therefore, practitioner provides a report assuring that nothing has come to practitioner's attention to suggest that these assumptions don't provide a reasonable basis for projection.
- Hence such type of assurance engagements provide only a moderate level of assurance

VII. DIFFERENCE BETWEEN HISTORICAL & PROSPECTIVE FINANCIAL INFORMATION

Former relates to information expressed in financial terms of entity about economic events, conditions, or circumstances occurring in past periods.
Latter relates to financial information based on assumptions about future events & possible actions by the entity.
Therefore, historical fi is rooted in past events which have already occurred , and prospective FI is related to future events.



Following standards are collectively known as Engagement standards:-

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 engagement other than audits & review of historical financial information
4. Standards on Related Services (SRS) which apply in agreed upon procedures to info, compilation engagement & other related service engagement.

Purpose of all these standards is to establish high quality standards & guidelines in areas of FS audits and other types of assurance services.

VIII. WHY ARE STANDARDS NEEDED?

1. Standards ensure carrying out of audit against established benchmarks at par with global practices.
2. Standards improve quality of financial reporting thereby helping users to make diligent decisions.
3. Standards promote uniformity as audit of financial statements is carried out following these Standards.
4. Standards equip professional accountants with professional knowledge and skill.
5. Standards ensure audit quality

IX. DUTIES IN RELATION TO ENGAGEMENT & QUALITY CONTROL

1. It is the duty of professional accountants to see that Standards are followed in engagements undertaken by them.
2. However, a situation may arise when a specific procedure as required in Standards would be ineffective in a particular engagement.
3. In such a case, he is required to document how alternative procedures performed achieve the purpose of required procedure.
4. Also, reason for departure has also to be documented unless it is clear. Further, his report should draw attention to such departures.
5. It is also to be noted that a mere disclosure in the report does not absolve a professional accountant from complying with applicable Standards.

X. QUALITIES OF AUDITOR

1. An auditor is concerned with the reporting on financial matters. Financial matters inherently are to be set with the problems of human fallibility; errors and frauds are frequent.
2. Tact, caution, firmness, good temper, integrity, discretion, industry, judgement, patience, clear headedness and reliability are some of qualities which an auditor should have.
3. In short, all those personal qualities that go to make a good businessman contribute to the making of a good auditor.
4. In addition, he must have the shine of culture for attaining a great height.
5. He must have the highest degree of integrity backed by adequate independence.
6. The auditor, who holds a position of trust, must have the basic human qualities apart from the technical requirement of professional training and education.
7. He critically reviews financial statements and it is obviously useless for him to attempt that task unless his own knowledge is that of an expert.
8. 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.

SA210 AGREEING THE TERMS OF AUDIT ENGAGEMENT

SA 210 Agreeing the terms of Audit engagement

- I. Objective
- II. Engagement Letter
- III. Cases
  1. What happens if precondition not present.
  2. Limitation on scope prior to acceptance.
  3. Δ in terms of audit engagement.
  4. Recourse for audit situation of Non-agreement
- IV. Recurring Audit

SA210 deals with the auditor's responsibilities in agreeing the terms of the audit engagement with management, and where appropriate Those Charged With Governance (TCWG).

I. Objective of the Auditor

Accept or continue an audit engagement only when the basis upon which audit is to be performed has been agreed, through:

1. Establishing whether the **preconditions** for an audit are present.
2. Confirming that there is a **common understanding** between the auditor and the management and where appropriate, TCWG of the terms of the audit engagement.

a. For the **preparation in the FS in accordance with Applicable Financial Reporting Framework (AFRF)**

b. For such **Internal Control** as management considers necessary to enable the preparation of FS that are free from Material misstatement, whether due to fraud or error, and

c. To provide the auditor with:

- **Access to all information** of which management is aware that is relevant to the preparation of Financial Statement such as records, documents etc.
- **Additional information** that the auditor may request from the management for the purpose of audit.
- **Unrestricted access to persons** within the entity from whom the auditor determines it necessary to obtain audit evidence.

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II. Engagement Letter

Why? How? What?

It is important for both the auditor and the client, that each party should be **clear about the nature of the engagement.** It must be reduced to **writing** and should exactly specify the **scope** of work.
The agreed terms of the Audit engagement shall be recorded in an audit EL or other suitable form of written agreement.
The Engagement Letter is **sent by the auditor to the client**. It is in the interest of both the auditor and the client to issue an Engagement Letter so that the possibility of misunderstanding is reduced to a great extent.

The **Engagement Letter includes:**

a) The **objective** and scope of the audit of Financial Statement
b) The **responsibilities** of the **auditor**
c) The **responsibilities** of the **management**
d) Identification of the **Applicable Financial Reporting Framework** for the preparation of Financial Statement
e) Reference to the **expected form and content** of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

If law or regulation prescribes in sufficient detail the terms of the audit engagement, the auditor need not record them in written agreement, except for the fact that such law or regulation applies, and that management acknowledges and understands its responsibilities.

III. Cases:

Case (i) What happens if preconditions for an audit are not present?

The auditor shall **discuss the matter with the management. Unless required by law or regulation to do** so **the auditor shall not accept** the proposed audit engagement:

a) If the auditor has determined that **the Financial Reporting Framework to be applied in the Financial Statement is unacceptable.**
b) If the agreement of management is not obtained on matters relating to understanding of responsibilities of the management on **preparation of Financial Statement, Internal Control and providing access to all information and unrestricted access** to persons within the entity.

Case (ii) Limitation on Scope of auditor's work prior to acceptance of Audit engagement

If the auditor believes the limitation will result in the auditor **disclaiming an opinion** on the Financial Statement, the auditor shall not accept a limited engagement.

Case (iii) Acceptance of a change in terms of Audit engagement

The auditor shall not accept where there no **"reasonable justification"** in doing so.

If there is a change in circumstance that is affecting the entity's requirements or a misunderstanding concerning the nature of the service originally requested may be considered a reasonable basis for requesting a change in the audit engagement.

Case (iv) Recourse for the auditor in a situation of non-agreement

to a change in terms of engagement and lack of permission from management to continue the original audit engagement.

a) Withdraw from the audit engagement.

b) Determine whether there is any obligation, either contractual or otherwise to report to owners, Those Charged With Governance or regulators.

IV. Terms of Engagement in Recurring Audit

Recurring audit is an audit which is performed by an auditor **over years.**

On recurring audits, the auditor shall assess whether the circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms of the audit engagement.

However, the following factors may make it appropriate to revise the terms of the audit engagement or to remind the entity of the existing terms:

a) Any **indication that the entity misunderstands the objective and scope** of audit.

b) Any **revised or special terms** of audit engagement

c) A recent **change of senior management**

d) A Significant **change in ownership**

e) A significant **change in nature or size of the entity's business**

f) A **change in legal or regulatory requirements**

g) A **change in the Financial Reporting Framework** adopted in the preparation of Financial Statement.

h) A **change in other reporting requirements**

SA 700 FORMING AN OPINION AND REPORTING ON FINANCIAL STATEMENTS

SA 700

- I. OBJECTIVE
- II. UNMODIFIED OPINION
- III. TO FORM OPINION – AUDITOR TO OBTAIN REASONABLE ASSURANCE
- IV. ELEMENTS / CONTENTS OF AUDIT

I. OBJECTIVE

To form an opinion on the FS based on an evaluation of the conclusions drawn from the AE obtained; and

To express clearly that opinion through a written report.;

II. UNMODIFIED OPINION

The auditor shall express an unmodified opinion when the auditor concludes that the FS are prepared, in all material respects, in accordance with the AFRF.

III. TO FORM OPINION – AUDITOR TO OBTAIN REASONABLE ASSURANCE

The auditor shall form an opinion on whether the FS are prepared, in all material respects, in accordance with the AFRF.

In order to form that opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance about whether the FS as a whole are free from MM, whether due to fraud or error.

That conclusion shall take into account:

(a) Whether sufficient appropriate AE has been obtained;

(b) Whether uncorrected misstatements are material, individually or in aggregate;

(c) The **evaluations**.

- Evaluations of qualitative aspects of the Accounting Practices
- Specific Evaluations by the Auditor

Further, when the FS are prepared in accordance with a fair presentation framework, the evaluation mentioned above shall also include an evaluation by the auditor as to whether the FS achieve fair presentation which shall include consideration of

- The overall presentation, structure and content of the FS; and
- Whether the FS, including the related notes, represent the underlying transactions and events in a manner that achieves fair presentation.

Qualitative Aspects	Specific Evaluations
judgements about the amounts and disclosures	Selected and applied significant accounting policies are adequately disclosed. & are consistent with AFRF.
possible bias in management's judgements	Accounting estimates by management are reasonable.
Indicators of a lack of neutrality • The selective correction of misstatements brought to management's attention • Possible management bias in the making of accounting estimates.	Information in FS is relevant, reliable, comparable and understandable.
Example for selective correction: Correcting misstatements with the effect of increasing reported earnings, but not correcting misstatements that have the effect of decreasing reported earnings.	Disclosures in FS are adequate to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements.
SA 260 (Revised) & SA 540	Terminology used in FS is appropriate.

IV. ELEMENTS / CONTENTS OF AUDIT REPORT

1. A title
2. An addressee
3. Opinion paragraph
4. Basis for opinion
5. Material uncertainty related to Going Concern (570)
6. Key Audit Matters (701)
7. Other Information
8. Responsibilities for the FS (by Management)
9. Auditor's Responsibilities for the audit of FS
10. Location of the description
11. Other reporting responsibilities
12. Signature of the auditor
13. Place of Signature
14. Date of Audit report
15. UDIN

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1. Title:

The AR shall have a title that clearly indicates that it is the report of an independent auditor.
For example, "Independent Auditor's Report,".

2. Addressee:

- The AR shall be addressed, as appropriate, based on the circumstances of the engagement.
- Law, regulation or the terms of the engagement may specify to whom the AR is to be addressed.
- The AR is normally addressed to those for whom the report is prepared, often either to the shareholders or to TCWG of the entity whose FS are being audited.
- In case of a company, the report is addressed to the shareholders of the company.

3. Auditor's Opinion:

The first section of the auditor's report shall include the auditor's opinion, and shall have the heading "Opinion."
The Opinion section of the auditor's report shall also:

- Identify the entity whose financial statements have been audited
- State that the financial statements have been audited;
- Identify the title of each statement comprising the financial statements;
- Refer to the notes, including the summary of significant accounting policies; and
- Specify the date of, or period covered by, each financial statement comprising the financial statements

When expressing an unmodified opinion on FS the auditor's opinion shall, unless otherwise required by law or regulation, use one of the following phrases, which are regarded as being equivalent:

a) In our opinion, the accompanying FS present fairly, in all material respects, [...] in accordance with [the AFRF]; or

b) In our opinion, the accompanying FS give a true and fair view of [...] in accordance with [the AFRF].

The phrases "present fairly, in all material respects," and "give a true and fair view" are regarded as being equivalent.
Not appropriate to use phrases such as "with the foregoing explanation" or "subject to" in relation to the Opinion.

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4. Basis for Opinion:

The AR shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that:

- States that the audit was conducted in accordance with SAs;
- Refers to the section of the AR that describes the auditor's responsibilities under the SAs;
- Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements.
- States whether the auditor believes that the AE the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's opinion.

5. Going Concern:

Where applicable, the auditor shall report in accordance with SA 570 (Revised).

- The FS are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future.
- When the use of the going concern basis of accounting is appropriate, assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business.
- The auditor shall evaluate whether SAAE has been obtained regarding, and shall conclude on, the appropriateness of management's use of the going concern basis.
- Whether any material uncertainty exists, relating to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.
- The likelihood of occurrence of material uncertainty (probability) - Appropriate disclosure of the nature and implications of the uncertainty is necessary for:
  - Fair presentation financial reporting framework - the fair presentation of the financial statements, or
  - Compliance framework - the financial statements not to be misleading.

6. Key Audit Matters:

Law or regulation may require communication of key audit matters for audits of entities other than listed entities.

Example

Entities characterized in such law or regulation as public interest entities. The auditor may also decide to communicate key audit matters for other entities for public interest such as banks, insurance companies, and pension funds, and other entities such as charitable institutions.

7. Other Information:

Where applicable, the auditor shall report in accordance with SA 720 (Revised).

8. Responsibilities for the Financial Statements:

The AR shall include a section with a heading "Responsibilities of Management for the Financial Statements."

This section of the auditor's report shall describe management's responsibility for:

- Preparing the FS in accordance with the AFRF, and for such IC as management determines is necessary to enable the preparation of FS that are free from MM, whether due to fraud or error.
- Assessing the entity's ability to continue as a GC and whether the use of the GC basis of accounting is appropriate as well as disclosing, if applicable, matters relating to GC.

Oversight of the financial reporting process:

This section of the auditor's report shall also identify those responsible for the oversight of the financial reporting process, when those responsible for such oversight are different from Management. In this case, the heading of this section shall also refer to "Those Charged with Governance" or such term that is appropriate in the context of the legal framework applicable to the entity.

9. Auditor's Responsibilities for the Audit of the Financial Statements:

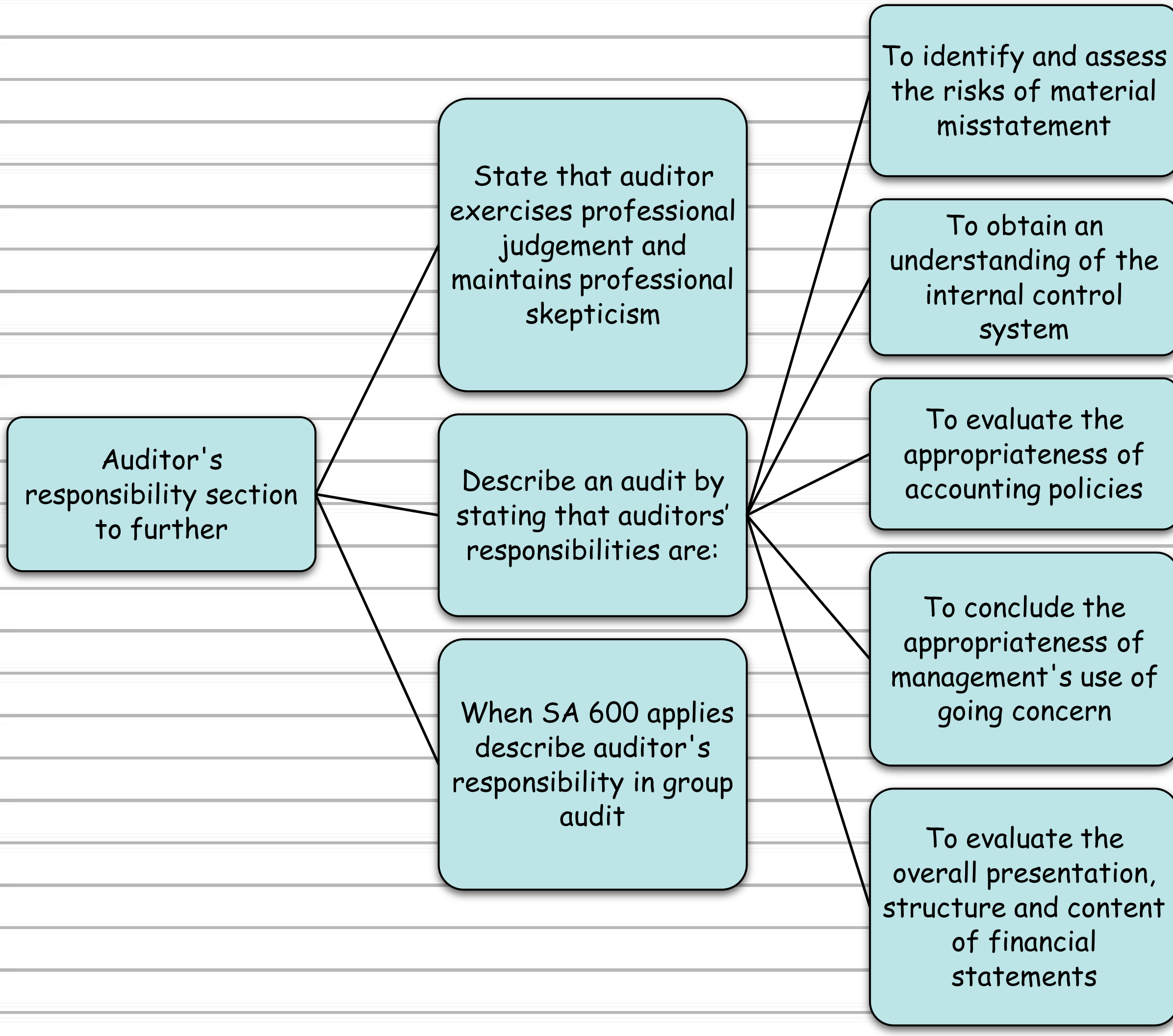
The auditor's report shall include a section with the heading "Auditor's Responsibilities for the Audit of the Financial Statements."

Auditors responsibility section to state

- Objectives of the auditor
- That reasonable level of assurance is high level of assurance and not guarantee
- That misstatements can arise from fraud and error

The Auditor's Responsibilities for the Audit of the Financial Statements section of the auditor's report also shall:

- State that the auditor communicates with TCWG regarding, the planned scope, timing of the audit and significant audit findings, including any significant deficiencies in IC
- For listed entities, state that the auditor provides a statement to TCWG that the auditor has complied with relevant ethical requirements regarding independence
- Where KAM is communicated in accordance with SA 701 (Listed / Other Entities), state that, from the matters communicated with TCWG, the matters were of most significant in the current period and are therefore the key audit matters.



10. Location of the description of the auditor's responsibilities for the audit of the financial statements:

The description of the auditor's responsibilities for the audit of the FS shall be included:

- Within the body of the AR
- Within an appendix to the AR, in which case the AR shall include a reference to the location of the appendix or
- By a specific reference within the AR to the location of such a description on a website of an appropriate authority, where law, regulation or national auditing standards expressly permit the auditor to do so

11. Other Reporting Responsibilities:

- If the auditor addresses other reporting responsibilities in the auditor's report on the financial statements that are in addition to the auditor's responsibilities under the SAs, these other reporting responsibilities shall be addressed in a separate section in the auditor's report with a heading titled.

"Report on Other Legal and Regulatory Requirements" or otherwise as appropriate to the content of the section, unless these other reporting responsibilities address the same topics as those presented under the reporting responsibilities required by the SAs in which case the other reporting responsibilities may be presented in the same section as the related report elements required by the SAs.

- If other reporting responsibilities are presented in the same section as the related report elements required by the SAs, the AR shall clearly differentiate the other reporting responsibilities from the reporting that is required by the SAs.

- If the AR contains a separate section that addresses other reporting responsibilities, the requirements stated above shall be included under a section with a heading "Report on the Audit of the Financial Statements." The "Report on Other Legal and Regulatory Requirements" shall follow the "Report on the Audit of the Financial Statements."

12. Signature of the Auditor:

- The partner/proprietor signing the AR also needs to mention the membership number assigned by the ICAI.
- They also include the registration number of the firm, wherever applicable, as allotted by ICAI, in the audit reports signed by them.

13. Place of Signature:

The auditor's report shall name specific location, which is ordinarily the city where the audit report is signed.

14. Date of the Auditor's Report:

The AR shall be dated no earlier than the date on which the auditor has obtained SAAE on which to base the auditor's opinion on the FS, including evidence that:

- All the statements that comprise the FS, including the related notes, have been prepared; and
- Those with the recognized authority have asserted that they have taken responsibility for those FS

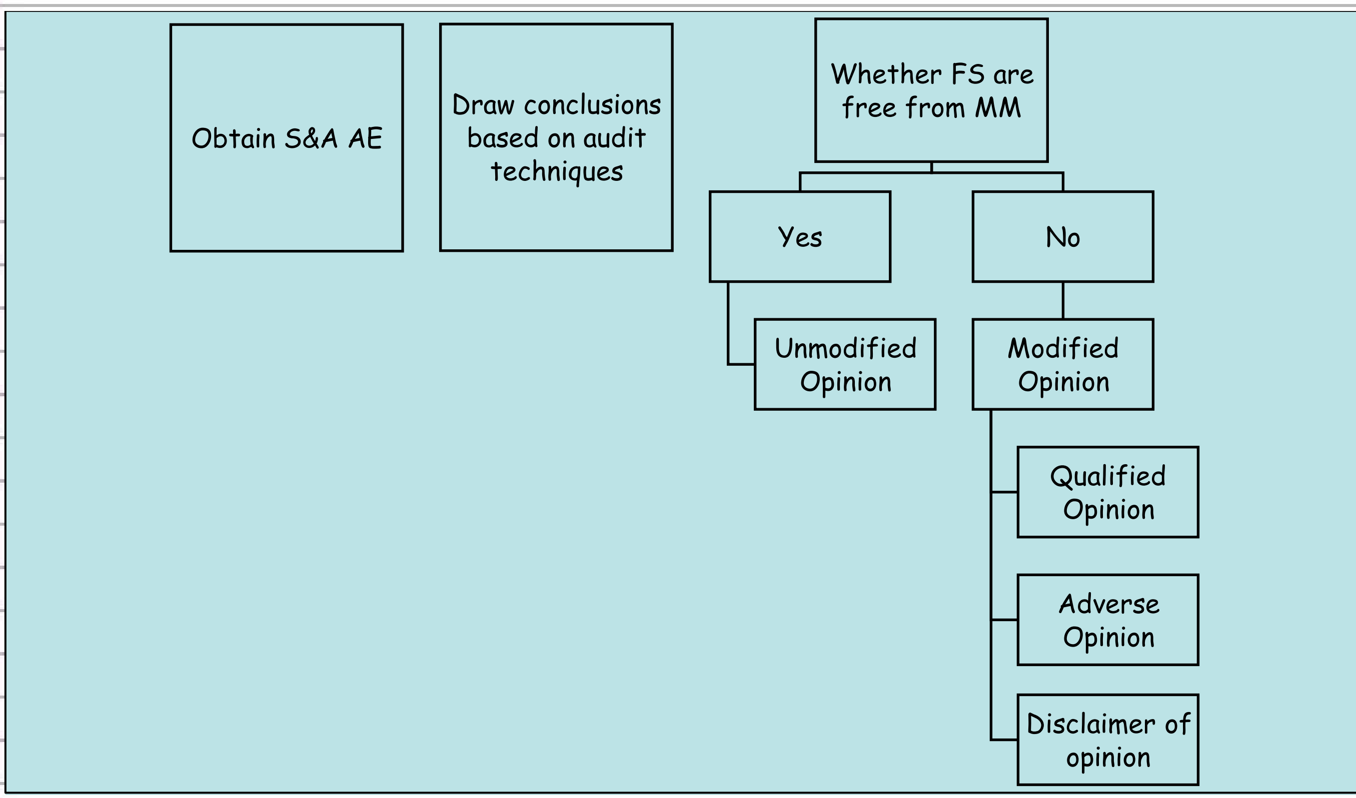
The date of the AR informs the user of the AR that the auditor has considered the effect of events and transactions of which the auditor became aware and that occurred up to that date.
The auditor's responsibility for events and transactions after the date of the auditor's report is addressed in SA 560.

15. UDIN

The 18-digit alpha numeric number at end of AR is Unique Document Identification number (UDIN).

- It is a system generated unique number.
- Its basic objective is to curb the malpractices of non-CAs impersonating themselves as CAs.
- It helps in securing reports and documents issued by practising CAs.

Accordingly, an auditor is required to mention the UDIN with respect to each audit report being signed by him, along with his membership number while signing an audit report.



Hello Nanbas & Nanbis

SA 701

SA 701

- I. KEY AUDIT MATTERS??
- II. DEFINITIONS
- III. OBJECTIVE
- IV. APPLICABILITY
- V. HOW TO DETERMINE KAM?
- VI. COMMUNICATING KAM
- VII. COMMUNICATING KAM- NOT A SUBSTITUTE FOR DISCLOSURE IN THE FS
- VIII. KAM WILL NOT BE COMMUNICATED IF
- IX. COMMUNICATION WITH TCWG

I. KEY AUDIT MATTERS??

The auditor may also decide to communicate KAM for other entities, including those that may be of significant public interest, for example because they have a large number and wide range of stakeholders and considering the nature and size of the business.

II. DEFINITIONS

Key Audit Matters are those matters that, in the auditor's professional judgement

were of most significance in the audit of the financial statements of the current period.

Key audit matters are selected from matters communicated with those charged with governance.

III. OBJECTIVE OF 701?

As per SA 701, "Communicating Key Audit Matters in The Independent Auditor's Report", the objectives of the auditor are to determine key audit matters and, having formed an opinion on the FS, communicate those matters by describing them in the AR.

IV. APPLICABILITY

This SA applies to audits of complete sets of general-purpose financial statements of:

- Listed entities and
- Circumstances when the auditor otherwise decides to communicate key audit matters in the auditor's report and
- Required by law or regulation to communicate key audit matters in the auditor's report

However, SA 705 (Revised) prohibits the auditor from communicating KAM when the auditor disclaims an opinion on the FS, unless such reporting is required by law or regulation

V. HOW TO DETERMINE KAM?

The auditor shall determine, from the matters communicated with TCWG, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall take into account the following:

a) Areas of higher assessed ROMM or significant risks identified in accordance with SA315
b) Significant auditor judgements relating to areas in the FS that involved significant management judgement, including accounting estimate that have been identified as having high estimation uncertainty
c) The effect on the audit of significant events or transactions that occurred during the period.

VI. COMMUNICATING KAM

The auditor shall describe each KAM, using an appropriate subheading, in a separate section of the auditor's report under the heading "Key Audit Matters". The introductory language in this section of the auditor's report shall state that:

- Key audit matters are those that, in the auditor's professional judgement, were of most significance in the audit of financial statements (of the current period); and
- These matters were addressed in the context of the audit of the FS as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters.

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VII. COMMUNICATING KAM- NOT A SUBSTITUTE FOR DISCLOSURE IN THE FS

Communicating Key audit matters is not a substitute for

- A substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation
- A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705 (Revised);
- A substitute for reporting in accordance with SA 570 when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern; or
- A separate opinion on individual matters.

VIII. KAM will not be communicated if

- Laws and regulations prohibit
- Possible adverse consequences
- Highly confidential

IX. COMMUNICATION WITH TCWG

The auditor shall communicate with TCWG:

a) Those matters the auditor has determined to be the KAM; or

b) If applicable, depending on the facts and circumstances of the entity and the audit, the auditor's determination that there are no KAM to communicate in the auditor's report.

Example

The following illustrates the presentation in the auditor's report if the auditor has determined there are no key audit matters to communicate:

- Key Audit Matters:

Except for the matter described in the Basis for Qualified (Adverse) Opinion section or Material Uncertainty Related to Going Concern section,] We have determined that there are no [other] key audit matters to communicate in our report.

SA 705 - MODIFICATIONS TO THE OPINION IN THE INDEPENDENT AUDITOR'S REPORT

SA 705

- I. SCOPE
- II. OBJECTIVE
- III. TYPES OF MODIFIED OPINION AS PER SA 705

- IV. WHICH TYPE OF OPINION IS APPROPRIATE?
- V. INABILITY TO OBTAIN SAAE - MGT LIMITATION

- VI. FORM AND CONTENT OF THE AR FOR MODIFIED OPINION
  - QUALIFIED OPINION
  - ADVERSE OPINION
  - DISCLAIMER OF OPINION
- VII. BASIS FOR OPINION (8 CASES)

- VIII. UDITOR'S RESPONSIBILITIES WHEN THE AUDITOR DISCLAIMS
- X. COMMUNICATION WITH TCWG

I. SCOPE

- This SA deals with the auditor's responsibility to issue an appropriate report in circumstances when, in forming an opinion in accordance with SA700 (revised), the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary.
- This SA also deals with how the form and context of the auditor's report is affected when the auditor expresses a modified opinion.

II. OBJECTIVE

The objective of the auditor is to express clearly an appropriately modified opinion on the financial statement that is necessary when:

- The auditor concludes, **based on the audit evidence obtained**, that the financial statements as a whole are not free from material misstatement; or
- The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

III. TYPES OF MODIFIED OPINION AS PER SA 705

1. **Qualified Opinion,**
2. **Adverse Opinion and**
3. **Disclaimer of Opinion**

QUALIFIED OPINION

The auditor shall express a qualified opinion when:

- The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or
- The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.

ADVERSE OPINION

The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

DISCLAIMER OF OPINION

The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

- TYPES OF OPINION
  - Unmodified Opinion SA 700
  - Modified Opinion SA 705
    - Qualified Opinion
    - Adverse Opinion
    - Disclaimer of opinion

PERVASIVE DEFINITION:

A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence.

Pervasive effects on the financial statements are those that, in the auditor's judgement:

i. Are not confined to specific elements, accounts or items of the financial statements;
ii. If so confined, represent or could represent a substantial proportion of the financial statements; or
iii. In relation to disclosures, are fundamental to users' understanding of the financial statements.

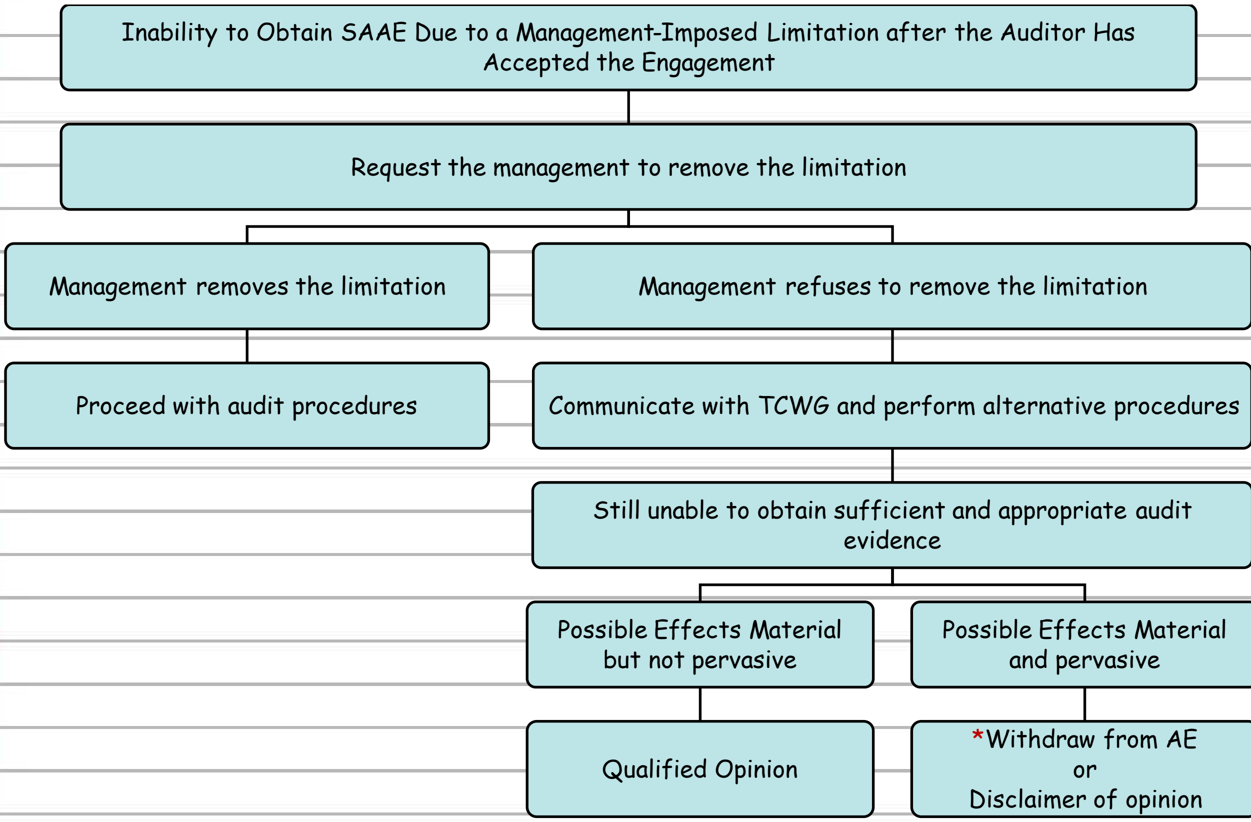
IV. WHICH TYPE OF OPINION IS APPROPRIATE?

The decision regarding which type of modified opinion is appropriate depends upon:

a) The nature of the matter giving rise to the modification, that is, whether the financial statements are materially misstated or, in the case of an inability to obtain sufficient appropriate audit evidence, may be materially misstated; and
b) The auditor's judgement about the pervasiveness of the effects or possible effects of the matter on the financial statements.

	S&A AE (500)	**MM**	**Pervasive**
Qualified	Yes	Yes	No
	No	Yes	No
Adverse	Yes	Yes	Yes
Disclaimer	No	Yes	Yes

V. INABILITY TO OBTAIN SAAE DUE TO A MGT IMPOSED LIMITATION AFTER THE AUDITOR HAS ACCEPTED THE ENGAGEMENT



*If the auditor withdraws from AE, before withdrawing, the auditor shall communicate to TCWG any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion.

VI. FORM AND CONTENT OF THE AUDITOR'S REPORT WHEN THE OPINION IS MODIFIED

Auditor's Opinion When the auditor modifies the audit opinion, the auditor shall use the heading "Qualified Opinion," "Adverse Opinion," or "Disclaimer of Opinion," as appropriate, for the Opinion section.

QUALIFIED OPINION

When the auditor expresses a qualified opinion due to a material misstatement in the financial statements, the auditor shall state that, in the auditor's opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion section,

a) When reporting in accordance with a fair presentation framework, the accompanying financial statements present fairly, in all material respects (or give a true and fair view of) [...] in accordance with [the applicable financial reporting framework]; or

b) When reporting in accordance with a compliance framework, the accompanying financial statements have been prepared, in all material respects, in accordance with [the applicable financial reporting framework].

When the modification arises from an inability to obtain sufficient appropriate audit evidence, the auditor shall use the corresponding phrase "except for the possible effects of the matter(s) ..." for the modified opinion.

ADVERSE OPINION

When the auditor expresses an adverse opinion, the auditor shall state that, in the auditor's opinion, because of the significance of the matter(s) described in the Basis for Adverse Opinion section,

a) When reporting in accordance with a fair presentation framework, the accompanying financial statements do not present fairly (or give a true and fair view of) [...] in accordance with [the applicable financial reporting framework]; or

b) When reporting in accordance with a compliance framework, the accompanying financial statements have not been prepared, in all material respects, in accordance with [the applicable financial reporting framework].

DISCLAIMER OF OPINION

When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall:

a) State that the auditor does not express an opinion on the accompanying financial statements;

b) State that, because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and

c) Amend the statement required by SA 700 (Revised), which indicates that the financial statements have been audited, to state that the auditor was engaged to audit the financial statements.

VII. BASIS FOR OPINION

When the auditor modifies the opinion on the financial statements, the auditor shall, in addition to the specific elements required by SA 700 (Revised):

Amend the heading "Basis for Opinion" required by SA 700 (Revised) to "Basis for Qualified Opinion," "Basis for Adverse Opinion," or "Basis for Disclaimer of Opinion," as appropriate; and

Within this section, include a description of the matter giving rise to the modification

CASE 1 - QUANTITATIVE DISCLOSURES

If there is a material misstatement of the financial statements that relates to specific amounts in the financial statements (including quantitative disclosures in the notes to the financial statements), the auditor shall include in the Basis for Opinion section a description and quantification of the financial effects of the misstatement, unless impracticable.

CASE 2 - NOT PRACTICABLE TO QUANTIFY

If it is not practicable to quantify the financial effects, the auditor shall so state in this section.

CASE 3 - NARRATIVE DISCLOSURES

If there is a material misstatement of the financial statements that relates to narrative disclosures, the auditor shall include in the Basis for Opinion section an explanation of how the disclosures are misstated.

CASE 4 - NON-DISCLOSURE

If there is a material misstatement of the financial statements that relates to the non-disclosure of information required to be disclosed, the auditor shall:

a. Discuss the non-disclosure with TCWG;
b. Describe in the Basis for Opinion section the nature of the omitted information; and
c. Unless prohibited by law or regulation, include the omitted disclosures, provided it is practicable to do so and the auditor has obtained sufficient appropriate audit evidence about the omitted information.

CASE 5 - INABILITY TO OBTAIN SAAE

If the modification results from an inability to obtain sufficient appropriate audit evidence, the auditor shall include in the Basis for Opinion section the reasons for that inability.

CASE 6 - QUALIFIED OR ADVERSE OPINION

When the auditor expresses a qualified or adverse opinion, the auditor shall amend the statement about whether the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion required by SA 700 (Revised) to include the word "qualified" or "adverse", as appropriate.

CASE 7 - DISCLAIMS AN OPINION

When the auditor disclaims an opinion on the financial statements, the auditor's report shall not include the following elements required by SA 700 (Revised).

a) A reference to the section of the auditor's report where the auditor's responsibilities are described; and
b) A statement about whether the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion.
c) Unless required by law or regulation, when the auditor disclaims an opinion on the FS, the auditor's report shall not include a KAM section in accordance with SA 701.

CASE 8 - BASIS FOR OPINION

Even if the auditor has expressed an adverse opinion or disclaimed an opinion on the financial statements, the auditor shall describe in the Basis for Opinion section the reasons for any other matters of which the auditor is aware that would have required a modification to the opinion, and the effects thereof.

VIII. DESCRIPTION OF AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE FS WHEN THE AUDITOR DISCLAIMS AN OPINION ON THE FS

When the auditor disclaims an opinion on the FS due to an inability to obtain SAAE the auditor shall amend the description of the auditor's responsibilities required by SA 700 (Revised) to include only the following:

a) A statement that the auditor's responsibility is to conduct an audit of the entity's financial statements in accordance with Standards on Auditing and to issue an auditor's report;
b) A statement that, however, because of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and
c) The statement about auditor independence and other ethical responsibilities required by SA 700 (Revised).

IX. COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE

When the auditor expects to modify the opinion in the AR, the auditor shall communicate with TCWG the circumstances that led to the expected modification and the wording of the modification.

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SA 706

SA 706

- I. SCOPE
- II. DEFINITIONS
- III. OBJECTIVE
- IV. EMPHASIS OF MATTER PARAGRAPH
  - SEPARATE SECTION FOR EMP
  - SOME EXAMPLES
- V. OTHER MATTER PARAGRAPH
  - SEPARATE SECTION FOR OMP
- VI. COMMUNICATION WITH TCWG

I. SCOPE

This SA deals with additional communication in the auditor's report when the auditor considers it necessary to draw users' attention to a matter or matters

a) presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements; or

b) other than those presented or disclosed in the financial statements that are relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

II. DEFINITIONS

EMPHASIS OF MATTER PARAGRAPH

Emphasis of Matter Paragraph is a paragraph included in the auditor's report → that refers to a matter appropriately presented or disclosed in the financial statements → that, in the auditor's judgment, is of such importance that it is fundamental to users understanding of the FS.

OTHER MATTER PARAGRAPH

Other Matter paragraph is a paragraph included in the auditor's report → that refers to a matter other than those presented or disclosed in the financial statements → that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

III. OBJECTIVES

AS per SA 706, the objective of the auditor, having formed an opinion on the financial statements, is to draw users' attention, when in the auditor's judgment it is necessary to do so, by way of clear additional communication in the auditor's report, to:

- A matter, although appropriately presented or disclosed in the FS, that is of such importance that it is fundamental to users' understanding of the FS; or
- As appropriate, any other matter that is relevant to users' understanding of the audit, the auditor's responsibilities or the AR.

IV. EMPHASIS OF MATTER PARAGRAPH

The auditor shall include an Emphasis of Matter paragraph in the auditor's report provided:

a) The auditor would not be required to modify the opinion in accordance with SA 705 (Revised) as a result of the matter; and

b) When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor's report.

SEPARATE SECTION FOR EMP

When the auditor includes an Emphasis of Matter paragraph in the AR, the auditor shall:

a) Include the paragraph within a separate section of the AR with an appropriate heading that includes the term "Emphasis of Matter";

b) Include in the paragraph a clear reference to the matter being emphasized and to where relevant disclosures that fully describe the matter can be found in the FS. The paragraph shall refer only to information presented or disclosed in the FS; and

c) Indicate that the auditor's opinion is not modified in respect of the matter emphasized.

Some examples of circumstances where the auditor may consider it necessary to include an Emphasis of Matter paragraph.

- An uncertainty relating to the future outcome of exceptional litigation or regulatory action.
- A significant subsequent event that occurs between the date of the financial statements and the date of the auditor's report.
- Early application (where permitted) of a new accounting standard that has a material effect on the financial statements.
- A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position

The inclusion of an EMP in the auditor's report does not affect the auditor's opinion

An Emphasis of Matter paragraph is not a substitute for:

a) A modified opinion in accordance with SA 705 (Revised) when required by the circumstances of a specific audit engagement;

b) Disclosures in the FS that the AFRF requires management to make, or that are otherwise necessary to achieve fair presentation; or

c) Reporting in accordance with SA 570 (Revised) when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a GC.

V. OTHER MATTER PARAGRAPH

The auditor shall include an Emphasis of Matter paragraph in the auditor's report provided:

a) This is not prohibited by law or regulation; and

b) When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the AR.

SEPARATE SECTION FOR OMP

When the auditor includes an OMP in the AR, the auditor shall include the paragraph within a separate section with the heading "Other Matter," or other appropriate heading.

VI. COMMUNICATION WITH TCWG

If the auditor expects to include an EMP or an OMP in the AR, the auditor shall communicate with TCWG regarding this expectation and the wording of this paragraph.

SA 710 "COMPARATIVE INFORMATION-CORRESPONDING FIGURES AND COMPARATIVE FS"

This standard deals with the auditor's responsibilities regarding comparative information in an audit of FS. When the FS of the prior period has been audited or not audited, the requirements and guidance under SA 510 also apply. The essential audit reporting differences between the approaches are:

- Comparative Information
  - Comparative FS
    - Auditor's opinion refers to each period
  - Corresponding figures
    - Auditor's opinion refers to current period only

SA 710

- Comparative information
  - **I.** Definition
  - **II.** Audit Procedures
- Corresponding information
  - **III.** Definition
  - **IV.** When does auditors opinion refer to corresponding figures?
- **V.** Comparative Financial Information

I. DEFINITION OF COMPARATIVE INFORMATION

The amounts and disclosures included in the FS → in respect of one or more prior periods in accordance with the AFRF

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II. AUDIT PROCEDURES REGARDING COMPARATIVE INFORMATION

- The auditor shall determine whether the FS includes comparative information required by the AFRF and whether such information is appropriately classified.
  - The comparative info agrees with the amounts and other disclosures presented in the prior period, and
  - The accounting policies are consistent with those in the current period.
- If the auditor becomes aware of a possible Misstatement in the comparative information while performing the current period audit, the auditor shall perform such additional audit procedures as are necessary in the circumstances to obtain SAAE to determine whether a MM exists. If the auditor has audited the prior period, the auditor shall follow the procedures as per SA 560
- As per SA 580, the auditor shall obtain Written representations for all periods referred to in the auditor's opinion. If there is any specific period which is disclosed in the current period, the auditor shall obtain separate Written representation for that period.

III. DEFINITION OF CORRESPONDING FIGURES

Comparative information where amounts and other disclosures for the prior period are included as an integral part of the current period FS

and are intended to be read only in relation to the amounts and other disclosures relating to the current period.

The level of detail presented in the corresponding amounts and disclosures is dictated primarily by its relevance to the current period figures.

IV. WHEN CORRESPONDING FIGURES ARE PRESENTED, THE AUDITOR'S OPINION SHALL NOT REFER TO THE CORRESPONDING FIGURES EXCEPT IN THE FOLLOWING CIRCUMSTANCES:

1. If the audit report on the prior period included a Qualified opinion, adverse or a disclaimer of opinion, and the matter which gives rise to modification is unresolved, the auditor shall modify in the current period FS. In the Basis for Modification paragraph in the auditor's report, the auditor shall either:
   a) Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or
   b) In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.
2. If the auditor obtains AE that a MM exists in the prior period on which an unmodified report has been issued, the auditor shall verify if the MM has been dealt with, if not, the auditor shall express a qualified or adverse opinion, modified wrt. Corresponding figures included therein.

3. If prior period FS are not audited, the auditor shall state in OMP in the auditor's report that corresponding figures are not audited.
4. If the prior period FS are audited by the predecessor auditor, the auditor shall refer that report for the corresponding figures and state in the OMP in the current audit report that:

a) The FS are audited by predecessor auditor
b) The type of opinion by the predecessor auditor & if modified, reasons for the same
c) The date of that report

V. COMPARATIVE FINANCIAL STATEMENT

Comparative information where amounts and other disclosures for the prior period are included for comparison with the FS of the current period but, if audited, are referred to in the auditor 's opinion.

The level of information included in those comparative financial statements is comparable with that of the FS of the current period.

When comparative financial statements are presented, the auditor's opinion shall refer to each period for which FS are presented and on which an audit opinion is expressed.
If the auditor's opinion on such prior period FS differs from the opinion of the auditor of that period, the auditor shall disclose the reason for difference as per SA 706 in OMP.

If the Prior period FS are audited by predecessor auditor, in addition to expressing an opinion on the current period, the auditor shall state in OMP,

1. The FS are audited by predecessor auditor
2. The type of opinion by the predecessor auditor & if modified, reasons for the same
3. The date of that report

If the auditor concludes that MM exists that affects the prior period FS and predecessor auditor has previously reported without modification, the auditor shall communicate with TCWG and request the predecessor auditor be informed. If the predecessor auditor agrees to issue a new audit report on the amended FS, the auditor shall report only on current period.
If prior period is not audited, the auditor will state in OMP that the comparative FS are unaudited. Such a statement doesn't however relieve the auditor to obtain SAAE that the opening balances does not contain MM.

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SA 299 "JOINT AUDIT OF FINANCIAL STATEMENTS"

SA 299

- I. Meaning
- II. Work divided based on:
- III. Responsibilities
- IV. Advantages and Disadvantages of Joint Audit
- V. Joint / combined responsibilities
- VI. Special considerations regarding Joint Audit

I. MEANING

Joint Audit 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. It is quite widespread in big companies and corporations.

II. GENERALLY WORK DIVIDED BASED ON:

- Items of Assets and Liabilities
- Income and Expenditure
- Geographical area
- Identified units
- Period of FS

III. RESPONSIBILITIES OF JOINT AUDITOR:

Responsibilities of the Joint Auditor

- Audit Work is divided → Individual/ separate responsibility
- Audit work is not divided → Joint/ combined responsibility

IV. ADVANTAGES AND DISADVANTAGES OF JOINT AUDITOR:

Advantages	Disadvantages
1. Sharing of Expertise	1. The fees being shared
2. Advantage of mutual consultation	2. Psychological problem where firms of different standing are associated in the Joint Audit
3. Lower workload	3. General superiority complex of some auditors
4. Better quality of performance	4. Problems of coordination of work
5. Improved service to the client	5. Areas of work of common concern being neglected.
6. In respect of MNC, 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.	6. Uncertainty about the liability for the work done
7. Lower staff development costs	
8. Lower costs to carry out the work	
9. A sense of healthy competition towards a better performance.	

V. JOINT/ COMBINED RESPONSIBILITY:

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 audit procedures. On the other hand, **all the joint auditors will be jointly and severally responsible for:**

a) The work which is not divided among the joint auditors and is carried out by all the auditors

b) Decisions taken by all the joint auditors under audit planning in respect of common audit areas

c) Matters which are brought to the notice of the joint auditors by any one of them, and there is an agreement among the joint auditors on such matters.

d) Examining that the FS comply with the requirements of relevant statutes

e) Presentation and disclosure of the FS as required by AFRF

f) Ensuring that the audit report complies with the requirements of the relevant statutes, applicable standards on auditing and other relevant pronouncements issued by ICAI

In case a joint auditor comes across matters which are relevant to the areas of responsibility of other joint auditors and which deserve the attention, or which require disclosure or require discussion with, or application of judgement 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.

It may be noted that the joint auditors may issue a 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. In such circumstances, the audit report(s) shall make a reference to each other's audit report(s).

[Mention in "Other matter para" as per SA ____]

VI. SPECIAL CONSIDERATIONS REGARDING JOINT AUDITOR:

a) The Engagement partner and other key members of the engagement team from each of the joint auditors shall be involved in planning the audit

b) The joint auditors should jointly establish an overall audit strategy which sets the scope, timing and direction of the audit.

c) Before the commencement of the audit, the joint auditors should discuss and develop a joint plan. In developing the joint audit plan, the auditors should:

a. Identify division of audit areas and common areas

b. Ascertain the reporting objectives of the engagement

c. Consider and communicate among all joint auditors the factors that are significant in directing the engagement team's efforts

d. Consider the results of preliminary engagement activities, or similar engagements performed earlier

e. Ascertain the nature, extent and timing of resources necessary to accomplish the engagement

d) Each of the joint auditors should consider and assess the Risk and communicate to the other auditors

e) The joint auditors should discuss and document the Nature, extent and timing of audit procedures for the common areas, and the specific allotted areas

f) The joint auditors should obtain a common engagement letter and a common Management Representation Letter

g) The work allocation document should be signed by all the joint auditors and communicated with TCWG

SA 230 AUDIT DOCUMENTATION

SA 230

- I. Definition
- II. Objective of auditor
- III. Purpose of Audit Documentation
- IV. Audit Documentation includes:
- V. Audit Documentation does not include:
- VI. Timing
- VII. Form, Content & Extent of Audit Documentation
- VIII. The form, content and extent of AD depends on factors such as:
- IX. Audit File
- X. Audit File Timing
- XI. The form, content and extent of AD depends on
- XII. Completion memorandum OR Audit documentation

I. DEFINITION

Audit documentation refers to the

- record of audit procedures performed,
- relevant audit evidence obtained and
- conclusions the auditor reached.

Audit documentation may be recorded on paper or on electronic or on other media.

Audit documentation is not a substitute for the entity's accounting records.

II. OBJECTIVE OF AUDITOR

To prepare documentation that provides:

a) Sufficient and appropriate record for the basis of audit report

b) Evidence that the audit was planned and performed in accordance with SA.

III PURPOSE OF AUDIT DOCUMENTATION

1. Assisting the engagement team to plan and perform the audit
2. Assisting members of the engagement team to direct and supervise the audit work, and to discharge their review responsibilities
3. Enabling the ET to be accountable for its work
4. Retaining a record of matters of continuing significance to future audits.
5. Enabling the conduct of external inspections in accordance with applicable legal,regulatory or other requirements.
6. Enabling the conduct of quality controls as per SQC 1

IV. AUDIT DOCUMENTATION INCLUDES:

e.g. (CLAAIMS)

- Correspondence (including email) concerning Significant Matters
- Checklists
- Letters of confirmation & representations
- Analyses
- Audit programme
- Issues Memoranda
- Summaries of significant matters

V. AUDIT DOCUMENTATION DOES NOT INCLUDE:

- Superseded drafts of working papers and financial statements
- Notes that reflect incomplete or preliminary thinking
- Previous copies of documents corrected for typographical or other errors
- And duplicates of documents

VI. TIMING

- The auditor shall prepare audit documentation on a timely basis.
- Preparing SAAE Documentation on a timely basis helps to enhance the quality of Audit.
- Documentation prepared after the audit is likely to be less accurate than the documentation prepared at the time of such work is performed.

VII. FORM, CONTENT & EXTENT OF AUDIT DOCUMENTATION

Timing:

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

1. The **NTE*** of Audit Procedures performed,
2. The results of the AP performed and the AE obtained
3. Significant matters arising during audit and the conclusions reached thereon and significant professional judgements made in reaching those conclusions.

Further in documenting the NTE* of audit procedures performed, the auditor shall record:

a) The identifying characteristics of the specific items or matters tested.

b) Who performed the audit work and the date such work was completed; and

c) Who reviewed the audit work performed and the date and extent of such review.

Discussion regarding significant matters:

The auditor shall document discussions of significant matters with Mgmt, TCWG, and others, including:

- The nature of the significant matters discussed
- & When and with Whom the discussions took place.

Inconsistency regarding significant matter?

If the auditor identified info that is Inconsistent with the auditor's Final conclusion regarding a significant matter,

The auditor shall **document how the auditor addressed the inconsistency.**

VIII. THE FORM, CONTENT AND EXTENT OF AD DEPENDS ON FACTORS SUCH AS:

1. The size and complexity of the entity
2. The nature of Audit Procedures to be performed
3. The Identified RoMM
4. The significance of the Audit Evidence obtained
5. The nature and extent of exceptions identified
6. The Audit methodology and tools used
7. The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or AE obtained.

IX. AUDIT FILE

Audit File may be defined as **one or more folders** or other storage media,

in physical form or electronic form, containing the records that comprise

the audit documentation for a specific engagement.

X. AUDIT FILE TIMING

CASE I: COMPLETION OF FINAL AUDIT FILE:

The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the AR.

The assembly of the final audit file after the date of AR is an administrative process that does not involve the performance of new audit procedures or the drawing of new conclusions.

Time Limit: The completion of the final audit file should be not more than 60 days (Less or equal to) after the date of auditor's report

CASE II: CHANGES TO AUDIT DOCUMENTATION DURING FINAL ASSEMBLY PROCESS

Changes can be made to the audit documentation **during the final assembly process, if they are administrative in nature.**

Examples of such changes include:

1. Deleting or discarding superseded documentation
2. Sorting, collating and cross referencing workpapers
3. Signing off on completion checklists relating to file assembly process
4. Documenting audit evidence that the auditor has obtained, discussed and agreed with the relevant members of the engagement team before the date of the AR.

CASE III: AFTER COMPLETION OF ASSEMBLING FINAL AUDIT FILE:

SQC-1 "Quality Control for Firms that perform Audits and Review of Historical Financial Information, and other assurance and Related Services" requires firms to establish policies and procedures for the timely completion for the assembly of audit files.

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.

SQC1 also requires firms to establish policies and procedures for the retention of engagement documentation.

The retention period for audit engagements is ordinarily no shorter than 7years from the date of the auditor's report, or if later, the date of the group auditor's report.

XI. DOCUMENTATION OF SIGNIFICANT MATTERS AND RELATED SIGNIFICANT PROFESSIONAL JUDGEMENTS:

Documentation of Significant Matters and Related Significant Professional Judgements:

Examples of significant matters include:

Matters that give rise to significant risks:

1. Results of audit procedures indicating

(a) That the financial statements could be materially misstated, or

(b) A need to revise the auditor's previous assessment of the ROMM and the auditor's responses to those risks.

2. Circumstances that cause the auditor significant difficulty in applying necessary audit procedures.

3. Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter Paragraph in the auditor's report.

Some e.g. of circumstances in which it is appropriate to prepare AD relating to the use of professional judgement include,

Where the matters and judgements are significant:

1. The rationale for the auditor's conclusion when a requirement provides that the auditor 'shall consider' certain information or factors, and that consideration is significant in the context of the particular engagement.

2. The basis for the auditor's conclusion on the reasonableness of areas of subjective judgements (for example, the reasonableness of significant accounting estimates)

3. The basis for the auditor's conclusions about the authenticity of a document when further investigation is undertaken in response to conditions identified during the audit that caused the auditor to believe that the document may not be authentic.

XII. COMPLETION MEMORANDUM OR AUDIT DOCUMENTATION SUMMARY:

The auditor may consider it helpful to prepare and retain as part of the audit documentation a summary (Sometimes known as completion memorandum) that describes-

- The significant matters identified during the audit and,
- How they were addressed

Such a summary may facilitate effective and efficient review and inspection of the AD, particularly for large and complex audits. It may also help the auditor to consider whether there is any individual relevant SA objective that the auditor cannot achieve that would prevent the auditor from achieving the overall objectives of the auditor.

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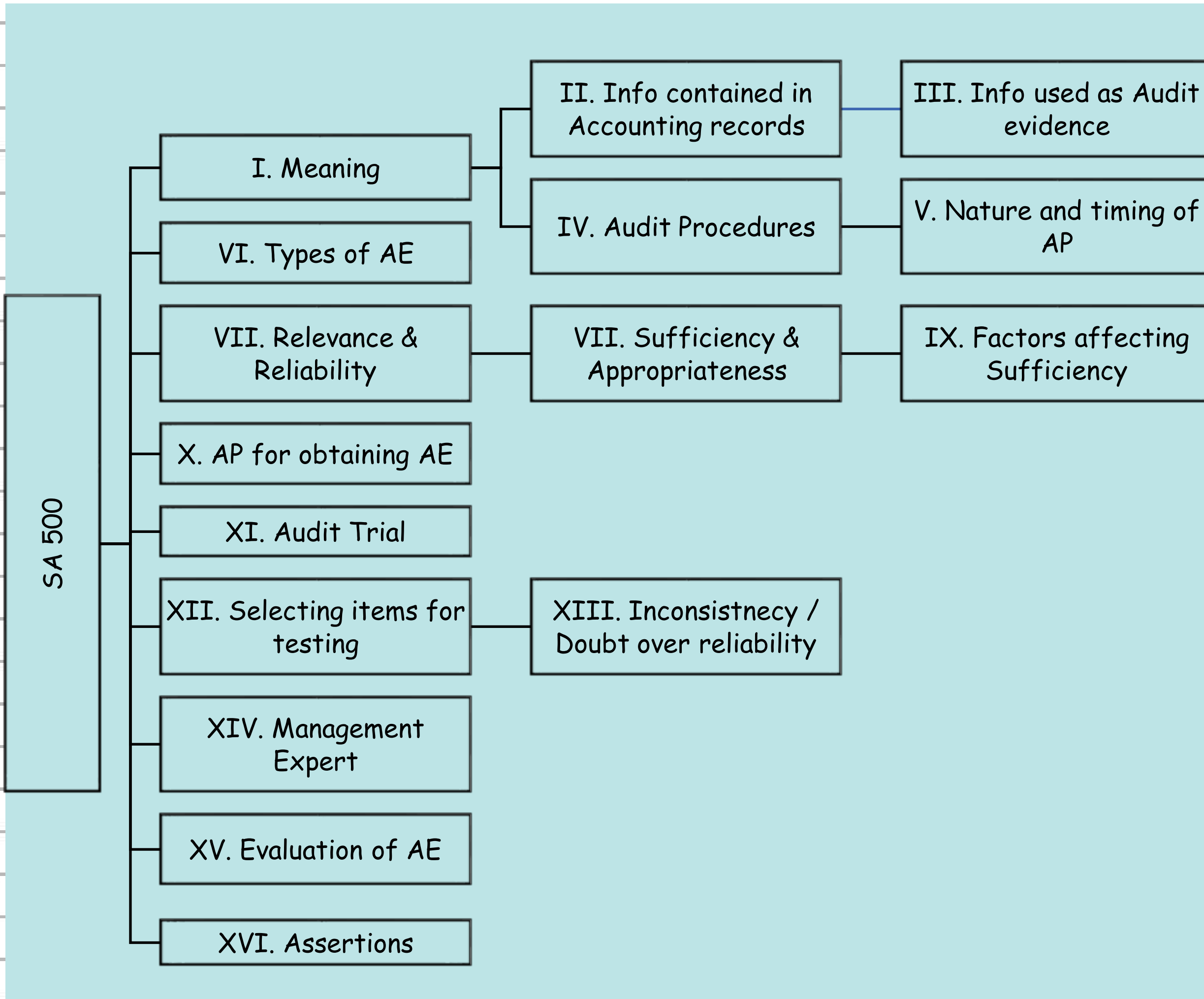
WHO IS THE OWNER OFAD?

- SQC 1 provides that, unless otherwise specified by law or regulation, AD is the property of the auditor.
- He may at his discretion make portions of, or extracts available to the clients, provided:
- Such a disclosure does not undermine validity of the work performed or the independence of the auditor or his personnel.

SA 500



I. MEANING

Audit evidence is the information used by the auditor in arriving at the conclusion on which auditors opinion is based.

Audit evidence includes both the information contained in accounting records underlying in the financial statements and other information.

II. INFORMATION CONTAINED IN ACCOUNTING RECORDS:

i. Accounting entries & supporting records such as cheques and EFT'S
ii. Invoices
iii. Contracts
iv. General & subsidy ledger & adjustments not reflected in journal entries
v. Worksheet/Spreadsheet

Other information that authenticates the accounting records

i. Minutes of the meetings
ii. Written information from trade receivables and trade payables
iii. Manuals containing IC and internal control policies and procedures, etc
iv. Information used as Audit evidence

II. INFORMATION TO BE USED AS AUDIT EVIDENCE:

A. Information by entity

i. Evaluate accuracy
ii. Evaluate completeness
iii. Evaluate if info is sufficient

B. Information by management expert

1. The nature and complexity of the matter to which the management's expert.
2. The risks of material misstatement in the matter.
3. The availability of alternative sources of audit evidence.
4. The nature, scope and objectives of the management's expert's work.
5. Whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services.
6. The extent to which management can exercise control or influence over the work of the management's expert.
7. Whether the management's expert is subject to technical performance standards or other professional or industry requirements.
8. The nature and extent of any controls within the entity over the management's expert's work.
9. The auditor's knowledge and experience of the management's expert's field of expertise.
10. The auditor's previous experience of the work of that expert.

IV. AUDIT PROCEDURES

INSPECTION

1. Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset.
2. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production.
   Eg : Inspection used as a test of controls is inspection of records for evidence of authorisation.
3. Some documents represent direct audit evidence of the existence of an asset,
   Eg : A document constituting the financial instrument such as a stock or bond.
4. Inspection of such documents may not necessarily provide audit evidence about ownership or value. In addition, inspecting an executed contract may provide audit evidence relevant to the entity's application of accounting policies, such as revenue recognition.
5. Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity's rights and obligations or the valuation of the assets.
6. Inspection of individual inventory items may accompany the observation of inventory counting.

INQUIRY

1. Inquiry consists of seeking information of knowledgeable persons, both financial and non- financial, within the entity or outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures.
2. Inquiries may range from formal written inquiries to informal oral inquiries.
3. Evaluating responses to inquiries is an integral part of the inquiry process.
4. Responses to inquiries may provide the auditor with information not previously possessed or with corroborative audit evidence.
5. Alternatively, responses might provide information that differs significantly from other information that the auditor has obtained, **for example**, information regarding the possibility of management override of controls. In some cases, responses to inquiries provide a basis for the auditor to modify or perform additional audit procedures.
6. Although corroboration of evidence obtained through inquiry is often of particular importance, in the case of inquiries about management intent, the information available to support management's intent may be limited.

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7. In these cases, understanding management's past history of carrying out its stated intentions, management's stated reasons for choosing a particular course of action, and management's ability to pursue a specific course of action may provide relevant information to corroborate the evidence obtained through inquiry.
8. In respect of some matters, the auditor may consider it necessary to obtain WR from management and, where appropriate, TCWG to confirm responses to oral inquiries.
9. Although inquiry may provide important audit evidence, and may even produce evidence of a misstatement, inquiry alone ordinarily does not provide sufficient audit evidence of the absence of a material misstatement at the assertion level, nor of the operating effectiveness of controls.

OBSERVATION

Observation consists of looking at a process or procedure being performed by others.

- Eg : the auditor's observation of inventory counting by the entity's personnel, or of the performance of control activities.

EXTERNAL CONFIRMATION

1. An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.
2. External confirmation procedures frequently are relevant when addressing assertions associated with certain account balances and their elements.
3. However, external confirmations need not be restricted to account balances only.
   - Eg : The auditor may request confirmation of the terms of agreements or transactions an entity has with third parties; the confirmation request may be designed to ask if any modifications have been made to the agreement and, if so, what the relevant details are.
4. External confirmation procedures also are used to obtain audit evidence about the absence of certain conditions.
   - Eg : The absence of a "side agreement" that may influence revenue recognition.

REPERFORMANCE

Reperformance involves the auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal control.

Eg : Re-performing the reconciliation of bank statement, re-performing the aging of accounts receivable.

RECALCULATION

Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.

ANALYTICAL PROCEDURES

1. Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial and non-financial data.
2. Analytical procedures also encompass the investigation of identified fluctuations and relationships that are inconsistent with other relevant information or deviate significantly from predicted amounts.

The following points are also relevant in respect of audit procedures for auditor's consideration:

a. The audit procedures inspection, observation, confirmation, recalculation, re- performance and analytical procedures, often in some combination, in addition to inquiry may be used as risk assessment procedures, tests of controls or substantive procedures, depending on the context in which they are applied by the auditor.

b. Audit evidence obtained from previous audits may, in certain circumstances, provide appropriate audit evidence where the auditor performs audit procedures to establish its continuing relevance.

V. NATURE AND TIMING OF THE AUDIT PROCEDURES :

a. 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.

- Eg : source documents, such as purchase orders and invoices, may exist only in electronic form when an entity uses electronic commerce, or may be discarded after scanning when an entity uses image processing systems to facilitate storage and reference.

b. Certain electronic information may not be retrievable after a specified period of time.

- Eg : if files are changed and if backup files do not exist. Accordingly, the auditor may find it necessary 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.

VI. TYPES OF AUDIT EVIDENCE

Depending upon nature

- **Visual.** For example, observing physical verification of inventory conducted by the client's staff.
- **Oral**. For example, discussion with the management and various officers of the client.
- **Documentary** For example, fixed deposit certificate, loan agreement, sales bill etc.

Depending upon Source

- **Internal.** Evidence which originates within the organisation being audited is internal evidence. (**Eg:** Sales invoice, Copies of sales challan and forwarding notes, goods received note, inspection report, copies of cash memo, debit and credit notes, etc.)
- **External.** The evidence that originates outside the client's organization is external evidence. (**Eg**: Purchase invoice, supplier's challan and forwarding note, debit notes and credit notes coming from parties, quotations, confirmations, etc.)

Which is more Reliable?

i. The external evidence is generally considered to be more reliable as they come from third parties who are not normally interested in manipulation of the accounting information of others. However, if the auditor has any reason to doubt the independence of any third party who has provided any material evidence e.g. an invoice of an associated concern, he should exercise greater vigilance in that matter.

ii. As an ordinary rule, the auditor should try to match internal and external evidence as far as practicable. Where external evidence is not readily available to match, the auditor should see as to what extent the various internal evidences corroborate one another.

VII RELEVANCE AND RELIABILITY

A. RELEVANCE

The quality of all audit evidence is affected by the relevance and reliability of the information upon which it is based.

i. Relevance deals with the logical connection with, or bearing upon, the purpose of the audit procedure and, where appropriate, the assertion under consideration. The relevance of information to be used as audit evidence may be affected by the direction of testing.

Example: If the purpose of an audit procedure is to test for overstatement in the existence or valuation of accounts payable, testing the recorded accounts payable may be a relevant audit procedure.

On the other hand, testing for understatement in the existence or valuation of accounts payable, testing the recorded accounts payable would not be relevant, but testing such information as subsequent disbursements, unpaid invoices, suppliers' statements, and unmatched receiving reports may be relevant.

ii. A given set of audit procedures may provide audit evidence that is relevant to certain assertions, but not others.

Example : inspection of documents related to the collection of receivables after the period end may provide audit evidence regarding existence and valuation, but not necessarily cut-off.

iii. Similarly, obtaining audit evidence regarding a particular assertion, for example, the existence of inventory, is not a substitute for obtaining audit evidence regarding another assertion,

Example : the valuation of that inventory. On the other hand, audit evidence from different sources or of a different nature may often be relevant to the same assertion.

iv. **Tests of controls** are designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level. Designing tests of controls to obtain relevant audit evidence includes identifying conditions (characteristics or attributes) that indicate performance of a control, and deviation in conditions which indicate departures from adequate performance. The presence or absence of those conditions can then be tested by the auditor.

v. **Substantive procedures** are designed to detect material misstatements at the assertion level. They comprise tests of details and substantive analytical procedures. Designing substantive procedures includes identifying conditions relevant to the purpose of the test that constitute a misstatement in the relevant assertion.

B. RELIABILITY

Information to be used as audit evidence should be reliable.

i. The reliability of information to be used as audit evidence, and therefore of the audit evidence itself, is influenced by its source and its nature, and the circumstances under which it is obtained, including the controls over its preparation and maintenance where relevant.

ii. Generalisations about the reliability of various kinds of audit evidence are subject to important exceptions. Even when information to be used as audit evidence is obtained from sources external to the entity, circumstances may exist that could affect its reliability.

Example: Information obtained from an independent external source may not be reliable if the source is not knowledgeable, or a management's expert may lack objectivity.

While recognising that exceptions may exist, the following generalisations about the reliability of audit evidence may be useful (Reliability increases when?) :

1. The reliability of audit evidence is increased when it is obtained from independent sources outside the entity.
2. The reliability of audit evidence that is generated internally is increased when the related controls, including those over its preparation and maintenance, imposed by the entity are effective.
3. Audit evidence obtained directly by the auditor (for example, observation of the application of a control) is more reliable than audit evidence obtained indirectly or by inference (for example, inquiry about the application of a control).
4. Audit evidence in documentary form, whether paper, electronic, or other medium, is more reliable than evidence obtained orally (for example, a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed).
5. Audit evidence obtained as original documents is more reliable than audit evidence obtained as photocopies or facsimiles, or documents that have been filmed, digitised or otherwise transformed into electronic form because in these cases the reliability of which may depend on the controls over their preparation and maintenance.

VIII. SUFFICIENCY & APPROPRIATENESS

a) **The sufficiency and appropriateness of audit evidence are interrelated.**

b) Sufficiency is the measure of the quantity of audit evidence.

c) 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)

d) Appropriateness is the measure of the quality of audit evidence; that is its relevance and its reliability in providing support for the conclusions on which the auditor's opinion is based.

Obtaining Sufficient and appropriate Audit Evidence by the Auditor :

a) The auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient and appropriate audit evidence.

b) Audit evidence is necessary to support the auditor's opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit.

c) Audit evidence comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions.

d) In addition, in some cases the absence of information (for example, management's refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence.

e) Most of the auditor's work in forming the auditor's opinion consists of obtaining and evaluating audit evidence.

IX. AUDITOR'S JUDGEMENT AS TO SUFFICIENCY MAYBE AFFECTED BY FACTORS

Materiality

It may be defined as the significance of classes of transactions, account balances and presentation and disclosures to the users of the f inancial statements. Less evidence would be required in case assertions are less material to users of the financial statements. But on the other hand if assertions are more material to the users of the financial statements, more evidence would be required.

Risk of Material Misstatement

It may be defined as the risk that the f inancial statements are materially misstated prior to audit. This consists of two components described as follows at the assertion level:

- Inherent risk—The susceptibility of an assertion to a misstatement that could be material before consideration of any related controls.
- Control risk—The risk that a misstatement that could occur in an assertion that could be material will not be prevented or detected and corrected on a timely basis by the entity's internal control.

Less evidence would be required in case assertions that have a lower risk of material misstatement. But on the other hand, if assertions have a higher risk of material misstatement, more evidence would be required.

Size & characteristics of the population

It refers to the number of items included in the population. Less evidence would be required in case of smaller, more homogeneous population but on the other hand in case of larger, more heterogeneous populations, more evidence would be required.

Source of audit evidence :

a) Some audit evidence is obtained by performing audit procedures to test the accounting records.

Example :

- through analysis and review,
- reperforming procedures followed in the financial reporting process,
- and reconciling related types and applications of the same information.

b) Through the performance of such audit procedures, the auditor may determine that the accounting records are internally consistent and agree to the FS.

c) More assurance is ordinarily obtained from consistent audit evidence obtained from different sources or of a different nature than from items of audit evidence considered individually.

Example : Corroborating information obtained from a source independent of the entity may increase the assurance the auditor obtains from audit evidence that is generated internally, such as evidence existing within the accounting records, minutes of meetings, or a management representation.

d) Information from sources independent of the entity that the auditor may use as audit evidence may include confirmations from third parties, analysts' reports, and comparable data about competitors.

X. AUDIT PROCEDURES FOR OBTAINING AE

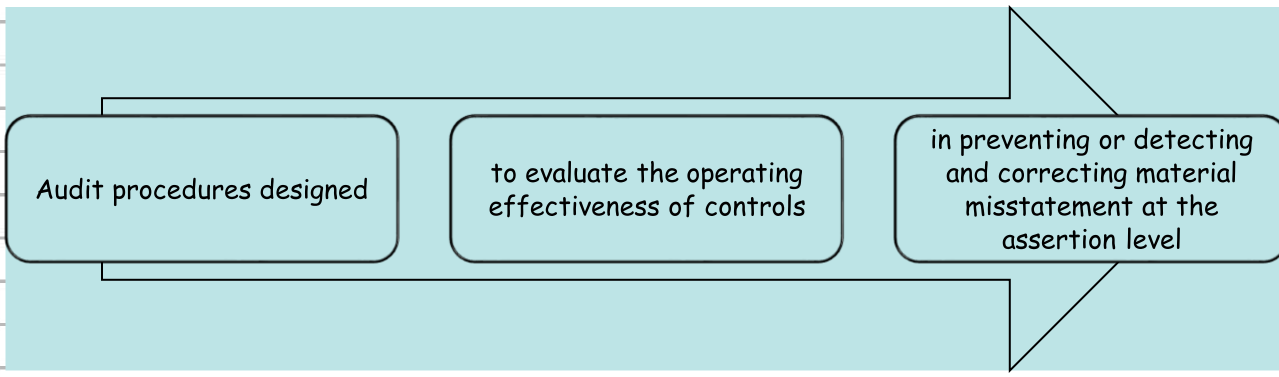
Audit evidence to draw reasonable conclusions on which to base the auditor's opinion is obtained by performing:

- **Risk Assessment Procedures**
- **Further Audit Procedures**
  - **Test of Controls**
  - **Substantive Procedures**
    - **Test of Details**
      - **Test of Transactions ie, Vouching**
      - **Test of Balances ie, Verification**
    - **Analytical Procedures**

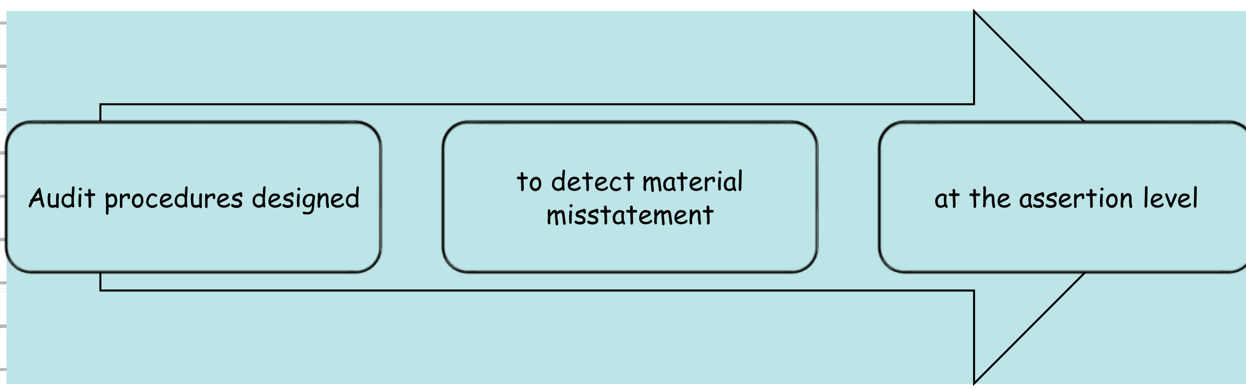
Risk Assessment Procedures:

Risk assessment procedures are the audit procedures performed to obtain an understanding of the entity and its environment to identify and assess the ROMM, at the FS and assertion levels.

Test of controls



Substantive procedures



XI. AUDIT TRAIL

1. An audit trail is a documented flow of a transaction.
2. It is used to investigate how a source document was translated into an account entry and from there it was inserted into financial statement of an entity.
3. It is used as audit evidence to establish authentication and integrity of a transaction.

4. Audit trails help in maintaining record of system and user activity. Like, in case of banks, there is an audit trail keeping track of log-on activity detailing record of log-on attempts and device used.
5. It is a step-by-step record by which accounting, trade details, or other financial data can be traced to their source.
6. Audit trails are used to verify and track many types of transactions including accounting and financial transactions.
7. Audit trails (or audit logs) act as record-keepers that document evidence of certain events, procedures or operations, because their purpose is to reduce fraud, material errors, and unauthorized use.
8. Audit trails help to enhance internal controls and data security.
9. Audit trails can help in fixing responsibility, rebuilding events and in thorough analysis of problem areas. For example, audit trails can track activities of users thus fixing responsibility for users.
10. Audit trail analysis can specify reason of the problem. It can also help in ensuring operation of system as intended. In this way, audit trails can help entities in their regular system operations.
11. However, audit trails involve costs. The cost is not only in terms of system expenditure but also in terms of time involved in analysing data made available by audit trails. However, use of automated tools can be made to analyse large volume of data thrown up by audit trails.
12. Systems which have a feature of audit trail inspires confidence in auditors. It helps auditors in verifying whether controls devised by the management were operating effectively or not.
13. It aids in verification whether a transaction was indeed performed by a person authorised to do it. Since audit trails also enhance data security, these can be used by auditor while performing audit procedures thus increasing reliability of audit evidence obtained.

XII SELECTING ITEMS FOR TESTING TO OBTAIN AE

A. Selecting all items (100%)
- 100% examination is unlikely in the case of tests of controls; however, it is more common for tests of details.
- 100% examination may be appropriate when,
    i. The population constitutes a small number of large value items;
    ii. There is a significant risk and other means do not provide sufficient appropriate audit evidence; or
    iii. The repetitive nature of a calculation or other process performed automatically by an information system makes a 100% examination cost effective.
    i. High value or key items. Eg : items that are suspicious, unusual, particularly risk-prone or that have a history of error.
    ii. All items over a certain amount.
    iii. Items to obtain information.

B. Selecting specific items

C. Audit sampling - SA 530

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XIII. INCONSISTENCY IN OR DOUBTS OVER RELIABILITY OF

i. If audit evidence obtained from one source is inconsistent with that obtained from another; or

ii. If 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, and shall consider the effect of the matter, if any, on other aspects of the audit.

Eg : responses to inquiries of mgmt, internal audit, and others are inconsistent.

SA 230 includes a specific documentation requirement if the auditor identified information that is inconsistent with the auditor's final conclusion regarding a significant matter.

XIV. MANAGEMENT EXPERT

Who is 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 to assist the entity in preparing the financial statements.

Relying on the work of a management's expert :

When information to be used as audit evidence has been prepared using the work of a management's expert, the auditor shall, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes;

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.

XV. EVALUATION OF AUDIT EVIDENCE :

- SA 500 "Audit Evidence" is applicable to all the audit evidence obtained during the course of the audit to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion.
- The auditor has to conclude whether sufficient appropriate audit evidence has been obtained to reduce audit risk to an acceptably low level, and thereby enable the auditor to draw reasonable conclusions on which to base the auditor's opinion, is a matter of professional judgment.

XVI ASSERTIONS

Assertions refer to representations by management, explicit or otherwise, that are embodied in the financial statements, as used by the auditor to consider the different types of potential misstatements that may occur. Assertions can be positive or negative or even explicit or implicit.

Occurrence	Completeness	Accuracy	Cut-off	Classification
• transactions and events that have been recorded have occurred and pertain to the entity.	• all transactions and events that should have been recorded have been recorded.	• amounts and other data relating to recorded transactions and events have been recorded appropriately.	• transactions and events have been recorded in the correct accounting period.	transactions and events have been recorded in the proper accounts.

Existence	Rights & Obligation	Completeness	Valuation & Allocation
• assets,liabilities, and equity interests exist.	• the entity holds or controls the rights to assets, and liabilities are the obligations of the entity.	• all assets, liabilities and equity interests that should have been recorded have been recorded.	• assets, liabilities, and equity interests are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.

Occurrence and rights and obligations	Completeness	Classification and understandability	Accuracy and valuation
• disclosed events, transactions, and other matters have occurred and pertain to the entity.	• all disclosures that should have been included in the financial statements have been included.	• financial information is appropriately presented and described, and disclosures are clearly expressed.	• financial and other information are disclosed fairly and at appropriate amounts.

Example ;

When we find in the balance sheet, an item under current assets reading as "cash in hand "₹10,000" the obvious assertions that would strike the mind are the following:

1. The firm concerned had "₹10,000" in hand in valid notes and coins on the balance sheet day;
2. That the cash was free and available for expenditure to the firm; and
3. That the books of account show a cash balance of identical amount at the end of the day on which the balance sheet is drawn up.

Example

Particulars		₹
Plant and Machinery (at cost)		2,00,000
Less: Depreciation till the end of previous year	70,000	
Depreciation for the year	13,000	83,000
		1,17,000

The assertions are as follows:

i. the firm owns the plant and machinery;

ii. the historical cost of plant and machinery is ₹2 lacs;

iii. the plant and machinery physically exists;

iv. the asset is being utilised in the business of the company productively;

v. total charge of depreciation on this asset is ₹83,000 to date on which ₹13,000 relates to the year in respect of which the accounts are drawn up;

vi. the amount of depreciation has been calculated on recognised basis and the calculation is correct.

From the above two illustrations we know the sort of assertions that are implied in the financial statements. Incidentally, the assertions are generally implied and not specifically spelt out, though some explicit assertions are also found in the financial statements.

Explicit assertions are made when otherwise the reader will be left with an incomplete picture; it may even be misleading.

Example:

Secured Loans ₹4,00,000

The description does not give us a complete picture. We do not know:

(i) the name of the lender, if it is relevant;

(ii) the nature of security provided; and

(iii) the rate at which interest in payable. A specific mention is required about these things for a proper appreciation of the item and the financial position.

Negative assertions are also encountered in the financial statements and the same may be expressed or implied. For example,

if it is stated that there is no contingent liability it would be an expressed negative assertion;

On the other hand, if in the balance sheet there is no item as "building", it would be an implied negative assertion that the entity did not own any building on the balance sheet date.

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AUDIT EVIDENCE – SPECIFIC CONSIDERATIONS FOR SELECTED ITEMS

SA 501- "Audit Evidence- Specific Considerations for Selected Items"

SA 501- "Audit Evidence- Specific Considerations for Selected Items"

- Inventory - Existence & condition
- Litigation & Claims – Completeness of litigation & claims involving the entity.
- Segment information – Presentation & Disclosure of segment information in accordance with AFRF

INVENTORY

When inventory is material to the FS, the auditor shall obtain SAAE regarding the existence and condition of inventory by:

a) Attendance at physical count of inventory, unless impracticable, to:

- Evaluate management's instructions and procedures for recording and controlling the results of the entity's physical inventory counting;
- Observe the performance of management's count procedures;
- Inspect the inventory; and
- Perform test counts.

b) Performing audit procedures over the entity's final inventory records to determine whether they accurately reflect the actual inventory count records.

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Attendance at Physical Inventory Counting Involves:

1. Inspecting the inventory to ascertain its existence and evaluate its condition, and performing test counts;
2. Observing compliance with management's instructions and the performance of procedures for recording and controlling the results of the physical inventory count; and
3. Obtaining audit evidence as to the reliability of management's count procedures.

PHYSICAL VERIFICATION OF INVENTORY

Case I: Auditor shall observe physical count on an alternative date	**Case II:** If the attendance of Physical inventory counting becomes impracticable	**Case III:** When the inventory is in the custody of the 3rd party

Case I: If the auditor is unable to attend the physical inventory counting due to unforeseen circumstances, the auditor shall observe physical count on an alternative date and perform audit procedures on **intervening transactions**. Whether changes in inventory amounts between the count date, or dates, and the final inventory records are properly recorded include:

- Whether the perpetual inventory records are properly adjusted.
- Reliability of the entity's perpetual inventory records.
- Reasons for significant differences between the information obtained during the physical count and the perpetual inventory records.

Case II: If the attendance of Physical inventory counting becomes impracticable, the auditor shall perform **alternative audit procedures** to obtain SAAE regarding the existence and condition of inventory.
If it is not possible to do so, the auditor shall modify the report as per SA 705.

Case III: **Impracticability maybe because of the nature or location of the inventory**.

When the inventory is in the Custody of the 3rd party, the auditor shall obtain S&A AE regarding the existence and condition of that inventory by performing one or both of the following:

a) Request confirmation from 3rd party as to the Quantity and Condition of inventory held on behalf of the entity.

b) Perform Inspection or other audit procedures appropriate in the circumstances.

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What are other Audit Procedures?

It includes: (ACID)

1. Inspecting documents regarding inventory held by 3rd party for ex: warehouse receipts
2. Requesting confirmation from other parties when inventories have been pledged as Collateral
3. Attending, or arranging for Another auditor to attend, the 3rd parties physical counting of inventory, if practicable.
4. Obtaining another auditor's report or a service auditor's report, on the adequacy of the 3rd party's Internal control for ensuring that inventory is properly counted and adequately safeguarded.

Matters relevant in planning attendance at physical inventory counting: (Q.may'25)

For example:

1. Nature of inventory.
2. Stages of completion of work in progress.
3. The ROMM related to inventory.
4. The nature of the Internal control related to inventory.
5. Whether Adequate procedures are expected to be established and proper instructions issued for physical inventory counting.
6. The Timing of physical inventory counting.
7. Whether the entity maintains a Perpetual inventory system.
8. The Locations at which inventory is held, including the materiality of the inventory and the risks of material misstatement at different locations, in deciding at which locations attendance is appropriate
9. Whether the Assistance of an auditor's expert is needed to obtain sufficient appropriate audit evidence.

LITIGATION & 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.

If the auditor assesses a ROMM regarding litigation or claims that have been identified, or when AP 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 legal counsel.

↓

The auditor shall do so through a **Letter of inquiry** requesting the entity's external legal counsel to communicate directly with the auditor.

↓

If the law or regulation prohibits any kind of direct contact, the auditor shall perform **Alternative audit procedures.**

The auditor may seek direct communication through a letter of specific inquiry.

(a) A list of litigation and claims;

(b) Where available, management's assessment of the outcome of each of the identified litigation and claims and its estimate of the financial implications, including costs involved; and

(c) A request that the entity's external legal counsel confirm the reasonableness of management's assessments and provide the auditor with further information if the list is considered by the entity's external legal counsel to be incomplete or incorrect.

When will the auditor judge it necessary to meet with the external legal counsel?

a) The auditor determines that the matter is of significant risk

b) The matter is complex

c) There is disagreement between management and the entity's external legal counsel. Ordinarily such meetings require management's permission and are held with a representative of management in attendance.

Further if,

i) 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

ii) the auditor is unable to obtain SAAE by performing alternative audit procedures, the auditor shall modify the opinion in the auditor's report in accordance with SA 705.

V. SEGMENT INFORMATION

SEGMENT INFORMATION

- **Obtain sufficient and appropriate audit evidence**
- **Understand the methods used by the management**
- **Auditor's responsibility regarding presentation & disclosure of segment information**

Definition: Segment Information refers to information about different types of products and services of an enterprise and its operations in different geographical areas.

The auditor shall obtain SAAE regarding the presentation and disclosure of segment information in accordance with AFRF:

1. Obtaining an understanding of the methods used by the management in determining segment information
   - Evaluating whether such methods are likely to result in disclosure in accordance with the AFRF; and
   - Where appropriate, testing the application of such methods; and
2. Performing analytical procedures and other audit procedures appropriate in the circumstances.

The Auditor's responsibility regarding the presentation and disclosure of segment information is in relation to the FS taken as a whole. Accordingly, the Auditor is not required to perform AP that would be necessary to express an opinion on the segment information presented on a standalone basis.

Example of matters that may be relevant when obtaining an understanding of the methods used by management in determining segment information:

1. Sales, transfers and charges between segments, and elimination of intersegment amounts.
2. Comparisons with budgets and other expected results, for example, operating profits as a percentage of sales.
3. The allocation of assets and costs among segments.
4. Consistency with prior periods, and the adequacy of the disclosures with respect to inconsistencies

SA 505 EXTERNAL CONFIRMATIONS

SA 505 "External Confirmations"

SA505 External Confirmation deals with the auditor's use of External confirmation procedures to obtain audit evidence. SA 500 indicates that the reliability of audit evidence is influenced by its source and by its nature, and is dependent on the individual circumstances under which it is obtained.

SA 505 - External Confirmations

- I. Objective
- II. Definitions
- III. Important terms
- IV. Uses of External Confirmation
- V. Procedures
  - Step 1: Information
  - Step 2: Select party
  - Step 3: Design requests
  - Step 4: Sending requests including follow- ups
- VI. Management's refusal to send External Confirmation
- VII. Results of External Confirmation procedure
- VIII. Negative Confirmations

I. Objective of the Auditor:

when using external confirmation procedures is to design and perform such procedures to obtain relevant and reliable audit evidence.

II. Definition- What is external confirmation?

It is the audit evidence obtained as a direct written response to the auditor from a third party, in paper form, or by electronic or other medium.

III. Important Terms

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.

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.

Non-Response: A failure of the confirming party to respond, or fully respond, to a positive confirmation request, or a confirmation request return undelivered.

Exception: A response which indicates a difference between information requested to be confirmed, or contained in the entity's records, and information provided by the confirming party. The exception needs to be assessed to the entire population after analysing the reason for difference.

IV. Uses of External Confirmation

- Confirming terms of agreement
- Contracts
- Transactions between entity and other party
- Amount due to lenders
- Property title deeds held by lawyers and financers as security

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V. External confirmation procedures

- Step 1: Determining the information to be confirmed or requested
- Step 2: Select the appropriate confirming party
- Step 3: Designing the confirmation requests
- Step 4: Sending the requests including follow up requests

Step 1: **Determining the information to be confirmed or requested:** External confirmation procedures frequently are performed to confirm or request information regarding account balances and their elements. They may also be used to confirm terms of agreements, contracts, or transactions between an entity and other parties, or to confirm the absence of certain conditions, such as a "side agreement".

Step 2: **Select the appropriate confirming party:** Responses to confirmation requests provide more relevant and reliable audit evidence when confirmation requests are sent to a confirming party the auditor believes is knowledgeable about the information to be confirmed. Ex: a financial institution official who is knowledgeable about the transactions or arrangements for which confirmation is requested may be the most appropriate person at the financial institution from whom to request confirmation.

Step 3: **Designing the confirmation requests:**

a) **Design of a confirmation request:** The design of a confirmation request may directly affect the confirmation response rate, and the reliability and the nature of the audit evidence obtained from responses.

b) **Factors to be considered by auditor when designing confirmation requests includes:**

1) The assertions being addressed
2) Specific identified risks of material misstatement, including fraud risks.
3) The layout and presentation of the confirmation request.

4) Prior experience on the audit or similar engagements.

5) The method of communication (for example, in paper form, or by electronic or other medium)

6) Management's authorization or encouragement to the confirming parties to respond to the auditor. Confirming parties may only be willing to respond to a confirmation request containing management's authorization.

7) The ability of the intended confirming party to confirm or provide the requested information (for example, individual invoice amount versus total balance)

c) **Positive confirmation request**

A positive external confirmation request asks the confirming party to reply to the auditor in all cases, either by indicating the confirming party's agreement with the given information, or by asking the confirming party to provide information. A response to a positive confirmation request ordinarily is expected to provide reliable audit evidence. There is a risk, however, that a confirming party may reply to the confirmation request without verifying that the information is correct. The auditor may reduce this risk by using positive confirmation requests that do not state the amount (or other information) on the confirmation request, and ask the confirming party to fill in the amount or furnish other information. On the other hand, use of this type of "blank" confirmation request may result in lower response rates because additional effort is required of the confirming parties.

d) **Determination of properly addressed requests:** Determining that requests are properly addressed includes testing the validity of some or all of the addresses on confirmation requests before they are sent out.

Step 4: **Sending the requests including follow up requests:**

The auditor may send an additional confirmation request when a reply to a previous request has not been received within a reasonable time. For example, the auditor may, having re-verified the accuracy of the original address, send an additional or follow-up request.

VI. Management's refusal 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 the management's refusal on the auditor's assessment of the relevant risks of material misstatement.
- 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 TCWG under SA 260

The auditor shall also determine the implications on the audit and the auditors opinion under SA705

If Management refuses to allow the auditor to send external confirmation.

- Inquire management and evaluate the implications.
- Reasonable > Perform Alternative audit procedures > Obtain sufficient and appropriate audit evidence
- Reasonable > Cannot perform Alternative audit procedures > SA260 & SA705
- Not Reasonable > SA260 & SA705

VII. RESULTS OF EXTERNAL CONFIRMATION PROCEDURES

Results

Doubt about reliability

Not reliable

<u>Reliability of responses to confirmation requests</u>

- If the auditor identifies factors that give rise to doubts about the reliability of the response to a confirmation request,
  - The auditor shall obtain further audit evidence to resolve those doubts.
- If the auditor determines that the response to a confirmation request is not reliable,
- The auditor shall evaluate the implications on the assessment of the relevant Risk of material misstateme

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VIII. Negative Confirmations

Negative confirmations provide less persuasive audit evidence than positive confirmations. Accordingly, the auditor shall not use negative confirmation requests as the sole substantive audit procedure to address an assessed risk of material misstatement at the assertion level unless all of the following are present:

1) The auditor has assessed the ROMM as low and has obtained sufficient and appropriate AE regarding the operating effectiveness of controls relevant to the assertions.
2) The population of items subject to negative confirmation procedures comprises a large number of small, homogeneous, account balances, transactions, or conditions.
3) A very low exception rate is expected.
4) The auditor is not aware of circumstances or conditions that would cause recipients of negative confirmation requests to disregard such requests.

SA 510- INITIAL AUDIT ENGAGEMENTS- OPENING BALANCES

SA 510

- I. DEFINITION
- II. OBJECTIVE
- III. AUDIT PROCEDURES
- IV. CASE 1
  CASE 2

This standard deals with the auditor's responsibilities relating to opening balances when conducting an initial audit engagement. In addition to financial statements amounts, opening balances include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

I. DEFINITION OF INITIAL AUDIT ENGAGEMENT

An engagement in which either:

- The FS for the prior period were not audited, or
- The FS for the prior period was audited by the predecessor auditor

II. OBJECTIVE OF AUDITOR with respect to opening balances- in conducting an initial audit engagement

In conducting an initial audit engagement, the objective of the auditor with respect to opening balances is to obtain Sufficient and Appropriate audit evidence whether:

a) Opening balances contain misstatements that materially affect the current period's financial statements and

b) 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 FRF

III. AUDIT PROCEDURES REGARDING OPENING BALANCES

1) The auditor shall read the most recent financial statements if any, and the predecessor auditor's report thereon, if any, for any information regarding opening balances, including disclosures.

2) **The auditor shall obtain sufficient and appropriate AE about whether the opening balances contain misstatements that materially affect the current period's FS by:**

- 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 CY statement of P&L
- Determining whether the opening balances reflect the application of appropriate accounting policies; and
- Performing one or more of the following:
  - Where the prior year FS are audited, perusing the copies of the audited FS including other relevant documents relating Prior period FS
  - Evaluating whether the audit procedures performed in the current period provide evidence relevant to the opening balances
  - Performing specific audit procedures to obtain evidence regarding the opening balances

IV. (i) CASE 1

If the auditor obtains audit evidence that the opening balances contain misstatements that could materially affect the current period's Financial statements, The auditor shall perform such additional audit procedures as are appropriate in the circumstances to determine the effect on the current period's FS

If the auditor concludes that such misstatements exist in the current period's FS, the auditor shall communicate with the appropriate levels of management and those charged with governance.

(ii) CASE 2

If the Auditor concludes that:

- The current period's accounting policies are not consistently applied in relation to the opening balances in accordance with AFRF; or
- A change in accounting policies is not properly accounted for or not adequately presented or disclosed in accordance with the AFRF.

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

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REPORTING SA705 BY AUDITOR REGARDING OPENING BALANCES:

i. 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

ii. If the auditor concludes that the opening balances contain a misstatement that materially affect the current period FS, 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

ADDITIONAL POINTS:

- Consistency of Accounting policies relating to opening balances
- Relevant information in the predecessor audit report
- Audit conclusions and reporting in relation to opening balances
- Modifications to the opinion in the predecessor audit report

SA 520 ANALYTICAL PROCEDURES

SA 520

I. Meaning

II. Types

III. Scope

IV. Purpose

V. Timing

VI. Factors to be considered

- Availability of data
- Disaggregation
- Account Type
- Source
- Predictability
- Nature of Assertion
- Inherent Risk or "What Can Go Wrong

VII. Techniques

- Trend Analysis
- Ratio Analysis
- Reasonableness test
- Structural modelling

VIII. Auditor's Responsibilities

- Suitability
- Reliability
- Expectation
- Acceptable difference

IX. Investigating Results

X. Conclusion

I. MEANING

Analytical Procedures means → evaluation of financial information → through analysis of plausible relationships → among both financial and non financial data.

II. TYPES

We can say that analytical procedures can be split broadly into 5 types

- Comparison of client and industry data
- Comparison of client data with similar prior period data
- Comparison of client data with client determined expected results
- Comparison of client data with client determined expected results, using non-financial data
- Comparison of client data with auditor determined expected results

III SCOPE OF SA 520 / OBEJECTIVE OF THE AUDITOR

a) To obtain relevant and reliable audit evidence when using substantive analytical audit procedures

b) To design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the FS are consistent with the auditor's understanding of the entity.

IV. PURPOSE OF ANALYTICAL PROCEDURES

Analytical procedures use comparisons and relationships to assess whether account balances and other data appear reasonable.

- Compare the balances on the Statement of P&L with that of the previous period
- Comparing certain expenses ratios with the same ratios for the PY, it is possible to ascertain the extent of increase or decrease
- Differences are found to be material, the auditor would ascertain the reasons have been manipulated to inflate or suppress profits.
- May help in identifying unusual transactions/events
- Helpful in detecting unusual state of affairs and mistakes in accounts and matters that may have audit implications.
- Unusual or unexpected relationships that are identified may assist the auditor in identifying risks of material misstatement, especially risks of material misstatement due to fraud.

V. TIMING OF ANALYTICAL PROCEDURES

Experienced auditors use analytical procedures in ALL the stages of the audit.

Planning stage	Testing stage	Completion stage

Analytical procedures may help the auditor in the planning stage to determine the NET of audit procedures that will be used to obtain audit evidence for specific Account balances, class of transactions.

VI. FACTORS TO BE CONSIDERED FOR SUBSTANTIVE ANALYTICAL AUDIT PROCEDURES

Availability of data	• Availability of relevant and reliable data will facilitate effective AP
Disaggregation	• The degree of disaggregation in available data can directly affect the degree of usefulness in detecting misstatements
Account type	• SAP are more useful for one type of account than others. P&L reflect accumulated transactions and are more predictable. & BS represent the net effect of transactions and requires management judgement.
Source	• Transactions of repititive nature like sales and purchase can be used for effecient AP. Significant classes of transactions (SCoTs) are not frequent and difficult to predict. Example: Expenditure on Research & Advertisement is not of routine nature and are subject to management judgement and therefor more difficult to predict.
Predictability	• SAP are more appropriate when an Account Balance or relationship between data is more predictable. • e.g., between sales and cost of sales or between trade receivables and cash receipts
Nature of Assertion	• SAP is more effective for some assertions (completenes/ valuation) than for others (rights/ obligations)
Inherent risk/ What can go wrong?	• When Significant risk is identified, AE solely from AP is not sufficient. • When side agreements with respect to revenue recognition have been identified as a significant or fraud risk, it is unlikely that an analysis of sales compared to cash receipts or cost of sales would be appropriate to respond to that risk.

VII. TECHNIQUES AVAILABLE AS SUBSTANTIVE AP

TREND ANALYSIS	RATIO ANALYSIS	REASONABLENESS TEST	STRUCTURAL MODELLING
• The most commonly used technique • The comparison of current data with the prior period balance or with a trend in two or more prior period balances. • implies analysing account fluctuations by comparing current year to prior year information and, also, to information derived over several years. • Example: The auditor may compare the salary paid by the company during the year under audit with the salary paid by the company for several earlier years. There may be some percentage increase in the salary expense over the years. However, an unusual increase in such expense amount may indicate that fraudulent payments are being made to fake employees.	• Useful for analysing asset and liability accounts as well as revenue and expense accounts • An individual balance sheet account is difficult to predict on its own, but its relationship to another account is often more predictable (e.g., the trade receivables balance related to sales) • Ratios can also be compared over time or to the ratios of separate entities within the group, or with the ratios of other companies in the same industry • Example 1: Financial ratios may include: Trade receivables or inventory turnover, Freight expense as a percentage of sales revenue. • Example 2: The statutory auditor can review the Gross profit ratio of the company for the year under audit. The auditor can further compare such GP ratio with the GP ratio of the company in the earlier years or the GP ratio of the other companies in the same industry for the year under audit.	• Unlike trend analysis, this analytical procedure does not rely on events of prior periods, but upon non-financial data for the audit period under consideration • Example: Interest expense against interest bearing obligations, Raw Material Consumption to Production (quantity), Wastage & Scrap % against production & raw material consumption (quantity), Work-in-Progress based on issued of materials & Sales (quantity), Sales discounts and commissions against sales volume, Rental revenues based on occupancy of premises	• modelling tool constructs a statistical model from financial and/or non-financial data of prior accounting periods to predict current account balances (e.g., linear regression)

VIII. ANALYTICAL PROCEDURES USED AS SUBSTANTIVE TESTS

When designing and performing AP, either alone or in combo of test of Details, the auditor shall: SRED

DETERMINE SUITABILITY OF AP	EVALUATE RELIABILITY OF DATA	DEVELOP AN EXPECTATION	DETERMINE ACCEPTABLE DIFFERENCE
• More applicable to large volumes of transactions that are predicatable over time • Application of AP is on the assumption that relationships among data exist • Suitability of a particular AP may depend on auditor's assessment in determining the MM • In some cases, even an unsophisticated predictive model maybe effective as an analytical procedure.	• Source of information available. For example, information may be more reliable when it is obtained from independent sources outside the entity; • Comparability of the information.Example, broad industry data may need to be supplemented to be comparable to that of an entity that produces and sells specialised products; • Nature and relevance of information. Example, whether budgets have been established as results to be expected rather than as goals to be achieved; and • Controls over the preparation of info that are designed to ensure its completeness, accuracy and validity. Example, controls over the preparation, review and maintenance of budgets.	• Accuracy of expected results can be predicted. Eg: the auditor may expect greater consistency in comparing gross profit margins from one period to another than in comparing discretionary expenses, such as research or advertising. • Degree of disgaggregation. Eg: substantive analytical procedures may be more effective when applied to financial information on individual sections of an operation or toFinancial statements of components of a diversified entity, than when applied to the financial statements of the entity as a whole. • Availability of financial and non financial data. Eg: the auditor may consider whether financial information, such as budgets or forecasts, and non-financial information, such as the number of units produced or sold, is available to design substantive analytical procedures. If the information is available, the auditor may also consider the reliability of the information.	• Auditor's determination of the amount of difference that can be accepted without further investigation is influenced by materiality.

IX. INVESTIGATING RESULTS OF ANALYTICAL PROCEDURES

If AP performed in accordance with SA 520 identify fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount, the auditor shall investigate such differences by:

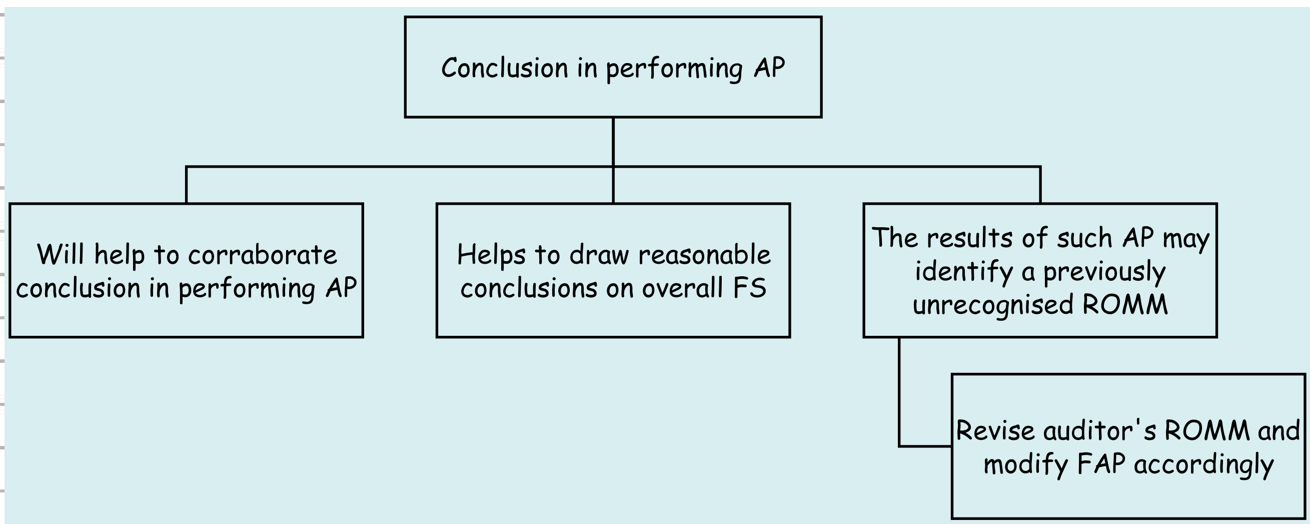
Inquiring of management and obtaining appropriate AE relevant to management's response

- Audit evidence relevant to management's responses may be obtained by evaluating those responses taking into account the auditor's understanding of the entity and its environment, and with other audit evidence obtained during the course of the audit.

Performing Other AP as necessary

- The need to perform other audit procedures may arise when, for example, management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate.

X. AUDITOR'S CONCLUSION



SA 530 AUDIT SAMPLING

SA 530

- I. Meaning
- II. Objectives
- III. Key Terms
- IV. Applicability
- V. Characteristics of population
- VI. Sampling unit
- VII. Approaches to sampling
- VIII. Difference between statistical vs non-statistical
- IX. Sampling vs Traditional methods of sampling
- X. Factors to be considered for extent of checking on sampling plan
- XI. Advantages of statistical sampling
- XII. Stratification and value weighted selection
- XIII. Sampling process
  - (i) Sample design
  - (ii) Sample size
  - (iii) Sample selection methods
    - Statistical
      - Random
      - Systematic
      - Value weighted
    - Non -Statistical
      - Haphazard
      - Block
  - (iv) Audit procedures
  - (v) Nature and cause of deviation
  - (vi) Projecting misstatements
  - (vii) Evaluating results of Audit
- XIV. Sampling Risk
- XV. Important terms

I. MEANING

Audit sampling refers to

- Application of audit procedures
- For less than 100% of items within a population relevant under audit,
- such that all the sampling units (i.e. all the items in the population)
- have an equal chance of being selected.

II. OBJECTIVES

To provide reasonable basis to draw a conclusion about the population from which the sample is selected

III KEY TERMS IN SAMPLING

Population	Sample design	Sample size	Sampling units
1.Entire set of data from which a sample is selected and about which the auditor wishes to draw conclusions. 2.The auditor should select sample items in such a way that the sample can be expected to be representative of the population. 3.All items in the population have an opportunity of being selected.	1.Consider the purpose of AP 2.Characteristics of population from which sample is drawn	1.Sufficient enough to reduce sampling risk	1.Individial items that make up the population 2.It is a selection from the population that is used as an extrapolation of the population. 3.The conclusion on the population is based on the AP applied on the sampling unit.

In planning the audit, the auditor makes judgements about the size of misstatements that will be considered material. These judgements provide a basis for:

a) Determining the nature, extent and timing of Risk Assessment procedure

b) Determining the nature, extent and timing of further audit procedures

c) Identifying and assessing the risk of material misstatement

The auditor has to apply his professional judgement in determining materiality, choosing appropriate benchmark and determining the level of benchmark.

IV. APPLICABILITY

Auditor decided to use sampling -Statistical/ non statistical sampling

Auditor decided not to use sampling - **Follow other standards**

V. CHARACTERISTICS OF POPULATION

(CAR)

1. APPROPRIATENESS

- The auditor will need to determine that the population from which the sample is drawn is appropriate for the specific audit objective.
- Appropriate -> population from which samples are drawn shall be relevant for the specific objective under audit.
- This is because when the samples are drawn, the AP are applied on the sample & conclusions are projected on the population.

E.g. If the auditor's obj is to test for overstatement of a/cs receivable, the population defined as the a/cs receivable listing. On the other hand, when testing for understatement of a/cs payable, the population would not be the a/cs payable listing, but rather subsequent disbursements, unpaid invoices, suppliers' statements, unmatched receiving reports, or other populations that would provide AE of understatement of a/cs payable

2. COMPLETENESS

- If the auditor intends to use the sample to draw conclusions about whether a control activity is operated effectively during the FR period, the population needs to include all relevant items i.e all the activities that form part of that relevant internal control, throughout the entire period.
- If population is complete in all respects, the conclusions drawn on the population will be considered to be reasonable.

3. RELIABLE

- The auditor performs audit procedures to ensure that the info upon which the audit sampling is performed is sufficiently complete & accurate. Auditor should obtain evidence about the reliability of population.

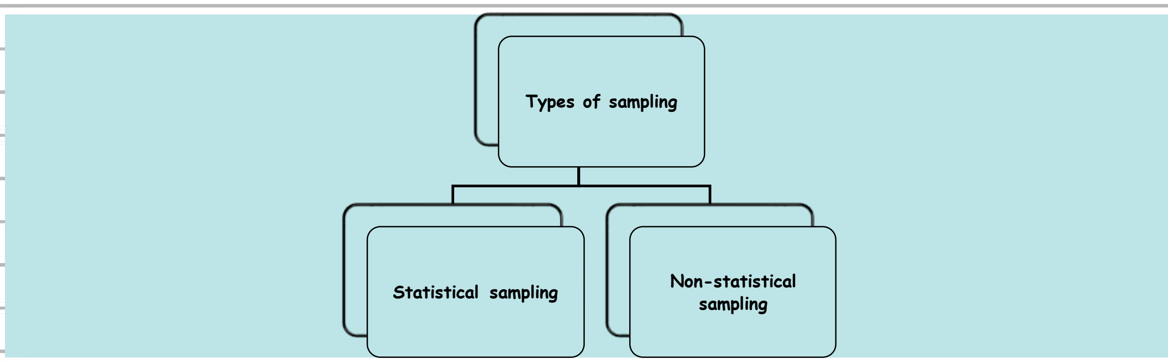
- If population is not reliable with respect to accuracy & source, the sample drawn will definitely not be relevant for the specific audit objective.

VI. SAMPLING UNIT

1. The individual items that make up the population are known as sampling units. The population can be divided into sampling units.
2. Audit procedures are applied on these units and the conclusions drawn from them are projected on the population.

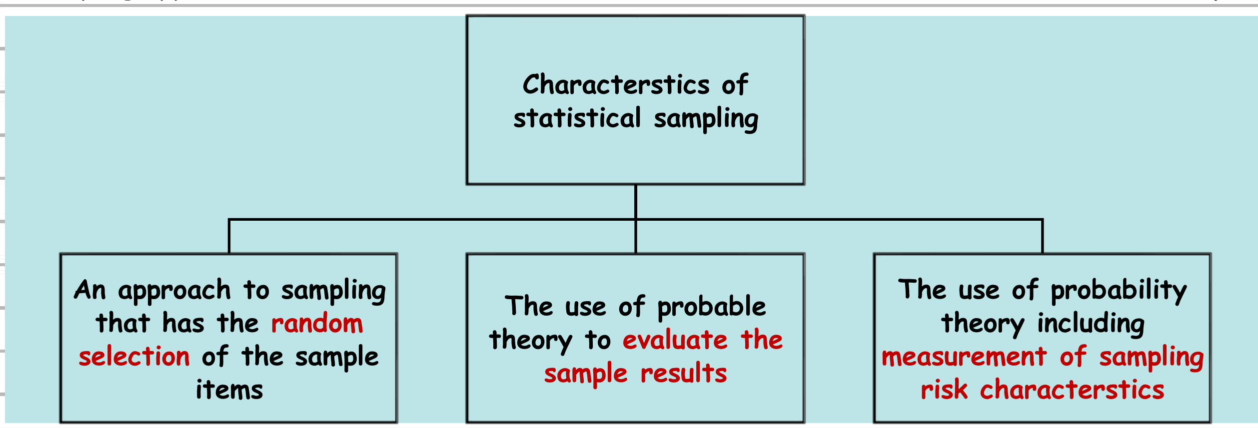
   Eg: If the auditor's objective were to test the validity of a/cs receivables, the sampling unit could be defined as customer balances or individual customer invoices. Auditor defines the sampling unit in order to obtain an efficient & effective sample to achieve the particular audit objectives.

VII. APPROACHES TO SAMPLING (TYPES OF SAMPLING)



Statistical sampling is an approach to sampling that has the random selection of the sample units; and the use of probability theory to evaluate sample results. Sample is chosen by applying certain mathematical and statistical methods.

A sampling approach that does not have the above features is considered as **Non-statistical sampling**.



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VIII. DIFFERENCE BETWEEN STATISTICAL AND NON-STATISTICAL SAMPLING

BASIS	STATISTICAL SAMPLING	NON - STATISTICAL SAMPLING
Probability	✓	✗
Bias	✗	✓
Accuracy	✓	✗
Scientific evaluation	✓	✗
Population	Large	Small
Representation	More	Less

IX. SAMPLING VS TRADITIONAL METHODS OF SAMPLING

1. The evidence available is not conclusive and the auditor always takes a calculated risk in giving his opinion. Even by 100% checking of the transactions, the auditor does not derive absolute satisfaction.
2. By adopting the sampling technique, the auditor only checks a part of the whole mass of transactions.
3. And he can put reliance on the internal controls and checks within the client's organisation because they provide the reliability of the records.
4. If the internal control is satisfactory in its design and implementation, a much smaller sample can give necessary reliability of the result he obtains.
5. On the other hand, if in certain areas controls are slack or not properly implemented, the auditor may have to take a much larger sample for getting satisfactory result.

   Eg: Mr. X may consider that in his estimation of stores valuation, an error of 2% may not be material; he also decides that he needs at least 98% reliability of the result.

X. THE FACTORS TO BE CONSIDERED FOR THE EXTENT OF CHECKING ON A SAMPLING

1. Size of the organisation under audit.
2. State of the internal control.
3. Adequacy and reliability of books and records.
4. Tolerable error range.
5. Degree of the desired confidence.

XI. ADVANTAGES OF STATISTICAL SAMPLING:

1. The amount of testing (sample size) does not increase in proportion to the increase in the size of the area (universe) tested.
2. The sample selection is more objective and thereby more defensible.
3. The method provides a means of estimating the minimum sample size associated with a specified risk and precision.
4. It provides a means for deriving a "calculated risk" and corresponding precision (sampling error) i.e. the probable difference in result due to the use of a sample in lieu of examining all the records in the group (universe), using the same audit procedures.
5. It may provide a better description of a large mass of data than a complete examination of all the data, since non-sampling errors such as processing and clerical mistakes are not as large.
6. It is widely accepted way of sampling as it is more scientific, without personal bias and the result of sample can be evaluated and projected in a more reliable way.

XII. STRATIFICATION AND VALUE WEIGHTED SELECTION:

STRATIFICATION	VALUE WEIGHTED SELECTION
1.Audit efficiency may be improved if auditor stratifies a population by dividing it into discrete sub-populations which have an identifying characteristics. **2.Objective** is to reduce the variability of items within each stratum & allow sample size to be reduced without increasing sampling risk. When performing TOD, population is often stratified by monetary value. 3.This allows greater audit effort to larger value items, as these items may be overstated. for e.g., when testing the allowance for doubtful a/cs in the valuation of a/cs receivable, balances may be stratified by age. 4.Results of samples drawn under each sub population are projected to that stratum. 5.To draw an opinion on the overall population, combine results of all stratums to check for possible deviation or ROMM. 6.Projected misstatements of each stratum will be combined to consider the possible effect of misstatement in the account balances and class of transactions E.g. 20% of the items in a population may make up 90% of the value of an account balance. Auditor may decide to examine a sample of these items.	1.When performing TODs, it may be efficient to identify the sampling unit as the individual monetary units that make up the population. 2.Selecting specific monetary units within the population for e.g., A/cs receivable balance, the auditor may then examine the items, individual balances, that contain those monetary units. 3.One benefit of this approach is that audit effort is directed to the larger value items because they have a greater chance of selection, & can result in smaller sample sizes. 4.This approach may be used in conjunction with the systematic method of sample selection & is most efficient when selecting items using random selection.

Results of this sample allow conclusion on 90% of value separately from remaining 10% (on which a further sample maybe taken or considered immaterial).	

XIII. SAMPLING PROCESS:

i. Sample design

↓

ii. Sample size

↓

iii. Sample selection methods

↓

iv. Audit procedures

↓

v. Nature and Cause of Deviations

↓

vi. Projecting Misstatements

↓

vii. Evaluating results of audit

i. SAMPLE DESIGN

When designing an audit sample,

i. The auditor's consideration includes the specific purpose to be achieved & the combination of AP that is likely to best achieve that purpose.

ii. Consideration of the nature of the AE sought and possible deviation or misstatement conditions or other characteristics relating to that AE will assist the auditor in defining what constitutes a deviation or misstatement and what population to use for sampling

iii. In fulfilling the requirement of SA 500 "Audit Evidence", when performing audit sampling, the auditor performs AP to obtain evidence that the population from which the audit sample is drawn is complete.

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ii. SAMPLE SIZE

1. Sample size sufficient to reduce sampling risk to an acceptably low level .
2. The level of sampling risk that the auditor is willing to accept affects the sample size required.
3. The lower the risk the auditor is willing to accept, the greater the sample size will need to be.

EXAMPLES OF FACTORS INFLUENCING SS FOR TOC :

1. An increase in extent to which the auditor's risk assessment takes into account relevant controls.
   - When the auditor's assessment of the **RoMM** at the assertion level includes an expectation of the operating effectiveness of controls, the auditor is required to perform **TOCs.**
   - Other things being equal, the greater the reliance the auditor places on the operating effectiveness of controls in the risk assessment, the greater is the extent of the auditor's **TOCs** (and therefore, the SS). Thus, **sample size will increase**.
2. If there is an increase in the tolerable rate of deviation. Then **sample size will decrease**, as lower the tolerable rate of deviation, larger the sample size needs to be. Tolerable error is the maximum error in the population that auditor is ready to accept in a given sample size.
3. When there is an increase in the expected rate of deviation of the population to be tested then **sample size will increase**, as higher the expected rate of deviation, larger the sample size needs to be
4. An increase in the auditor's desired level of assurance that the tolerable rate of deviation is not exceeded by the actual rate of deviation in the population will **increase the sample size**.
5. In case of large populations, the actual size of the population has little or NO effect on sample size. there will be **negligible effect** on sample size due to increase in the number of sampling units in the population.

EXAMPLES OF FACTORS INFLUENCING SS FOR TOC :

1. **The higher the auditor's assessment of RoMM, the larger the sample size needs to be**:
   - The auditor's assessment of the RoMM is affected by inherent risk and control risk.

   For e.g. if the auditor does not perform TOCs, the auditor's Risk assessment cannot be reduced for the effective operation of internal controls with respect to the assertion.
   - The more AE that is obtained from **TODs,** the **larger the sample size** will need to be. To reduce audit risk to an acceptably low level, the auditor needs a low detection risk and will rely more on substantive procedures.

2. **The more the auditor is relying on other substantive procedures** (TODs or substantive analytical procedures) to reduce to an acceptable level the detection risk regarding a particular population, the less assurance the auditor will require from sampling & therefore, **the smaller the sample size can be.**

3. **Increase in the auditor's desired level of assurance that** tolerable misstatement is not exceeded by actual misstatement in the population **will increase the sample size.**

4. **An increase in tolerable misstatement** will decrease the sample size as lower the tolerable misstatement, **the larger the sample size** needs to be.

5. **The greater the amount of misstatement** the auditor expects to find in the population, **the larger the sample size needs** to be in order to make a reasonable estimate of the actual amount of misstatement in the population.

6. **When stratification of the population** is appropriate **then sample size will decrease** as when there is a wide range (variability) in the monetary size of items in the population, it may be useful to stratify the population.

7. For large populations, **the actual size of the population** has **Little or NO effect on sample size**. There will be negligible effect on sample size due to number of sampling units in the population.

iii. SAMPLE SELECTION METHODS

1. Random Sampling
2. Systematic Sampling
3. Monetary Unit Sampling
4. Haphazard Sampling
5. Block Sampling

1. **Random Sampling:** includes two very popular methods which are discussed below–

(i) Simple Random Sampling:

- Each unit of the whole population e.g. purchase or sales invoice has an equal chance of being selected.
- It is Considered that random number tables are simple and easy to use and
- Also provide assurance that the auditors' bias does not affect the selection.

Each item in a population is selected by use of random no table either with a help of computer or picking up a number in a random way e.g. Random number generator.

This method is considered appropriate provided the population to be sampled consists of reasonably similar units and fall within a reasonable range. i.e. it is suitable for a homogeneous population having a similar range.

Eg: The population can be considered homogeneous, if say, trade receivables balances fall within the range of ₹ 55,000 to ₹ 2,25,000 and not in the range between ₹ 525 to ₹ 10,50,000.

(ii) Stratified Sampling:

- Dividing the whole population to be tested in a few separate groups called strata and taking a sample from each of them.
- Each stratum is treated as a separate population and if proportionate of items are selected from each of these stratums.
- The number of groups into which the whole population has to be divided is determined on the basis of auditor judgment.

E.g. In the above case, trade receivables balances may be divided into four groups as follows: -

1. Balances in excess of ₹ 10,00,000;
2. Balances in the range of ₹ 7,75,001 to ₹ 10,00,000;
3. Balances in the range of ₹ 5,50,001 to ₹ 7,75,000;
4. Balances in the range of ₹ 2,25,001 to ₹ 5,50,000;

- Highly diversified population,
- The stratified sampling is simply an extension of simple random sampling.

2. Interval Sampling or Systematic Sampling:

Is a selection method in which the no. of sampling units in the population is divided by the SS to give a sampling interval.

for e.g.: 50, and having determined a starting point within the first 50, each 50th sampling unit thereafter is selected.

- To minimise the effect of the possible known buyers through a pattern in the population, more than one starting point may be taken.
- The multiple random starting point is taken because it minimises the risk of interval sampling pattern with that of the population being sampled.

3. Monetary Unit Sampling:

It is a type of value-weighted selection in which sample size, selection and evaluation results in a conclusion in monetary amounts.

4. Haphazard sampling:

- In which the auditor selects the sample without following a structured technique. Although no structured technique is used, the auditor would nonetheless avoid any conscious bias or predictability

E.g.: avoiding difficult to locate items, or always choosing or avoiding the first or last entries on a page.

- **Haphazard sampling has** no structured approach, does not involve judgement & does not even use the random no. tables.

5. **Block Sampling:**
   - This method involves selection of a block(s) of contiguous items from within the population.
   - Block selection cannot ordinarily be used in audit sampling because

   most populations are structured & have similar characteristics to each other, but different characteristics from items elsewhere in the population.

   Eg: Take the first 200 sales invoices from the sales day book in the month of September, alternatively take any four blocks of 50 sales invoices.

iv. PERFORMING AUDIT PROCEDURES

i. The auditor shall perform AP, appropriate to the purpose, on each item selected.

ii. If the audit procedure is not applicable to the selected item, the auditor shall perform the procedure on a Replacement item.

iii. If the auditor is unable to apply the designed AP, or suitable alternative procedures, to a selected item,

iv. the auditor shall treat that item as a **Deviation** in case of TOCs, or a **Misstatement**, in the case of TODs.

If AAP is also not possible:-

Test Of Control - deviation

Test Of Detail – Misstatement

v. NATURE AND CAUSE OF DEVIATIONS AND MISSTATEMENTS:

COMMON FEATURE:

1. In analysing the deviations and misstatements identified, The auditor may observe that many have a **common feature**, for example, type of transaction, location, product line or period of time.
2. In such circumstances, the auditor may decide to identify all items in the population. that possess the **common feature**, and **extend AP** to those items.

INVESTIGATION:

1. In addition, such deviations or misstatements may be intentional, and may indicate the possibility of fraud.
2. The auditor shall **investigate** the nature and causes of any deviations or misstatements identified, and
3. Evaluate their possible effect on the purpose of the AP & on other areas of the audit.

In the extremely rare circumstances when the auditor considers a misstatement or deviation discovered in a sample to be an anomaly, **the auditor shall obtain a** high degree of certainty **that such misstatement or deviation** is not representative of the population.

vi. PROJECTION OF MISSTATEMENTS:

i. The auditor is required to **project misstatements** for the population to obtain a broad view of the scale of misstatement but this projection may not be sufficient to determine an amount to be recorded.

ii. When a **misstatement** has been established as an **anomaly**, it may be excluded when projecting misstatements to the population. However, the effect of any such misstatement, if uncorrected, still needs to be considered in addition to the projection of the non-anomalous misstatements.

iii. For **TOD**, the auditor shall project misstatements found in the sample to the population whereas for **TOC**, no explicit projection of deviations is necessary since the **sample deviation rate is also the projected deviation rate** for the population as a whole.

vii. EVALUATION OF SAMPLE RESULTS:

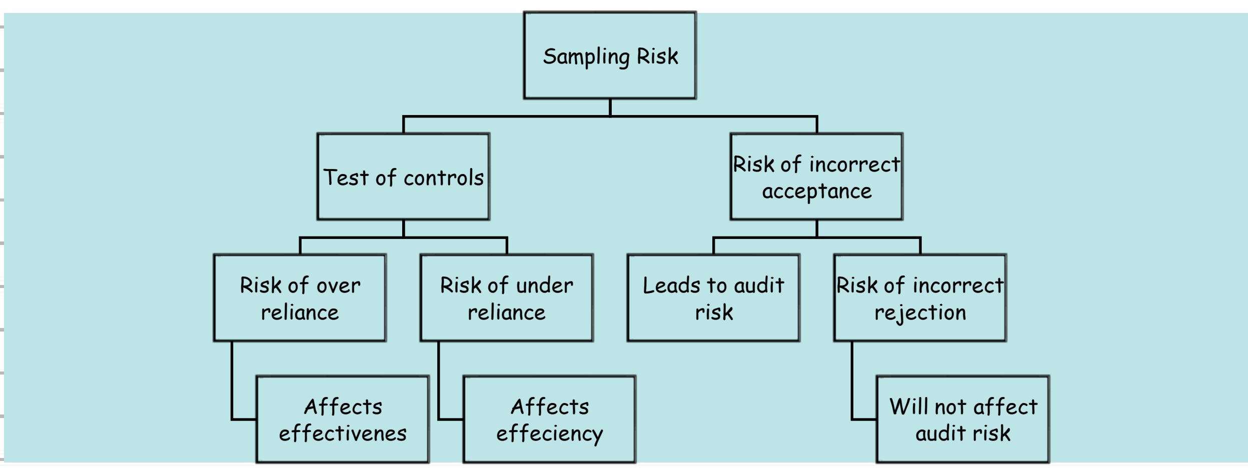
The auditor shall evaluate-

(a) The results of the sample; and

(b) Whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

XIV. SAMPLING RISK

Risk- Sampling and Non sampling risk



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Non-Sampling risk:

Eg:

- Inappropriate audit procedures
- Misinterpretation of AE
- Sources
    - Human mistake
    - Misinterpreting sample result
    - Relying on erroneous information

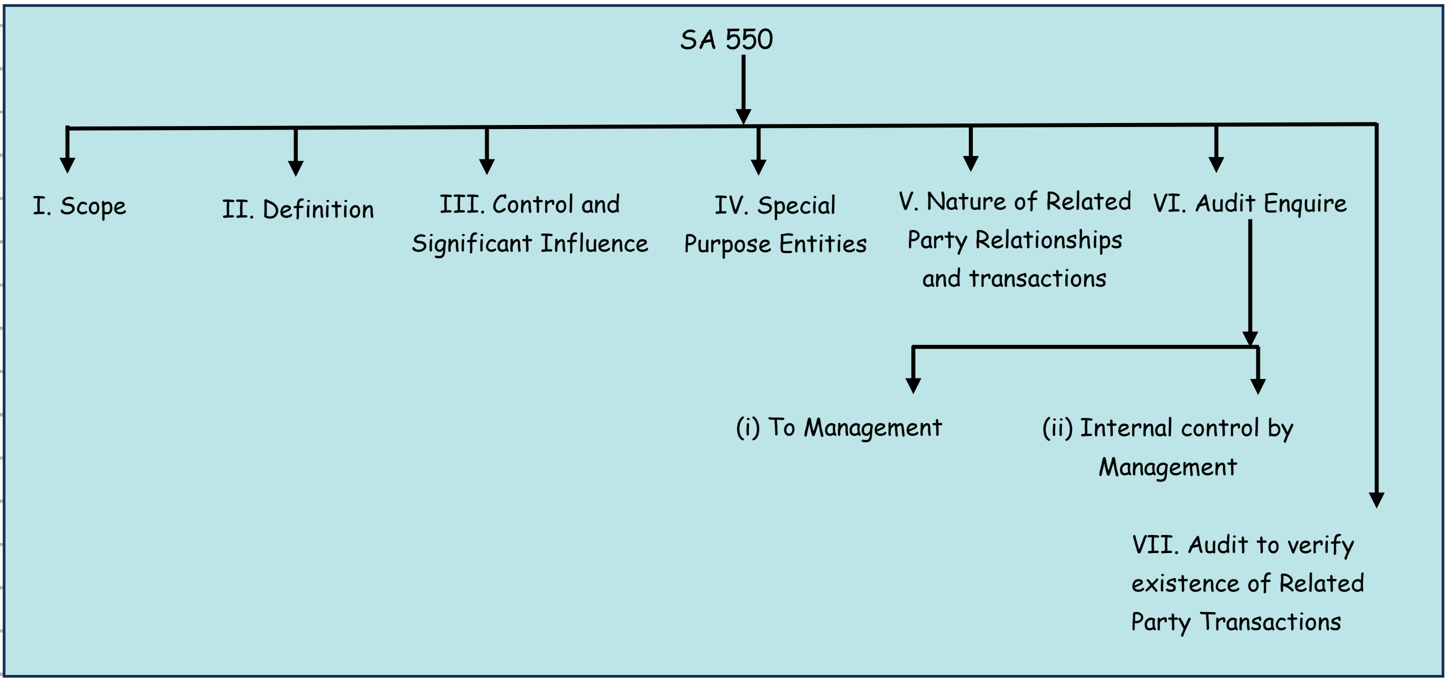
XV. IMPORTANT TERMS

1. **Stratification** – The process of dividing a population into sub-populations, each of which is a group of sampling units which have similar characteristics (often monetary value).

2. **Tolerable misstatement** – A monetary amount set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the monetary amount set by the auditor is not exceeded by the actual misstatement in the population.

3. **Tolerable rate of deviation** – A rate of deviation from prescribed internal control procedures set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the rate of deviation set by the auditor is not exceeded by the actual rate of deviation in the population.

SA 550 RELATED PARTIES



I. SCOPE

SA 550 deals with the auditor's responsibilities regarding related party relationships and transactions when performing an audit of Financial Statement. Specifically, it applies in relation to the risk of material misstatement associated with related party relationships and transactions.

II. Definition of Related party:

1. A party that is defined in the Applicable Financial Reporting Framework (AFRF) or
2. Where Applicable Financial Reporting Framework (AFRF) establishes minimal or no RP requirements;

a. A person or other entity having **control or significant influence** directly or indirectly through one or more intermediaries over the reporting entity.

b. Another entity over which the reporting entity **has control or significant influence**, directly or indirectly, through one or more intermediaries.

c. Another entity that is under the common control over the reporting entity through having
   - Common controlling ownership
   - Owners who are close family members
   - Common key management

However, 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.

III. Control & Significant influence:

1. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.
2. Significant influence which may be gained by share of ownership, statute or agreement, is the power to participate in the financial and operating policy decisions of an entity but is not in control over those policies.

The existence of the following relationships can indicate the presence of control or significant influence:
1. Direct/ indirect equity holdings or other financial interests in the entity
2. The entity's holdings of direct/indirect equity holdings or other financial interest in other entities
3. Being part of Those Charged With Governance (TCWG) or Key Management Personnel
4. Being a close family member of (3)
5. Having significant business relationship with (3)

IV. Meaning of Special Purpose Entities:

A special-purpose entity may be a related party of the entity because the entity may in substance control it, even if the entity owns little or none of the special- purpose entity's equity.

V. Nature of related party relationships and transactions:

Many related party transactions are in the normal course of business. In such circumstances they may carry no higher ROMM of FS than similar transactions with unrelated parties.
However, in some cases, the nature of the related party relationships and transactions give rise to higher ROMM of the FS than transactions with unrelated parties.

For example
(A) Related parties may operate through 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 summarizing 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 with no exchange of consideration.

VI. (i) The auditor shall inquire the management regarding:

1. The identity of the entity's related parties, including changes from the prior period.
2. The nature of the relationships between the entity and these related parties
3. Whether the entity entered into any transactions with these related parties and if so, the type and purpose of the transactions.

(ii) The auditor shall enquire the management and others within the entity, and perform other RAP considered appropriate, to obtain an understanding of the controls, if any, that the management has established to:

1. Identify, account for, and disclose related party relationships and transactions in accordance with the Applicable Financial Reporting framework (AFRF).
2. Authorise and approve significant transactions and arrangements with Related parties, and
3. Authorise and approve significant transactions and arrangements outside the normal course of business.

VII. How can an auditor verify the existence of related party relationships and transactions? [SRI CLIPS CCC]

He may inspect the following records or documents that may provide information about related party relationships and transactions. For example,

1. Entity income tax returns
2. Information supplied by the entity to regulatory authorities.
3. Shareholder registers to identify the entity's principal shareholder.
4. Statement of conflicts of interest from management and Those Charged With Governance
5. Records of the entity's investments
6. Contracts with and agreements with the Key Management Personnel and Those Charged With Governance
7. Significant contracts and agreements not in the ordinary course of business
8. Specific invoices and correspondence from the entity's professional advice
9. Life insurance policies acquired by the entities.
10. Internal auditor's report
11. Significant contracts re negotiated with the entity.
12. Documents filed with entity's securities regulator

SA 560 – SUQSEQUENT EVENTS

SA 560

- I. Subsequent Event
  II. Objectives
  Meaning:
  Date of FS Issued
- III. Events occurring btw the date of the FS and the date
- IV. Facts which become known to the auditor after the date of the AR but before the date of the FS are issued
- V. Facts which become known to the auditor after the FS have been issued

I. SUBSEQUENT EVENT

Subsequent Events are those events that occurred btw the date of FS and the date of AR and the facts become known to the auditor after the date of AR.

FS may be affected by certain events that occur after the date of the FS. Many FRF specifically refer to such events. Such FRF ordinarily identify two types of events: -

- Those that provide evidence of conditions that existed at the date of FS
- Those that provide evidence of conditions that arose after the date of FS

Examples of events providing evidence of conditions that existed at the date of the FSs

- Declaration of insolvency of a major debtor of the entity btw the date of FSs and the date of AR providing evidence on the recoverability of the money due from debtor as on date of the FSs.
- Settling a legal claim outside the court at a reduced amount btw the date of FSs and the date of AR for which provision has already been made in FSs. It provides evidence on adjustment in provision amount already made in FSs, if any.

Examples of events providing evidence of conditions that arose after the date of the FS

- Issue of new share capital.
- Planned merger of the company.
- Destruction of substantial inventories due to fire btw the date of the FS and the date of AR.

Subsequent Events

- Events occurring between the date of the Financial Statements and the date of the auditor's report
- Facts which become known to the auditor after the date of the auditor's report but before the date of the financial statements are issued
- Facts which become known to the auditor after the FS have been issued

II. OBJECTIVES OF THE AUDITOR IN ACCORDANCE WITH SA 560

i) Obtain SAAE about whether the events occurring btw the date of the FS and the date of the AR that require adjustment of, or disclosure in, the FS are appropriately reflected in the FS and,

ii) Respond appropriately to the facts that become known to the auditor after the date of the AR, that, had they been known to the auditor at that date, may have caused the auditor to amend the audit report.

CASE I

III. EVENTS OCCURRING BTW THE DATE OF THE FS & THE DATE OF THE AR

Audit Procedures relating to events occurring btw the date of the FSs and the date of the AR

The auditor shall perform audit procedures designed to obtain sufficient and appropriate audit evidence that all events occurring btw the date of the FS and the date of the audit report, that require adjustment of, or disclosure, in FS have been identified.

- Obtain an **understanding** of any procedures management has established to ensure that subsequent events are identified.
- **Inquiring** of management & Those Charged With Governance as to whether any subsequent events have occurred which affect the FS [chart below]
- Reading **minutes** if any, of meetings of entity's owners, managements, TCWG that have been held after the date of the FS and inquiring if such minutes of the meetings are not yet available.

Reading the entity's latest subsequent **interim** FS. Also read the **budgets**.

When as a result of the procedures performed, the auditor identifies events that require adjustments or disclosures in the FS , the auditor shall determine whether each such event is appropriately reflected in those FS.

The auditor shall request the management and where appropriate TCWG to provide a written representation [SA 580 Written Representation] that all events occurring subsequent to the date of the FS and for which the Applicable Financial Reporting Framework requires adjustments or disclosures have been adjusted or disclosed.

Inquiry with management & TCWG

New commitments borrowings and Guarantees	Sale or acquisition of assets	Developments regarding contingencies
Assets have been appropriated by govt or destroyed	Unusual accounting adjustments	Appropriateness of accounting policies used in the FS

DATE THE FINANCIAL STATEMENTS ARE ISSUED

Meaning of "Date the FS are issued":

- It reflects the date that the AR and audited FS are made available to third parties.
- The date the FS are issued generally depends on the regulatory environment of the entity.
- In some circumstances, the date the FS are issued may be the date that they are filed with a regulatory authority.
- Since audited FS cannot be issued without an AR,
  - the date that the audited FS are issued must not only be at or later than the date of the AR,
  - but must also be at or later than the date the AR is provided to the entity.

CASE II

IV. FACTS WHICH BECOME KNOWN TO THE AUDITOR AFTER THE DATE OF THE AR BUT BEFORE THE DATE OF THE FS ARE ISSUED:

After the FSs have been issued, the auditor has **NO OBLIGATION** to perform any audit procedures regarding such FS. If after the issue of the FS, a fact becomes known to the auditor, which may have caused the auditor to amend the AR, the auditor shall:

a) Discuss the matter with management and where appropriate TCWG
b) Determine whether the FS needs amendments and if so,
c) Inquire how the management intends to address the matter in the FSs.

Auditor identified the subsequent events & informed the management

- Before the date of FS are issued → Management response
  - Management amends
  - Management does not amend the FS
- After the date of FS are issued → Management response
  - Management amends
  - Management does not amend the FS

Before the date of FS are issued:

RESPONSE BY THE MANAGEMENT

Management Amends the FS → Carry out audit procedures → Obtain Sufficient & appropriate AE

Management does not amend the FS

Audit Report not yet provided	Audit Report provided	Nevertheless, subsequently issued without amendments
Modify the opinion as per SA 705	Notify Management & TCWG not to issue FS to 3rd parties	Auditor to take appropriate actions to prevent reliability on Audit Report

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CASE III

V. FACTS KNOWN TO THE AUDITOR AFTER THE FSS HAVE BEEN ISSUED:

After the FSs have been issued, the auditor has **NO OBLIGATION** to perform any audit procedures regarding such FS. If after the issue of the FS, a fact becomes known to the auditor, which may have caused the auditor to amend the AR, the auditor shall:

a) Discuss the matter with management and where appropriate TCWG
b) Determine whether the FS needs amendments and if so,
c) Inquire how the management intends to address the matter in the FSs.

After the FS are issued
RESPONSE BY THE MANAGEMENT

Management amends the FS	Management does not take necessary steps
• Carry out audit procedures • Inform the situation to already issued users of FS • Obtain amended FS • Provide new audit report • Mention in EMP & OMP as per SA 706	• Take appropriate action to seek prevent reliance on AR

SA 570 "GOING CONCERN"

SA 570

- I. Meaning
- II. Significance
- III. Deals with
- IV. Objectives

- V. Responsibility For assessment for entity's ability to continue as GC
- VI. Responsibility of Auditor

- VII. RAP and related activities (SA 315)
- VIII. Examples of events or conditions that may cast doubt on GC

- IX. Evaluating management's assessment
- X. Additional AP
  - Examples of AP

- XI. Auditor's conclusions
- XII. Adequacy of disclosures
  - Material uncertainty exists
  - No Material uncertainty exists

- XIII. Implications
  1. Use of Going Concern appropriate
  2. Material uncertainty exists
  3. Management unwilling to extend assessment

I. Meaning of "Going concern":

1. Going concern is one of the fundamental accounting assumptions. The enterprise is normally viewed as a GC, that is, as continuing in operation for the foreseeable future.
2. Under the going concern basis of accounting, the FS are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future.
3. General purpose FS are prepared using the going concern basis of accounting, unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so.

II. Significance of GC

1. The significance of GC is due to its effect on preparation of FS.
2. Ability or otherwise of an enterprise to be viewed as GC affects its preparation of FS.
3. When the use of the GC basis of accounting is appropriate, assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business.
4. When an enterprise is not viewed as a GC, the FS are prepared on liquidation basis.
5. For example, inventories may need to be written down as these may be sold for a lower price. Assets may have to be recorded at the likely prices they will fetch.

III. SA 570 on "Going concern" deals with:

The auditor's responsibilities in the audit of FS relating to GC	The implications for the auditor's report

IV. Objectives of the auditor

To obtain SAAE regarding , and conclude on the appropriateness of the management's use of the GC basis of accounting in the preperation of FS	To conclude based on the AE obtained, whether a material unceratinty exists related to events or conditions that may cast a significant doubt on the entity's ability to continue as GC	To report in accordance with this SA

V. Responsibility for assessment for the entity's ability to continue as GC:

Management has to make an assessment of the entity's ability to continue as GC involves making a judgement, at a particular point in time, about inherently uncertain future outcomes of events or conditions.

The following factors are relevant for the judgement:

1. The degree of uncertainty associated with an outcome of an event.
2. The size and complexity of the entity, the nature and conditions of the business and the degree to which it is affected by external factors.
3. Any judgement about the future based on info available at the time at which the judgement is made.

VI. Responsibility of the Auditor:

1. The auditor's responsibilities are to obtain SAAE regarding and conclude on the appropriateness of management's use of the going concern basis of accounting in the preparation of the FS and to conclude, based on the AE obtained, whether a material uncertainty exists about the entity's ability to continue as a GC.

2. These responsibilities exist even if the FRF used in the preparation of the FS does not include an explicit requirement for management to make a specific assessment of the entity's ability to continue as a GC.
3. However, as described in SA 200, the potential effects of inherent limitations on the auditor's ability to detect MMs are greater for future events or conditions that may cause an entity to cease to continue as a GC.
4. The auditor cannot predict such future events or conditions.
5. Accordingly, the absence of any reference to a material uncertainty about the entity's ability to continue as a GC in an auditor's report cannot be viewed as a guarantee as to the entity's ability to continue as a GC.

VII. Risk assessment procedures and related activities (SA315)

Assessment performed: The auditor shall discuss the assessmnet with the mgt and determine whether mgt has identified events or conditions affecting the Going concern of the entity

Assessment not performed: The auditor shall discuss with the management the basis for the intended use of GC basis of accounting, and enquire the management whether events or conditions exist, that individually/ collectively cast a significant doubt on the entity's ability to continue as going concern

VIII. Examples of events or conditions that may cast doubt on G

The following are examples of events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a GC

Financial events or conditions

i. Net liability or net current liability position
ii. Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment; or excessive reliance on short-term borrowings to finance long-term assets
iii. Indications of withdrawal of financial support by creditors
iv. Negative operating cash flows indicated by historical or prospective financial statements
v. Adverse key financial ratios
vi. Substantial operating losses or significant deterioration in the value of assets used to generate cash flows
vii. Arrears or discontinuance of dividends
viii. Inability to pay creditors on due dates
ix. Inability to comply with the terms of loan agreements
x. Change from credit to cash-on-delivery transactions with suppliers
xi. Inability to obtain financing for essential new product development or other essential investments

Operating events or conditions

i. Management intentions to liquidate the entity or to cease operations
ii. Loss of key management without replacement
iii. Loss of a major market, key customer(s), franchise, license, or principal supplier(s)
iv. Labour difficulties
v. Shortages of important supplies
vi. Emergence of a highly successful competitor

Other events or conditions

i. Non-compliance with capital or other statutory or regulatory requirements, such as solvency or liquidity requirements for financial institutions
ii. 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
iii. Changes in law or regulation or government policy expected to adversely affect the entity
iv. Uninsured or underinsured catastrophes when they occur

IX. Evaluating management's assessment

The auditor shall evaluate management's assessment of the entity's ability to continue as a GC.

It is not the auditor's responsibility to rectify the lack of analysis by management. In some circumstances, however, the lack of detailed analysis by management to support its assessment may not prevent the auditor from concluding whether management's use of the going concern basis of accounting is appropriate in the circumstances.

For example, when there is a history of profitable operations and a ready access to financial resources, management may make its assessment without detailed analysis. In this case, the auditor's evaluation of the appropriateness of management's assessment may be made without performing detailed evaluation procedures if the auditor's other audit procedures are sufficient to enable the auditor to conclude whether management's use of the GC basis of accounting in the preparation of the FS is appropriate in the circumstances.

In other circumstances, evaluating management's assessment of the entity's ability to continue as a GC, may include an evaluation of the process management followed to make its assessment, the assumptions on which the assessment is based and management's plans for future action and whether management's plans are feasible in the circumstances.

In evaluating management's assessment of the entity's ability to continue as a GC, the auditor shall cover the same period as that used by management to make its assessment as required by the AFRF or by law or regulation if it specifies a longer period. If management's assessment of the entity's ability to continue as a GC covers less than twelve months from the date of the financial statements, the auditor shall request management to extend its assessment period to at least twelve months from that date.

X. Additional audit procedures

If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a GC, the auditor shall obtain SAAE to determine whether or not a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a GC through performing additional audit procedures, including consideration of mitigating factors.

These procedures shall include: -

a) Where management has not yet performed an assessment of the entity's ability to continue as a going concern, requesting management to make its assessment.

b) Evaluating management's plans for future actions in relation to its going concern assessment, whether the outcome of these plans is likely to improve the situation and whether management's plans are feasible in the circumstances.

c) Where the entity has prepared a cash flow forecast, and analysis of the forecast is a significant factor in considering the future outcome of events or conditions in the evaluation of management's plans for future actions:

i. Evaluating the reliability of the underlying data generated to prepare the forecast; and
ii. Determining whether there is adequate support for the assumptions underlying the forecast.

d) Considering whether any additional facts or information have become available since the date on which management made its assessment.

e) Requesting written representations from management and, where appropriate, TCWG, regarding their plans for future actions and the feasibility of these plans.

EXAMPLES OF AUDIT PROCEDURES:

1. Analysing and discussing cash flow, profit and other relevant forecasts with management
2. Analysing and discussing the entity's latest available interim financial statements
3. Reading the terms of debentures and loan agreements and determining whether any have been breached
4. Reading minutes of the meetings of SH, TCWG and relevant committees for reference to financing difficulties
5. Inquiring of the entity's legal counsel regarding the existence of litigation and claims and the reasonableness of management's assessments of their outcome and the estimate of their financial implications
6. Confirming the existence, legality and enforceability of arrangements to provide or maintain financial support with related and third parties and assessing the financial ability of such parties to provide additional funds
7. Evaluating the entity's plans to deal with unfilled customer orders
8. Performing audit procedures regarding subsequent events to identify those that either mitigate or otherwise affect the entity's ability to continue as a GC
9. Confirming the existence, terms and adequacy of borrowing facilities
10. Obtaining and reviewing reports of regulatory actions
11. Determining the adequacy of support for any planned disposals of assets

The auditor shall evaluate whether sufficient appropriate audit evidence has been obtained regarding, and shall conclude on, the appropriateness of management's use of the GC basis of accounting in the preparation of the FS.

Based on the AE obtained, the auditor shall conclude whether, in the auditor's judgment, a material uncertainty exists related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.

A material uncertainty exists when the magnitude of its potential impact and likelihood of occurrence is such that, in the auditor's judgment, appropriate disclosure of the nature and implications of the uncertainty is necessary.

XII. Adequacy of disclosures

Material uncertainty exists

If the auditor concludes that management's use of the GC basis of accounting is appropriate in the circumstances but a material uncertainty exists, the auditor shall determine whether the FS:

a) Adequately disclose the principal events or conditions that may cast significant doubt on the entity's ability to continue as a GC and management's plans to deal with these events or conditions and

b) Disclose clearly that there is a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a GC and,

Therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business.

No material uncertainty exists

If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a GC but, based on the AE obtained the auditor concludes that no material uncertainty exists, the auditor shall evaluate whether, in view of the requirements of the AFRF the FS provide adequate disclosures about these events or conditions.

XIII. Implications for the auditor's report

Case I . If use of going concern basis of accounting is inappropriate: -

If the Financial Statement (FS) have been prepared using the going concern basis of accounting, but in the auditor's judgement, management's use of the going concern basis of accounting in the preparation and presentation of Financial Statement (FS) is inappropriate, **the auditor shall express an adverse opinion.**

Case II. If the use of going concern basis of accounting is appropriate, but a material uncertainty exists: -

Adequate disclosure is made in the FS	Adequate disclosure of material uncertainty is not made in the FS
• Auditor shall express an **unmodified opinion** & the auditor's report shall include a seperate section under the heading "Material uncer atinty relating to going concern" • Draw attention to the note in the FS that discloses such matters. • State that these events or conditions indicate that **a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern** and that the auditor's opinion is not modified in respect of the matter.	• The auditor shall express a **qualified/ adverse opinion** (SA 705). • Express a Qualified or adverse opinion, as appropriate in accordance as per SA705 • In the basis for Qualified(adverse) opinion section, state that **a material uncertainty exists that may cast a significant doubt on the going concern** and the FS does not adequately disclose this matter.

Case III. Management unwilling to make or extend its assessment: -

The auditor shall consider the implications for the audit report- **Qualified opinion or Disclaimer of opinion** maybe appropriate, because it may not be possible to obtain SAAE regarding management's use of Going concern basis of accounting in the preparation of FS.

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SA 580 WRITTEN REPRESENTATION

Meaning of Written Representation:

SA 580- Written representations deals with the auditor's responsibility to obtain written representations from management and, where appropriate,

Objective of auditor:

I. To obtain Written Representation

- To obtain WR from management and TCWG that they believe that they have fulfilled their **responsibility** for the preperation of FS and for the completeness of information provided to the auditor

II. To support other Audit Evidence

- To support other AE relevant to the FS or specific assertions in the FS by means of WR, if determined by the auditor or required by other SAs.

III. To respond appropriately

- To respond appropriately for the written representations provided by the management and where appropriate TCWG or,
  if the mgmt or TCWG do not provide the WR provided by the auditor.

Although Written representations provide necessary audit evidence, they do not provide sufficient appropriate audit evidence on their own (**MCQ-MAY'25**) about any of the matters with which they deal.

I. Written Representations about management's responsibilities

It involves confirmation of fulfilment of management's responsibilities in:

1. Preparation of the FS
2. Information provided and completeness of transactions.

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Why is written representation about management's responsibilities necessary?

This is because the auditor is not able to judge solely on other AE whether mgmt has P&P the FS and provided info to the auditor on the basis of the agreed acknowledgement and understanding of its responsibilities.

This is particularly appropriate when:

1. Those who signed the terms of the audit engagement on behalf of the entity no longer have the relevant responsibilities
2. The terms of Audit engagement was prepared in the previous year
3. There is any indication that the management misunderstands those responsibilities
4. Changes in circumstances make it appropriate to do so.

Management's responsibilities shall be described in the **"Written representations required about management responsibilities"** in the manner in which these responsibilities are described in the terms of the audit engagement.

In some cases, however, management may decide to make inquiries of others who participate in **P&P** of the FS and assertions therein, including individuals who have specialized knowledge relating to the matters about which WR are requested.

Such individuals may include:

1.An actuary responsible for actuarially determined accounting measurements.

2.Staff engineers who may have responsibility for and specialized knowledge about environmental liability measurements.

3.Internal counsel who may provide information essential to provisions for legal claims.

II. Other Written Representations

May supplement but do not form part of the Written Representation relating to management's responsibilities.
They may include representations about the following: -

1.Whether the selection and application of Accounting policies are appropriate and

2.Whether matters such as the following, where relevant under the AFRF, have been recognized, measured, presented or disclosed in accordance with that framework:

i) Plans or intentions that affect the carrying value of asset

ii) Liabilities, both actual or contingent

iii) Title to, or control over the assets, the leins or encumbrances on assets, and assets pledged as collateral

iv) Aspects of laws, regulations and contractual agreements that may affect the FS including non-compliance

DATE OF WRITTEN REPRESENTATION:

The date of the WR should be as near as practicable but not after, the date of the auditor's report on the FS. The WR shall be for all the FS and the period(s) referred to in the auditor's report.

III. To respond appropriately

(If provided, he will check the reliability. If not provided, what should auditor do?)

Doubts as to the reliability

If the auditor has concerns about the competence, integrity, ethical values or diligence of management, or about its commitment to, or enforcement of these, the auditor shall determine the effect of such concerns on the reliability of the representations and audit evidence in general.

In particular, if the WR are inconsistent with the other AE, the auditor shall perform audit procedures to attempt to resolve the matter. If the matter remains unresolved, the auditor shall reconsider the assessment and shall determine the effect of such concerns on the AE.
If the auditor concludes that the WR are not reliable,

The auditor shall take appropriate actions: **SA705- Disclaimer of opinion**

If Requested WR not provided: -

The auditor shall:

1. Discuss the matter with the management
2. Re-evaluate the integrity of the management
3. Take appropriate actions, including determining the possible effect on the opinion in accordance with SA 705 having regard to the **Disclaimer of opinion**.

DISCLAIMER OF OPINION INCASE OF:

1. The auditor concludes that there is sufficient doubt about the Integrity of management such that the **WR** about management fulfilling its responsibilities regarding preparation of FS and about information provided and completeness of transactions are not reliable;

2. Management does not provide the written representations relating to fulfilling its responsibilities regarding preparation of FS and about information provided and completeness of transactions.

SA 450 "EVALUATION OF MISSTATEMENTS IDENTIFIED DURING AUDIT"

SA 450

- I. Objective
- II. Accumulation of misstatements
- III. Consideration of identified misstatements
- IV. Communication and correction of misstatements
- V. Evaluating the effect of uncorrected misstatements
- VI. Communication TCWG (SA 260)
- VII. Written Representation (SA 580)
- VIII. Disclosures

I. Objective of the auditor is to evaluate:

- The effect of identified misstatements on the audit
- The effect of uncorrected misstatements, if any, on the FS

II. Accumulation of misstatements identified during the audit

The auditor shall accumulate misstatements other than that is clearly trivial. A misstatement may arise from a variety of factors. Examples:

- An inaccuracy in gathering or processing data
- Omission of an amount or disclosure
- Entity wrongly capitalised an expense overstating the profits

III. Consideration of identified misstatement as the audit

The auditor shall determine whether audit strategy and audit plan needs to be revised if:

a. The nature of identified misstatements and the circumstances of their occurrence indicate that other misstatements may exist that, when aggregated with misstatements accumulated during the audit could be material or,

b. The aggregate of misstatements accumulated during the audit approaches materiality determined in accordance with SA 320

The auditor may request management to examine a class of transactions, account balance or disclosure (ABCD) , in order for management to understand the cause of a MM identified by the auditor, perform

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procedures to determine the actual amount of MM in the ABCD and to make appropriate adjustments to the FS. Such a request maybe made, for eg: Based on Auditor's projection of MM (SA 530)

If at the auditor's request, management has examined account balance, class of transactions or disclosure (ABCD) and corrected MM that were detected, the audit shall perform Additional audit procedures to determine whether MM remain.

IV. Communication and Correction of Misstatements:

The auditor shall communicate on a timely basis all misstatements accumulated during the audit with the appropriate level of management, unless prohibited by law or regulation. The auditor shall request management to correct those misstatements. Timely communication of misstatements to the appropriate level of management is important as it enables management to evaluate whether the items are misstatements, inform the auditor if it disagrees and take action as necessary.

The correction by management of all misstatements, including those communicated by the auditor, enables management to maintain accurate accounting books and records and reduces the risks of material misstatement of future financial statements because of the cumulative effect of immaterial uncorrected misstatements related to prior periods.

- If management refuses to correct a misstatement
- The auditor shall obtain an understanding of management's reasons for not making the corrections and shall take that understanding into account when
- Evaluating whether the FS as a whole are free from material misstatements

V. Evaluating the effect of uncorrected misstatements

The auditor shall determine whether uncorrected misstatements are material, individually or in aggregate. In making this determination, the auditor shall consider:-

a) The size and nature of the misstatements, both in relation to particular classes of transactions, account balances or disclosures and the financial statements as a whole, and the particular circumstances of their occurrence and

b) The effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole.

VI. Communication with TCWG [SA 260]

The auditor shall communicate with TCWG regarding uncorrected Misstatements and the effect that they individually or in aggregate may have an opinion in the AR, unless prohibited by law or regulation. The auditor shall request that the MM be corrected.

The auditor shall also communicate with TCWG the effect of uncorrected MM related to the prior periods on the relevant ABCD and the FS as a whole.

VII. Written Representation [SA 580]

The auditor may request from management and appropriate TCWG whether they believe the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the FS as a whole. A summary of such items shall be included in WR.

VIII. Documentation regarding Misstatements [SA 230]

Audit documentation shall include:

1. The amount below which misstatements would be regarded as clearly trivial
2. All misstatements accumulated during the audit and whether they have been corrected
3. The auditor's conclusion as to whether the uncorrected misstatements are material individually or aggregate, and the basis for the conclusion.

SA 600 "USING THE WORK OF ANOTHER AUDITOR"

SA 600

- I. Definitions
  - (i) PA
  - (ii) OAs
  - (iii) Component
- II. Procedure by PA
- III.
  - (i) Sec 128(1)
  - (ii) Sec 128(2)
  - (iii) Sec 143(8)

I. DEFINITIONS

Principal Auditor	Means the auditor with responsibility for reporting on the FI of an entity when that FI includes the FI of one or more components audited by anOA.
Other Auditor	Means the auditor, other than the PA, with responsibility for reporting on the FI of a component which is included in the FI audited by the PA.
Component	Means the division, branch, subsidiary, Joint venture, associated enterprise, or other entity whose FI is included in the FI audited by the PA.

II. PROCEDURES BY PRINCIPAL AUDITOR:

The PA should perform procedures to obtain sufficient and appropriate AE, that the work of the OA is adequate for the PA's purposes.

The principal should ordinarily perform the following procedures when he is using the work of anOA.

a) Advise the OA of the use that is to be made of the OA's work and report and make sufficient arrangements for coordination of their efforts at the planning stage of the audit. The PA would inform the OA of matters such as are requiring special considerations, procedures for the identification of inter component transactions that may require disclosure, and the time table for the completion of audit.

b) Advise the OA about the significant accounting, auditing and other reporting requirements and obtain representation as to compliance with them.

The PA might discuss with the OA the audit procedures applied or review a written summary of the audit procedures and the findings which maybe in the form of completed checklist or questionnaire.

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III. SEC 128(1) OF THE COMPANIES

Every company shall prepare and keep at its registered office, BoA and other relevant books and papers and FS for every financial year which give a true and fair view of the state of affairs of the company, including that of its branch office or offices. Such books shall be kept on accrual basis and according to double entry system of accounting.

All or any of the BoA can be kept in such other place in India as the BoD may decide, the company shall then, file with the registrar a notice in writing, giving a full address of the place.

Company may also keep such BoA or relevant papers in electronic mode in such manner as maybe prescribed.

(ii) SEC 128(2)

Where a company has a branch office in India or outside India, it shall be deemed to have been complied with the provisions of (1), if proper BoA of the branch office are kept at that office and summarised returns are periodically sent by the branch office to the company at its registered office or the other place as referred to in (1)

(iii) SEC 143(8)

Duties and powers of the company's auditor wrt the audit of the branch or branch auditor

Where a company has a branch office, and the accounts of that office shall be audited either by auditor appointed for the company, or by any other person appointed as per S139. If the branch office is situated outside India, the accounts of the branch auditor will be audited by the company's auditor or by any person duly qualified to act as an auditor in accordance with the laws of the country. The branch auditor will prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such a manner as he considers necessary.

SA 610

- SA 610
  - I . Meaning
    - 1. Activities relating to Governance
    - 2. Activities relating to Risk Management
    - 3. Activities relating to IC
  - II . Ways
  - III . Scope
  - IV . Objectives
  - V . Using the work of IA
    - A) How to evaluate
    - B) When cannot be used?
    - C) When can be used?(Examples)
    - D) Circumstances where Less work of IA and more direct work
    - E) If External auditor plans to use the work of the IA
  - VI . Direct Assistance
    - A) Meaning
    - B) How to evaluate the internal audit function
    - C) The external auditor shall not use IA to provide direct assistance to perform procedures - When?
    - D) Prior to use Internal auditor

I. What is Internal audit?

Internal audit function refers to a function of an entity that performs assurance and consulting activities designed to evaluate and improve the effectiveness of the entity's governance, risk management and Internal Control process.

1. Activities relating to Governance:

The internal audit function may assess the governance process in its accomplishment of objectives on ethics and values, performance management and accountability, communicating risk and control information to appropriate areas of the organization and effectiveness of communication among TCWG, external and internal auditors, and management.

2. Activities relating to Risk Management:

- The internal audit function may assist the entity by identifying and evaluating significant exposures to risk and contributing to the improvement of risk management and internal control (including effectiveness of the FRP).
- The internal audit function may perform procedures to assist the entity in the detection of fraud

3. Activities relating to Internal Control:

Evaluation of IC	Examination of Financial and operating information	Review of operating activities	Review of compliance with laws and regulations
• The internal audit function may be assigned specific responsibility for ; • Reviewing controls, • Evaluating their operation, and • Recommending improvements thereto. • Eg ; The IA function might plan and perform tests or other procedures to provide assurance to mgmt. and TCWG regarding the design, implementation and operating effectiveness of IC.	• The internal audit function may be assigned to review ; • The means used to identify, • recognize, • measure, • classify and report financial and operating information, and • to make specific inquiry into individual items, including detailed testing of transactions, balances and procedures.	• The internal audit function may be assigned to review ; • the economy, • efficiency and • effectiveness of operating activities, including non-financial activities of an entity.	The internal audit function may be assigned to review compliance with laws, regulations, and other external requirements, and with management policies and directives and other internal requirements.

II. Ways in which the external auditor may make use of the function for purposes of the

i. To obtain information that is relevant to the external auditor's assessments of the ROMM due to error or fraud.

ii. Unless prohibited, or restricted to some extent, by law or regulation, the external auditor, after appropriate evaluation, may decide to use work that has been performed by the internal audit function during the period in partial substitution for audit evidence to be obtained directly by the external auditor.

iii. Unless prohibited, or restricted to some extent, by law or regulation, the external auditor may use internal auditors to perform audit procedures under the direction, supervision and review of the external auditor (referred to as "direct assistance").

III Scope : SA 610 deals with the external auditor's responsibilities if using the work of Internal

I. Using the work of internal audit function in obtaining audit evidence

II. Using internal auditors in providing direct assistance under the direction, supervision and review of the external auditor.

The external auditor has the sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the external auditor's use of the work of the internal audit function or the internal auditors to provide direct assistance on the engagement.

IV. Objectives

To modify the nature or timing, or reduce the extent, or to use the internal auditors for direct assistance, the objectives are:

i. To determine whether the work of the IA can be used or whether the direct assistance can be taken and if so, in what areas and what extent.

ii. If using the work of the IA function, whether the work is adequate for the purposes of audit.

iii. If using the direct assistance of the IA function, to appropriately, DS and R of their work.

V. Using the work of Internal Auditor

A) How to evaluate internal audit function?

The external auditor has to evaluate the following:

Objectivity	Level of Competence	Systematic & Discipline approach
Objectivity refers to the ability to perform those tasks without allowing bias , conflict of interest or undue influence to override professional judgements	Competence refers to the attainment and maintenance of knowledge and skills of the function as a whole.	The application of a systematic and disciplined approach to planning, performing, supervising reviewing and **documenting** its activities distinguishing the IA function from other monitoring activities performed by the entity

Objectivity - Factors that may affect the external auditor's evaluation :

i. Whether the organizational status of the internal audit function, including the function's authority and accountability, supports the ability of the function to be free from bias, conflict of interest or undue influence of others to override professional judgments.

Eg ; Whether the IA function reports to TCWG or an officer with appropriate authority, or if the function reports to management, whether it has direct access to TCWG

ii. Whether TCWG oversee employment decisions related to the internal audit function.

Eg ; Determining the appropriate remuneration policy.

iii. Whether there are any constraints or restrictions placed on the internal audit function by management or TCWG.

Eg ; In communicating the IA function's findings to the external auditor.

iv. Whether the IA function is free of any conflicting responsibilities,

Eg ; Having managerial or operational duties or responsibilities that are outside of the IA function.

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Competence - Factors that may affect the external auditor's determination :

i. Whether the IA function is adequately and appropriately resourced relative to the size of the entity and the nature of its operations.

ii. Whether there are established policies for hiring, training and assigning internal auditors to internal audit engagements.

iii. Whether the IA have adequate technical training and proficiency in auditing.

iv. Whether the IA possess the required knowledge relating to the entity's FR & AFRF.

Systematic and Disciplined Approach - Factors that may affect the external auditor's determination:

i. The existence, adequacy and use of documented internal audit procedures or guidance covering such areas as risk assessments, work programs, documentation and reporting, the nature and extent of which is commensurate with the size and circumstances of an entity.

ii. Whether the internal audit function has appropriate quality control policies and procedures.

B) Circumstances when work of the internal audit function CANNOT be used:

i. The function's organizational status and relevant policies and procedures do not adequately support the objectivity of internal auditors.

ii. The function lacks sufficient competence.

iii. The function does not apply a systematic and disciplined approach including quality control.

iv. The EA needs to determine the nature and extent of the work of the IA function to be used, which is of relevance to the external auditor's overall audit strategy and audit plan.

C) Eg. of work of the IA function that can be used by the EA include the

1. Testing of the operating effectiveness of controls.
2. Substantive procedures involving limited judgement.
3. Observations of inventory counts.
4. Tracking transactions through the information system relevant to financial reporting.
5. Testing of compliance with regulatory requirements.

D) Circumstances in which the EA shall plan to use less of the work of the IA function

a. The more judgment is involved in:

i) Planning and performing relevant audit procedures; and

ii) Evaluating the audit evidence gathered;

b. The higher the assessed ROMM at the assertion level, with special consideration given to risks identified as significant;

c. The less the internal audit function's organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors; and

d. The lower the level of competence of the internal audit function.

E) If the external auditor plans to use the work of the Internal Audit, the EA shall:

i. Discuss the planned use of its work with the function as a basis for coordinating their respective activities.

ii. Read the reports of the internal audit function and related findings.

iii. Perform sufficient audit procedures on the body of work on the internal audit function as a whole that the external auditor plans to use, to determine its adequacy for the purpose of the audit.

Discussion and Coordination with the IA Function useful to address the following :

i. The timing of such work.

ii. The nature of the work performed.

iii. The extent of audit coverage.

iv. Materiality for the financial statements as a whole (and, if applicable, materiality level or levels for particular classes of transactions, account balances or disclosures), and performance materiality.

v. Proposed methods of item selection and sample sizes.

vi. Documentation of the work performed.

vii. Review and reporting procedures.

Coordination between the EA and the IA function is effective when, for eg;

i) Discussions take place at appropriate intervals throughout the period.

ii) The EA informs the IA function of significant matters that may affect the function.

iii) The EA is advised of and has access to relevant reports of the IA function and is informed of any significant matters that come to the attention of the function

VI. Direct Assistance

A) Meaning

Direct assistance refers to the use of internal auditors to perform audit procedures under the direction, supervision and review of the external auditor.

The external auditor may be prohibited by law or regulation from obtaining direct assistance from the internal auditor.

B) How to evaluate the IA function?

i. There are significant threats to the objectivity of the Internal auditor.
ii. The Internal auditor lacks sufficient competency to perform the proposed work.

C) The EA shall not use IA to provide direct assistance to perform procedures that:

i. Involve making significant judgements in the audit.
ii. Related to higher assessed risk of material misstatement.
iii. Relate to work which the internal auditors have been involved and which has already been or will be, reported to the management or TCWG by the internal audit function.
iv. Relates to the decisions the external auditor makes in accordance with this SA

Prior to using IA for direct assistance, the EA shall:

i. Obtain Written agreement from the authorized representative of the entity that the internal auditor will be allowed to follow the external auditor's instructions, and that the entity will not intervene in the work of the IA.
ii. Obtain written agreement from the Internal auditor that they will keep confidential matters as instructed by the External auditor and inform the external auditor of any threat to their objective.

Difference between internal financial control and internal control over financial reporting ?

1. The term Internal Financial Controls (IFC) refers to the policies and procedures put in place by companies for ensuring reliability of financial reporting, effectiveness and efficiency of operations, compliance with applicable laws and regulations, safeguarding of assets and prevention and detection of frauds.
2. On the other hand, IC over FR is required where auditors are required to express an opinion on the effectiveness of an entity's IC over FR, such opinion is in addition to and distinct from the opinion expressed by the auditor on the FS.
3. Therefore, "internal financial control" is a wider term where as "internal controls over financial reporting" is a narrower term restricted to entity's internal controls over financial reporting only.

REPORTING UNDER COMPANIES AUDITOR'S REPORT ORDER, 2020

APPLICATION:

It shall refer to every company including a foreign company except:

- Banking company as defined in Section 5(c) of the Banking Regulation Act, 1949
- Insurance company as defined under the Insurance Act 1938
- Company licensed to operate under section 8 of the companies Act
- One person company & small company as defined in Sec 2(62) and Sec 2(85) of the Companies Act
- A private limited company,

i. not being a subsidiary or holding company of a public company

ii. having a paid up capital and Reserves and surplus not more than one crore rupees as on Balance sheet date and

iii. which does not have total borrowings exceeding one crore rupees from any bank or Financial institution at any point in time during the financial year and

iv. which does not have a total revenue as disclosed in Sch III to the companies act (including revenue from discontinuing operations) exceeding 10 crore rupees during the FY as per the FS.

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I. FIXED ASSET

RECORDS: Whether a company is maintaining proper records showing full particulars including quantitative details and situation of PPE

RECORDS: Whether the company is maintaining proper records showing full particulars of Intangible assets

Whether these PPE have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with BOA

Whether the title deeds of all the immovable properties disclosed in the FS are held in the name of the company, if not provide the details in the format below *

Whether the company has revalued its PPE or intangible asset or both during the year, and if so, whether the revaluation is based on the valuation by a registered valuer; specify the amount of change, if the change is 10% or more in the aggregate of the net carrying value of each class of PPE or IA

Whether any proceedings have been initiated or are pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act and rules made thereunder , and whether company has disclosed the details in its FS

*

Description of property	Gross carrying value	Held in name of	Whether promoter, director, relative or employee	Period held, indicate range where appropriate	Reason for not being held in name of comp

II. INVENTORY

whether physical verification of inventories have been conducted at reasonable intervals by mgmt and whether, in the opinion of the auditor coverage and procedure of such verification by mgmt is appropriate ; whether any discrepancies of 10% or more in aggregate for each class of inventory was noticed, if so, whether they have been properly dealt with in the books of accounts.

Whether during any point of time of the year, the company has been sanctioned WC limits in excess of 5 crore rupees, in aggregate ,from banks and FI on the basis of security of current assets; whether the quarterly returns or statements filed by the co with such banks/fi are in agreement with the BoA of the co, if not- give details.

III. LOANS, INESTMENTS, GUARANTEE, SECURITY

Whether during the year the company has provided any loans or advances in the nature of loan, or stood guarantee or security to any entity, if so indicate
[NA to companies whose principal business is to give loans]

The aggregate amt during the year, the balance outstanding at the BS date wrt. loans, advances, guarantees, security to subsidiary, JV & associates.	The aggregate amt during the year, the balance outstanding at the BS date wrt. loans, advances, guarantees, security to other than subsidiary, JV & associates.

whether investments made, loans or advances given are not prejudicial to the interest of the company

in respect of loans and advances in the nature of loans, whether the schedule of repayment of principal and payment of interest has been stipulated and the whether the repayments or receipts are regular

if amount is overdue, state the amount overdue more than 90 days, whether reasonable steps have been taken for the recovery

Whether any loans or advance in the nature of loan, has been renewed or extended, or fresh loan has been granted to settle the overdues of the existing loans- if so, specify the aggregate amount ofdues renewed/extended/fresh loans and the percentage of the aggregate to the total loans or advances **[NA to companies whose principal business is to give loans]**

whether the company has granted loans or advances which are repayable on demand or without specifying any terms or period of repayment, if so, specify the aggregate amount, percentage of total loans granted, aggregate amount of loans granted to promoters, Related parties

IV. LIGS PROVIDED [185,186]

In respect of Loans, investments, guarantees or security- whether the provisions of section 185 and 186 of the Companies Act have been complied with, if not provide details thereof.

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V. DEPOSITS [73-36]

In respect of deposits accepted by the company whether the provisions of Section 73 to 76 have been complied with, if not, the nature of contraventions be stated, if an order has been passed by company law board or NCLT or RBI or any court or any tribunal, whether same has been complied.

VI. COST RECORDS [148(1)]

Whether the maintenance of the cost records has been specified by the CG under Section 148(1) of the companies Act and whether such a/cs have been so made and maintained

VII. STATUTORY DUES [DISPUTED AND UNDISPUTED]

Undisputed statutory dues:-

- Whether the company is regular in depositing the undisputed statutory dues including GST, PF, ST, sales tax, employees state insurance, customs and excise duty and any other statutory dues to the appropriate authorities- if not, extent of arrears of o/s statutory dues on the last day of the FY concerned for a period of more than 6 months from the date they became payable, shall be indicated;

Disputed statutory dues:-

- Where statutory dues have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned(a mere representation to the concerned dept shall not be treated as a dispute)

VIII. UNDISCLOSED INCOME

Whether any transactions not recorded in the BoA have been surrendered or disclosed as income during the year in the tax assessments under the IT Act 1961, if so whether the previously unrecorded income has been properly recorded in the BoA during the year.

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IX. REPAYMENT OF LOAN

Whether company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, the period and the amount of default to be reported as per format*

Whether the company is a declared as wilful defaulter by any bank or FI or other lender;

Whether term loans were applied for the purpose for which the loans were obtained, if not, the amount of loan so diverted and the purpose for which it is used may be reported;

Whether funds raised on short term basis have been utilized for LT purposes, if yes, the nature and amount to be indicated;

Whether the company has taken any funds from any entity or person on a/c of to meet the obligations of its subsidiary, associate or JV, if so give details of with nature of such transactions and amount in each case

Whether the company has raised loans during the year on the pledge of securities held in its subsidiaries, JV or associate companies, if so give details and also if company has defaulted in the repayment of such loans raised

Format*

Nature of borrowing incl debt securities	Name of lender	Amount not paid on due date	Whether principal or interest	No of days delay or unpaid	Remarks, if any

X. ISSUE PROCEEDS - IPO & FPO

Whether money raised by way of IPO or FPO (incl debt inst) during the year were applied for the same purpose for which those are raised, if not, details together with delays or default and subsequent rectification has to be reported

Whether company has made any preferential allotment or private placement of shares or convertible debentures (fully,partially or optionally convertible) during the year, and if so, whether the requirements of Sec 42 and 62 have been complied with and the funds have been used for the purpose for which the funds were raised, if not provide details in respect of amount involved and nature of non-compliance

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X1. FRAUD

Whether any fraud by the company or any fraud on the company has been noticed or reported during the year, if yes, nature and the amount involved

Whether any report under section 143(12) of the companies Act has been filed by the auditors in Form ADT 4 as prescribed under rule 13 of companies (Audit and Auditors) Rules,2014 with the CG

Whether the auditor has considered any whistle-blower complaints, if any, received during the year by the company.

XII. NIDHI COMPANY

Whether the nidhi company has complied with the net owned funds to deposits in the ratio of 1:20 to meet out the liability

Whether the nidhi company is maintaining 10% unencumbered term deposits as specified in nidhi rules to meet out liability

Whether there has been any defaults in repayment or payment of interest, and if so, details thereof.

XIII. RELATED PARTY TRANSACTIONS [177&188]

Whether all the compliances under the Section 177 and 188 have been complied with, and the details have been disclosed in the FS as required by AS

XIV. INTERNAL AUDIT

Whether the company has an internal audit system commensurate with the size and nature of the business.

Whether the reports of the Internal auditor were considered by the statutory auditor

XV. NON-CASH TRANSACTIONS - 192

Whether the company has entered into any non cash transactions with directors or persons connected with him, and if so, whether the provisions of Section 192 have been complied with.

XVI. RBI REGISTRATION

Whether the company is required to be registered under section 45IA of the RBI Act,1934; and if so, whether the registration has been obtained	Whether the company has undertaken any non banking financial or housing financial activities without a valid certificate of registration from the RBI	Whether the company is a core investment company, as defined in the regulations made by the RBI, if so whether it fulfils the criteria	Whether the group has more than one CIC as part of the group, if yes, indicate the number of CICs part of the group

XVII. CASH LOSSES

whether the company has incurred cash losses in the FY and in the immediately preceeding FY, if so, state the amount of cash losses

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XVIII. RESIGNATION OF STATUTORY AUDITORS

Whether there has been any resignation of statutory auditors during the year, and if so, whether the auditor has taken into consideration the issues, objections or concerns raised by the outgoing auditors.

XIX. GOING CONCERN

On the basis of the financial ratios, ageing and expected dates pf realisation of financial assets and payment of financial liabilities, whether the auditor is of the opinion that no material uncertainty exists as on the date of AR that company is capable of meeting its liabilities existing at the date of BS as and when they fall due within a period of one year.

XX. CSR

Other than ongoing project

- Whether in respect of other than ongoing projects, the company has transferred unspent amount to a fund specified in Schedule VII to the companies act within a period of 6 months to the expiry of the FY in compliance with second proviso to subsection (5) of section 135

Ongoing project

- Whether any amount remaining unspent, pursuant to any ongoing project, has been transferred to special account in compliance with 135 (6)

XXI. CONSOLIDATED FINANCIAL STATEMENTS

Whether there have been qualification or adverse remarks by the respective auditors under CARO in the CFS, if yes, indicate the details of the company and the para numbers of CARO Report

COMPANY AUDIT

I. REPORTING REQUIREMENT RELATING TO MATTERS STATED IN SECTION 143(1)

Under section 143(1), auditor shall inquire into following matters given as under: -

1. Whether loans & advances made by the co on the basis of security have been properly secured & whether the terms on which they have been made are prejudicial to the interests of the co or its members;
2. Whether transactions of the co which are represented merely by book entries are prejudicial to the interests of the co;
3. Where the co not being an investment co or a banking co, whether so much of the assets of the co as consist of shares, debentures & other securities have been sold at a price less than that at which they were purchased by the co;
4. Whether loans & advances made by the co have been shown as deposits;
5. Whether personal expenses have been charged to revenue a/c;
6. Where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually received, whether the position as stated in the a/c books and the BS is correct, regular, and not misleading.

NOTE: Auditor is not required to report on the matters specified in sub-section (1) unless he has any special comments to make on any of the items Auditor should make a report to the members in case, he finds answer to any of these matters in adverse.

II. REPORTING ON ACCOUNTS EXAMINED:

Under provisions of Section 143(2), the auditor shall make a report to the members of the co on the a/cs examined by him and on every FS which are required by or under this Act to be laid before the co in GM and the report shall after taking into a/c the provisions of this Act, the a/c & auditing standards and matters which are required to be included in the audit report under the provisions of this Act or any rules made thereunder or under any order made under sub section (11)

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DUTY TO REPORT SECTION 143(3): -

The auditor's report shall also state

a) Whether he has sought and obtained all the info and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such info on the FS;

b) Whether, in his opinion, proper BOA as required by law have been kept by the co so far as appears from his examination of those books & proper returns adequate for the purposes of his audit have been received from branches not visited by him;

c) Whether the report on the a/cs of any branch office of the co audited under sub-section (8) by a person other than the co's auditors has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;

d) Whether the Co's BS and P&L a/c dealt with in the report are in agreement with BOA & returns;

e) Whether, in his opinion, the FS comply with the accounting standards;

f) The observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the co;

g) Whether any director is disqualified from being appointed as a director under sub- section (2) of the section 164;

h) Any qualification, reservation or adverse remark relating to the maintenance of a/cs and other matters connected therewith;

i) **Internal financial controls (IFCs) with reference to financial statements shall not be applicable to a private company** which is a–

- One person company; or
- Small company; or
- Company having turnover less than ` 50 crore as per latest audited FS & having aggregate borrowings from banks or FI or any body corporate at any point of time during the FY less than ` 25 crore.

j) **Such other matters as are prescribed in Rule 11 of the Companies (Audit and Auditors) Rules, 2014 which are as under: -**

1. Whether the Co has disclosed the impact,; if any, of pending litigations on its financial position in its FS;
2. Whether the Co has made provision, as required under any law or AS, for material foreseeable losses, if any, on long term contracts including derivative contracts;
3. Whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.
4. Whether the mgmt has represented that, to the best of it's knowledge and belief, **other than as disclosed** in the notes to the a/cs, no funds have been advanced or loaned or invested (either from borrowed funds or share premium or any other sources or kind of funds) by the co to or in any other person(s) or entity(ies), including foreign entities ("Intermediaries"),

i. Whether recorded in writing or otherwise, that the Intermediary shall, whether, directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the Co ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries;

ii. Whether the mgmt has represented, that, to the best of its knowledge and belief, other than as disclosed in the notes to the a/cs, no funds have been received by the company from any person(s) or entity(ies), including foreign entities ("Funding Parties") with the understanding, whether recorded in writing or otherwise,

iii. Based on such audit procedures that the auditor has considered reasonable and appropriate in the circumstances, nothing has come to their notice that has caused them to believe that the representations under sub clause (1) and (2) contain any material misstatement.

5. Whether the dividend declared or paid during the year by the company is in compliance with section 123 of the Companies Act, 2013.
6. Whether the company has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and the same has been operated throughout the year for all transactions recorded in the software and the audit trail feature has not been tampered with and the audit trail has been preserved by the company as per the statutory requirements for record retention.

III REPORTING ON ANY OTHER MATTER SPECIFIED BY CENTRAL GOVERNMENT:

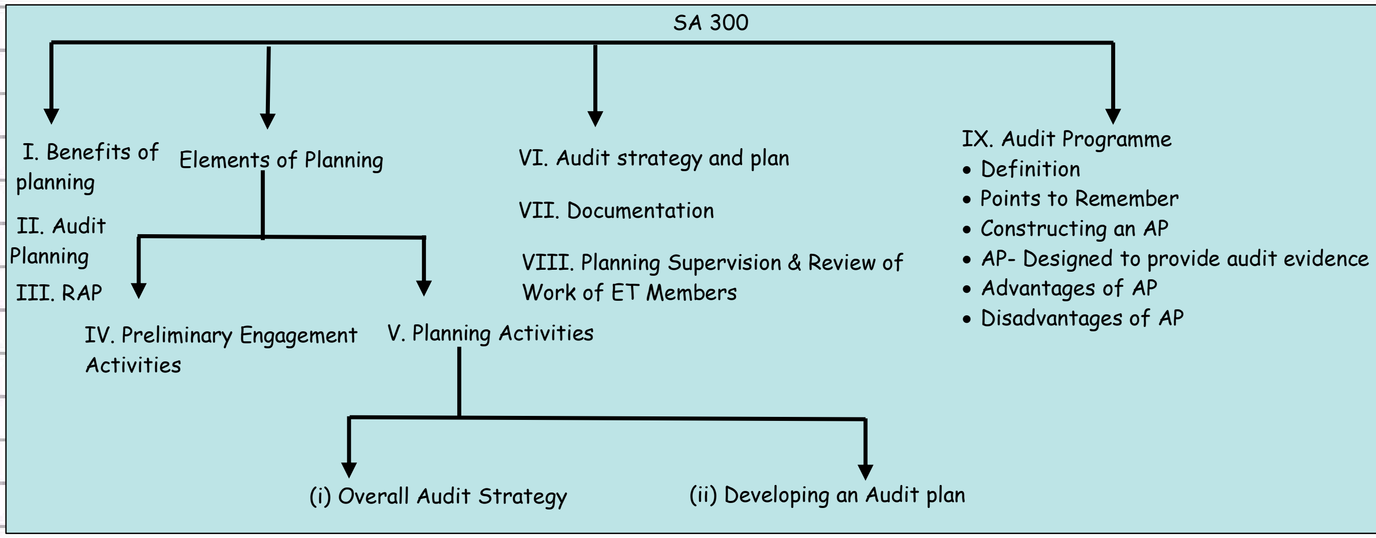
As per section 143(11), the CG may, in consultation with the National Financial Reporting Authority, by general or special order, direct, in respect of such class or description of Co's, as may be specified in the order, that the AR shall also include a statement on such matters as may be specified therein.

IV. REPORTING ON FRAUDS:

A. **Reporting to the Central Government**- As per section 143(12) of the Co's Act, 2013 read with Rule 13 of the Co's (Audit and Auditors) Rules, 2014, if an auditor of a Co in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of `1 crore or above, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the CG within such time and in such manner as prescribed.

B. **Reporting to the Audit Committee or Board**- In case of a fraud involving lesser than the specified amount [i.e. less than ` 1 crore], the auditor shall report the matter to the audit committee constituted under section 177 or to the Board in other cases within such time and in such manner as prescribed.
Besides, auditor has also to report matters pertaining to fraud at point (xi) of paragraph 3 of CARO,2020 which is discussed subsequently.

SA 300 PLANNING AN AUDIT OF FS



I. WHY PLANNING IS NECESSARY OR BENEFITS OF PLANNING?

1. Helping the auditor to devote proper attention to important areas of the audit
2. Helping the auditor identify and resolve potential problems on a timely basis
3. Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner.
4. Assisting in the selection of Engagement Team (ET) members and proper assignment of work to them.
5. Facilitating the direction and supervision of ET members and review their work.
6. Assisting, where applicable, in coordination of work done by others such as experts

After establishing of the overall audit strategy, an audit plan can be developed to address the various matters identified in the overall audit strategy, taking into account the need to achieve the audit objectives through the efficient use of the auditor's resources.

II. AUDIT PLANNING:

Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement.

Planning includes the needs to consider prior to the auditor's identification and assessment of Risk of Material Misstatement, such matters as:

1. The analytical procedures to be applied as risk assessment procedures.
2. Obtaining a general understanding of the legal and regulatory framework applicable to the entity and how the entity is complying with that framework.
3. The determination of materiality.
4. The involvement of experts.
5. The performance of other risk assessment procedures.

III RISK ASSESSMENT PROCEDURES:

Risk assessment procedures are audit procedures performed to obtain an understanding of the entity and its environment, including the entity's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error at the financial statement and assertion levels.

Planning is NOT a separate or distinct phase of an audit. It is to be viewed as a continual and repetitive process. It is a continuous process that begins with completion of previous audit and continues till the completion of current audit engagement.

Involvement of key engagement team members in planning audit:

The engagement partner and other key members of the engagement team shall be involved in planning the audit including planning and participating in the discussion among engagement team members. The involvement of the engagement partner and other key members of the engagement team in planning the audit draws on their experience and insight, thereby enhancing the effectiveness and efficiency of the planning process.

Planning Process- Elements of Planning:

SA 300 "Planning an audit of FS"

- Elements of planning process
  - IV. Preliminary Engagement Activities
  - V. Planning Activities
    - i. Overall Audit Strategy
    - ii. Developing an audit plan

IV. PRELIMINARY ENGAGEMENT ACTIVITIES:

1. Performing procedures regarding the continuance of client relationship

It should be ensured that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed and that conclusions reached in this regard are appropriate.

The firm should obtain information considered necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client.

Matters such as integrity of principal owners and key management, competence of engagement team to perform the audit engagement and implications of matters that have arisen during current and previous audit engagement may need to be considered.

2. Evaluating Compliance with ethical requirements including

The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall: -

i. Obtain relevant information from the firm to identify and evaluate circumstances and relationships that create threats to independence.

ii. Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for the audit engagement and

iii. Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is permitted by law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action.

3. Establishing an understanding of terms of engagement

It is in the interests of both the entity and the auditor that the auditor sends an audit engagement letter before the commencement of the audit to help avoid misunderstandings with respect to the audit. It ensures that there is no confusion with the client regarding terms of the engagement.

Performing preliminary engagement activities assists the auditor in identifying and evaluating events or circumstances that may affect auditor's ability to plan and perform audit engagement.

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V. PLANNING ACTIVITIES

(i) Establishing Overall Audit Strategy

Overall audit strategy sets the scope, timing and the direction of the audit and guides the development of a more detailed audit plan.

The process of establishing the overall audit strategy assists the auditor to determine, subject to the completion of the auditor's risk assessment procedures, such matters as:

i. The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high-risk areas or the involvement of experts on complex matters

ii. The amount of resources to allocate to specific audit areas, such as the number of team members assigned to observe the inventory count at material locations, the extent of review of other auditors' work in the case of group audits, or the audit budget in hours to allocate to high risk areas

iii. When these resources are to be deployed, such as whether at an interim audit stage or at key cut-off dates

iv. How such resources are managed, directed and supervised, such as when team briefing and debriefing meetings are expected to be held, how engagement partner and manager reviews are expected to take place (for example, on-site or off-site), and whether to complete engagement quality control reviews

In establishing an overall audit strategy, the auditor shall consider these factors:

1. Identify the scope of engagement
2. Ascertain the reporting objectives of the engagement
3. Consideration of significant factors in directing the engagement team's efforts
4. Consider the results of preliminary engagement activities
5. Ascertain the NTE of resources required for the engagement

1. **Identify the characteristics of the engagement that define its scope**

It is important for auditor to identify scope of the engagement. Only a well identified scope can lead to establishment of a sound audit strategy. There are many characteristics of engagement defining its scope. Some of characteristics are as under: -

a) Applicable financial reporting framework applicable to the entity
b) Nature of business segments to be audited including the need for specialized knowledge
c) Industry specific reporting requirements required by industry regulators
d) Expected use of audit evidence obtained in previous audits

2. **Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required**

The ascertaining of reporting objectives of engagement helps the auditor to plan timing of different audit procedures and also nature of communications.

Some of the instances are given under: -

a) The entity's timetable for reporting
b) Organization of meetings to discuss of nature, timing and extent of audit work with management
c) Discussion with management regarding the expected type and timing of reports to be issued including the auditor's report
d) Discussion with management regarding the expected communications on the status of audit work throughout the engagement.
e) Expected nature and timing of communications among engagement team members, including the nature and timing of team meetings and timing of the review of work performed.

3. **Consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts**

The auditor needs to direct efforts of engagement team towards matters that in his professional judgment are significant. Preliminary identification of material classes of transactions, account balances and disclosures help auditor in establishing overall audit strategy. More energies need to be devoted to significant matters to obtain desired outcomes. Few examples are listed as under: -

a. Volume of transactions which may determine whether it is more efficient for the auditor to rely on internal control
b. Significant industry developments such as changes in industry regulations and new reporting requirements.
c. Significant changes in the financial reporting framework, such as changes in accounting standards.
d. Other significant relevant developments, such as changes in the legal environment affecting the entity.

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4. Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant

Considering results of preliminary engagement activities and knowledge gained from similar engagements goes a long way in establishing sound audit strategy. Examples are listed as under:

a. Results of previous audits that involved evaluating the operating effectiveness of internal control, including the nature of identified deficiencies and action taken to address them.

b. The manner in which the auditor emphasizes to engagement team members the need to maintain a questioning mind and to exercise professional skepticism in gathering and evaluating audit evidence.

5. Ascertain the nature, timing and extent of resources necessary to perform the engagement

Selection of engagement team and assignment of audit work to team members is a significant factor in establishing overall audit strategy. Experienced team members may be assigned in areas where there is higher risk of material misstatement. Similarly, engagement budgeting and devotion of more time to areas of higher risk of material misstatement are to be kept in mind.

(ii) Development of Audit Plan

Once the overall audit strategy has been established, an audit plan can be developed to address the various matters identified in the overall audit strategy.

SA 300 “Planning an Audit of FS” states that auditor shall develop an audit plan that shall include description of-

- Nature, timing and extent of planned Risk Asst procedures
- The nature, timing and extent of planned Further audit procedures at assertion level
- Other planned audit procedures that are required to be carried out so that the engagement complies with SAs

The audit plan is more **detailed** than the audit strategy. Planning for these audit procedures takes place over the course of the audit.

VI. RELATIONSHIP BETWEEN AUDIT STRATEGY & AUDIT PLAN

Audit strategy sets the broad overall approach to the audit whereas audit plan addresses various matters identified in the overall audit strategy. Audit strategy determines scope, timing and direction of audit. Audit plan describes how the strategy is going to be implemented.

Who has the **responsibility** for establishing the overall audit strategy and planning for the audit- The responsibility lies with the **auditor** only.

Can the Planning decisions Change during the course of the audit? **YES**. The auditor shall update and change the overall audit strategy and the audit plan as necessary when as a result of unexpected events and changes in conditions or audit evidence obtained as a result of audit procedures differs significantly when the auditor planned the audit procedures.

VII. DOCUMENTATION

The auditor shall document:- Q: **JAN'25**

a. The overall audit strategy
b. The audit plan and
c. any significant changes made during the audit engagement to the overall audit strategy or the audit plan, and the reasons for such changes.

The documentation of the overall audit strategy is a record of the key decisions considered necessary to properly plan the audit and to communicate significant matters to the engagement team.
The documentation of the audit plan is a record of the planned nature, timing and extent of risk assessment procedures and further audit procedures at the assertion level in response to the assessed risks. It also serves as a record of the proper planning of the audit procedures that can be reviewed and approved prior to their performance.
A record of the significant changes to the overall audit strategy and the audit plan, and resulting changes to the planned nature, timing and extent of audit procedures, explains why the significant changes were made, and the overall strategy and audit plan finally adopted for the audit. It also reflects the appropriate response to the significant changes occurring during the audit.

VIII. PLANNING SUPERVISION AND REVIEW OF WORK OF ET

The auditor shall plan the NTE of direction and supervision of engagement team members and the review of their work. The NTE of the direction and supervision of engagement team members and review of their work vary depending on many factors, including: -

1. The size and complexity of the entity.
2. The area of the audit.
3. The assessed risks of material misstatement
4. The capabilities and competence of the individual team members performing the audit work.

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IX. AUDIT PROGRAMME

AN AUDIT PROGRAMME is a detailed plan and consists of a series of verification procedures to be applied to the financial statements and accounts of a given company for the purpose of obtaining sufficient & appropriate evidence to enable the auditor to express an informed opinion on such statements. For framing an audit programme, the following points should be kept in view:

Audit objective ⇨ Audit procedure to be applied ⇨ Extent of check ⇨ Special instruction based on past experience of auditee ⇨ Allocation of work amongst the team members ⇨ Timing of check

Points to remember for Audit programme:

1. Evolving one audit program- Not practicable for all businesses

- Businesses vary in nature, size and composition; work which is suitable to one business may not be suitable to others; efficiency and operation of internal controls and the exact nature of the service to be rendered by the auditor are the other factors that vary from assignment to assignment

2. The assistant to keep an open mind

- an auditor having regard to the nature, size and composition of the business and the dependability of the internal control and the given scope of work, should frame a programme which should aim at providing for a minimum essential work which may be termed as a standard programme.

3. Periodic review of the audit programme

- There should be periodic review of the audit programme to assess whether the same continues to be adequate for obtaining requisite knowledge and evidence about the transactions.

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CONSTRUCTING AN AUDIT PROGRAMME

For the purpose of programme construction, the following points should be kept in mind:

a) Stay within the scope and limitation of the assignment.
b) Prepare a written audit programme.
c) Determine the evidence reasonably available and identify the best evidence.
d) Apply only those steps which are useful in accomplishing the verification purpose.
e) Include the audit objectives for each area.
f) Consider all possibilities of error.
g) Co-ordinate the procedures to be applied to related items.

AUDIT PROGRAMME – DESIGNED TO PROVIDE AE

An auditor picks up evidence from a variety of fields and it is generally of the following broad types:

a) Documentary examination
b) Physical examination
c) Statements and explanation of management, officials and employees
d) Statements and explanations of third parties
e) Arithmetical calculations by the auditor
f) State of internal controls and internal checks
g) Inter-relationship of the various accounting data
h) Subsidiary and memorandum records
i) Minutes
j) Subsequent action by the client and by others.

Example

1. For cash in hand, the best evidence is 'count'.
2. For investment pledged with a bank, the banker's certificate.
3. For verifying assertions about book debts, the client's ledger invoices, debit notes, credit notes, monthly accounts statement sent to the customers are all evidence: some of these are corroborative, other being complementary. In addition, balance confirmation procedure is often resorted to, to obtain greater satisfaction about the reliability of the assertion.

ADVANTAGES OF AUDIT PROGRAMME

1. Provides assistant a clear set of instructions to be generally done
2. It is essential, for major audits, to provide a total perspective of the work to be performed
3. Selection of assistants for the job becomes easier when the work is rationally planned, defined and segregated
4. Without a written and predetermined prog, work is carried out with a mental plan. There is always a danger of overlooking imp books/ records Under a properly framed programme, such danger is significantly less and the audit can proceed systematically.
5. The assistants, by putting their signature on programme, accept the responsibility for the work carried out by them individually and, if necessary, the work done may be traced back to the assistant.
6. The principal can control the progress of various audits
7. Serves as a guide for audits to be carried out in the succeeding year
8. A properly drawn up audit programme serves as evidence in the event of any charge of negligence being brought against the auditor. It may be of considerable value in establishing that he exercised reasonable skill and care that was expected of professional auditor.

DISADVANTAGES OF AUDIT PROGRAMME

1. The work may become mechanical and particular parts of the programme may be carried out without any understanding of the object of such parts in the whole audit scheme.
2. The programme often tends to become rigid and inflexible following set grooves; the business may change in its operation of conduct, but the old programme may still be carried on.
3. Inefficient assistants may take shelter behind the programme i.e., defend deficiencies in their work on the ground that no instruction in the matter is contained therein.
4. A hard and fast audit programme may kill the initiative of efficient and enterprising assistants.

All these disadvantages may be eliminated by

imaginative supervision of the work carried on by the assistants; the auditor must have a receptive attitude as regards the assistants; the assistants should be encouraged to observe matters objectively and bring significant matters to the notice of supervisor/principal.

SA 315 "IDENTIFYING AND ASSESSING THE RISK OF MATERIAL MISSTATEMENT"

Basics before SA 315

- I. What is Audit Risk
- II. What is Material Misstatement
- III. What is Risk of Material Mistatement
  - Inherent Risk
  - Control Risk
  - Detection Risk
    - Sampling Risk
    - Non Sampling Risk

I. Audit Risk

Audit Risk means the risk that the auditor gives an inappropriate audit opinion when the FS are materially misstated.

Audit risk is a function of the risk of material misstatement and detection risk

II. What is meant by misstatement?

Misstatement refers to the difference between amount, classification, presentation or disclosure of a reported FS item, and the amount, classification, presentation or disclosure that is required for the item to be in accordance with the AFRF.

Misstatements can arise from fraud or error.

Misstatement can exists at two levels	**Overall financial statement level**	ROMM that relate pervasively to the FS as a whole and potentially affect many assertions
	The assertion level for account balances, class of transaction, and disclosure	ROMM at assertion is assessed in order to determine the NET of FAP to obtain SAAE.

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III. Components of Risk of Material misstatement

Inherent risk is the susceptibility of assertion about a class of transaction, account balance or disclosure (ABCD) to a misstatement that could be material, either individually or when aggregated with other misstatements before consideration of any related controls as described in SA-200

Few examples of inherent risks could include: -

1.An accounting standard provides guidance on some complex issue which might not be understood by the management. Therefore, recording of this issue in financial statements carries inherent risk of being misstated

2.There are large number of business failures in an industry. Therefore, assertions in financial statements of an entity operating in such an industry carry an inherent risk of being misstated.

Control risk is the risk that a misstatement that could occur in an assertion about ABCD and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's internal control.

Examples of control risk could include: -

1.Co has devised control that cash and cheque books should be kept in a locked safe and access is granted to authorized personnel only. There's risk that control is not being followed.

2.An entity has devised a control that fire extinguishers and smoke detectors are in place and are in working condition at all times to reduce the risk of damage to inventories caused by fire. There is a risk that fire extinguishers in place are expired and are not being refilled. Similarly, there is a possibility that smoke detectors are not working.

3.A company has devised a control relating to petty cash that items of expenditure of only less than ` 10000 should be routed through imprest system of petty cash. There is a risk that control is not being followed.

Detection risk is the risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements

For eg :-

1. Sizeable work-in-progress inventories are expected in financial statements of a company. However, auditor of the company does not devote time to attending inventory count. Instead, he chooses to rely upon alternative audit procedures.

2.The auditor of a company has audited revenue of a company by taking a sample. However, there is a risk that sample of revenue is not representative of overall revenue.

Sampling risk is the risk that the auditor's conclusion based on the sample maybe different from the conclusion if the entire population were subjected to the same audit procedure. The sample was not representative of the population from which it was chosen.

Non sampling risk is the risk that the auditor reaches an erroneous conclusion for any reason not related to sampling risk. E.g. Inappropriate audit procedures

The auditor can influence only the detection risk. The inherent and control risk belong to the entity and are influenced only by the entity.

Therefore, auditor should reduce detection risk to keep the audit risk at a low level. Detection risk may be reduced by: increasing area of checking, testing larger samples, and by including competent and experienced persons in the ET.

AUDIT RISK= RISK OF MATERIAL MISSTATEMENT X DETECTION RISK
AUDIT RISK= INHERENT RISK X CONTROL RISK X DETECTION RISK

QUESTIONS:

1.Wear & Tear Private Limited is a "start-up" engaged in providing holistic solutions to problem of paddy stubble burning mainly catering to needs of farmers of North western India. Due to importance given by governments to this issue, companies have entered in the market in past few years. Many of these companies have not been successful and have gone bust. As an auditor of the company, can you spot the component of risks of material misstatement involved in above?

2.A company has devised a control that its inventory of perishable goods is stored in appropriate conditions- in a controlled environment to prevent any damages to inventory. Responsibility is fixed on two persons to monitor environment using sensors and to report on deviations. Identify the component of risks of material misstatement involved as an auditor of the company.

3.Shree Foods Private Limited is engaged in manufacturing of garlic bread. The auditors of company have planned audit procedures in respect of recognition of being alluded to? revenues of the company. Despite that, there is a possibility that misstatements in revenue recognition are not identified by planned audit procedures. Which risk is

SA 315 "Identifying and Assessing the Risk of material misstatement through understanding the entity and its environment"

Risk Assessment Procedures (RAP)	**Internal Controls (IC)**

Objective of SA 315

1. To identify and assess the ROMM at
   - The FS level
   - The assertion level for ABCD

   to provide a basis for designing and performing FAP.
2. For the purpose of identifying and assessing the ROMM, the auditor shall:
   a. Identify risks throughout the process of obtaining an understanding of the entity and its environment
   b. Assess the identified risks and evaluate whether they relate more pervasively to the FS as a whole and potentially affect many assertions.
   c. Relate the identified risks to what can go wrong at the assertion level
   d. Consider the likelihood of misstatement including the possibility of multiple misstatements and whether potential misstatement is of a magnitude that can result in a material misstatement.

Risk Assessment procedure

RAP includes the following:		
A. Inquiries of mgmt and others within the entity	B. Analytical procedures	C. Observation and Inspection

A. **Inquiries of Management and Others Within the Entity**: -

The auditor may obtain information, or a different perspective in identifying ROMM, through inquiries of others within the entity and other employees with different levels of authority.

- Inquiries directed toward internal audit personnel may provide info about internal audit procedures performed during the year relating to the design and effectiveness of the entity's internal control and whether management has satisfactorily responded to findings from those procedures.
- Inquiries of employees involved in initiating, processing or recording complex or unusual transactions may help the auditor to evaluate the appropriateness of the selection and application of certain accounting policies.
- Inquiries directed toward in-house legal counsel may provide information about such matters as litigation, compliance with laws and regulations, knowledge of fraud or suspected fraud affecting the entity, warranties, post-sales obligations, arrangements (such as joint ventures) with business partners and the meaning of contract
- Inquiries directed towards marketing or sales personnel may provide info about changes in the entity's marketing strategies, sales trends, or contractual arrangements with its customers.
- Inquiries directed to the risk management function (or those performing such roles) may provide info about operational and regulatory risks that may affect financial reporting.
- Inquiries directed to information systems personnel may provide info about system changes, system or control failures, or other information system- related risks.

B. **Analytical Procedures**: -

Analytical procedures performed as risk assessment procedures may include both financial and non-financial information, for eg:- relationship between sales and square footage of selling space or volume of goods sold

C. **Observation and inspection: -**

- The entity's operations. control manuals.
- Documents (such as business plans and strategies), records, and internal
- Reports prepared by mgmt (such as quarterly mgmt reports and interim FS) and TCWG (such as minutes of board of director's meetings)
- The entity's premises and plant facilities.

UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT

It helps the auditor in planning the audit and in identifying areas requiring special attention.

a) **Relevant industry, regulatory and other external factors including the applicable Financial reporting framework**

Relevant industry factors include industry conditions such as the competitive environment, supplier and customer relationships, and technological developments.

E.g. of matters the auditor may consider include market and competition, whether entity is engaged in seasonal activities, product technology relating to entity's products

Relevant regulatory factors include the regulatory environment.

Regulatory environment includes the AFRF and legal and political environment.

E.g. of matters include a/c principles & industry specific practices, regulatory framework for a regulated industry, legislation and regulation that significantly affect the entity's operations, including direct supervisory activities, taxation, government policies currently affecting the entity's business.

b) **The nature of the entity, including: -**

- its operations;
- its ownership and governance structures;
- the types of investments that the entity is making and plans to make, including investments in special-purpose entities; and
- the way that the entity is structured and how it is financed; to enable the auditor to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements

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Eg of matters that the auditor may consider while obtaining understanding of nature of entity include:

1. Business operations such as nature of revenue sources, products or services, conduct of operations, location of production facilities, key customers and suppliers of goods and services structure etc.
2. Investment and investment activities such as capital investment activities and planned or recently executed acquisitions
3. Financing and financing activities such as major subsidiaries, debt
4. Financial reporting such as accounting principles and revenue recognition practices

c) **The entity's selection and application of accounting policies, including the reasons for changes: -**

The auditor shall evaluate whether the entity's a/c policies are appropriate for its business and consistent with the AFRF and a/c policies used in the relevant industry.

d) **The entity's objectives and strategies and those related business risks that may result in ROMM: -**

An understanding of the business risks facing the entity increases the likelihood of identifying ROMM, since most business risks will eventually have financial consequences and, therefore, an effect on the FS. However, the auditor does not have a responsibility to identify or assess all business risks because not all business risks give rise to ROMM.

Eg. of matters include: -

1. Industry developments eg: entity does not have the personnel or expertise to deal with the changes in the industry
2. New products and services for eg, increased product liability
3. Expansion of the business for eg, that the demand has not been accurately estimated

e) **The measurement and review of the entity's financial performance: -**

Understanding of the entity's performance measures assists the auditor in considering whether pressures to achieve performance targets may result in mgmt actions that increase the ROMM, including those due to fraud.

Examples for measuring and reviewing financial performance which may be used by an auditor may include:

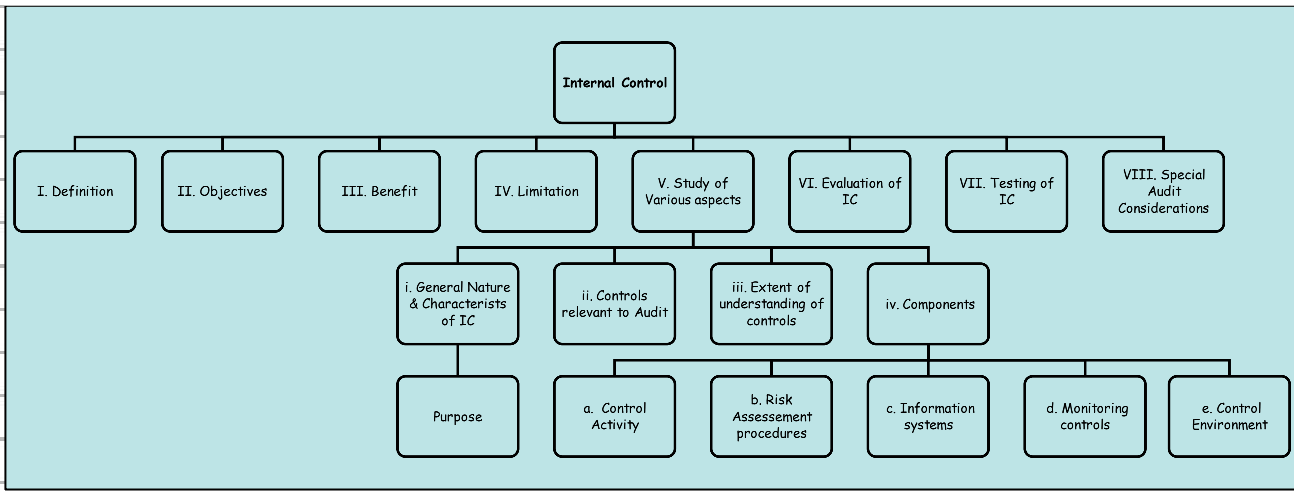
1. Key performance indicators (financial and non-financial) and key ratios, trends and operating statistics
2. Period-on-period financial performance analyses.
3. Budgets, forecasts, variance analyses, and departmental or other level performance reports.
4. Credit rating agency reports

Understanding the entity-a continuous process:-

The understanding establishes a frame of reference within which the auditor plans the audit and exercises professional judgment throughout the audit, for example, when:

1. Assessing RoMM of the FS.
2. Determining Materiality in accordance with SA 320
3. Considering the appropriateness of the selection & application of Accounting policies
4. Identifying areas where special audit consideration may be necessary, for example, related party transactions, the appropriateness of management's use of the going concern assumption, or considering the business purpose of transactions
5. Developing expectations for use when performing analytical procedures (SA520)
6. Evaluating the SAAE obtained such as the appropriateness of assumptions and of management's oral and written representations (SA 580)

INTERNAL CONTROL



I. Definition

As per SA 315, Internal Control may be defined as:

The process designed, implemented, and maintained by TCWG, management and other personnel to provide reasonable assurance about the achievement of the entity's objectives, with regard to reliability of financial reporting, effectiveness, and efficiency of operations, safeguarding of assets and compliance with applicable laws and regulations. The term controls refer to any aspects of one or more components of internal control.

II. Objectives of IC

- Transactions are executed in accordance with management's general or specific authorization
- All transactions are promptly recorded in correct amounts, in the appropriate accounts and in the accounting period in which it is executed.
- Assets are safeguarded from unauthorised access, use or disposition
- The recorded assets are compared with the existing assets at reasonable intervals. (Physical verification)

III. Benefits of understanding of IC:

The understanding of IC assists the auditor in:

1. Identifying types of potential misstatements
2. Identifying factors that affect the Risk of material misstatement
3. Designing the nature, timing and extent of Further audit procedures

IV. Limitations of Internal Control:

1. **Internal control can provide only reasonable assurance:**
   Internal control can provide only reasonable assurance about achieving the entity's financial reporting objectives. The likelihood of their achievement is affected by inherent limitations of internal control.

2. **Human judgment in decision making:**
   Realities that human judgment in decision-making can be faulty and that breakdowns in internal control can occur because of human error. For example, there may be an error in the design of, or in the change to, a control

3. **Lack of understanding the purpose:**
   the operation of a control may not be effective, such as where information produced for the purposes of internal control for example, an exception report is not effectively used because the individual responsible for reviewing the information does not understand its purpose or fails to take appropriate action.

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4. **Collusion among people:**

Controls can be circumvented by the collusion of two or more people or inappropriate management override of internal control. For example, management may enter into side agreements with customers that alter the terms and conditions of the entity's standard sales contracts, which may result in improper revenue recognition.

5. **Judgements by management:**

In designing and implementing controls, management may make judgments on the nature and extent of the controls it chooses to implement, and the nature and extent of the risks it chooses to assume

6. **Limitations in case of Small Entities:**

Smaller entities often have fewer employees due to which segregation of duties is not practicable. However, in a small owner-managed entity, the owner-manager may be able to exercise more effective oversight than in a larger entity. This oversight may compensate for the generally more limited opportunities for segregation of duties.

V. Study of various aspects of IC:

i. GENERAL NATURE AND CHARACTERISTICS OF IC:

Purpose of Internal Control:

Internal control addresses identified business risks that threaten the achievement of any of the entity's objectives that concern:

1. The reliability of entity's financial reporting
2. The effectiveness and efficiency of its operations
3. Its compliance with applicable laws and regulations
4. Safeguarding of assets

ii. EXISTENCE OF A SATISFACTORY CONTROL ENVIRONMENT-NOT AN ABSOLUTE DETERRENT TO FRAUD

1. The existence of a satisfactory control environment can be a positive factor when the auditor assesses the risks of material misstatement.
2. However, it may help reduce the risk of fraud, a satisfactory control environment is not an absolute deterrent to fraud.
3. Conversely, deficiencies in the CE may undermine the effectiveness of controls, in particular in relation to fraud.

4. For example, mgmt's failure to commit sufficient resources to address IT security risks may adversely affect IC by allowing improper changes to computer programs or to data, or unauthorized transactions to be processed.
5. The CE in itself does not prevent, or detect and correct, a material misstatement.
6. However, influence the auditor's evaluation of the effectiveness of other controls (for example, the monitoring of controls and the operation of specific control activities) and thereby, the auditor's assessment of the risks of material misstatement

iii. ARE ALL CONTROLS RELEVANT TO THE AUDIT?

There is a direct relationship between an entity's objectives and the controls it implements to provide reasonable assurance about their achievement.

Factors relevant to the auditor's judgment about whether a control, individually or in combination with others, is relevant to the audit may include such matters as the following: [SLM NCC DRS]

1. Materiality
2. The significance of the Related risk.
3. The Size of the entity.
4. The Nature of the entity's business.
5. The Diversity and complexity of the entity's operations.
6. Applicable Legal and regulatory requirements.
7. The circumstances and the applicable Component of internal control.
8. The nature and Complexity of the systems.
9. Whether, and how, a Specific control, individually or in combination with others, prevents, or detects and corrects, material misstatement.

iv. NATURE AND EXTENT OF THE UNDERSTANDING OF IC

Evaluating the design of a control involves considering whether the control is capable of effectively preventing, or detecting and correcting, material misstatements. Implementation of a control means that the control exists and that the entity is using it. An improperly designed control may represent a significant deficiency in internal control.

Risk assessment procedures (IIO -T) to obtain AE about the design and implementation of relevant controls may include-
- -Inquiring of entity personnel.
- -Observing the application of specific controls.
- -Inspecting documents and reports.
- -Tracing transactions through the information system relevant to financial reporting.

Obtaining an understanding of an entity's controls is not sufficient to test their operating effectiveness.

v. CONTROLS OVER THE COMPLETENESS AND ACCURACY OF INFORMATION:

- Controls over the completeness and accuracy of information produced by the entity
- may be relevant to the audit if the auditor intends to make use of the information
- in designing and performing further procedures.

For example, in auditing revenue by applying standard prices to records of sales volume, the auditor considers the accuracy of the price information and the completeness and accuracy of the sales & volume data.

vi. INTERNAL CONTROL OVER SAFEGUARDING OF ASSETS:

Internal control over safeguarding of assets against unauthorised acquisition, use, or disposition may include controls relating to both financial reporting and operating objectives.

For example, use of access controls, such as passwords, that limit access to the data and programs that process cash disbursements may be relevant to a financial statement audit.

vii. COMPONENTS OF INTERNAL CONTROL: [C R I M E]

The Control Environment	Entity's Risk Assessment Process	Information System	Control Activities	Monitoring of Controls

a. Control Environment

The auditor shall obtain an understanding of the control environment. As part of obtaining this understanding, **the auditor shall evaluate whether:**

1. Management has created and maintained a culture of honesty and ethical behaviour; and

2. The strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control.

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Elements of the Control Environment [S H A P E - P C]

- Commitment to competence
- Participation by those charged with governance
- Management's philosophy and operating style
- Organizational Structure
- Assignment of authority and responsibility
- Human resource policies and practices

b. The Entity's Risk Assessment Process - Component of Internal Control [I S P A]

The auditor shall obtain an understanding of whether the entity has a process for:

1. Identifying business risks relevant to financial reporting objectives;
2. Estimating the Significance of the risks;
3. Assessing the likelihood of their occurrence; (Probability) and
4. Deciding about Actions to address those risks.

c. The IS, including the related business processes, relevant to FR and communication

The auditor shall obtain an understanding of the information system, including the business processes, relevant to financial reporting, including the following areas:

a. The classes of transactions in the entity's operations that are significant to the financial statements;

b. The procedures by which those transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in financial statements;

c. Backup records

d. How the information system captures events and conditions that are significant to the financial statements;

e. The financial reporting process used to prepare the entity's financial statements;

f. Controls surrounding journal entries

Control Activities:

The auditor shall obtain an understanding of control activities relevant to the audit, which the auditor considers necessary to assess the ROMM. An audit requires an understanding of only those control activities related to a **significant class of transactions, account balance, and disclosure** in the FS and the assertions which the auditor finds relevant in his RAP

Control activities are policies and procedures that help ensure management activities are carried out. [I S P P A]

Examples of specific control activities include those relating to the following-

- Authorization
- Performance Reviews
- Segregation of Duties
- Physical Controls
- Information Processing

Control activities that are relevant to the audit are:

- Control activities that relate to significant risks and those that relate to risks for which substantive procedures alone do not provide sufficient appropriate audit evidence; or
- Those that are considered to be relevant in the judgment of the auditor;
- 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.

d. Monitoring of Controls

The auditor shall obtain an understanding of the major activities that the entity uses to monitor internal control over financial reporting.

1. Monitoring of Controls defined: Monitoring of control is a process to assess the effectiveness of internal control performance over time.
2. Helps in assessing the effectiveness of controls on a timely basis
3. Management accomplishes monitoring of controls through ongoing activities, separate evaluations, or a combination of the two.
4. Management's monitoring activities may include using information from communications from external parties such as customer complaints and regular comments that may indicate problems or highlight areas in need of improvement.

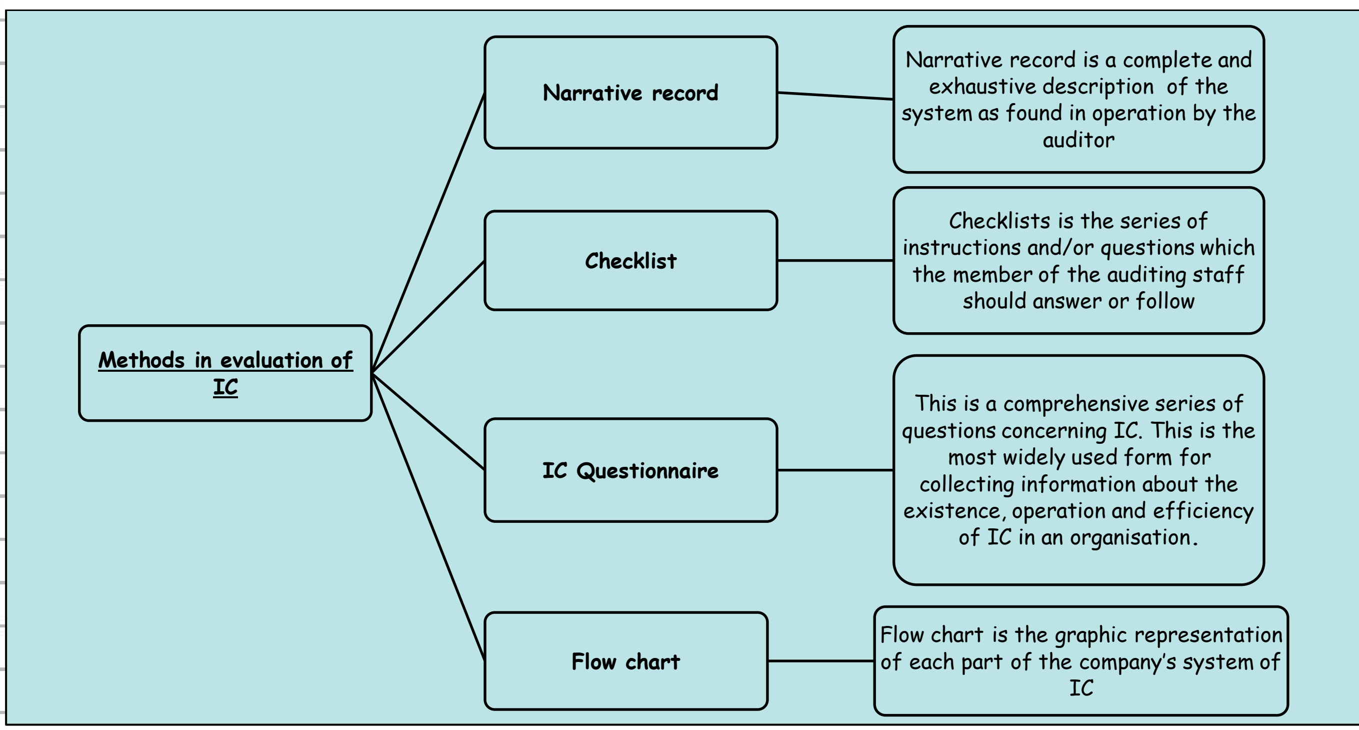
5. In case of Small Entities: Mgmt's monitoring of control is often accomplished by mgmt's or the owner -manager

VI. BENEFITS OF EVALUATION OF IC BY AUDITOR

The auditor should gain an understanding of the accounting system and the related internal controls and should study and evaluate the operations of these IC upon which he wishes to rely in determining the nature, timing and extent of other audit procedures.

The review of IC will enable the auditor to know:

- Whether errors and frauds are likely to be located in the ordinary course of operations of the business
- Whether an adequate IC system is in use and operating as planned by the management
- Whether an adequate IC system is in use and operating as planned by the management
- Whether any administrative control has a bearing on his work
- Whether the controls adequately safeguard the assets
- How far and how adequately the management is discharging its functions in so far as correct recording of transactions is concerned
- How reliable, the reports, records and the certificate to the management can be.
- The extent and the depth of the examination he needs to carry out in different areas of accounting
- What would be the appropriate audit technique and the audit procedure in the given circumstances
- What are the areas where control is weak and where it is excessive
- Whether some worthwhile suggestions can be given to improve the control system



VII. TESTING OF INTERNAL CONTROLS [I I O- TR]

Testing of controls are performed to obtain AE about the effectiveness of:

a. Design of the accounting and IC system and,

b. Operations of the IC throughout the period

Test of controls may include:

- Inspection of documents supporting transactions and other events to gain AE that the IC have operated properly
- Inquiries about and Observation of, IC which leave no audit trail
- Reperformance involves the auditor's independent execution of procedures or controls that were originally performed as part of the entity's IC
- Testing of IC operating on specific computerised applications or over the overall information technology function.

VIII. RISKS THAT REQUIRE SPECIAL AUDIT CONSIDERATION:

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) The complexity of transactions

d) Whether the risk involves significant transactions with related parties

e) The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty and

f) Whether the risk involves significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual

IDENTIFYING SIGNIFICANT RISKS:

Significant risks are inherent risks with both a higher likelihood of occurrence and a higher magnitude of potential misstatement. The auditor assesses assertions affected by a significant risk as higher inherent risk. The following are always significant risks:

1. Risks of material misstatement due to fraud
2. Significant transactions with related parties that are outside the normal course of business for the entity

Risks of Material Misstatement – Greater for Significant Non-Routine Transactions

Risks of material misstatement may be greater for significant non-routine transactions arising from matters such as the following:

1. Greater management intervention to specify the accounting treatment.
2. Greater manual intervention for data collection and processing.
3. Complex calculations or accounting principles.
4. The nature of non-routine transactions, which may make it difficult for the entity to implement effective controls over the risks.

Risks of material misstatement– Greater for Significant Judgmental Matters:

Risks of material misstatement may be greater for significant judgmental matters that require the development of accounting estimates, arising from matters such as the following:

1. Accounting principles for accounting estimates or revenue recognition may be subject to differing interpretation.
2. Required judgment may be subjective or complex, or require assumptions about the effects of future events, for example, judgment about fair value

SA 320 MATERIALITY

SA 320

- I. What is SA 320?
- II. Auditor's Responsibility?
- III. Maturity as per FRF
- IV. Judgement about size of Materiality provides basic For
- V. Statutory Requirements
- VI. Professional Judgement (Auditor's assumption about users)

- VII. Performance Materiality

- VIII. BENCHMARK
- IX. Factors affecting identification of BM
- X. Relevant Financial data for BM
- XI. Professional Judgement

- XII. Lesser than materiality affecting user decision
- XIII. Documenting the materiality

- XIV. Audit Risk

I. What is SA 320?

SA320 Materiality in planning and performing an audit state that misstatements, including omissions, are material, if they individually or in aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Materiality is not always a matter of relative size. For example, a small amount lost by fraudulent practices of certain employees can indicate a serious flaw in the enterprise's Internal Control system requiring immediate attention to avoid greater losses in the future.

II. Auditor's Responsibilities

The concept of materiality is applied by the auditor in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the FS and in forming an opinion in the auditor's report.

SA320 deals with the auditor's responsibility in planning and performing an audit of FS.

III Financial Reporting Frameworks

often discuss the concept of materiality in the context of the preparation and presentation of financial statements. Although financial reporting frameworks may discuss materiality in different terms, they generally explain that

- Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements;
- Judgments about materiality are made in the light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both; and
- Judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.

IV. In planning the audit, the auditor makes judgements about the size of misstatements that will be considered material. These judgements provide a basis for:

a) Determining the nature, extent and timing of Risk Assessment procedure
b) Determining the nature, extent and timing of further audit procedures
c) Identifying and assessing the risk of material misstatement

The auditor has to apply his professional judgement in determining materiality, choosing appropriate benchmark and determining the level of benchmark.

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V. Statutory Requirements

If there is any statutory requirement of disclosure, it is to be considered material irrespective of the value of amount. Examples are given below: -

- As per Division I of schedule III of Companies Act, 2013, any item of income or expenditure which exceeds one percent of the revenue from operations or ₹ 1,00,000, whichever is higher, needs to be disclosed separately.
- A company should disclose in notes to accounts, shares in the company held by each shareholder holding more than 5 per cent shares specifying the number of shares held as per requirements of Division I of Schedule III of Companies Act,2013.

VI. Determination of Materiality- A matter of professional judgement

It is reasonable for the auditor to assume that the users:

a) Have a reasonable knowledge of business and economic activities and accounting and willingness to study the information in the FS with reasonable diligence.

b) Understand that the FS are prepared, presented and audited to levels of materiality.

c) Recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgement and consideration of future events.

d) Make reasonable economic decisions on the basis of the information in the FS.

VII. Performance Materiality

Practically it is difficult for auditors to design tests to identify individual misstatements. When misstatements are material in aggregate, it takes us to the concept of Performance materiality.

PM means the amount or amounts set by the auditor at less than materiality for the FS as a whole to reduce to an appropriately low level the probability of the aggregate uncorrected and undetected misstatement exceeds materiality for the FS as a whole.

PM is always set at a lower value than overall materiality. It lowers the risk that the auditor will not be able to identify misstatements that are material when added together.

The auditor must determine materiality and Performance Materiality while planning the audit:

If for a particular Account balance, Class of transaction or disclosure- misstatements of lesser amounts than materiality could reasonably be expected to affect the economic decisions of the users of the FS, the auditor shall also determine materiality for each of ABCD.

VIII BENCHMARKS

Benchmarks (BM) in determining materiality for the FS as a whole.

A percentage is normally applied to the benchmark to determine the materiality. Examples of BM that maybe appropriate depending on the circumstances of the entity include categories of reported income such as PBT, Total revenue, gross profit, total expenses, total equity or net asset value.

IX. Factors that may affect the identification of an appropriate

a) Elements of FS like Assets, liabilities, Equity, revenue, Expenses

b) Whether item/items require the attention of users. For example, for the purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets.

c) The nature of the entity. (The industry, economic environment, ownership structure and the way it is financed)

d) The relative volatility of the benchmark

X. In relation to the chosen BM, relevant financial data

a) Prior period financial results

b) Period to date financial results

c) Budget or forecasts for the current period

d) Adjusted for significant changes in the circumstances of the entity (Eg. Business acquisition) and changes in the conditions of the economic environment.

XI. Determining a percentage to be applied to a chosen BM involves the exercise of Professional

There is a relationship between the percentage and the chosen benchmark, such that a percentage applied to profit before tax from continuing operations will normally be higher than a percentage applied to total revenue.

Consider, for example, that the auditor may consider 5% of profit before tax from continuing operations to be appropriate for a profit-oriented entity in a manufacturing industry, while the auditor may consider 1% of total revenue or total expenses to be appropriate for a not-for-profit entity. Higher or lower percentages, however, may be deemed appropriate in different circumstances.

XII. Materiality Level or Levels for Particular Classes of Transactions, Account Balances or Disclosures (ABCD lesser than materiality affecting user's decision)

Factors that may indicate the existence of one or more particular classes of transactions, account balances or disclosures (ABCD) for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements include the following:

1. Whether law, regulations or the applicable financial reporting framework affect users' expectations regarding the measurement or disclosure of certain items like in case of related party transactions, and the remuneration of management and those charged with governance.
2. The key disclosures in relation to the industry in which the entity operates. For example, research and development costs for a pharmaceutical company.
3. Whether attention is focused on a particular aspect of the entity's business that is separately disclosed in the financial statements like in case of newly acquired business.

XIII. Documenting the Materiality

a) Materiality for the FS as a whole
b) If applicable, the materiality levels for a particular ABCD
c) Performance Materiality
d) Any revision of the above (a-c) as the audit progressed.

? Can you revise materiality as audit progresses?

XIV. Materiality and Audit Risk

They are considered throughout the audit when:

a) Identifying and assessing the Risk of Material Misstatement
b) Determining the NET of FAP
c) Evaluating the effect of uncorrected misstatements on the FS and forming an opinion in the auditor's report.

AUTOMATED ENVIRONMENT

Automated Environment

- I. What?
- II. Key Features?
- III. Understanding and documenting automated environment
- IV. Risks arising from the use of IT
- V. Impact of IT related risks
- VI. Types of controls
  - 1. General IT
  - 2. Application
  - 3. IT dependent controls
- VII. General IT vs Application Controls
- VIII. Characteristics of manual and automated controls
- IX. Suitability
- X. Testing methods in an automated environment
- XI. Audit approach in an automated environment
- XII. Data Analytics
- XIII. Digital Audit
- XIV. IFC
- XV. Documenting the risks
- XVI. Assess and report

I. WHAT IS AUTOMATED ENVIRONMENT?

An automated environment basically refers to a business environment where the processes, operations, accounting and even decisions are carried out by using computer systems – also known as Information Systems (IS) or Information Technology (IT) systems. Nowadays, it is very common to see computer systems being used in almost every type of business.

II.

Key Features of an automated Environment:

1. Enables faster business operation
2. Accuracy in data processing and computation
3. Ability to process large volume of transactions
4. Integration amongst business operations
5. Better security and controls
6. Less prone to human errors
7. Provides latest information
8. Connectivity and networking capability

III.

Understanding and Documenting automated environment

1. Information systems being used (one or more application systems and what they are)
2. Their purpose (financial and non-financial)
3. Location of IT systems - local vs global
4. Architecture (desktop based, client-server, web application, cloud based)
5. Version (functions and risks could vary in different versions of same application).
6. Interfaces within systems (in case multiple systems exist).
7. In-house vs Packaged.
8. Outsourced activities (IT maintenance and support).
9. Key persons (CIO, CISO, Administrators)

IV. RISK ARISING FROM THE USE OF IT SYSTEMS

1. Inaccurate processing of data, processing inaccurate data, or both.
2. Unauthorized access to data.
3. Direct data changes (backend changes).
4. Excessive access / Privileged access (super users).
5. Lack of adequate segregation of duties.
6. Unauthorized changes to systems or programs.
7. Failure to make necessary changes to systems or programs.
8. Loss of data

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V. IMPACT OF IT RELATED RISKS

- **Impact on substantive checking:**
  Inability to address above discussed risks may lead to non-reliance of data obtained from systems. In such a case, all information, data, and reports would have to be tested thoroughly for their completeness and accuracy. It could lead to increased substantive checking i.e., detailed checking.
- **Impact on controls:**
  It can lead to non-reliance on automated controls; system calculations and accounting procedures built into applications. It may result in additional audit work.
- **Impact on reporting:**
  Due to regulatory requirements in respect of internal financial controls (discussed in subsequent paras) in case of companies, it may lead to modification of auditor's report in some instances.

VI. TYPES OF CONTROLS IN AN AUTOMATED ENVIRONMENT

1. General IT controls

General IT controls are policies and procedures that relate to many applications and support the effective functioning of application controls. These are IT controls generally implemented to mitigate the IT specific risks and applied commonly across multiple IT systems, applications and business processes. Hence, General IT controls are known as "pervasive" controls or "indirect" controls.

GENERAL IT CONTROLS

a) Data centre and network operations

b) Program change

c) Access security

d) Application system acquisition, development, and maintenance (Business Applications)

a) **Controls over Data centre and network operations: -** The objective of controls over Data centre and network operations is to ensure that production systems are processed to meet financial reporting objectives. These include activities such as overall management of computer operation activities, preparing, scheduling, and executing of batch jobs, monitoring, storage, and retention of backups. Matters such as BCP (Business continuity plan) and DRP (Disaster recovery plan) which deal with recovery from failures are also taken care of by such type of controls

b) **Program Change**: -

The objective of program change controls is to ensure that modified systems continue to meet financial reporting objectives. It includes activities such as change management process, recording, managing and tracking change requests, making and testing changes etc.

c) **Access Security: -**

The objective of controls over access security is to ensure that access to programs and data is authenticated and authorized to meet financial reporting objectives. It includes activities such as security organization & management, security policies & procedures, application security, data security, operating system security, network security, physical security etc.

d) **Application system acquisition, development, and maintenance: -**

The objective of such controls is to ensure that systems are developed, configured and implemented to meet financial reporting objectives. It includes overall management of development activities, project initiation, analysis & design, construction, testing & quality assurance etc.

2. Application Controls:

Application controls include both automated or manual controls that operate at a business process level. Automated Application controls are embedded into IT applications viz., ERPs and help in ensuring the completeness, accuracy and integrity of data in those systems. Examples of automated applications include edit checks and validation of input data, sequence number checks, user limit checks, reasonableness checks, mandatory data fields.

3. IT dependent controls:

IT dependent controls are basically manual controls that make use of some form of data or info or report produced from IT systems and applications. In this case, even though the control is performed manually, the design and effectiveness of such controls depends on the reliability of source data. Due to the inherent dependency on IT, the effectiveness and reliability of automated application controls and IT dependent controls require the General IT controls to be effective.

VII. GENERAL IT CONTROLS VS. APPLICATION CONTROLS:

1. These two categories of control over IT systems are interrelated.
2. The relationship between the application controls and the General IT Controls is such that General IT Controls are needed to support the functioning of application controls, and both are needed to ensure

complete and accurate information processing through IT systems.

VIII. CHARACTERISTICS OF MANUAL AND AUTOMATED ELEMENTS OF IC RELEVANT TO THE AUDITOR'S RISK ASSESSMENT

The characteristics of Manual or Automated elements are relevant to the auditor's risk assessment and FAP based thereon. The use of Manual or Automated elements in IC also affects the manner in which transactions are initiated, recorded, processed, and reported:

1. **Controls in Manual systems** may include such procedures as approvals and reviews of transactions, and reconciliations and follow-up of reconciling items. Alternatively, an entity may use automated procedures to initiate, record, process, and report transactions, in which case records in electronic format replace paper documents.

2. **Controls in IT systems** consist of a combination of automated controls e.g. controls embedded in computer programs and manual controls. Further, manual controls may be independent of IT, may use info produced by IT, or may be limited to monitoring the effective functioning of IT & automated controls, & to handling exceptions.

IX. SUITABILITY OF MANUAL AND AUTOMATED CONTROLS:

Manual elements are more suitable:

1. Large, unusual or non-recurring transactions.
2. Circumstances where errors are difficult to define, anticipate or predict
3. In changing circumstances that require a control response outside the scope of an existing automated control.
4. In monitoring the effectiveness of automated controls.

Manual Elements less suitable:

1. High volume or recurring transactions, or in situations where errors that can be anticipated or predicted can be prevented, or detected and corrected, by control parameters that are automated.
2. Control activities where the specific ways to perform the control can be adequately designed and automated.

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X. TESTING METHODS IN AN AUTOMATED ENVIRONMENT:

(IIO-

1.Inquiry → 2.Inspection → 3.Observation → 4.Reperformance

1. Inquiry is the most efficient audit test but it also gives the least audit evidence.
2. Inquiry should always be used in combination with any one of the other audit testing methods.
3. Inquiry alone is not sufficient.
4. Reperformance is most effective as an audit test and gives the best audit evidence.
5. However, testing by reperformance could be very time consuming and least efficient most of the time.
6. Generally, Applying inquiry in combination with inspection gives the most effective and efficient audit evidence.

However, which audit test to use, when and in what combination is a matter of professional judgement and will vary depending on several factors including risk assessment, control environment, desired level of evidence required, history of errors/misstatements, complexity of business, assertions being addressed etc.

XI. AUDIT APPROACH IN AN AUTOMATED ENVIRONMENT:

Risk assessment	Understand and evaluate	Test for operating effectiveness	Reporting
• Identify significant A/cs and disclosures • Qualitative and Quantitative considerations • Relevant Financial statement assertions(FSA) • Identify likely sources of misstatement • Cosider risk arising from use of IT systems	• Document understanding of business processes using flowcharts/ narrative • Prepare risk and control matrices (RCM) • Understand design of controls by performing walkthroughs of end-to-end process • Process wide considerations for entity level controls, segregation of duties • IT general controls, Application controls	• Assess NTE of controls tesing • Assess reliability of source data; completeness of population • Testing of key reports and spreadsheets • Sample testing • Consider competence and independence of staff/team performing controls testing	• Evaluate control deficiencies • Significant deficiencies, material weaknesses • Remediation of control weaknesses • Internal controls memo (ICM) or mgmt letter • Auditor's report

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XII. DATA ANALYTICS FOR AUDIT

The combination of processes, tools and techniques that are used to tap vast amounts of electronic data to obtain meaningful information is called Data Analytics. Auditors can make use of similar tools and techniques in the audit process and obtain good results. The tools and techniques that auditors use in applying the principles of data analytics are known as Computer Assisted Auditing Techniques or CAATs in short.

Data analytics can be used in testing of electronic records and data residing in IT systems using spreadsheets and specialized audit tools viz., IDEA and ACL to perform the following:

1. Check completeness of data and population that is used in either TOCs or substantive audit tests.
2. Selection of audit samples – i.e. random sampling, systematic sampling.
3. Re-computation of balances – reconstruction of trial balance from transaction data.
4. Reperformance of mathematical calculations – e.g. Depreciation, bank interest calculation.
5. Analysis of journal entries
6. Fraud investigation.
7. Evaluating impact of control deficiencies.

XIII. DIGITAL AUDIT

1. Entities are embracing digitization as part of their operations to keep pace with changing times.
2. New technologies are helping companies revamp their operations and rethink the way business is conducted.
3. Companies are restructuring their business models driven by technology.
4. Automation is key to Digitization.
5. In such a business environment, Use of digital technology is being made by auditors right from planning to expression of Final opinion.
6. Auditors are making use of artificial intelligence, data analytics & other latest technologies to help understand business processes in a better way.
7. By using such tools, Auditors can conduct audit in a better way & devote more attention to areas requiring greater focus.
8. Digital audit is helping auditors to better identify risks making use of technology.

XIV. INTERNAL FINANCIAL CONTROLS

The term Internal Financial Controls (IFC) basically refers to the policies & procedures put in place by companies for ensuring : -

1. Reliability of financial reporting
2. Effectiveness and efficiency of operations

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3. Compliance with applicable laws and regulations
4. Safeguarding of assets
5. Prevention and detection of frauds

XV. DOCUMENTING THE AUDIT

The auditor shall document:

1. The discussion among the engagement team and the significant decisions reached
2. Key Elements of the understanding obtained regarding each of the aspects of the entity and its environment & each of the IC components, the sources of info from which the understanding was obtained; and the RAP performed.
3. The identified and assessed RoMM at the FS level and at the Assertion level and
4. The risks identified, & related controls about which the auditor has obtained an understanding.

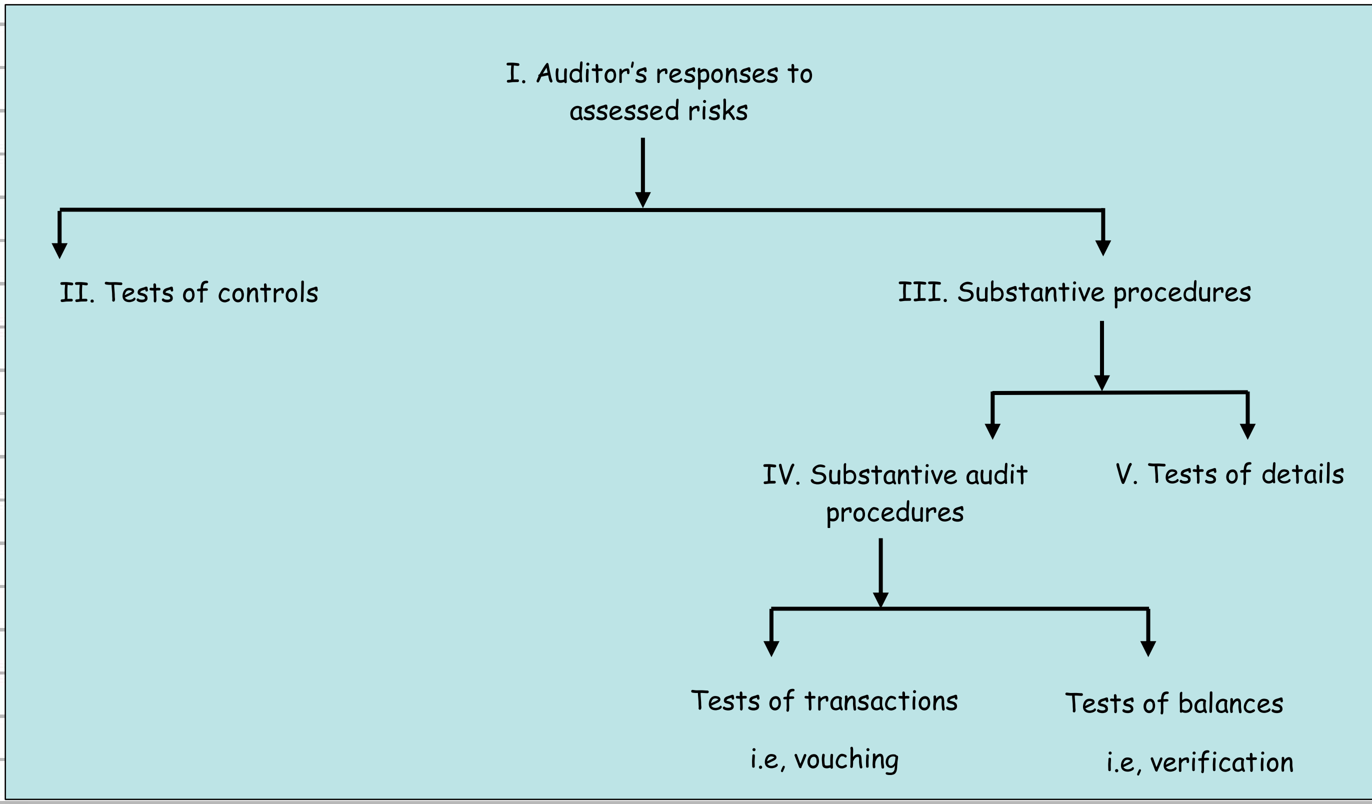
XVI. ASSESS AND REPORT AUDIT FINDINGS

At the conclusion of each audit, there will be certain findings or exceptions in IT environment & IT controls of the company that need to be assessed & reported to relevant Stakeholders incl Mgmt and TCWG viz., BOAs, Audit committee.

Some **points to consider** are as follows:

1. Are there any weaknesses in IT controls?
2. What is the impact of these weaknesses on overall audit?
3. Report deficiencies to management – ICM or Mgmt Letter.
4. Communicate in writing any Sign. deficiencies to TCWG

SA 330 THE AUDITOR'S RESPONSES TO ASSESSED RISKS



I. SA 330- THE AUDITOR'S RESPONSES TO ASSESSED RISKS:

SA 330- The auditor's responses to assessed risks deals with the auditor's responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor in accordance with SA 315, "Identifying and Assessing Risks of Material Misstatement Through Understanding the Entity and Its Environment" in a financial statement audit.

SA 330 states that: -

a) The auditor shall design and implement overall responses to address the assessed RoMM at the FS level.

b) The auditor shall design and perform FAP whose NTE are based on and are responsive to the assessed RoMM at the assertion level.

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In designing the FAP to be performed, the auditor

a) Consider the reasons for the assessment given to the RoMM at the assertion level for each class of transactions, account balance, and disclosure, including:

- The likelihood of material misstatement due to the particular characteristics of ABCD (i.e., the inherent risk); and
- Whether the risk assessment takes into account the relevant controls (i.e., the control risk), thereby requiring the auditor to obtain AE to determine whether the controls are operating effectively (i.e., the auditor intends to rely on the operating effectiveness of controls in determining the NTE of substantive procedures); and

b) Obtain more persuasive AE, the higher the auditor's assessment of risk.

The auditor shall design and perform TOCs to obtain SAAE as to the operating effectiveness of relevant controls when:

a) The auditor's assessment of ROMM 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 NTE of substantive procedures); or

b) Substantive procedures alone cannot provide SAAE at the assertion level.

II. TEST OF CONTROLS

i. Extent	ii. Designing & Performing TOC	iii. Timing	iv. Using AE obtained in Previous Audits	v. Specific enquiries when deviations are detected

i. EXTENT

Matters the auditor may consider in determining the **extent** of test of controls include the following:

ii. IN DESIGNING AND PERFORMING TEST OF CONTROLS, THE AUDITOR SHALL

1. Perform other Audit procedures in combination with Inquiry to obtain AE about the operating effectiveness of the controls, including:
   - How the controls were applied at relevant times during the period under audit.
   - The consistency with which they were applied.
   - By whom or by what means they were applied.

2. Determine whether the controls to be tested depend upon other controls (indirect controls), and if so, whether it is necessary to obtain audit evidence supporting the effective operation of those indirect controls

Inquiry alone is not sufficient to test the operating effectiveness of controls. Accordingly, other audit procedures are performed in combination with inquiry. In this regard, Inquiry combined with Inspection or Reperformance may provide more assurance than Inquiry and Observation, since an observation is pertinent only at the point in time at which it is made.

iii. TIMING OF TEST OF CONTROLS

The auditor shall test controls for the particular time, or throughout the period, for which the auditor intends to rely on those controls in order to provide an appropriate basis. AE pertaining only to a point in time may be sufficient for the auditor's purpose. for example, when testing controls over the entity's physical inventory counting at the period end.

iv. USING AE OBTAINED IN PREVIOUS AUDITS

In determining whether it is appropriate to use AE about the operating effectiveness of controls obtained in previous audits, and the length of the time period that may elapse before retesting a control, **the auditor shall consider the following:**

1. The effectiveness of other elements of IC, including the control Environment, the entity's Monitoring of controls, and the entity's Risk assessment process i.e. CRIME
2. The Risks arising from the characteristics of the control, including whether it is manual or automated
3. The effectiveness of General IT-controls
4. The effectiveness of the control and its application by the entity, including the nature and extent of deviations in the application of the control noted in previous audits, and whether there have been personnel changes that significantly affect the application of the control

5. Whether lack of a change in a particular control poses a risk due to changing circumstances and
6. The ROMM and the extent of reliance on the control

v. SPECIFIC INQUIRIES BY AUDITOR WHEN DEVIATIONS FROM CONTROLS ARE DETECTED:

When deviations from controls upon which the auditor intends to rely are detected, the auditor shall make **specific inquiries** to understand these matters and their potential consequences, and shall determine whether:

a. The Test of controls that have been performed provide an appropriate basis for reliance on the controls
b. Additional TOCs are necessary or
c. The potential RoMM need to be addressed using substantive procedures.

Irrespective of the assessed ROMM, the auditor shall design and perform substantive procedures for each Material class of transactions, account balance, and disclosure.

III. SUBSTANTIVE PROCEDURES

Substantive procedures are audit procedures designed to detect material misstatements at the assertion level. Substantive procedures comprise:

1. TODs (of classes of transactions, account balances, disclosures), and → 2. Substantive Analytical procedures

IV. SUBSTANTIVE ANALYTICAL PROCEDURES

What is analytical procedures- given in SA 520!

NATURE AND EXTENT OF SUBSTANTIVE PROCEDURES

Depending on the circumstances, the auditor may determine that:

1. Performing only substantive analytical procedures will be sufficient to reduce audit risk to an acceptably low level. E.g. where the auditor's assessment of risk is supported by audit evidence from tests of controls.
2. Only tests of details are appropriate.

3. A combination of substantive analytical procedures and tests of details are most responsive to the assessed risks.

Because the assessment of the risk of material misstatement takes account of internal control, the extent of substantive procedures may need to be increased when the results from test of controls are unsatisfactory. In designing tests of details, the extent of testing is ordinarily thought of in terms of the sample size.

V. TEST OF DETAILS

Tests of details are further classified into :

1.Tests of transactions **i.e., vouching**
2.Tests of balances **i.e., verification.**

For example, for a test of transaction a purchase transaction may be verified by examining the related purchase invoice, goods received note, inward gate entry register. Such tests of transactions help in establishing the authenticity of transactions recorded in BOAs.

Tests of balances consist of verification of assets as well as liabilities. Verification of an item of fixed asset, e.g. would help in establishing existence of that asset as on date of BS. by reviewing entity's plan for performing physical verification of fixed assets and obtaining evidence for performance of physical verification of fixed assets by mgmt.

SA 260 "COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE"

SA 260

- I. Why SA 260?
- II. Objectives
- III. Matters to be communicated by the auditor
- IV. Communication process
- V. Adequacy
- VI. Documentation

I. Why SA 260?

SA 260 deals with the auditor's responsibility to communicate with Those Charged With Governance in an audit of Financial statements.

II. Objective of auditor:

- To communicate clearly with TCWG the responsibilities of the auditor in relation to the FS audit and an overview of the planned scope and timing of the audit
- Obtain information relevant to the audit from TCWG
- Provide TCWG with timely observations from the audit that are significant and relevant to their responsibility to oversee the FR process
- To promote effective 2 way communication

III Matters to be communicated by the auditor:

1. The auditor's responsibilities in relation to the financial statement audit

2. Planned scope and timing of the audit.
3. Significant findings from the audit

- The auditor shall communicate with TCWG: -

i. 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 AFRF, not to be most appropriate to the particular circumstances of the entity

ii. Significant difficulties, if any, encountered during the audit;

iii. Unless all of TCWG are involved in managing the entity: -

➢ Significant matters arising during the audit that were discussed, or subject to correspondence, with management;

➢ Written representations the auditor is requesting

iv. Circumstances that affect the form and content of the auditor's report, if any and

v. 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.

Communication of auditor's independence in case of listed entities :

a. A statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence and

b. (i) 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. These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor and

(ii) The related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level

IV. Communication process

The auditor shall communicate with those charged with governance the form, timing and expected general content of communications. 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. Written communications need not include all matters that arose during the course of the audit. The auditor shall communicate in writing with those charged with governance regarding auditor independence when required in case of listed entities. The auditor shall communicate with those charged with governance on a timely basis

In the case of listed entities, auditor shall communicate with TCWG about auditor's independence:

A statement that the ET and others in the firm as appropriate, have complied with relevant ethical requirements regarding independence

V. Adequacy of the communication process

The auditor shall evaluate whether the two-way communication between the auditor and those charged with governance 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.

VI. Documentation

Where matters required by SA260 to be communicated are communicated orally, the auditor shall include them as per SA 230 about when and to whom, what is communicated.
Where matters have been communicated in writing, the auditor shall retain a copy of the communication as part of the documentation.
Communicating significant deficiencies in Internal control in writing to TCWG reflects the importance of these matters and assists TCWG in fulfilling their oversight responsibilities.

SA 265 "COMMUNICATING DEFICIENCIES IN INTERNAL CONTROL TO THOSE CHARGED WITH GOVERNANCE AND MANAGEMENT"

SA 265

- I. Deficiency exists when
- II. Significant deficiency in IC
- III. Communication
- IV. Examples
- V. Examples of indicators
- VI. Written communication

I. Deficiency exists when:

Deficiency in Internal Control- This exists when

- A control is designed, implemented or operated in such a way that it is unable to prevent, detect and correct misstatements in the FS on a timely basis
- A control necessary to prevent or detect and correct misstatements in the FS on a timely basis is missing

II. Significant deficiency in IC - It exists when

A deficiency or a combination of deficiencies in the Internal Control that is of sufficient importance tomerit the attention of TCWG

The auditor shall determine whether on the basis of audit work performed, the auditor has identified one or more deficiencies in the Internal control.

The auditor shall further identify if individually or in combination, they constitute significant deficiencies.

III. Communication against significant deficiencies in Internal Control to TCWG

The auditor shall communicate in writing significant deficiencies in Internal Control identified during the audit to TCWG on a timely basis. The auditor shall also communicate with the management on a timely basis:

- In writing, significant deficiencies in IC that the auditor has communicated or intends to communicate with TCWG, unless it is inappropriate to communicate with the management
- Other deficiencies in the IC identified during the audit that have not been communicated to the management and are of sufficient importance to merit management's attention

IV. Examples of matters that the auditor may consider in determining whether a deficiency or combination of deficiencies in internal control constitutes a significant

- The likelihood of the deficiencies leading to material misstatements in the financial statements in the future.
- The susceptibility to loss or fraud of the related asset or liability.
- The subjectivity and complexity of determining estimated amounts, such as fair value accounting estimates.

- The financial statement amounts exposed to the deficiencies.
- The volume of activity that has occurred or could occur in the account balance or class of transactions exposed to the deficiency or deficiencies.
- The cause and frequency of the exceptions detected as a result of the deficiencies in the controls.
- The interaction of the deficiency with other deficiencies in internal control.
- The importance of the controls to the financial reporting process,

for example:

- General monitoring controls (such as oversight of management).
- Controls over the prevention and detection of fraud.
- Controls over the selection and application of significant accounting policies.
- Controls over significant transactions with related parties.
- Controls over significant transactions outside the entity's normal course of business.
- Controls over the period-end financial reporting process (such as controls over non-recurring journal entries

V. Examples of indicators of significant deficiencies in internal control

- Evidence of ineffective aspects of the control environment, such as:
  - Indications that significant transactions in which management is financially interested are not being appropriately scrutinised by those charged with governance.
  - Identification of management fraud, whether or not material, that was not prevented by the entity's internal control.
  - Management's failure to implement appropriate remedial action on significant deficiencies previously communicated.
- Absence of a risk assessment process within the entity where such a process would ordinarily be expected to have been established.
- Evidence of an ineffective entity risk assessment process, such as management's failure to identify a risk of material misstatement that the auditor would expect the entity's risk assessment process to have identified.
- Evidence of an ineffective response to identified significant risks (e.g., absence of controls over such a risk).
- Misstatements detected by the auditor's procedures that were not prevented, or detected and corrected, by the entity's internal control.
- Disclosure of a material misstatement due to error or fraud as prior period items in the current year's Statement of Profit and Loss.
- Evidence of management's inability to oversee the preparation of the financial statements.

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VI. The auditor shall include in the written communication to the management and

A description of deficiencies and explanation of their potential effects	Sufficient information to enable TCWG and management to understand the context of communication

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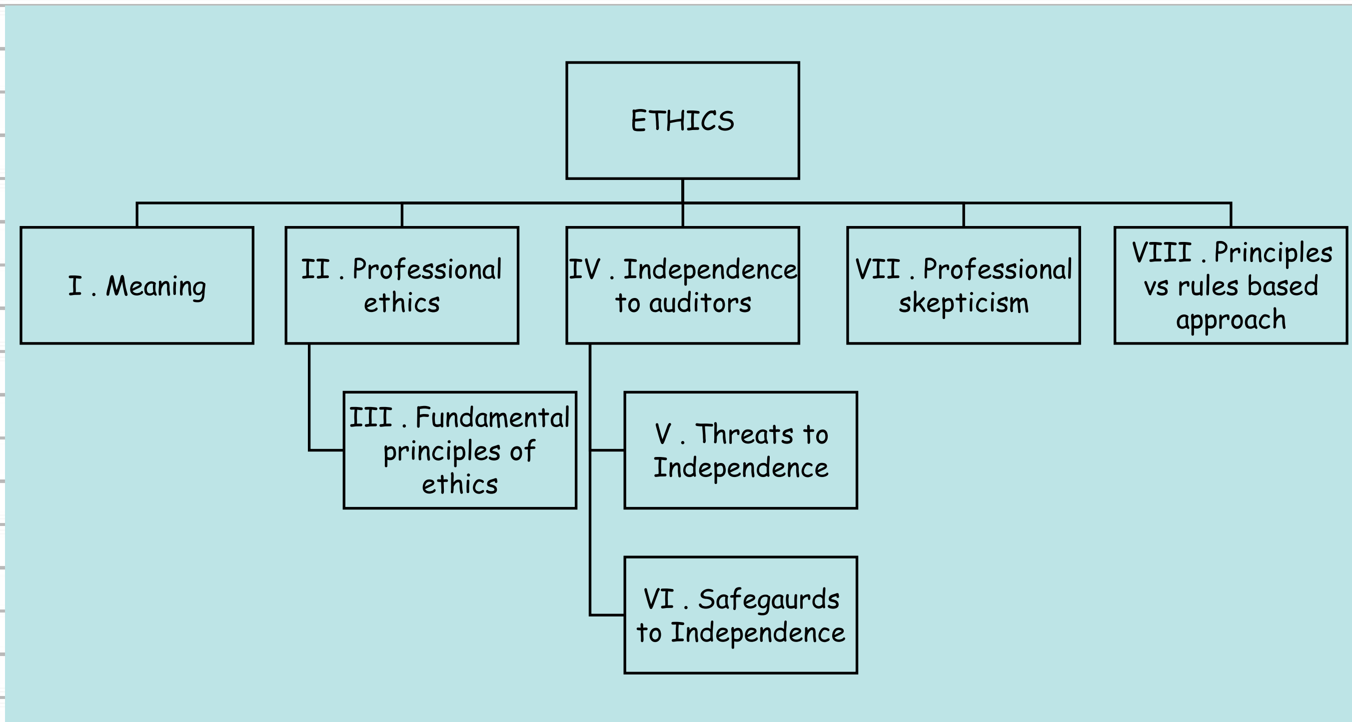
ETHICS



I. MEANING OF ETHICS

The term "Ethics" means moral principles which govern a person's behaviour. Ethics is something which comes from an individual intrinsically. It has to be inculcated in the habit and temperament of an individual, so that there is an overall culture of ethics; the force has to be strong enough to withstand any selfish motive or temptation. It is a state of mind to act and perform in accordance with moral principles. Ethics is the science of morals in human conduct. Such moral principles and rules of conduct impose obligations upon individuals

II. PROFESSIONAL ETHICS

Professional ethics seek to protect the interests of the profession as a whole and act as a shield that enables us to command respect. A Chartered Accountant, either in practice or in service, has to abide by ethical behaviours. They are expected to follow the fundamental principles of the profession.

The deviation from the ethical responsibilities brings the disciplinary mechanism into action against the Chartered Accountants which may result into fines, suspension of membership, removal from membership or other disciplinary actions.

III. FUNDAMENTAL PRINCIPLES OF PROFESSIONAL ETHICS

Principle 1: Objectivity

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

Principle 2: Professional competence and due care-

Requires an accountant to attain and maintain professional knowledge and skill at the level required to ensure that a client or employing organization receives competent professional service, based on current technical and professional standards and relevant legislation;

Principle 3: Integrity

A professional accountant shall comply with the principle of integrity, which requires an accountant to be straightforward and honest in all professional and business relationships. Integrity implies fair dealing and truthfulness. A professional accountant shall not knowingly be associated with reports, returns, communications or other information where the accountant believes that the information contains a materially false or misleading statement;

Principle 4: Confidentiality

Confidentiality principle requires a professional accountant to respect the confidentiality of information acquired as a result of professional or business relationships.

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.

Principle 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.

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IV. INDEPENDENCE TO AUDITOR'S ETHICS

Independence of mind – the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism; and

Independence in appearance –

the avoidance of facts and circumstances that are so significant that a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm's, or a member of the assurance team'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 relationship between the auditor and his client should be such that firstly, he is himself satisfied about his independence and secondly, no unbiased person would be forced to the conclusion that, on an objective assessment of the circumstances, there is likely to be an abridgement of the auditors' independence.

There are two interlinked perspectives of independence of auditors, one, independence of mind and two, independence in appearance.

V. THREATS TO INDEPENDENCE

Threat 1: Self interest threats

Self-interest threats occur when an auditing firm, its partner or associate could benefit from a financial interest in an audit client.

Examples include

a. direct financial interest or materially significant indirect financial interest in a client

b. loan or guarantee to or from the concerned client

c. undue dependence on a client's fees and, hence, concerns about losing the engagement

d. close business relationship with an audit client

e. potential employment with the client and

f. contingent fees for the audit engagement

Threat 2: Self review threats

Self-review threats occur when during a review of any judgement or conclusion reached in a previous audit or non- audit engagement, or when a member of the audit team was previously a director or senior employee of the client. Non audit services include any professional services provided to an entity by an auditor, other than audit or review of the financial statements. These include management services, internal audit, investment advisory service etc.

- Instances where such threats come into play are: -
  - when an auditor having recently been a director or senior officer of the company.
  - when auditors perform services that are themselves subject matters of audit.

Threat 3: Advocacy

Advocacy threats occur when the auditor promotes, or is perceived to promote, a client's opinion to a point where people may believe that objectivity is getting compromised, e.g., when an auditor deals with shares or securities of the audited company, or becomes the client's advocate in litigation and third party disputes. In such situations, auditor can be perceived as backing and championing causes of auditee client and it may lead to belief that auditor is not acting and working objectively.

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Threat 4: Familiarity threats

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 including:

- o close relative of the audit team working in a senior position in the client company
- o former partner of the audit firm being a director or senior employee of the client
- o long association between specific auditors and their specific client counterparts and
- o acceptance of significant gifts or hospitality from the client company, its directors or employees.

Provisions in Companies Act, 2013 regarding rotation of auditors mainly address these very familiarity threats. Such provisions prescribe that auditor is rotated after a certain number of years so that auditors do not become too familiar with their clients.

Threat 5: Intimidation Threats

Intimidation threats 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 or being threatened with litigation. Such threats attempt to intimidate auditors to deter them from acting objectively.

VI. SAFEGUARDS TO INDEPENDENCE

Safeguards are actions, individually or in combination, that the professional accountant takes that effectively reduce threats to comply with the fundamental principles to an acceptable level.

To address the issue, the following guiding principles are to be applied: -

i. For the public to have confidence in the quality of audit, it is essential that auditors should always be and appears to be independent of the entities that they are auditing.

ii. Before taking on any work, an auditor must conscientiously consider whether it involves threats to his independence.

iii. When such threats exist, the auditor should either desist from the task or eliminate the threat or at the very least, put in place safeguards which reduce the threats to an acceptable level. All such safeguards measures need to be recorded in a form that can serve as evidence of compliance with due process.

iv. If the auditor is unable to fully implement credible and adequate safeguards, then he must not accept the work.

VII. 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 includes being alert to, for example:

a) Audit evidence that contradicts other audit evidence obtained.
b) Information that brings into question the reliability of documents and responses to inquiries to be used as audit evidence.
c) Conditions that may indicate possible fraud.
d) Circumstances that suggest the need for audit procedures in addition to those required by the SAs.

Maintaining professional skepticism throughout the audit is necessary if the auditor is to reduce the risks of:

i. Overlooking unusual circumstances.
ii. Over generalising when drawing conclusions from audit observations.
iii. Using inappropriate assumptions in determining the nature, timing, and extent of the audit procedures and evaluating the results thereof.

VIII. PRINCIPLES BASED APPROACH VS RULES BASED APPROACH TO ETHICS

PRINCIPLES BASED APPROACH	RULES BASED APPROACH
It requires compliance with spirit of ethics.	It strictly follows clearly established rules.
It requires accountants to exercise professional judgment in every situation based upon their professional knowledge, skill and expertise.	It may lead to a narrow outlook and spirit of ethics may be overlooked while strictly adhering to rules.
It requires that accountants should use professional judgment to evaluate every situation to arrive at conclusions.	Rules- based approach is somewhat rigid as it may not be possible to deal with every practical situation relying upon rules.

SQC 1 & SA220 AUDIT QUALITY

AUDIT QUALITY

The purpose of independent audit is to provide confidence to the users of the FS. Therefore, high audit quality is essential to maintain confidence in the independent assurance provided by the auditors. It is the responsibility of the auditor to maintain high quality.

- SQC 1
  - All engagements including audits, reviews and other assurance and related service engagements.
- SA 220
  - Applies to audit engagement only

- **SQC 1 QUALITY CONTROL FOR FIRMS THAT PERFORM AUDITS AND REVIEWS OF HISTORICAL FINANCIAL INFORMATION, AND OTHER ASSURANCE AND RELATED SERVICE ENGAGEMENTS**
- **SA 220 QUALITY CONTROL FOR AN AUDIT OF FS**

SA 220 is premised on the basis that the firm is subject to SQC1 As per SA220, the objective of the auditor is to implement quality control procedures at the **engagement level** that provide the auditor with reasonable assurance that: -

a) The audit complies with professional standards and regulatory and legal requirements.

b) The auditor's report issued is appropriate in the circumstances

SQC 1 AND SA220

- Leadership Responsibilities for quality on audits
- Relevant Ethical requirements
- Acceptance and continuance of client relationships and audit engagements
- Assignment of engagement teams
- Engagement performance
- Monitoring

	SQC 1	SA 220
Leadership responsibilities for quality within the firm	▪ SQC1 requires firms to establish policies and procedures designed to promote an internal culture. ▪ The policy should require the CEO or the partner to assume ultimate responsibility. ▪ Further persons assigned operational responsibility by the CEO/ partner should have Sufficient and Appropriate (S&A) experience, ability and the necessary authority.	▪ The Engagement Partner takes the overall leadership responsibility for quality of each engagement. ▪ The actions of the Engagement Partner emphasise- 1. The importance of Audit quality of: -Performing work that complies with professional standards and regulatory and legal requirements -complying with firm's quality control policies -Issuing audit report that is appropriate -Engagement team's ability to raise concern without fear 2. The fact that quality is essential in performing audit engagement

Relevant Ethical Requirements	The firm should establish policies and procedures designed to provide it with Reasonable Assurance (RA) that the firm and its personnel comply with relevant ethical requirements contained in code of ethics issued by ICAI. Such policies should enable the firm to - communicate its independence requirements. -identify and evaluate circumstances and relationships that create threats to independence.	The responsibility of Engagement Partner (EP) in relation to ethics of audit engagement: ▪ Identifying a threat to independence ▪ Reporting by Engagement Partner to relevant persons within the firm to determine appropriate action
Acceptance & continuance of client relationships and specific engagements	A firm before accepting an engagement should acquire vital info about the client about- • Integrity of client★ • Competence to perform engagement • Compliance with ethical requirements	A firm before accepting an engagement should acquire vital info about the client about- • Integrity of client • Competence to perform engagement • Compliance with ethical requirements *<<Same as SQC1>>*
Human Resources	The firm should establish policies and procedures designed to provide with Reasonable Assurance (RA) that it has sufficient personnel with the capabilities, competence and commitment in accordance with professional standards, regulatory and legal requirements.	Assignment of engagement team – Engagement Partner (EP) should ensure that the ET along the experts who are not part of the Engagement Team (ET) collectively have the appropriate competence and capabilities to perform the engagement in accordance with professional standards

Engagement performance	Engagement Quality Control Reviewer (EQCR) partner- Significant judgements will be reviewed by an EQCR partner for taking an objective view before the report is issued. EQCR is mandatory for All listed entities. For other engagements, firms should devise criteria. There might be differences of opinion with ET and the EQCR- the report should be issued only after resolving such issues. The matter of differences should be solved by following established procedures of firm like by, consulting with another practitioner or firm or a professional or regulatory body	Engagement Partner (EP) has the responsibility for direction, supervision and performance of audit engagement. If EQCR is required, EP shall: - Determine that EQCR is appointed -Discuss significant matters -Not date the Audit Report until EQCR review is complete.
Monitoring	The firm should ensure the policies and procedures relating to the system of quality control is relevant, adequate and operating effectively. It should also include a periodic inspection of a selection of completed engagements.	The EP should document the following pertaining to audit engagement: -Issues identified with respect to compliance with ethical requirements and how they were resolved -Conclusions on compliance - Conclusions regarding the acceptance and continuance of client

★ **With regard to the integrity of a client, matters that the firm considers include, for example:**

- ➢ The identity and business reputation of the client's principal owners, key management, related parties and those charged with its governance.
- ➢ The nature of the client's operations, including its business practices.
- ➢ Information concerning the attitude of the client's principal owners, key management and those charged with its governance towards such matters as aggressive interpretation of accounting standards and the internal control environment.
- ➢ Whether the 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.

BANK AUDIT

BANK AUDIT

- I. Types of Banks in India
- II. RBI Responsibilities and functions
- III. Regulatory framework
- IV. Bank Audit Approach
- V. Form and content of FS
- VI. Appointment of Auditor
- VII. Remuneration of Auditor
- VIII. Powers of Auditor
- IX. Auditor's Report
- X. Types of Auditor's Reports to be issued
- XI. Conducting an Audit
- XII. Advances
- XIII. Drawing power
- XIII. Drawing power
- XIV. Audit of advances
- XV. Audit of income
- XVI. Audit of expenses

I. TYPES OF BANKS IN INDIA

- Commercial banks
- Cooperative bank
- Development banks (Known as long term lending institutions)
- Regional rural banks
- Payment banks
- Small finance banks

1. **Commercial banks** are the widest spread banking institutions in India, that provide a no of products and services to general public and other segments of economy.
   Two of its main functions are: - accepting deposits and granting advances.
2. **Regional Rural Banks known as RRBs** are the banks that have been set up in rural areas in different states of the country to cater to the basic banking and financial needs of the rural communities.
   Eg: - Punjab Gramin Bank, Tripura Gramin Bank, Allahabad UP Gramin Bank, Andhra Pradesh Grameen Vikas Bank, etc.
3. **Co-operative Banks** function like Commercial Banks only but are set up on the basis of Cooperative Principles & reg under the Cooperative Societies Act of the respective state or the MSCS Act and usually cater to the needs of the agricultural and rural sectors.
   Eg: - The Gujarat State Co-operative Bank Ltd., Chhattisgarh Rajya Sahakari Bank Mayardit, etc.

4. **Payments Banks** are a new type of banks which have been recently introduced by RBI. They are allowed to accept restricted deposits & they cannot issue loans and credit cards. However, customers can open Current & Savings accounts and avail the facility of ATM cum Debit cards, Internet-banking & Mobile banking.
   Eg: - Airtel Payments Bank, India Post Payments Bank, Paytm Payments Bank, etc.
5. **Development Banks** had been conceptualized to provide funds for infrastructural facilities imp for the economic growth of the country.
   Eg: - Industrial Finance Corporation of India (IFCI), Industrial Development Bank of India (IDBI), Small Industries Development Bank of India (SIDBI), etc.
6. **Small Finance Banks** have been set up by RBI to make available basic financial and banking facilities to the unserved and unorganised sectors like small marginal farmers, small & micro business units, etc.
   Eg: - Equitas Small Finance Bank, AU Small Finance Bank, etc.

II. RBI RESPONSIBILITIES & FUNCTIONS

RBI is responsible for: -

a) Development and supervision of the constituents of the Indian financial system (which comprises banks and non-banking financial institutions)
b) Determining with CG, the monetary and credit policies
c) Regulating the activities of commercial and other banks

Important functions of RBI are: -

1. Issuance of currency;
2. Regulation of currency issue;
3. Acting as banker to the central and state govts; and
4. Acting as banker to commercial and other types of banks including term lending institutions + regulating the activities of commercial and other banks.

Note: No bank can commence the business of banking or open new branches without obtaining license from RBI. The RBI also has the power to inspect any bank.

III. REGULATORY FRAMEWORK

- Banking Regulation Act, 1949.
- State Bank of India Act, 1955.
- Companies Act, 2013
- Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970
- Regional Rural Banks Act, 1976.
- Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980.
- Information Technology Act, 2000
- Prevention of Money Laundering Act, 2002
- Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
- Credit Information Companies Regulation Act, 2005.
- Payment and Settlement Systems Act, 2007

Peculiarities involved:

i. Huge volumes and complexity of transactions;
ii. Wide geographical spread of banks' network;
iii. Large range of products and services offered;
iv. Extensive use of technology;
v. Strict vigilance by the banking regulator etc.

IV. BANK AUDIT APPROACH

1. Drawing an Audit Plan based on:

i. the nature and level of operations,
ii. nature of adverse features,
iii. level of compliance based on previous reports and
iv. audit risks based on inadequacy in or breach of internal controls and the familiarization exercise carried out,

2. Control Environment at the Bank:

A bank should have appropriate controls to mitigate its risks. The following are certain common questions /steps, while performing control activities:

Nature of Questions	Questions to be considered / answered
Who	• Who performs the control? • Does the above person have requisite knowledge and authority to perform the control?
What	• What evidence is available to demonstrate /prove that the control is performed?
When	• When and with what frequency is the control performed? • Is the frequency enough to prevent, detect and correct risk of material misstatements?
Where	• Where is the evidence of performance of the control retained? • For how long is the evidence retained? • Is the evidence accessible/ available for audit?
Why	• Why is the control being performed? • What type of errors are prevented or detected through the performance of the control?
How	• How is the control performed? • What are the control activities? • Can these activities be bypassed? • Can the bypass, if any, be detected? • How are exceptions / deviations resolved on identification? • What is the time frame for resolving the exceptions / deviations?

3. Engagement Team Discussions: - (done at planning stage of audit)

The engagement team discussion ordinarily includes a discussion of the following matters:

a) Errors that may be more likely to occur;
b) Errors which have been identified in prior years;
c) Method by which fraud might be perpetrated by bank personnel or others within account balances and/or disclosures;
d) Audit responses to Engagement Risk, Pervasive Risks & Specific Risks;
e) Need to maintain professional skepticism throughout the audit engagement;
f) Need to alert for information or other conditions that indicates that a material misstatement may have occurred
(e.g., the bank's application of accounting policies in the given facts and circumstances).

Advantages of such a discussion:

a) Specific emphasis to the susceptibility of the bank's fs to material misstatement due to fraud that enables the ET to consider an appropriate response to fraud risks, incl those related to engagement risk, pervasive risks, and specific risks.

b) EP delegates the work to the experienced ET members & determine the procedures to be followed when fraud is identified.

c) Engagement partner may review the need to involve specialists to address the issues relating to fraud.

V. FORM AND CONTENT OF FS

- Form A contains the form of B/S
- Form B contains the form of P&L

VI. APPOINTMENT OF AUDITOR

- Banking Company- at the AGM of SH;
- Nationalised Bank- by bank through BOD
- Regional Rural Bank - by bank with approval of CG

VII. REMUNERATION OF AUDITOR

- Banking company - fixed in accordance with S.142 of the CA, 2013
- Nationalised banks & SBI - fixed by the RBI in consultation with the CG.

VIII. POWERS OF AUDITOR

- The auditor of a banking company, nationalised bank, SBI, or regional rural bank has same powers of the company auditors in the matter of access to books, accounts, documents and vouchers

IX. AUDITOR'S REPORT:

In the case of a NATIONALISED BANK, the auditor is required to make a report to the CG in which he has to state the following:

a) Whether, in his opinion, the FS present a true and fair view of the affairs of the bank and in case he had called for any explanation or information, whether it has been given & whether it is satisfactory;
b) Whether or not the transactions of the bank, which have come to his notice, have been made within the powers of that bank;
c) Whether or not the returns received from the offices and branches of the bank have been found adequate for the purpose of his audit;
d) And any other matter which he considers should be brought to the notice of the CG.

LONG FORM AUDIT REPORT:

1. Terms of appointment of auditors of public sector banks, private sector banks and foreign banks (as well as their branches), require the auditors to also furnish a Long Form Audit Report (LFAR).
2. The matters which the banks require their auditors to deal with in LFAR have been specified by the RBI.
3. The Statutory Central Auditors are required to submit the LFAR to the banks latest by 30th June every year.
4. To ensure timely submission of LFAR, proper planning for completion of the LFAR is required.
5. While the format of LFAR does not require an executive summary to be given, members may consider providing the same to bring out the key observations from the whole document.

REPORTING TO RBI:

1. The RBI issued a Circular relating to implementation of recommendations of Committee on Legal Aspects of Bank Frauds applicable to all scheduled commercial banks (excluding Regional Rural Banks). Regarding liability of accounting and auditing profession, the said circular provided as under:
   "If an accounting professional, whether in the course of internal or external audit or in the process of institutional audit finds
   a) anything susceptible to be fraud or
   b) fraudulent activity or act of excess power or
   c) smell any foul play in any transaction,
   d) he should refer the matter to the regulator.

   Any deliberate failure on the part of the auditor should render himself liable for action". As per req, member shall report the kind of matters stated in circular to RBI.
2. Auditor should also consider the provisions of **SA 250, "Consideration of Laws and Regulations in an Audit of Financial Statements".** The said Standard explains that the duty of confidentiality is over-ridden by statute, law, or courts.
3. **SA 240, "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements"** states that an auditor conducting an audit in accordance with SAs is responsible for obtaining reasonable assurance

that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error.

Note: Auditor is not expected to look into each and every transaction but to evaluate the system as a whole. Therefore, if the auditor while performing his normal duties comes across any instance, he should report the matter to the RBI in addition to Chairman/Managing Director/Chief Executive of the concerned bank.

X. TYPES OF AUDIT REPORTS TO BE ISSUED GENERALLY

Presently, the Statutory Central auditors have to furnish the following reports in addition to the main reports:

1.Report on adequacy and operating effectiveness of Internal Controls over FR incase of banks which are registered as Companies under the Companies Act in terms of Section 143(3)(i) of the CA, 2013

2.Long form audit report

3.Report on compliance with SLR requirements

4.Report on whether the treasury operations of the bank have been conducted in accordance with instructions issued by the RBI from time to time

5.Report on whether the income recognition, asset classification and provisioning have been made as per the guidelines issued by the RBI from time to time.

6.Report on whether any serious irregularity was noticed in the working of the bank which requires immediate action.

7.Report on status of the compliance by the bank with regard to the implementation of recommendations of the Ghosh committee relating to frauds and malpractices and of the recommendations of Jilani committee of internal control and inspection/ credit system.

8.Report on instances of adverse credit deposit ratio in the rural areas

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XI. CONDUCTING AN AUDIT

1. Initial consideration by the statutory auditor

i. Declaration of Indebtedness:

RBI has advised, before appointing statutory central/branch auditors, should obtain a declaration of indebtedness. Indebtedness refers to the situation of owing money to the bank.

ii. Internal Assignments in Banks by Statutory Auditors:

The audit firms shouldn't undertake statutory audit assignment while associated with internal assignments in the bank during the same year, like Concurrent audits (Internal Audit of Banks conducted monthly during the year)

iii. Planning:

SA 300 requires that the auditor shall undertake the following activities prior to starting an initial audit:

a. Performing procedures required by SA 220 regarding the acceptance of the client relationship & specific audit engg; and
b. Establish understanding of terms of engg. as per SA 210.

iv. Communication with Previous Auditor:

As per Clause (8) of the Part I of the First Schedule to the Chartered Accountants Act, 1949, a CA in practice cannot accept position as auditor previously held by another CA without first communicating with him in writing. He should get a NO Objection Certificate (NOC) from the previous auditor whether he has any objections to such an appointment made, for any valid reasons.

v. Terms of Audit Engagements:

Agree on the terms of the audit engg. before beginning fieldwork.

vi. Initial Engagements:

Perform audit procedures as mentioned in SA 510 and if the auditor concludes that the opening balances contain misstatements which materially affect the FS for the current period & the effect of the same is not accounted for and adequately disclosed, the auditor should express a qualified opinion or an adverse opinion.

vii. Assessment of Engagement Risk:

Done prior to the audit engagement since it affects the decision of accepting the engagement & also in planning decisions if the audit is accepted.

viii. Establish the Engagement Team:

Assignment of qualified and experienced professionals.

ix. Understanding the Bank and its Environment:

Understanding of the entity & its environment, including its internal control, to identify and assess ROMM of the FS whether due to fraud or error & sufficient to design and perform FAP.

2. Identifying and Assessing the ROMM:

SA 315 requires the auditor to identify and assess the ROMM at the FS level and the assertion level for ABCD to provide a basis for designing and performing further audit procedures.

3. Understanding the Bank and Its Environment including Internal Control:

Enables the auditor:

a. to identify and assess risk;

b. to develop an audit plan, determine the operating effectiveness of the controls and

c. to address the specific risks.

4. Understanding the Bank's Accounting Process:

The accounting process produces financial & operational information for Mgt use and it also contributes to the bank's IC. Thus, understanding of the accounting process is necessary to identify and assess the ROMM whether due to fraud or not and to design and perform FAP.

5. Understanding the Risk Management Process:

An effective risk management system in a bank generally requires the following:

(a) Oversight and involvement in the control process by those charged with governance:

TCG (BOD/MD) should approve written risk mgt policies.

(b) Identification, measurement, and monitoring of risks:

Risks should be identified, measured and monitored against pre-approved limits and criteria.

(c) Control activities:

A bank should have appropriate controls to mitigate its risks including effective SOD'S (particularly between front and back offices), accurate measurement and reporting of positions, verification and approval of transactions, reconciliation of positions and results, setting up limits, reporting and approval of exceptions, physical security and contingency planning.

(d) Monitoring activities:

Risk mgt models & assumptions used to measure & mitigate risk should be regularly assessed and updated. This function may be conducted by the independent risk management unit.

(e) Reliable information systems:

Banks require reliable info systems that provide adequate financial, operational and compliance information on a timely and consistent basis.

6. Engagement Team Discussions:

The engagement team should hold discussions to gain better understanding of banks and its environment, including IC, & also to assess the potential for MM of the FS.

7. Establish the Overall Audit Strategy:

Establish the overall audit strategy, prior to the commencement of an audit; & involve key ET members & other appropriate specialists

8. Develop the Audit Plan:

SA 300 deals with the auditor's responsibility to plan an audit of financial statements in an effective manner.

It requires the involvement of all the key members of the engagement team while planning an audit.

9. Audit Planning Memorandum:

The auditor should summarise the audit plan by preparing an audit planning memorandum in order to:

a) Describe the expected scope and extent of the audit procedures to be performed by the auditor.

b) Highlight all significant issues and risks identified during their planning and risk assessment activities, as well as the decisions concerning reliance on controls.

c) Provide evidence that they have planned the audit engagement appropriately and have responded to engagement risk, pervasive, specific risks.

10. Determine Audit Materiality:

It's is a matter of professional judgment and depends upon the knowledge of the bank, assessment of engagement risk and the reporting requirements for the financial statements.

11. Consider Going Concern:

While obtaining an understanding of the bank, the auditor should consider whether there are events and conditions which may cast significant doubt on the bank's ability to continue as a going concern.

12. Assess the Risk of Fraud including Money Laundering:

As per SA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", the auditor's objective is to identify and assess the risks of material misstatement in the financial statements due to fraud, to obtain sufficient appropriate audit evidence on those identified misstatements and to respond appropriately.

13. Assess Specific Risks:

The auditors should identify and assess the risks of material misstatement at the financial statement level which refers to risks that relate pervasively to the financial statements as a whole and potentially affect many assertions.

14. Risk Associated with Outsourcing of Activities:

The modern-day banks make extensive use of outsourcing as a means of both reducing costs as well as making use of services of an expert not available internally. There are, however, a number of risks associated with outsourcing of activities by banks and therefore, it is quintessential for the banks to effectively manage those risks.

15. Response to the Assessed Risks:

SA 330 requires the auditor to design and implement overall responses to address the assessed ROMM at the FS level. The auditor should design & perform FAP whose NTE are based on & are responsive to the assessed ROMM at the assertion level.

16. Stress Testing:

Stress testing is a software testing activity that determines the robustness of software by testing beyond the limits of normal operation. Stress testing

a) Particularly important for "mission critical" software,
b) RBI has required that all commercial banks shall put in place a Board approved 'Stress Testing framework'

17. BASEL III framework:

International Banking regulations issued by the BCBS. The Basel Committee on Banking Supervision (BCBS) & the Financial Stability Board (FSB) has undertaken an extensive review of the regulatory framework in the wake of the sub-prime crisis.

18. Reliance on / review of other reports:

The auditor should take into account the adverse comments, if any, on advances appearing in the following-

1. Previous year's audit reports.
2. Latest internal inspection reports of bank officials.
3. Reserve Bank's latest inspection report, Concurrent / Internal audit report.
4. Report on verification of security.
5. Any other internal reports specially related to particular accounts.
6. Manager's charge-handing-over report when incumbent is changed

NOTE: Above reports should be reviewed in detail. The Statutory Central Auditors must review the Annual Financial Inspection report of RBI relating to the bank and ensure that the variations in provisions, etc. reported by RBI have been properly considered by the bank management.

XII. ADVANCES

Advances are amount of money or credit, given as a loan from a bank to another party with an agreement that the money will be repaid.

What do ADVANCES comprise:

Advances comprise of funded amounts by way of:

1. Term loans
2. Cash credits, Overdrafts, Demand Loans
3. Bills Discounted and Purchased
4. Participation on Risk Sharing basis
5. Interest-bearing Staff Loans

CLASSIFICATION OF ADVANCES:

SECTOR WISE

a) RBI issues common guidelines for lending to Priority Sector which banks are required to follow.
b) Covering rate of interest; service charges, receipt, sanction, rejection, disbursement Register; issue of Loan Application Acknowledgement.
c) RBI also issues targets for banks for lending to Priority Sector.
Examples of Priority Sectors are Agriculture, MSME, Education, Housing, etc.

SECURITY WISE

Banks ask Security or Collateral while lending to assure that the Borrower will return the money to bank in prescribed time else the Banks have legal authority to sell the collateral to recover its money.

NATURE OF SECURITY:

a) Primary security refers to the security offered by the borrower for bank finance or the one against which credit has been extended by the bank. This security is the principal security for an advance.

b) Collateral security is an additional security. Security can be in any form i.e. tangible or intangible asset, moveable, or immovable asset.

Examples of **most common types of securities** accepted by banks are the

1. Personal Security of Guarantor
2. Goods/Stocks/Debtors/Trade Receivables
3. Gold Ornaments and Bullion e.g.: Immovable Property Plantations (For Agricultural Advances)
4. Third Party Guarantees
5. Banker's General Lien
6. Life Insurance Policies LIC
7. Stock Exchange Securities and Other Instruments

MODE OF CREATION OF SECURITY:

Depending on the nature of the item concerned, creation of security may take the form of a mortgage, pledge, hypothecation, assignment, set-off or lien as follows:

(i) Mortgage:

Mortgage are of several kinds but the most important are the Registered Mortgage & the Equitable Mortgage.

a) **Registered Mortgage** can be affected by a registered instrument called the 'Mortgage Deed' signed by the mortgagor. It registers the property to the mortgagee as a security.

b) **Equitable mortgage**, on the other hand, is affected by a mere delivery of title deeds or other documents of title with intent to create security thereof.

(ii) Pledge:

a) It involves bailment or delivery of goods by the borrower to the lending bank with the intention of creating a charge thereon as security for the advance.

b) The legal ownership of the goods remains with the pledger while the lending banker gets certain defined interests in the goods. Pledge of goods constitutes a specific (or fixed) charge.

(iii) Hypothecation:

a) Its creation of an equitable charge

(i.e., a charge created not by an express enactment but by equity and reason),

b) which is created in favour of the lending bank by execution of hypothecation agreement in respect of the moveable securities belonging to the borrower. Neither ownership nor possession are transferred to the bank.

c) The borrower holds the physical possession of the goods as an agent/trustee of the bank.

d) The borrower periodically submits statements regarding quantity & value of hypothecated assets (stocks, debtors, etc.) to the lending banker on the basis of which the drawing power of the borrower is fixed.

(iv) Assignment:

a) Transfer of an existing or future debt, right or property belonging to a person in favor of another person.

b) Only actionable claims such as book debts and life insurance policies are accepted by banks as security by way of assignment.

c) An assignment gives the assignee absolute right over the moneys/debts assigned to him.

(v) Set-off:

a) Set-off is a statutory right of a creditor to adjust, wholly or partly, the debit balance in the debtor's account against any credit balance lying in another account of the debtor.

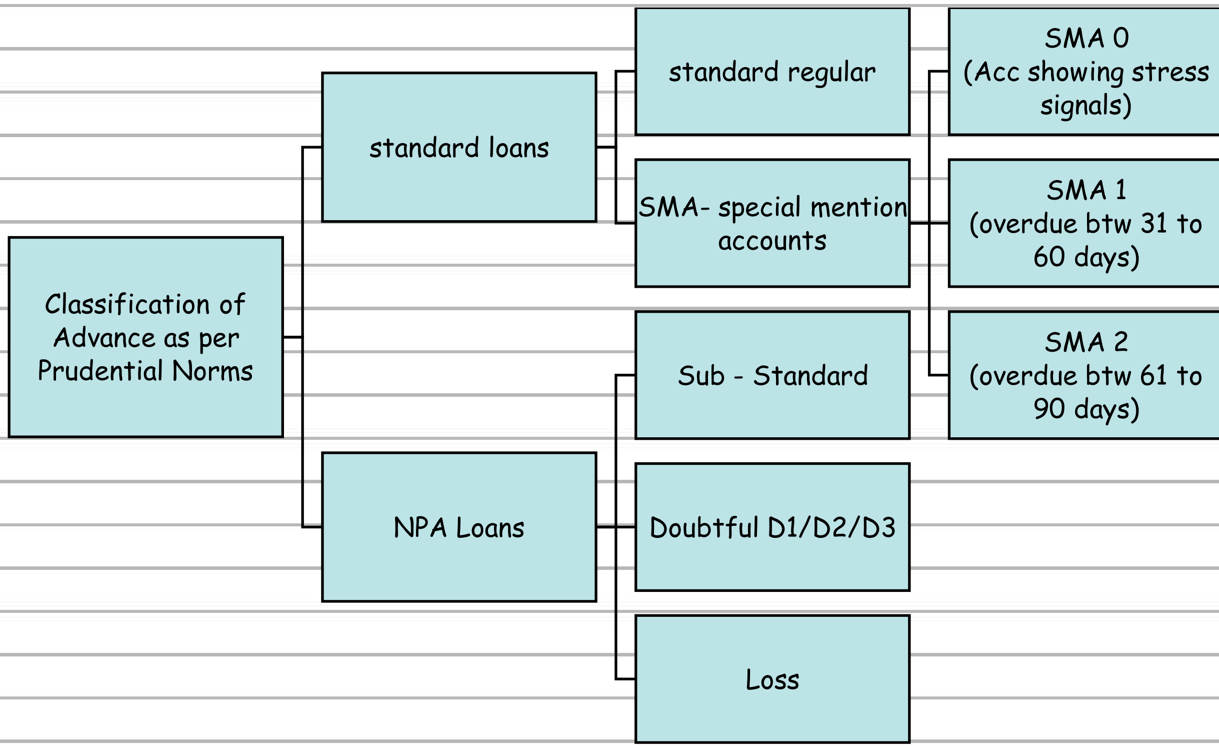
b) The right of set-off enables a bank to combine two accounts (a deposit account and a loan account) of the same person provided both the accounts are in the same name and same right (i.e., the capacity of the account holder in both the accounts should be the same).

c) The right of set-off can be exercised in respect of time-barred debts also.

(vi) Lien:

Lien is creation of a legal charge with consent of the owner, which gives lender a legal right to seize and dispose / liquidate the asset under lien.

Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances:



(i) Non-performing Assets:

An asset becomes NPA when it ceases to generate income for the Bank. A non-performing asset (NPA) is a loan or an advance where -:

- Interest and/ or instalment of principal remain overdue for a period of > 90 days in respect of a term loan;
- The account remains 'out of order' in respect of an Overdraft/Cash Credit (OD/ CC);
- The bill remains overdue for a period of > 90 days in the case of bills purchased and discounted.

(ii) Out of Order:

An account should be treated as 'out of order' if: -

- The o/s balance remains continuously in excess of the sanctioned limit/ DP or
- In cases where the o/s balance in the principal operating a/c is < sanctioned limit/ DP, but there are no credits continuously for 90 days as on the date of BS; or
- Credits are there but are not enough to cover the interest debited during the same period, these accounts should be treated as '**out of order**'.

(iii) Overdue:

Any amount due to the bank under any credit facility is 'overdue' if it is not paid on the due date fixed by the bank.

	Categories of Non-Performing Assets:	Provision required
1	Substandard Assets:	
	Would be one, which has remained NPA for a period less than or equal to 12 months.	15%
2	Doubtful Assets:	
	Would be one, which has remained in the substandard category for a period of 12 months.	
	Sub-categories:	Secured + Unsecured
	Doubtful up to 1 Year (D1)	25% + 100%
	Doubtful 1 to 3 Years (D2)	40% + 100%
	Doubtful more than 3 Years (D3)	100% + 100%
3	Loss Assets:	
	Would be one, where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly.	100%

Note:

1. **Classification as NPA should be based on the record of recovery.** Availability of security or net worth of borrower/guarantor is not to be considered for purpose of treating an advance as NPA or otherwise.
2. **Asset classification would be borrower-wise and not facility-wise.** All facilities including investments in securities would be termed as NPA.

Example:

Mr. Raman has availed two Loan facilities - a Car Loan as well as a Housing Loan from XYZ Bank Ltd. He is regular in depositing the Housing loan EMI but has not deposited the last 4 EMI's of the Car Loan due to paucity of funds. Hence, in this case, not only the Car loan but the Housing Loan would also be treated as an NPA, although it is going good and there are no irregularities because the NPA classification is Borrower wise (Mr. Raman) and not Facility wise (Car & Housing Loan individually).

(iv) Accounts regularized near the Balance Sheet Date:

a) Where the account indicates inherent weakness on the basis of the data available, the account should be deemed as NPA.

b) Auditor should check for sample transactions immediately before the closing of the FY & immediately after the closing of the FY to get a knowledge of the obj behind the transactions if they have any relation to each other in the Borrower a/cs o

c) If any/some transactions are being reversed during the first few days after closing which might show an arrangement to prevent the Borrower account(s) from slipping into the NPA category.

(v) Government Guaranteed advances:

a) CG guaranteed Advances, where the guarantee is not invoked/ repudiated would be classified as Standard Assets, but regarded as NPA **for Income Recognition purpose**.

b) The situation would be different if the advance is guaranteed by SG, where advance is to be considered NPA if it remains overdue for more than 90 days **for both Provisioning** and **Income recognition purposes**.

(vi) Advances under Consortium:

a) Consortium advances mean advancing loans to a borrower by two or more Banks jointly by forming a Consortium.

b) **Joint appraisal, control, and monitoring** will facilitate for exchange of valuable info among the Banks. Usually, a Bank with a higher share will lead the consortium.

c) Consortium advances should be based on the record of recovery of the respective individual member banks & other aspects having a bearing on the recoverability of the advances.

d) Where the remittances by the borrower under consortium lending arrangements are pooled with one bank and/or

e) Where the bank receiving remittances is not parting with the share of other member banks, the account should be treated as not serviced in the books of the other member banks and therefore, an NPA.

f) The banks participating in the consortium, therefore, need to arrange to get their share of recovery transferred from the lead bank or to get an express consent from the lead bank for the transfer of their share of recovery, to ensure proper asset classification in their respective books.

Note: - Drawing Power Allocation in case of Consortium Cash Credit Account:

The Lead Bank would be responsible for computing the drawing power (DP) of the borrower and allocate the same to member banks.

In certain special circumstances, at the request of the Borrower, the Lead Bank may allot a higher or lower share of drawing power to the member bank, as against their share of advances.

The proforma DP Allocation Letter is presented hereunder for reference

ACCOUNTS WHERE THERE IS EROSION IN THE VALUE OF SECURITY / FRAUDS COMMITTED BY BORROWERS

Erosion means the gradual destruction or diminution of something not prudent to follow stages of asset classification. It should be straight-away classified as doubtful or loss asset as appropriate as follows: -

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(i) **Erosion in the value of security** can be reckoned as significant when the realisable value of the security is < 50% of the value assessed by the bank or accepted by RBI at the time of last inspection. Such NPAs may be straight-away classified under doubtful category and provisioning should be made as applicable to doubtful assets.

(ii) If the **Realisable value of the security**, as assessed by the bank/ approved valuers/ RBI is < 10% of the o/s in the borrower a/cs, the existence of security should be ignored & the asset should be straight-away classified as loss asset. It may be either written off or fully by the bank.

XIII. ADVANCES AGAINST TERM DEPOSITS, NSCS, KVPS/ IVPS, ETC:

Advances against Term Deposits, NSCs eligible for surrender, KVP/IVP and life policies need not be treated as NPAs, provided adequate margin is available in the accounts.

XIV. AGRICULTURAL ADVANCES AFFECTED BY NATURAL

a) Master Circular issued by the RBI deals elaborately with the classification and income recognition issues due to impairment caused by natural calamities.

b) Banks may decide on their own relief measures, viz., conversion of the short-term production loan into a term loan or re-schedulement of the repayment period and the sanctioning of fresh short-term loan, subject to the guidelines contained in RBI's latest Master Circular.

c) In such cases, the NPA classification would be governed by such rescheduled terms

XV. ADVANCES TO STAFF:

a) Interest-bearing staff advances as a banker should be included as part of advances portfolio of the bank.

b) In the case of housing loan or similar advances granted to staff members where interest is payable after recovery of principal, interest need not be considered as overdue from the 1st quarter onwards.

c) Such loans/advances should be classified as NPA only when there is a default in repayment of instalment of principal or payment of interest on the respective due dates.

d) The staff advances by a bank as an employer and not as a banker are required to be included under the sub-head 'Others' under the schedule of Other Assets.

XVI. AGRICULTURAL ADVANCES:

As per the guidelines, Agricultural Advances are of two types:

i. Agricultural Advances for "long duration" crops; and

ii. Agricultural Advances for "short duration" crops.

The "long duration" crops would be crops with crop season longer than one year & crops, which are not "long duration" crops would be treated as "short duration" crops.

The crop season for each crop, which means the period up to harvesting of the crops raised, would be determined by the State Level Bankers' Committee in each State.

The following NPA norms would apply to agricultural advances (including Crop Term Loans):

a) A loan granted for short duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for two crop seasons; and

b) A loan granted for long duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for one crop season.

XVII. COMPUTATION OF DRAWING POWER:

1. Meaning:

Drawing Power generally addressed as "DP" is an important concept for Cash Credit (CC) facility availed from banks and financial institutions. Drawing power is the limit up to which a firm or company can withdraw from the working capital limit sanctioned.

2. Different from Sanctioned Limit:

The Sanctioned limit is the total exposure that a bank can take on a particular client for facilities like cash credit, overdraft, export packing credit, non-funded exposures etc..

3. Considerations:

All accounts should be always kept within both the drawing power and the sanctioned limit. The accounts which exceed the sanctioned limit or drawing power or are against unapproved securities or are otherwise irregular should be brought to the notice of the Management/Head Office regularly.

4. Bank's Duties:

Banks should ensure that drawings in the working capital account are covered by the adequacy of the current assets. Drawing power is required to be arrived at based on current stock statement.

5. Auditor's Concern:

The stock statements, quarterly returns and other statements submitted by the borrower to the bank should be scrutinized in detail. The audited Annual Report submitted by the borrower should be scrutinized properly.

6. Computation of DP:

It needs to be ensured that the drawing power is calculated as per the extant guidelines formulated by the BOD of the respective bank & agreed upon by the concerned statutory auditors.

7. Stock Audit:

The stock audit should be carried out by the bank for all accounts having funded exposure of more than 5 crores. Branches should obtain the stock audit reports from lead bank in the cases where the Bank is not leader of the consortium of working capital. The report submitted by the stock auditors should be reviewed during the audit and special focus should be given to the comments made by the stock auditors on valuation of security and calculation of drawing power.

	Particulars of current assets			DP
(A)	**Stocks**			
	Stocks at realizable value		1000	
	Less: Unpaid stocks:			
	- Sundry creditors	300		
	- Acceptances/LCs etc.	300	600	
	Paid for stocks		400	
	Margin @ 25%		100	300
(B)	**Debtors**			
	Total Debtors		1000	
	Less: Ineligible debtors		200	
	Eligible debtors		800	
	Margin @ 40%		320	480
	Total DP			780

XVIII. AUDIT OF ADVANCES:

Advances generally constitute the major part of the assets of the bank. There are large number of borrowers to whom variety of advances are granted. The audit of advances requires the major attention from the auditors.

In carrying out audit of advances, the auditor is primarily concerned with obtaining evidence about the following:

1.Amounts included in balance sheet in respect of advances which are o/s at the date of the BS.

2.Advances represent amounts due to the bank.

3.Amounts due to the bank are appropriately supported by loan documents and other documents as applicable to the nature of advances.

4.There are no unrecorded advances.

5.The stated basis of valuation of advances is appropriate and properly applied and the recoverability of advances is recognised in their valuation.

6.The advances are disclosed, classified, and described in accordance with recognised accounting policies and practices & relevant statutory and regulatory requirements.

7.Appropriate provisions towards advances have been made as per the RBI norms, AS GAAP.

The auditor can obtain sufficient appropriate audit evidence about advances by study and evaluation of internal controls relating to advances, and by:

1. Examining the validity of the recorded amounts;
2. Examining loan documentation;

3. Reviewing the operation of the accounts;
4. Examining the existence, enforceability, and valuation of the security;
5. Checking compliance with RBI norms including appropriate classification and provisioning; and
6. Carrying out appropriate analytical procedures. **(sa 520)**

Evaluation of Internal Controls over Advances:

In general, the internal controls over advances should include, inter alia, the following:

1.The bank should make an advance only after satisfying itself as to the credit worthiness of the borrower and after obtaining sanction from the appropriate authorities of the bank. 2.

2.All the necessary documents (e.g., agreements, demand promissory notes, letters of hypothecation, etc.) should be executed by the parties before advances are made.

3.The compliance with the terms of sanction and end use of funds should be ensured.

4.Sufficient margin as specified in the sanction letter should be kept against securities taken to cover for any decline in the value thereof. The availability of sufficient margin needs to be ensured at regular intervals.

5.If the securities taken are shares, debentures, etc., the ownership of the same should be transferred in the name of the bank and the effective control of such securities be retained as a part of documentation.

6.All securities requiring registration should be registered in the name of the bank or otherwise accompanied by documents sufficient to give title to the bank.

7.In the case of goods in the possession of the bank, contents of the packages should be test checked at the time of receipt. The godowns should be frequently inspected by responsible officers of the branch concerned, in addition to the inspectors of the bank.

8.DP Register should be updated every month to record the value of securities hypothecated. These entries should be checked by an officer.

9.The accounts should be kept within both the drawing power and the sanctioned limit.

10.All the accounts which exceed the sanctioned limit or drawing power or are otherwise irregular should be brought to the notice of the controlling authority regularly.

11.The operation of each advance account should be reviewed at least once a year and at more frequent intervals in the case of large advance

XIX. AUDIT OF INCOME:

Audit Approach and Procedures:

Auditor's Concern:

Recorded income arose from transactions, which took place during the relevant period & pertained to the bank, there is no unrecorded income and the income is recorded at appropriate amt.

RBI's Directions:

RBI has advised that in respect of

1. any income which > 1% of the total income of bank if the income is reckoned on a gross basis or
2. 1% of the PBT if the income is reckoned net of costs,
3. should be considered on accrual as per Accounting Standard 9.

Materiality:

If any income is not considered to be material as per the above norms, it may be recognised when received and the auditors need not qualify their report in that situation.

Revenue Certainty:

Banks recognise income (such as interest, fees and commission) on accrual basis, i.e., as it is earned. It is an essential condition for accrual of income that it should not be unreasonable to expect its ultimate collection. In modern day banking, the entries for interest income on advances are automatically generated through a batch process in the CBS system.

Revenue Uncertainty:

a) In view of the significant uncertainty regarding ultimate collection of income arising in respect of NPAs, the guidelines require that banks should not recognize until it is realised.

b) When a credit facility is classified as NPA for the 1st time, interest accrued & credited to the income account in the corresponding PY which has not been realized should be reversed or provided for.

c) This will apply to Government guaranteed a/cs also.

Advances against Securities:

Interest on advances against Term Deposits, National Savings Certificates (NSCs), Indira Vikas Patras (IVPs), Kisan Vikas Patras (KVPs) and Life policies may be taken to income account on the due date, provided adequate margin is available in the a/cs.

Bills Purchased:

Bills purchased o/s at the close of year the discount received thereon should be properly apportioned between the two years.

a) [The Unexpired discount/ rebate on bills discounted i.e., where part of receipt comprising discount charges on bills purchased relate to the period beyond the year-end, should be recorded as "Other Liabilities"].

b) Interest (discount) component paid by Bank/Branch on rediscount of bills from other financial institutions, is not to be netted off from the discount earned on bills discounted.

Bills for Collection:

Examine the procedure for crediting the party on whose behalf the bill has been collected.

a) Procedure is usually such that the customer's a/c is credited only after the bill has been collected from the drawee either by the bank itself or through its agents, etc.

b) Commission of the branch due only when the bill collected.

Renegotiations:

Fees & commissions earned by the banks because of re-negotiations or rescheduling of o/s debts should be recognised on an accrual basis over the period covered by the re-negotiated or rescheduled extension of credit.

a) Test check the interest earned by the banks for the sample selected.

b) Test check the fees & commissions earned by the banks made for commission on bills for collection, letters of credit & bank guarantees.

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Reversal of Income:

1. If any advance becomes NPA as at the close of any year, interest accrued & credited to income a/c in the past periods, should be reversed or provided for if the same is not realised. Apply to Government guaranteed A/cs also.
2. For NPAs, fees, commission and similar income that have accrued should cease to accrue in the current period should be or provided for w.r.t past periods, if uncollected.
3. In case of banks which have wrongly recognised income in the past should reverse the interest as income during the current year or make a provision for an equivalent amount if it was recognized as income in the previous year(s).
4. Auditor should enquire if there are any large debits in the Interest Income a/c that have not been explained.
5. Enquire whether there are any communications from borrowers pointing out differences in interest charge & whether appropriate action taken

On leased assets:

Component of finance income (as defined in AS 19 – Leases) on the leased asset which was accrued & credited to the income a/c before the asset became NPA & remaining unrealised, should be reversed or provided for in the current a/c period.

On Take-out finance:

Takeout loan is a method of financing whereby a loan that is procured later is used to replace the initial loan. It is long-term financing that the lender promises to provide at a particular date or when criteria for completion of a project are met. Commonly used in property development.

In such case, if based on record of recovery, a/c is classified by the lending bank as NPA, not recognize income unless realised from the borrower/taking-over institution (if the arrangement so provided).

On Partial Recoveries in NPAs:

i. In the absence of agreement between the bank and the borrower for appropriation of recoveries in NPAs (i.e., towards principal or interest due), banks are required to adopt an accounting policy and exercise the right of appropriation of recoveries in a uniform & consistent manner.

ii. The appropriate policy to be followed is to recognise income as per AS 9 when certainty attaches to realisation and accordingly amount reversed/derecognised or not recognised in the past should be accounted. Interest partly/fully realised in NPAs can be taken to income.

iii. However, it should be ensured that the credits towards interest in the relevant a/cs are not out of fresh/additional credit facilities sanctioned to the borrowers concerned.

Memorandum Account

1. Account turning NPA, banks should reverse the interest already charged & not collected by debiting P&L a/c & stop further application of intt.
2. However, Banks may continue to record such accrued interest in a Memorandum account in their books for control purposes.
3. For computing Gross Advances, interest recorded in the Memorandum account should not be taken into a/c.

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Income from Investments

Interest Income on Investments:

- Includes all income derived from Govt securities, bonds, and debentures of corporate & other investments by way of interest and dividend, except income earned by way of dividends, etc., from subsidiaries & joint ventures abroad/in India.
- Broken period interest paid on securities purchased and amortisation of premium on SLR investments is net off from the interest income on investments.

Profit on Sale of Investments:

Net profit or loss on sale of investments is taken to P&L a/c.

Profit/Loss on Revaluation of Investments:

As per RBI guidelines, investments to be valued at periodical intervals and depreciation or appreciation in valuation should be taken to P&L a/c.

XX. AUDIT OF EXPENSES:

Interest Expense

1. **Ratio Analysis:** Auditor is primarily concerned with assessing the overall reasonableness of amt of int expense by analysing ratios of intt. paid on different types of deposits & borrowings to the avg quantum of respective liabilities during year. In modern day banking, entries for interest expenses are automatically generated through a batch process in the CBS system.
2. **Weighted average int rate**: Auditor should obtain from the bank analysis of various types of deposits o/s at the end of each quarter. From such info, auditor may work out a weighted average int rate.
3. **Compare with PY:** Auditor should also compare avg rate of interest paid on relevant deposits with corresponding figures for PY and analyse any material differences
4. **Month On Month analysis:** The auditor should obtain general ledger break-up for the int expense incurred on deposits (savings and term deposits) and borrowing each month/qtr. Analyse MOM (or QOQ) cost analysis and document reasons for the variances as per benchmark stated. Examine whether the int exp considered in the cost analysis agrees with the general ledger.
5. **Average balance:** The auditor should understand the process of computation of the avg balance and re-compute the same on sample basis.

The auditor should, on a test check basis, verify the calculation of interest and ensure that:

(a) Int has been provided on all deposits upto the date of the B/S.

(b) Int rates are in accordance with the bank's internal regulations, the RBI directives, and agreements with the respective deposit holder;

(c) Int on savings a/cs are in accordance with the rules framed by the bank/RBI in this behalf.

(d) Int on inter-branch balances have been provided at the rates prescribed by the head office/RBI.

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Audit of Operating expenses

The auditor should: -

1. Study and evaluate the system of IC relating to exp, including authorization procedures in order to determine the NET of his other AP.
2. Examine whether there are any divergent trends in respect of major items of expenses.
3. Perform substantive analytical procedures (proforma given below for reference) in respect of these expenses. e.g. assess reasonableness of expenses by working out their ratio to total operating expenses and comparing it with the corresponding fig for PYs.
4. Verify expenses with reference to supporting documents and check the calculations wherever required

Audit of Provisions and contingencies

The auditor should: -

1. **Compliances:** Ensure compliances for provisioning as contained in the various circulars have been fulfilled.
2. **Understanding:** Obtain an understanding as to how bank computes provision on std assets & NPAs. It will primarily include checking the basis of classification of loans & receivables into standard, sub-standard, doubtful, loss and non-performing assets. The auditor may verify the loan classification on a sample basis.
3. **Break up of Loans:** Obtain the detailed break up of std loans, NPA loans and agree the o/s balance with the general ledger.
4. **Tax provision:** Obtain the tax provision computation from the bank's mgt & verify the nature of items debited & credited to P&L a/c to ascertain that the same are appropriately considered in the tax provision computation.
5. **Other provisions**: for expenses examining vis-a-vis the circumstances warranting the provisioning & adequacy of the same by discussing ith mgt.

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SPECIAL FEATURES OF AUDIT OF DIFFERENT TYPES OF ENTITIES

GOVERNMENT AUDIT

Government Audit is the **objective, systematic, professional and independent examination of financial, administrative and other operations** of a **public entity** made subsequently to their execution for the purpose of evaluating and verifying them, presenting a report containing explanatory comments on audit findings together with **conclusions and recommendations** for future actions by the responsible officials, and in the case of examination of FS, expressing the appropriate professional **opinion** regarding the fairness of presentation.

The U.N. Handbook on Government Auditing and Developing Countries defines government auditing in a comprehensive manner which is as follows:

Government auditing is:

- The objective, systematic, professional and independent examination
- of financial, administrative and other operations
- of a public entity
- made subsequently to their execution
- for the purpose of evaluating and verifying them,
- presenting a report containing explanatory comments on audit findings together with conclusions and recommendations for future actions
- by the responsible officials
- and in the case of examination of financial statements, expressing the appropriate professional opinion regarding the fairness of the presentation.

Objectives of Govt Audit:

1.Accounting for public funds: Government audit serves as a mechanism or process for public accounting of government funds.

2.Apprasial of govt policies: It also provides public accounting of the operational, management, programme and policy aspects of public administration as well as accountability of the officials administering them.

3.Base for corrective action: Audit observations based on factual data collection also serve to highlight the lapses of the lower hierarchy, thus helping supervisory level officers to take corrective measures.

I. ADMINISTRATIVE ACCOUNTABILITY:

1. Govt audit is neither equipped nor intended to function as an investigating agency, to pursue every irregularity or misdemeanour to its logical end.
2. Main objective of audit is a combination of ensuring accountability of administration to legislature and functioning as an aid to administration.
3. In India, the function of Govt Audit is discharged by the independent statutory authority of the C&AG through the agency of the Indian Audit & A/cs Dept (IIAD).
4. Audit is a necessary function to ensure accountability of
   - the executive to Parliament, and
   - within the executives of the spending agencies to the sanctioning or controlling authorities.
5. C&AG watches that various authorities act as per the Constitution & laws made by Parliament, and conform to the rules or orders made thereunder.

APPOINTMENT & REMOVAL

The C&AG of India by prescribing shall be appointed by the President of India	Shall not be removed from office except on the ground of proven mis-behaviour or incapacity	Can be removed only when each House of Parliament decides to do so by a majority of not less than 2/3rd of the members of house present & voting	Parliament is competent to make laws to determine salary and other conditions of service

II. DUTIES OF THE C & AG:

1. Compile and submit Accounts of Union and States

a) The C&AG shall be responsible for compiling the a/cs of the Union and of each State from the initial and subsidiary a/cs

b) The C&AG shall, from the a/cs compiled by him (including, in the case of a/cs compiled by him, appropriation a/cs) showing under the respective heads the annual receipts and disbursements for the purpose of the Union, of each State and of each UTLA, and shall submit those accounts to the President or the Governor of a State or Administrator of the UTLA

NOTE: - The C&AG Act of 1971 has provisions for relieving him of this responsibility to give information and render assistance to the Union and States

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2. General Provisions Relating to Audit –

It shall be the duty of the C&AG —

a) to audit and report on all exp from the CFoI and of each State and of each UTLA and to ascertain whether the moneys shown in the a/cs as having been disbursed were legally available for and applicable to the service or purpose to which they have been applied or charged and whether the exp conforms to the authority which governs it;

b) to audit and report all transactions of the Union and of the States relating to Contingency Funds and Public A/cs;

c) to audit and report on all trading, manufacturing, and P&L accounts and BS & other subsidiary a/cs kept in any dept of the Union or of a State.

3. Audit of Receipts and Expenditure -

Where anybody or authority is substantially financed by grants or loans from the CFOI or of any State or of any UTLA, the C&AG shall, subject to the prov of any law for the time being in force applicable to the body or authority, as the case may be, audit all R&E of that body or authority and to report on the receipts and exp audited by him.

Meaning of Substantially financed :- Where the grant or loan to a body or authority from the CFoI or of any State or of any UTLA in a FY is not less than ` 25 lakhs and the amt of such grant or loan is not less than 75% of the total exp of that body or authority, for this purpose to be substantially financed by such grants or loans as the case may be.

4. Audit of Grants or Loans -

Where any grant or loan is given for any specific purpose from the CFoI or of any State or of any UTLA to any authority or body, the C&AG shall scrutinise the procedures by which the sanctioning authority satisfies itself as to the fulfilment of the conditions subject to which such grants or loans were given.

5. Audit of Receipts of Union or States –

It shall be the duty of the C&AG to audit all receipts which are payable into the CFoI and of each State and of each UTLA & to satisfy himself that the rules and procedures in that behalf are designed to secure an effective check on the assessment, collection & proper allocation of revenues are being duly observed.

6. Audit of Accounts of Stores and Inventory –

The C&AG shall have authority to audit and report on the a/cs of stores & inventory kept in any office or dept of the Union or of a State.

7. Audit of Government Companies and Corporations -

The duties and powers of the C&AG in relation to the audit of the a/cs of govt cos shall be performed and exercised by him in accordance with the prov of the Cos Act, 2013. The C&AG of India shall appoint the auditor under section 139(5) or 139(7) (i.e. appointment of First Auditor or Subsequent Auditor) the auditor so appointed shall submit a copy of the audit report to the C&AG of India

The C&AG Act gives the following powers to the C&AG in connection with the performance of his duties-

Powers of C&AG

1. To inspect any office of a/cs under the control of the Union or a State Govt incl office responsible for the creation of the initial or subsidiary a/cs
2. To require that any a/cs, books, papers & other docs which deal with or otherwise relevant to the transactions under audit, be sent to specified places
3. To put such Questions or make suc observations as he may consider necessary to the person in charge of the office & to call for such info as he may require for the preparation of any account or report which is his duty to prepare
4. In carrying out the audit, the C&AG has the power to dispense with any part of detailed audit of any accounts or class of transactions and to apply such limited checks in relation to such a/cs or transactions as he may determine

EXPENDITURE AUDIT

The audit of government expenditure is one of the major components of government audit.

Audit against rules and orders:	Audit of sanctions	Audit against provision of funds:	Propriety audit:	Performance audit:
It aims to ensure that the expenditure conforms to the relevant provisions of the constitution and of the laws and rules made thereunder. It also seeks to satisfy that the expenditure is in accordance with the financial rules, regulations and orders issued by a competent authority.	The auditor has to ensure that each item of expenditure is covered by a sanction , either general or special of the competent authority	Audit against provision of funds aim at ascertaining that the expenditure incurred has been on the purpose for which the grant and appropriation had been provided and that the amt of the expenditure does not exceed the appropriation made.	The auditor tries to bring out cases of improper, avoidable or ineffective expenditure eventhough the expenditure has been incurred in conformity with the existing rules and regulations. Some general principles have been laid down in the Audit code, which have for long been recognised as standards of financial propriety.	**Efficiency** looks into whether the various schemes/ projects are executed & their operations are conducted economical & whether they are yielding the results expected of them. **Economy audit** looks into whether the government have acquired the financial, human and physical resources in an economical manner. **Effectiveness audit** is an appraisal of the performance of the programmes, schemes, projects

1. Audit against Rules & Orders –

These rules, regulations, and orders against which regularity audit is conducted mainly fall under the following categories:

a. Rules and orders regulating the powers to incur and sanction expenditure from the CFoI or of a State (and the Contingency Fund of India or of a State);

b. Rules and orders dealing with the mode of presentation of claims against govt, withdrawing moneys from the CFoI, Contingency Fund and Public A/cs of the Govt of the India and of the States, & in general the financial rules prescribing the detailed procedure to be followed by govt servants in dealing with govt transactions; and

c. Rules and orders regulating the conditions of service, pay and allowances, and pensions of govt servants.

It is the function of audit to carry out examination of the various rules, regulations and orders issued by the executive authorities to see that:

(a) They are not inconsistent with any provisions of the Constitution or any laws made thereunder;

(b) They are consistent with the essential requirements of audit and a/cs as determined by the C&AG;

(c) They do not come in conflict with the orders of, or rules made by, any higher authority; and

(d) In case, they have not been separately approved by competent authority, the issuing authority possesses the necessary rule-making power.

2. Audit of sanctions: -

The auditor has to ensure that each item of expenditure is covered by a sanction, either general or special, of the competent authority. The audit of sanctions is directed both in respect of ensuring that the expenditure is properly covered by a sanction, vested in it by the provisions of the Constitution and of the law, rules or orders made thereunder, or by the rules of delegation of financial powers made by an authority competent to do so.

3. Audit against provision of funds: -

Audit against provision of funds aims at ascertaining that the expenditure incurred has been on the purpose for which the grant and appropriation had been provided and that the amount of such expenditure does not exceed the appropriation made.

4. Propriety audit: -

According to 'Propriety audit', the auditors try to bring out cases of improper, avoidable, or ineffective expenditure even though the expenditure has been incurred in conformity with the existing rules and regulations.

Audit against propriety seeks to ensure that expenditure conforms to these principles which have been stated as follows:

a) The expenditure should not be prima facie more than the occasion demands. Every public officer is expected to exercise the same vigilance in respect of expenditure incurred from public moneys as a person of ordinary prudence would exercise in respect of expenditure of his own money.

b) No authority should exercise its powers of sanctioning expenditure to pass an order which will be directly or indirectly to its own advantage.

c) Public moneys should not be utilised for the benefit of a particular person or section of the community unless

- The amount of expenditure involved is insignificant; or
- A claim for the amount could be enforced in a Court of law; or
- The expenditure is in pursuance of a recognised policy or custom; and
- The amount of allowances, such as travelling allowances, granted to meet expenditure of a particular type should be so regulated that the allowances are not, on the whole, sources of profit to the recipients.

Note: - It is the responsibility of the executive departments to enforce economy in public expenditure.

5. Performance audit: –

The scope of audit has been extended to cover efficiency, economy and effectiveness audit or performance audit, or full scope audit: -

1. **Efficiency audit** looks into whether the various schemes/projects are executed and their operations conducted economically and whether they are yielding the results expected of them.
2. **Economy audit** looks into whether government have acquired the financial, human and physical resources in an economical manner, and whether the sanctioning and spending authorities have observed economy.
3. **Effectiveness audit** is an appraisal of the performance of programmes, schemes, projects with reference to the overall targeted objectives as well as efficiency of the means adopted for the attainment of the objectives.
4. **Efficiency- cum-performance audit**, wherever used, is an objective examination of the financial and operational performance of an organisation, programme, authority, or function and is oriented towards identifying opportunities for greater economy, and effectiveness.

The procedure for conducting performance audit covers:

1. Identification of topic,
2. Preliminary study,
3. Planning ,
4. Execution of audit, and
5. Reporting.

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AUDIT OF RECEIPTS

An auditor provides for checking:

1. Whether all revenues or other debts due to government have been correctly assessed, realised and credited to government account by the designated authorities;

2. Whether adequate regulations and procedures have been framed by the department/agency concerned to secure an effective check on assessment, collection and proper allocation of cases;

3. Whether such regulations and procedures are actually being carried out;

4. Whether adequate checks are imposed to ensure the prompt detection and investigation of irregularities, double refunds, fraudulent or forged refund vouchers or other loss of revenue through fraud or wilful omission or negligence to levy or collect taxes or to issue refunds; and

5. Review of systems and procedures to see that the internal procedures adequately secure, correct and regular accounting of demands collection and refunds and pursuant of dues up to final settlement and to suggest improvement.

6. The extent and quantum of audit required to be done under each category of audit are determined by the C&AG. These are neither negotiable nor questioned. Extent and quantum of audit are structured in accordance with the design of test check, random sampling, general review, in-depth study of specified areas.

AUDIT OF STORES AND INVENTORY

1. Ascertain whether the regulations governing purchase, receipt and issue, custody, sale, and inventory taking of stores are well devised and properly carried out.

2. To bring to the notice of the govt any defeciencies in quantities of stores held or any defects in the system of IC

3. To verify that the purchases are properly sanctioned, economical and made in accordance with the rules for purchase laid by competent authority.

4. To ensure that the prices paid are reasonable and in agreement with those shown in the contract for the supply of stores and certificates for quality and quantity are furnished by inspecting and receiving units.

5. To check the accounts of receipts, issues and balances regarding accuracy, correctness and reasonableness. Any excess or idle inventory is specifically mentioned in the report. The auditor should check that the price charged is reasonable and the valuation of inventories have to be seen carefully.

AUDIT OF COMMERCIAL ACCOUNTS

- Departmental concern engaged in commercial and trading operations
- Statutory bodies or corporations
- Government companies- Audit board

1. **Departmental concerns** are undertaken in the same manner as any dept of govt where commercial accounts are kept.
2. **Statutory bodies or corporations** depends on the nature and type of the statute governing the bodies or corporations. Financial / a/cs audit is conducted by the C&AG, and where compilation of accounts is vested with the C&AG. Functions, norms, and standards of works usually followed by the professional auditors are adopted mutatis mutandis.
3. **Government companies** is conducted by their own auditors under the statute appointed by C&AG. In addition, the C&AG conducts a supplementary test audit of the a/cs, as well as periodical financial audit and appraisal of performance. These are reviewed, and condensed in the audit reports to the govt/legislatures. C&AG has adopted the mechanism of an Audit Board-comprising of representatives of the audit and nominees of govt.

ROLE OF C & AG

(1) Power to appoint Govt Co Auditor: Section 143(5) of the Act states that, in the case of a Govt co or any other co or controlled, directly or indirectly, by the CG, or by any SG or Govts, or partly by the CG and partly by one or more SGs, the C&AG of India shall appoint the auditor under sub-section (5) or sub-section (7) of section 139 i.e. appointment of First Auditor or Subsequent Auditor & auditor so appointed shall submit a copy of the AR to the C&AG of India

(2) Power to conduct Supplementary Audit & comment thereupon :-

The C&AG of India shall within 60 days from the date of receipt of the AR have a right to,

(a) Conduct a supplementary audit under section 143(6)(a), of the FS of the co by such person or persons as he may authorize in this behalf; & for the purposes of such audit, require info or addl info to be furnished to any person or persons, as the C&AG of India may direct; and

(b) Comment upon or supplement such AR under section 143(6)(b). the AR shall be sent by the co to every person entitled to copies of audited FS under sub-section of section 136 and be placed before the AGM of the co at the same time.

(3) Test Audit:

Further, without prejudice to the provs relating to audit and auditor, the C&AG of India may, in case of any co covered under sub-section (5) or sub-section (7) of section 139, if he considers necessary, by an order, test audit to be conducted of the a/cs of such co and the provs of section 19A of the C&AG's (Duties, Powers and Conditions of Service) Act, 1971, shall apply to the report of such test audit.

AUDIT OF COOPERATIVE SOCIETIES

A cooperative is an "autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly owned enterprise."

Law governing :

- Cooperative Societies Act 1912 (Central Act)
- Multi state corporate societies Act, 2002
- State Corporate society law (eg APCSA, TNCSA, MCSA)

Cooperative society is a business organisation with a special mode of doing business, by pulling together all the means of production co-operatively, elimination of middlemen and exploitation from outside forces.

Professional services rendered by CA

- Guidance in accounts writing
- Installation of accounting system
- Internal audit
- Management accounting services
- Taxation etc

POWERS OF CO-OPERATIVE SOCIETIES:

The registrar shall audit or cause to be audited by some person authorised by him by a general or a special order in writing the accounts of every registered society once at least in every year.

The registrar, the collector shall at all times have access to the books, accounts, papers, securities of a society.

Qualification of Auditor:

- Apart from CA, some the state corp act permits persons with a government diploma in coop accounts and accountancy and also a person who has served as an auditor in the coop dept of a govt to act as an auditor

Appointment of the auditor:

- By the registrar and auditor submits report to him and the society. Audit fees paid by the society as as per statutory scale of fees prescribed by the registrar

Records, books and Accounts:

- SG can frame rules to prescribe the BOA to be kept by a coop society. Maharashtra co-op society act rules: all sums of money recd or expended by the society and the matters in respect of which R&E takes place; all sales and purchases ; assets and liab. AT THE DISCRETION OF THE SOCIETY but must be presented in a clear and best possible manner

Restriction on share holding:

- If liability of a member of the society is limited, no member, of a society other than a registered society, can hold such portion exceeding a max of 20% or of the value of shareholding to Rs.1000. Auditor will also check if any by laws are contradicting the stating provision

Restriction on loans:

- A registered society shall not make a loan to any person other than a member. However with special sanction of registrar, he can make a loan to another reg society

Restriction on borrowings:

- A reg society can accept loans and deposits from other than members subject to the restrictions of by laws

Investment of funds:

- Can invest in: Central or State coop bank, securities u/s 20 of Indian Trusts Act
  Shares, securities, bonds, debentures of any other society with limited liability.
- In any coop bank other than central or state coop bank Any other money as permitted by CG/SG

Appropriation of profits:

- A prescribed % of the profits to be transferred to reserve fund before distributing dividend / bonus to members

Contribution to charitable persons:

- They can contribute not more than 10% of the Net Profits after the compulsary transfer to reserves fund

Investment of reserve fund:

- State acts provide that the reserve fund can be used in the business of society as WC may invest as per the provisions of the act.
- may be used for public purposes to promote the object of the society.
  The auditor should ensure strict compliance with state acts and rules.

Contribution of Education fund:

- Some state acts provide that every society should contribute annually towards the education fund of the state federal society. **It is a charge on profits & not appropriation.**

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SPECIAL FEATURES OF COOPERATIVE AUDIT:

Examination of overdue debts
- Whether affecting wc position and viewpoint of chances of recovery.
- Classification: 6months-5yrs & >5years

Overdue interest
- OD interest should be excluded from int outstanding and accrued due while calculating profits

Certification of bad debts
- Maharashtra state coop rules: bad debts can be written off only when they are certified by the auditor. Where no such law requires the auditor to certify, the managing committee has to authorise the write off.

Valuation of assets and liabilities
- No specific provisions are there. The auditor has to ascertain existence, ownership and valuation of assets.
- FA= Cost - Dep +CoA & Inst to be capitalised.
- CA= Cost or MP WEL
- Liab= known liab bought into account and contingent liab= notes

Adherance to cooperative principle
- How far the objects are achieved, not in perspective of profits, but in terms of extending benefits to members. Cost accounting methods, store control method, standard costing, budgetary control should be adopted.

Observations of provisions of act and rules
- Auditor should point out infringements with the prov of act, rule and bylaws. Financial implication must be assessed and reported. Some state acts contain restriction on payment of dividend.

Members registers and passbook
- Examination of entries in member's passbook reg loan given and repayment and confirmation of loan balances in person to assure entries are free from manipulation

Special report to the registrar
- Serious irregularities which are detrimental to the interest of the society has to be reported to the registrar
- **Personal profiteering** by members of managing comm
- detection of **fraud** relating to expenses, purchases, property and stores
- **mismanagement** - urban coop banks
- **disproportionate advances** to vested interest groups. No security.

Audit classification of society
- Auditor has to award a class to the society. Judgemenet is based on the criteria specified by the registrar. If management not satisfied with the class, he can appeal to the registrar and the Registrar will direct to review the audit classification

Draft audit report
- The auditor should ask the secretary of the society to convene a managing committee meeting to discuss the draft audit report. Never finalised without discussion

AUDIT OF MULTI STATE COOPERATIVE SOCIETY

Qualification of auditor: Only a Chartered Accountant within the meaning of the Chartered Accountant's Act, 1949.

Following persons not eligible for appointment for multi-state coop society:

1. A body corporate
2. An officer or employee of multi state coop society
3. A person who is a member or who is in the employment of an officer or employee
4. A person who is indebted to the MSCS or has given guarantee or provided any security for an amount exceeding Rs. 1000

If auditor becomes subject to disqualification after appointment, he shall deem to vacate office.

APPOINTMENT OF AUDITORS

- First Auditor
  - By board within 1 month of registration
    - He will hold office till conclusion of first AGM
- Subsequent auditor
  - MSCS in General meeting at each AGM
    - They will hold office till the conclusion of the next AGM

POWERS AND DUTIES OF AUDITORS

- Right to access books, vouchers, whether kept at head office or elsewhere
- Require officers or employees to such info and explanation for performance of duties of the auditor.

The auditor shall make the following inquiries under Section 73(2):

- Whether loans and advances on the basis of security are properly secured and whether the terms are not prejudicial to the interest of the MSCS
- Whether transaction which are merely represented as book entries are not prejudicial to the interest of the MSCS
- Whether personal expenses have been charged to revenue account
- If shares have been allotted for cash, whether such cash is actually received, and if no cash has been so received, whether position as stated in the account books and the BS as correct regular and not misleading

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CONTENT OF AUDITOR'S REPORT

The financial statements should represent a true and fair view as per the information and explanation given to the auditor:

- In the case of Balance sheet, as at the end of the FY
- In the case of profit and loss account- **the auditor's report shall state:**

1. Whether he has obtained all information and explanations to the best of his knowledge necessary for audit
2. Whether proper BOA have been kept by the MSCS and proper returns have been received from the branches/offices **not visited by him**.
3. Whether the report on accounts of any branch office audited by a person **other than the auditor** of the MSCS auditor has been forwarded to him and how it has been dealt with.
4. Whether the MSCS's report containing BS and PL are **in agreement** with the BOA.

iii and iv, needs reasons in the AR

SPECIAL AUDIT

If affairs are not managed in accordance with prudent commercial practices or coop principles/sound business principles	Managed as it would cause injury to interest of trade or industry or business	Financial position is such as would endanger its insolvency

ACTION BY CG:

CG may at any time **by order** direct that a special audit of a MSCS accounts of such period/(s) as may be specified in the order shall be conducted.

→ CG may **appoint** a CA or the auditor of the MSCS himself to conduct spl audit

→ CG shall order for spl audit only if that govt or SG either by itself or both together **hold 51% or more** of the paid up share capital in such MSCS

→ The spl auditor shall have the **same powers** and duties as the auditor of MSCS. However the spl auditor shall make the **report to the CG** and not to members.

→ Expenses of and incidental to, any special audit shall be determined by the CG and paid by the MSCS.

The govt may take action on the receipt of the report from the auditor. However if the CG does not take any action **within 4 months** from the date of receipt, that government shall send to the MSCS a copy of, or relevant extract from the report, with its comments thereon and require to circulate it to the members or have the copy or extracts read before the MSCS in its next general meeting.

INQUIRY / INSPECTION BY CENTRAL REGISTRAR [SECTION 78 & 79]:

The Central Registrar on a request from below shall hold an inquiry or direct a person authorised by him by order in writing in his behalf to hold inquiry into the constitutions, working and financial condition of a MSCS [General or special order is required for inspection]

1.A federal cooperative to which a MSCS is affiliated	2.A creditor	3.Not less than 1/3rd board members	4.Not less than 1/5th members of the MSCS

However, before holding such inquiry, atleast **15 days' notice** must be given to MSCS.

The CG or the person authorised by him, shall have the following **powers:**

Inquiry

- He shall at any reasonable time have access to books, accounts, documents, securities, cash and other properties belonging to or in the custody of MSCS and may summon any person in possession or responsible for the custody of books, accounts, documents, securities, cash or other properties to produce the same at any place specified by him.
- He may, require the officers of the society to call for a GM by giving notice of **not less than 7 days** at such time and place at the head quarters of the society, or if the officers fail to call such a meeting, he shall have the power to call it himself.
- He may summon any person who is reasonably believed by him to have known the affairs of the MSCS to appear before him at any place at the HQ of the society or any branch and may examine any person on oath.

Inspection

- He shall at all times have access to all books, accounts, papers, vouchers, securities, stock and other property of that society, and in the event of serious irregularity , take them into custody, and shall have power to verify the cash balance of the society and subject to the general or special order of the central registrar to call a meeting of the society where such general meeting is, in his opinion necessary.
- Every officer or member of the society may furnish information wrt the working of society as the central reg/ person making inspection may require.

The Central registrar shall, within a period of **3 months**, of the date of receipt of the report, communicate the report of inquiry to the MSCS, the financial institutions if any, to which the society is affiliated and to the person or authority, if any, at whose instance the inquiry is needed.

AUDIT OF LOCAL BODIES

1. A Municipality can be defined as a unit of local self-government in an urban area. **'local self-government'** is administration of a locality – a village, a town, a city or any other area smaller than a state – by a body representing the local inhabitants, possessing fairly large autonomy, raising at least a part of its revenue through local taxation & spending its income on services which are regarded as local and, therefore, distinct from state & central services.

2. **Municipal government in India covers five distinct types of urban local authorities-**
   - the municipal corporations,
   - the municipal councils,
   - the notified area committees,
   - the town area committees &
   - the cantonment committees.

3. **Municipal authorities are endowed with specific local functions covering** regulatory, maintenance & development activities.

4. **Expenditure incurred by the municipalities & corporations can be broadly classified under the following heads:**
   a) general administration & revenue collection,
   b) public health,
   c) public safety,
   d) education,
   e) public works, &
   f) others such as interest payments, etc.

5. **Property taxes** & **octroi** are the major sources of revenue of the municipal authorities; other municipal taxes are profession tax, non-mechanised vehicles tax, taxes on advertisements, taxes on animals & boats, tolls, show-tax, etc.

6. **Local bodies may receive different types of grants from the state administration as well.**
   Broadly, the revenue grants are of three categories:
   a) **General purpose grants:** These are primarily intended to substantially bridge the gap between the needs & resources of the local bodies.
   b) **Specific purpose grants:** These grants which are tied to the provision of certain services or performance of certain tasks.
   c) **Statutory & compensatory grants**: These grants, under various enactments, are given to local bodies as compensation on account of loss of any revenue on taking over a tax by SG from local government.

7. **The important objectives of Audit of local bodies are:**
   a) reporting on the fairness of the content & presentation of financial statements;
   b) reporting upon the strengths & weaknesses of systems of financial control;
   c) reporting on the adherence to legal and/or administrative requirements;

d) reporting upon whether value is being fully received on money spent; &

e) detection & prevention of error, fraud & misuse of resources.

8. **Financial Administration:**

Some of the aspects are as under:

a) **Budgetary Procedure:** This is geared to subserve the twin considerations of financial accountability & control of expenditure.

- Main objective is to ensure that funds are raised & moneys are spent are in accordance with the rules & regulations & within the limits of sanction & authorisation by the legislature or council.
- Budget preparation is usually the occasion for determining the levels of taxation & rates & the ceilings on expenditure.
- Budget formats & heads of accounts vary from state to state. There are variations between the corporation & municipalities. One important feature of the municipal budgets is that there is no strict separation between revenue & capital items; usually there is a 'head' called extraordinary items which cover most of the capital transactions.
- There are no of special funds (e.g. roads) or in some cases separate budgets for specific municipal functions (e.g. education) or enterprise activities (e.g., water supply & sanitation, transport, electricity, etc.)

b) **Expenditure Control:** The system of financial control existing in the state & CG level is conditioned by the fact that there is a clear demarcation between the legislature & executive.

- integration of legislation & executive powers in the municipal council makes it difficult for its executive to function as its inquisitorial body as well.
- This leaves the system of external audit by SG as the only instrument of controlling municipal expenditure.

c) **Accounting System**: Municipal accounting & budget format have been criticised as neither simple nor comprehensible, sometimes providing inadequate info & at other times a surfeit of info. Both these situations are not conducive to a proper system of management info.

Audit Programme for Local Bodies

i. **APPOINTMENT: -**The Local Fund Audit Wing of the State Govt. is generally in-charge of the audit of municipal accounts. Sometimes bigger municipal corporations e.g. Delhi, Mumbai etc. have power to appoint their own auditors for regular external audit

ii. **AUDITOR'S CONCERNS: -**The auditor while auditing the local bodies should report on the

a. fairness of the contents & presentation of financial statements,

b. the strengths & weaknesses of system of financial control,

c. the adherence to legal and/or administrative requirements;

d. whether value is being fully received on money spent.

e. His objective should be to detect errors & fraud & misuse of resources.

iii. **RULES & REGULATIONS: -** The auditor should ensure that the expenditure incurred conforms to the relevant provisions of the law & is in accordance with the financial rules & regulations framed by the competent authority.

iv. **AUTHORISATIONS: -** He should ensure that all types of sanctions, either special or general, accorded by the competent authority.

v. **PROVISIONING: -** He should ensure that there is a provision of funds & the expenditure is incurred from the provision & the same has been authorized by the competent authority.

vi. **PERFORMANCE: -** The auditor should check that the different schemes, programmes & projects, where large financial expenditure has been incurred, are running economically & getting the expected results.

AUDIT OF NGO

Non-Governmental Organisations are generally incorporated as societies under the Societies Registration Act, 1860 or as a trust under the India Trust Act, 1882, or under any other law corresponding to these Laws enforced in any part of India. NGOs can also be incorporated as a company under section 8 of the Companies Act, 2013.

SOURCES: -

1) **The main sources** of funds include grants & donations, fund raising programmes, advertisements, fees from the members, technical assistance fees / fee for services rendered, subscriptions, gifts, sale of produce or publications, etc.

a) Donations & grants received in the nature of promoter's contribution are capital receipts & shown as liabilities in the BS of NGO.
Either be in the form of corpus contribution or a contribution towards revolving fund. A Contribution towards the capital or the corpus of an NGO known as corpus contribution. Donors generally specify whether donation/grant shall form part of corpus of NGO.

b) Section 11(1)(d) of the Income Tax Act 1961 also states that income in the form of voluntary contributions made with a specific direction that they shall form part of the corpus of the trust or institution shall not be included in the computation of total income.

c) objective of a contribution or grant towards a Revolving Fund is to rotate the amt by giving temporary loans from the fund to other NGO or beneficiaries & then recover the loan to give temporary loans again. However, interest earned from the beneficiary on such temporary loans from the revolving fund could be either added back to the fund or credited to the Income & Expenditure A/c depending on restrictions laid down by the authority providing the contribution (for the revolving fund) or by the rules & regulations of NGO.

d) Donations & grants received for acquisition of specific fixed assets are those grants whose primary condition is that NGO accepting them should purchase, construct or otherwise acquire the assets for which the grant is given.

e) Many a times NGOs receive contributions in kind.
These contributions include assets such as land, buildings, vehicles, office equipment, etc. & articles related to programmes / projects such as food, books, building materials, clothes, beds, & raw material for training purposes, e.g., Wool, reeds, cloth, etc.

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2) The areas of **application of funds** for an NGO include Establishment Costs, Office & Administrative Expenses, Maintenance Expenses, Programme / Project Expenses, Charity, Donations & Contributions given, etc.

PLANNING THE AUDIT: -

i. Knowledge of the NGO's work, its mission & vision, areas of operations & environment in which it operate.

ii. Updating knowledge of relevant statutes especially with regard to recent amendments, circulars, judicial decisions viz. Foreign Contribution (Regulation) Act 2010, Societies Registration Act, 1860, Income Tax Act 1961 etc. & the Rules

iii. Reviewing the legal form of the Organisation & its MOA, AOA, Rules & Regulations.

iv. Reviewing the NGO's Organisation chart, then Financial & Administrative Manuals, Project & Programme Guidelines, Funding Agencies Requirements & formats, budgetary policies if any.

v. Examination of minutes of the Board/Managing Committee/Governing Body/ Management & Committees thereof to ascertain the impact of any decisions on the financial records.

vi. Study the accounting system, procedures, internal controls & internal checks existing for the NGO & verify their applicability.

vii. Setting of materiality levels for audit purposes.

viii. The nature & timing of reports or other communications.

ix. The involvement of experts & their reports.

x. Review the previous year's Audit Report.

The audit programme should include in a sequential order all assets, liabilities, income & expenditure ensuring that no material item is omitted.

i. **Corpus Fund:** The contributions / grants received towards corpus be vouched with special reference to the letters from the donor(s). The interest income be checked with Investment Register & Physical Investments in hand.

ii. **Reserves:** Vouch transfers from projects / programmes with donors letters & board resolutions of NGO. Also check transfer of gross value of asset sold from capital reserve to general reserve & adjustments during the year.

iii. **Ear-marked Funds:** (Earmarking refers to a fund allocation practice in which an entity, a government, or an individual sets aside a determined amt of funds to use for a specific goal). Check requirements of donors institutions, board resolution of NGO, rules & regulations of the schemes of the ear marked funds.

iv. **Project / Agency Balances:** Vouch disbursements & expenditure as per agreements with donors for each of the balances.

v. **Loans:** Vouch loans with loan agreements, counterfoil of receipt issued.

vi. **Fixed Assets:** Vouch all acquisitions / sale or disposal of assets including depreciation & the authorisations for the same. Also check donor's letters/ agreements for the grant. In the case of immovable property check title, etc.

vii. **Investments:** Check Investment Register & the investments physically ensuring that investments are in the name of the NGO. Verify further investments & dis- investments for approval by the appropriate authority & reference in the bank accounts for the principal amt & interest.

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viii. **Cash in Hand:** Physically verify the cash in hand & imprest balances, at the close of the year & whether it tallies with the books of account.

ix. **Bank Balance:** Check the bank reconciliation statements & ascertain details for old outstanding & unadjusted amts.

x. **Inventory:** Verify inventory in hand & obtain certificate from the management for the quantities & valuation of the same.

xi. **Programme & Project Expenses:** Verify agreement with donor/contributor(s) supporting the particular programme or project to ascertain the conditions with respect to undertaking the programme/project & accordingly, in the case of programmes/projects involving contracts, ensure that income tax is deducted, deposited & returns filed & verify the terms of the contract.

xii. **Establishment Expenses:** Verify that PF, life insurance premium, employees state insurance & their administrative charges are deducted, contributed & deposited within the prescribed time. Also check other office & administrative expenses such as postage, stationery, travelling, etc.

The receipt of income of NGO may be checked on the following lines:

i. **Contributions & Grants for projects & programmes:** Check agreements with donors & grants letters to ensure that funds received have been accounted for. Check that all foreign contribution receipts are deposited in the foreign contribution bank account as notified under the Foreign Contribution (Regulation) Act, 2010

ii. **Receipts from fund raising programmes:** Verify in detail the internal control system & ascertain who are the persons responsible for collection of funds & mode of receipt. Ensure that collections are counted & deposited in the bank daily.

iii. **Membership Fees:** Check fees received with Membership Register. Ensure proper classification is made between entrance & annual fees & life membership fees. Reconcile fees received with fees to be received during the year.

iv. **Subscriptions:** Check with subscription register & receipts issued. Reconcile subscription received with printing & dispatch of corresponding magazine / circulars / periodicals. Check the receipts with subscription rate schedule.

v. **Interest & Dividends:** Check the interest & dividends received & receivable with investments held during the year.

AUDIT OF SOLE TRADER

Sole trader is under no legal obligation to have his accounts audited.

Appointment of Auditor: Auditors of sole- proprietary concern shall be appointed by the sole proprietor himself. In case of change of auditor, it would be duty of incoming auditor to communicate with the previous auditor.

As such, sole proprietor can determine the scope of the audit as well as the conditions under which it will be carried out.

The advantages & audit procedure discussed in following paragraphs of audit in case of partnership firm would be similar in case of proprietorship.

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AUDIT OF FIRM

Matters to be considered before starting audit: Also, before starting the audit, he should examine the partnership agreement & note the provisions therein as regards the following matters:

1. The name & style under which the business shall be conducted.
2. The duration of the partnership, if any, that has been agreed upon.
3. The amt of capital that shall be contributed by each partner—whether it will be fixed or could be varied from year to year.
4. Period at the end of which the accounts of the partnership will be closed periodically & the proportions in which the profit shall be divided among the partners or losses shall have to be contributed by them; whether the losses shall be borne by the partners .
5. Provisions for maintenance of books of accounts & determining the profits of the firm available for division among the partners e.g., creation of reserves, provision for depreciation, etc
6. Borrowing capacity of the partnership (when it is not implied as in the case of non-trading firms).
7. Rate at which interest will be allowed on the capitals & loans provided by partners & the rate at which it will be charged on their drawings & current a/c.
8. Whether any salaries are payable to the partners or withdrawals are permitted against shares of profits and, if so, to what extent?
9. Duties of the partners as regards the management of business of the firm; also, the partners who shall act as managing partners.
10. Who shall operate the bank account of the firm? How will the surplus funds of the partnership be invested?
11. Limitations & restrictions that have been agreed upon, the rights & powers of partners & on their implied authority to pledge the firm's credit or to render it liable.

Advantages of Audit of a Partnership Firm - On broad considerations, the advantages of audit of accounts of a partnership could be stated as follows:

1. **Disputes:** - Audited a/cs provide a convenient & reliable means of settling a/cs between the partners & the possibility of occurrence of a dispute among them is mitigated.
2. **Dissolution:** - On the retirement or death of a partner, a/cs, which have been accepted by the partners, constitute reliable evidence for computing the amts due to the retiring partner or to the representative of the deceased partner in respect of his share of capital, profits & goodwill.
3. **Reliable:** - Audited a/cs are relied upon by the banks when advancing loans, as well as by prospective purchasers of the business, as evidence of the profitability of the concern & its financial position
4. **Admission:** - Audited a/cs can be helpful in the negotiations to admit a person as a partner, especially when they are available for a no. of past years.
5. **Control:** - An audit is an effective safeguard against any undue advantage being taken by a working partner especially in the case of those partners who are not actively associated with the working of the firm.

Matters which should be specially considered in the audit of accounts of a partnership:

1. **Letter of Appointment: -** Confirming that the letter of appointment, signed by a partner, duly authorised, clearly states the nature & scope of audit contemplated by the partners, especially the limitation, if any, under which the auditor shall have to function.
2. **Partnership Documents: -** Studying minute book, if any, maintained to record the policy decision taken by partners specially minutes relating to authorisation of extraordinary & capital expenditure, raising of loans; purchase of assets, extraordinary contracts & other such matters
3. **Objects of Partnership: -** Verifying that the business in which the partnership is engaged is authorised by the partnership agreement
4. **Books of Account: -** Examining whether books of a/c appear to be reasonable & considered adequate in relation to the nature of the business
5. **Mutual Interest: -** Verifying that interest of no partner has suffered prejudicially by an activity engaged by partnership which was not authorised to do under the partnership deed or any violation of partnership agreements
6. **Provision for Taxes: -** Confirming that a provision for the firm's tax payable by the partnership has been made in the a/cs before arriving at the amt of profit divisible among the partners.
7. **Division of Profits: -** Verifying that the profits & losses have been divided among the partners in their agreed profit-sharing ratio.

LLP AUDIT

LLP is governed by Limited Liability Partnership Act, 2008. Minimum of 2 Partners can form an LLP & atleast two partners would be Designated Partners who would be required to take DPIN (Designated Partner Identification Number)

It defines a Small Limited Liability Partnership to denote any LLP:

a) Contribution <= 25,00,000 or such higher amt, not exceeding Rs.5cr &

b) Turnover for immediately preceding financial year <= 40,00,000 or such higher amt, not exceeding rs.50cr

LLP's are required to maintain books of accounts which shall contain-

1. Particulars of all sums of money received & expended by the LLP & the matters in respect of which the receipt & expenditure takes place
2. A record of the assets & liabilities of the LLP,
3. Statements of costs of goods purchased, inventories, work-in-progress, finished goods & costs of goods sold,
4. Any other particulars which the partners may decide.

Audit of the Accounts of an LLP: -

Any LLP, whose t/o <= rs.40L , or contribution <= Rs.25L -> No audit

In other words, only if t/o > 40L & contribution > 25L -> Audit is required

However, if partners of such LLP decide to get a/cs of such LLP audited, such a/cs shall be audited in accordance with such rule.

Returns to be maintained & filed by LLP:

Annual return in form 11 with ROC within 60days of closer of FY

eg: for FY2024-25 -> FILED BY 30TH MAY 2025

Advantages / Purpose / Need of Audit:-

1. **Detection of Errors**: - Auditing the accounts of a LLP helps in detecting errors & frauds & verification of financial statements.
2. **Disputes:** -Disputes, if any between any partners in the matter of accounts can be settled with the help of audited accounts.
3. **Reliability:** - Banks & financial institutions lend money to the firms only on the basis of audited accounts.
4. **Better Compliance & Management**: -Periodical visits & suggestions by the auditor will be helpful in improving the management of the LLP.
5. **Reconstitution**: - For settling accounts between partners at the time of admission, death, retirement, insolvency, insanity, etc. audited accounts are accepted by those concerned who have dealings with the LLP.

Appointment of Auditor: The auditor may be appointed by the designated partners of the LLP

1. At any time for the 1st FY but before the end of 1stFY
2. At least thirty days prior to the end of each FY (other than the 1st FY),
3. To fill the casual vacancy in the office of auditor,
4. To fill the casual vacancy caused by removal of auditor.

Auditors' duty regarding audit of LLP:

1. **Engagement Letter: -** The auditor should get definite instructions in writing as to the work to be performed by him
2. **Minutes Book:-** If partners maintain minute book he shall refer it for any resolution passed regarding the accounts
3. **LLP Agreement: - The auditor should read the LLP agreement & note the following provisions**

(a) Nature of the business of the LLP.
(b) Amt of capital contributed by each partner.
(c) Interest – in respect of additional capital contributed.
(d) Duration of partnership.
(e) Drawings allowed to the partners.
(f) Salaries, commission etc. payable to partners.
(g) Borrowing powers of the LLP.
(h) Rights & duties of partners.
(i) Method of settlement of accounts between partners at the time of admission, retirement, admission etc.
(j) Any loans advanced by the partners.
(k) Profit sharing ratio

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4. **Reporting: - The auditor should mention**

(a) Whether the records of the firm appear to be correct & reliable.

(b) Whether he was able to obtain all info & explanation necessary for his work.

(c) Whether any restriction was imposed upon him.

AUDIT OF CHARITABLE INSTITUTION

GENERAL:

i. Studying the constitution under which the charitable institution has been set up.

ii. Verifying whether the institution managed in the manner contemplate under which it has been set up.

iii. Examining the system of internal check, especially as regards accounting of amts collected.

iv. Verifying in detail the income & confirming that the amt deposited in the bank regularly

v. Examine the Trust Deed or the Regulations as laid down.

Subscriptions & donations

I. Ascertaining, if any, the changes made in amt of annual or life membership subscription during the year.

II. Whether official receipts are issued;

a) confirming that adequate control is imposed over unused receipt books;

b) obtaining all receipt books covering the period under review;

c) test checking the counterfoils with the cash book; any cancelled receipts being specially looked into;

d) obtaining the printed list of subscriptions & donations & agreeing them with the total collections shown in the accounts;

e) verifying the total subscriptions & donations received with any figures published in reports, etc. issued by the charity.

Legacies: – Verifying the amts received by reference to correspondence with any figures & other available info.

Grants: -

(i) Vouching the amt received with the relevant correspondence, receipts & minute books.

(ii) Obtaining a certificate from a responsible official showing the amt of grants received.

Investments Income: -

(i) Vouching the amts received with the dividend & interest counterfoils.

(ii) Checking the calculations of interest received on securities bearing fixed rates of interest.

(iii) Checking that the appropriate dividend has been received where any investment has been sold ex-dividend or purchased cum-dividend.

(iv) Comparing the amts of dividend received with schedule of investments making special enquiries into any investments held for which no dividend has been received.

Rent: -

(i) Examining the rent roll & inspecting tenancy agreements, noting in each case:

(a) the amts of the rent,

(b) the due dates.

(ii) Vouching the rent on to the rent roll from the counterfoils of receipt books & checking the totals of the cash book.

Special function, etc. –

i. Vouching gross receipts & outgoings in respect of any special functions, e.g. concerts, dramatic performance, etc., held in aid of the charity with such vouchers & cash statements as are necessary.

ii. verifying that the proceeds of all tickets issued have been accounted for, after making the allowance for returns.

Income tax refunds: -

Where income-tax has been deducted at source from the Investment income, it should be seen that a refund thereof has been obtained since charitable institutions are exempt from payment of Income tax. This involves:

(i) vouching the Income-tax refund with the correspondence with the Income- tax Department; &

(ii) checking the calculation of the repayment of claims.

Expenditure: -

i. Vouching payment of grants, also verifying that the grants have been paid only for a charitable purpose(s) within the purview of the objects for which it was set up & no trustee, director or member of the Managing Committee has benefited

ii. Verify the schedules of securities held & inventories of properties both movable & immovable by inspecting the securities & title deeds of property & physical verification of movable properties on a test- basis.

iii. Verifying the cash & bank payments.

iv. Ascertaining that any funds contributed for a special purpose have been utilised for the purpose.

AUDIT OF EDUCATIONAL INSTITUTIONS

GENERAL: -

1. Examine the Trust Deed or Regulations, in the case of school or college & note all the provisions affecting accounts. In the case of a university, refer to the Act of Legislature & the Regulation framed thereunder.
2. Read through the minutes of the meetings of the Managing Committee

FEE FROM STUDENTS: -

1. Check names entered in the Students Fee Register for each month or term, with the respective Class Registers, showing names of students on rolls & test amt of fees charged.
2. Check fees received by comparing counterfoils of receipts granted with entries in the Cash Book
3. Total up the various columns of the Fees Register for each month or term to ascertain that fees paid in advance have been carried forward.
4. Check admission fees with admission slips signed by the head of the institution & confirm that the amt has been credited to a Capital fund.
5. Check free studentship & concessions granted by a person authorised
6. Confirm that fines for late payment or absence, etc. have been either collected or remitted under proper authority.
7. Confirm that hostel dues were recovered before student's a/cs were closed & caution money deposit refunded.

Other Receipts/Grants & Donations: -

1. Verify rental income from landed property with the rent rolls, etc.
2. Vouch income from endowments & legacies, & interest & dividends from investment; also inspect the securities in respect of investments held.
3. Verify any Govt or local authority grant with memo of grant. If any expense has been disallowed for purposes of grant, ascertain the reasons thereof.

Expenditure: -

1. Verify that the Provident Fund money of the staff has been invested in appropriate securities.
2. Vouch donations, if any with the list published with the annual report. If some donations were meant for any specific purpose, see that the money was utilised for the purpose.
3. Vouch, all capital expenditure in the usual way & verify the same with the sanction for the Committee as contained in the minute book.
4. Vouch, in the usual manner, all establishment expenses & enquire into any unduly heavy expenditure under any head.
5. See that increase in the salaries of the staff have been sanctioned & minuted by the Committee.

Assets & Liabilities: -

1. Report any old heavy arrears on account of fees, dormitory rents, etc. to the Managing Committee.
2. Confirm that caution money & other deposits paid by students on admission, have been shown as liability in BS not transferred to revenue, unless they are not refundable.
3. See that the investments representing endowment funds for prizes are kept separate & any income in excess of the prizes has been accumulated & invested along with the corpus.
4. Ascertain that system ordering inspection on receipt & issue of provisions, foodstuffs, clothing & other equipment is efficient & all bills are duly authorised & passed before payment.
5. Verify inventories of furniture, stationery, clothing, provision & all equipment etc. These should be checked by reference to Inventory Register or corresponding inventories of the PY & values applied to various items should be test checked.

Compliances: -

1. Confirm that the refund of taxes deducted from the income from investment (interest on securities etc.) has been claimed & recovered since the institutions are generally exempted from the payment of income-tax.
2. verify the annual statements of a/c & see that separate statements of a/c prepared as regards Poor Boys Fund, Games Fund, Hostel & Provident Fund of staff, etc.

AUDIT OF HOSPITALS

1. **Register of Patients:** Vouch the Register of patients with copies of bills issued. Verify bills for a selected period with the patients' attendance record to see that the bills have been correctly prepared. Also see that bills have been issued to all patients from whom an amt was recoverable as per rules of hospital.

2. **Collection of Cash:** Check cash collections as entered in the Cash Book with the receipts, counterfoils & other evidence for example, copies of patient's bill, counterfoils of dividend & other interest warrants, copies of rent bills, etc.

3. **Income from Investments, rent etc:** See with reference to the property & Investment Register that all income that should have been received by way of rent on properties, dividends, & interest on securities have been collected.

4. **Legacies & Donations:** Ascertain that legacies & donations received for a specific purpose have been applied in the manner agreed upon.

5. **Reconciliation of Subscriptions:** Trace all collections of subscription & donations from the Cash Book to the respective Registers. Reconcile the total subscriptions due (as shown by the Subscription Register & the amt collected & that still outstanding).

6. **Authorisation & Sanctions**: Vouch all purchases & expenses & verify that the capital expenditure was incurred only with the prior sanction of the Trustees or the Managing Committee & that appointments & increments to staff have been duly authorised.

7. **Grants & TDS:** Verify that grants, if any, received from Government or local authority has been duly accounted for. Also, that refund in respect of taxes deducted at source has been claimed.

8. **Budgets:** Compare the totals of various items of exp & income with the amt budgeted for them & report to the Trustees or the Managing Committee, significant variations

9. **Internal Check:** Examine the internal check as regards the receipt & issue of stores; medicines, linen, apparatus, clothing, instruments, etc. to ensure that purchases have been properly recorded in the Inventory Register & that issues have been made only against proper authorisation.

10. **Depreciation:** See that depreciation has been w/off against all the assets at the appropriate rates.

11. **Registers:** Inspect the bonds, share scrips, title deeds of properties & compare their particulars with those entered in the property & Investment Registers.

12. **Inventories:** Obtain inventories, especially of stocks & stores as at the end of the year & check a percentage of the items physically; also compare their total values with respective ledger balances.

13. **Management Representation & Certificate:** Get proper Mgt Representation & Certificate w.r.t various aspects covered during the course of audit.

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AUDIT OF CLUB

1. Entrance Fee: - Vouch the receipt on account of entrance fees with members' applications, counterfoils issued to them, as well as on a reference to minutes of the Managing Committee.

2. Subscriptions: - Vouch members' subscriptions with the counterfoils of receipt issued to them, trace receipts for a selected period to the Register of Members; also reconcile the amt of total subscriptions due with the amt collected & that outstanding.

3. Arrears of Subscriptions: - Ensure that arrears of subscriptions for the previous year have been correctly brought over & arrears for the year under audit & subscriptions received in advance have been correctly adjusted.

4. Arithmetical accuracy: - Check totals of various columns of the Register of members & tally them across.

5. Irrecoverable Member Dues: - See the Register of Members to ascertain the Member's dues which are in arrear & enquire whether necessary steps have been taken for their recovery; the amt considered irrecoverable should be mentioned in the Audit Report.

6. Pricing: - Verify the internal check as regards members being charged with the price of foodstuffs & drinks provided to them & their guests, as well as, with the fees chargeable for the special services rendered, such as billiards, tennis, etc.

7. Member Accounts: - Trace debits for a selected period from subsidiary registers maintained in respect of supplies & services to members to confirm that the account of every member has been debited with amts recoverable from him.

8. Purchases: - Vouch purchase of sports items, furniture, crockery, etc. & trace their entries into the respective inventory registers.

9. Margins earned: - Vouch purchases of foodstuffs, cigars, wines, etc., & test their sale price so as to confirm that the normal rates of gross profit have been earned on their sales. The inventory of unsold provisions & stores, at the end of year, should be verified physically & its valuation checked.

10. Inventories :- Check the inventory of furniture, sports material & other assets physically with the respective inventory registers or inventories prepared at the end of the year.

11. Investments :- Inspect the share scrips & bonds in respect of investments, check their current values for disclosure in final accounts; also ascertain that the arrangements for their safe custody are satisfactory.

12. Management Powers :- Examine the financial powers of the secretary and, if these have been exceeded, report specific case for confirmation by the Managing Committee.

AUDIT OF CINEMA

1. **Verify the** internal control mechanism**-**
   - (a) that entrance to the cinema-hall during shown only through printed tickets;
   - (b) that they are serially numbered & bound into books;
   - (c) no. of tickets issued for each show & class, are different though the numbers of the same class for the show on the same day, each week, run serially;
   - (d) for advance booking a separate series of tickets is issued; &
   - (e) the inventory of tickets is kept in the custody of a responsible official.
2. Confirm that at the end of show, Statement of tickets sold is prepared & cash collected is agreed with it.
3. Verify that a record is kept of the 'free passes' & that these are issued under proper authority.

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4. Reconcile the amt of Tax collected with the total no. of tickets issued for each class & vouch & verify the tax returns filed each month.
5. Vouch the entries in the Cash Book w.r.t cash collected on sale of tickets for different shows on a reference to Daily Statements which have been test checked as aforementioned with record of tickets issued for the different shows held.
6. Verify the charges collected for advertisement slides & shorts by reference to the Register of Slides & Shorts Exhibited kept at the cinema as well with the agreements, entered with advertisers in this regard.
7. Vouch the expenditure incurred on advertisement, repairs & maintenance. No part of such expenditure should be capitalized.
8. Confirm that depreciation on machinery & furniture has been charged at an appropriate rate.

AUDIT OF HIRE PURCHASE & LEASING COMPANIES

A Hire-purchase agreement means an agreement under which goods are let on hire & under which the hirer has an option to purchase them in accordance with the terms of the agreement & includes an agreement under which-

(i) possession of goods is delivered by the owner thereof to a person on condition that such person pays the agreed amt in periodical instalments,

(ii) the property in the goods is to pass to such person on the payment of the last of such instalments, &

(iii) such person has a right to terminate the agreement at any time before the property so passes.

While checking the hire- purchase transaction, the auditor may examine the following:

1. Hire purchase agreement is in writing & is signed by all parties.
2. Hire purchase agreement specifies clearly-
   a) The hire-purchase price of the goods to which the agreement relates;
   b) The cash price of the goods, that is to say, the price at which the goods may be purchased by the hirer for cash;
   c) The date on which the agreement shall be deemed to have commenced;
   d) The no. of instalments by which the hire- purchase price is to be paid, the amt of each of those instalments, & the date, or the mode of determining the date, upon which it is payable, & the person to whom & the place where it is payable; &
   e) The goods to which the agreement relates, in a manner sufficient to identify them.
3. Ensure that instalment payments are being received regularly as per the agreement.

LEASES: -

1. In a lease agreement, a party (called 'lessee') acquires the right to use an asset for an agreed period of time in consideration of payment of rent to another party (called 'lessor').
2. In certain lease agreements, the legal ownership of the asset remains with the lessor (the leasing company), but in substance, all the risks & rewards of ownership of the asset are transferred to the lessee.
   i. Finance Lease:

   The lease arrangement transfers ownership of the asset to the lessee at the end of the lease term;

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- The lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised;
- The lease term is for the major part of the economic life of the asset even if title is not transferred;

Auditor's Procedures: -

- The object clause of leasing company to see that the goods like capital goods, consumer durables etc. in respect of which the company can undertake such activities. Further, to ensure that whether company can undertake financing activities or not.
- Whether there exists a procedure to ascertain the credit analysis of lessee like lessee's ability to meet the commitment under lease, past credit record, capital strength, availability of collateral security, etc.
- **The lease agreement should be examined**
- Examine the lease proposal form submitted by the lessee requesting the lessor to provide him the equipment on lease.
- Ensure that the invoice is retained safely as the lease is a long-term contract.
- Examine the acceptance letter obtained from the lessee indicating that the equipment has been received in order & is acceptable to the lessee.
- See the Board resolution authorising a particular director to execute the lease agreement has been passed by the lessee.
- See that the copies of the insurance policies have been obtained by the lessor for his records.

AUDIT OF HOTELS

The special considerations in a hotel audit can be summarised as follows:

1. **Internal Controls –**

1. Pilfering is one of the greatest problems in any hotel & the importance of internal control cannot be undermined.

2. The auditor should obtain these regular trading accounts for the period under review, examine them & obtain explanations for any apparent deviations.

3. If the internal control in a hotel is weak or perhaps breaks down, then a very serious problem exists for the auditor.

4. Mgmt should prepare regular perhaps weekly, trading A/cs for each sales point & detailed scrutiny of the resulting pft %, with any deviation.

5. The auditor should verify a few restaurant bills by reference to K.O.T.s (Kitchen Order Tickets) or basic record.

6. As a result of his clients' records, the auditor must rely to a very large extent on the gross margin shown by the A/cs, he will have to considered qualifying his AR.

2. Room Sales & Hall Bookings

- The charge for room sales is normally posted to guest bills by the receptionist/ front office or in the case of large hotels by the night auditor.
- The source of these entries is invariably the guest register & audit tests should be carried out to ensure that the correct numbers of guests are charged for the correct period.
- Any difference between the charged rates used on the guests' bills & the standard room rate should be investigated to ensure that they have been properly authorised.
- In many hotels, the housekeeper prepares a daily report of the rooms which were occupied the previous night & the no. of beds kept in each room.
- This report tends not to be permanently retained & the auditor should ensure that a sufficient no. of reports are available for him to test both with the guest register & with the individual guest's bill.
- The auditor should ensure that proper records are maintained for booking of halls & other premises for special parties & recovered on the basis of the tariff.

3. Inventories -

The inventories in any hotel are both readily portable & saleable particularly the food & beverage inventories.	All movements & transfers of such inventories should be properly documented to enable control to be exercised over each individual stores areas & sales point.
The auditor should carry out tests to ensure that all such documentation is accurately processed.	Areas where large quantities of inventory are held should be kept locked, the key being retained by the departmental manager.
The key should be released only to trusted personnel & unauthorised persons should not be permitted in the stores areas except under constant supervision.	Many hotels use specialised professional valuers to take & value the inventories on a continuous basis throughout the year.

4. Fixed Assets –

i. The accounting policies for fixed assets of individual hotels are likely to differ.

ii. The auditor should see that costs of repairs & minor renovation & redecoration are treated as revenue expenditure, where as costs of major alterations & additions to the hotel building & facilities capitalised.

5. Casual Labour –

The hotel trade operates to very large extent on casual labour. The records maintained of such wage payments are frequently inadequate. The auditor should ensure that defalcation on this account does not take place by suggesting proper controls to the management.

6. **Travel Agents & Shops –**

   i. For ledgers coming through travel agents or other booking agencies the bills are usually made on the travel agents or booking agencies. The auditor should ensure that money are recovered from the travel agents or booking agencies as per the terms of credit allowed.

   ii. Commission, if any, paid to travel agents or booking agents should be checked by reference to the agreement on that behalf.

AUDIT OF TRUSTS & SOCIETIES

There are three basic legal forms of charitable entities under Indian law: trusts, societies, & section 8 companies.

- If the charitable institution is formed as a Public Trust, it will be governed by the Public Trust Act applicable in the relevant State.
- Society will be governed by the Societies Registration Act, 1860.
- Non-profit company under section 8 of the Companies Act, 2013.
- Apart from the above legislations, the Income Tax Act 1961 will be applicable to charitable institutions.
- And in the case of foreign contributions to these charitable institutions, the Foreign Contribution (Regulation) Act, 2010 will be applicable.

BOOKS OF ACCOUNT:-

Whether the Trust has maintained proper books of accounts, including the following, namely: -

1. Cash book	2. ledger	3. journal
4. copies of bills, & copies or counterfoils of machine numbered or otherwise serially numbered receipts issued by the trust	5. original bills wherever issued to the person & receipts in respect of payments made by the person;	6. any other book;

AUDIT WORK PAPERS:

Such working papers should include his notes on the following, amongst other matters:

a) work done while conducting the audit & by whom;

b) explanation & info given to him during the course of the audit & by whom;

c) decision on the various points taken;

d) the judicial pronouncements relied upon by him while drafting the audit report;

e) certificates issued by the client / management letters.

TRUSTS

The auditor has to ascertain:-

1. Whether accounts are maintained regularly & in accordance with the provisions of the applicable Act & the rules;	2. Whether receipts are properly & correctly shown in the accounts & money received in the form of donations is being applied as per the objects of the trust.	3. whether the cash balance & vouchers in the custody of the manager or trustee on the date of audit were in agreement with the accounts;
4. Whether all books, deeds, accounts, vouchers or other documents or records required by the auditor were produced before him;	5. Whether the maximum & minimum no. of the trustees is maintained;	6. Whether the meeting are held regularly as provided in such instrument
7. Whether the minute books of the proceedings of the meeting is maintained	8. Whether any of the trustees has any interest in the investment of the trust	9. Whether any of the trustees is a debtor or creditor of the trust.

SOCIETIES

The auditor's considerations:-

- The auditor should ascertain governing legislation of society i.e. Societies Registration act, 1860 or any applicable state law under which it has been registered.
- Object of society needs to be ascertained from its MOA/bye laws. Its activities may include charitable, social, cultural or educational activities.
- Ascertain whether society has obtained registration under Foreign Contribution (Regulation) Act, 2010 in case foreign contributions are received.
- Ascertain whether it is also registered under relevant provisions of Income Tax Act which may make it eligible for tax exemption on its income.
- Obtain an understanding of internal control to design audit procedures with special reference to donations & various expenditures incurred in relation to achievements of objects of society

AUDIT OF ITEMS OF FS

AUDIT OF ITEMS OF FS

- BS ITEMS
- PL ITEMS
- ADD. IMPORTANT DISCLOSURE

BS ITEMS

LIABILITIES
1. SHARE CAPITAL
2. RESERVES AND SURPLUS
3. BORROWINGS
4. TRADE PAYABLES AND OCL
5. PROVISION AND CONTINGENT LIABILITIES

ASSESTS
1. PPE
2. INTANGIBLE ASSETS
3. TRADE RECEIVABLES
4. INVENTORIES
5. CASH AND CASH EQUIVALENT

SHARE CAPITAL

- I. AUDIT PROCEDURES
- II. SHARES ISSUED AT PREMIUM (ICAI SM)
- III. SHARES ISSUED AT A DISCOUNT (MAY'24)
- IV. ISSUE OF SWEATY EQUITY SHARES (SES)
- V. REDUCTION OF CAPITAL
- VI. DISCLOSURES

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I. AUDIT PROCEDURES

- Tally period end share capital balance – authorized, issued and paid up to PY audited FS.
- If no change during the year, obtain written confirmation/representation from CS that there were no changes to entity's capital structure during the year.
- In case there's any change, verify whether paid-up capital at period- end within limits of authorized capital. Authorized capital should be verified by examining MOA.
- Obtain certified copies of relevant resolutions passed at meetings of BOD, shareholders authorizing increase/decrease in authorized share capital if required, or paid-up share capital
- In case of Fresh issue made in CY. check compliance of Companies Act 2013 w.r.t. Return of Allotment, Minimum Subscription, minimum application money to be collected, maintenance of separate Bank A/c, payment of underwriting commission as per Sec 40.
- No shares have been issued at Discount (Sec. 53 of Companies Act)
- Check if the shares are issued for cash or for Consideration other than cash (Eg: To promoters for their services, underwriters for commission payable to them, etc.)
- Compliance with SEBI regulations and guidelines.
- Obtain and verify copies of forms filled with Ministry of Corporate Affairs (MCA)
- Form SH-7 notice to Registrar of any alteration of share capital, Form PAS-3 company making allotment of shares / securities required to file a return of allotment to the Registrar) and with RBI.
- (Form FCGPR in case of Foreign Direct Investment (FDI) by a Non – resident shareholder) and verify no. of securities issued along with issue price.
- In case of increase in share capital, verify whether Co, has accurately calculated fee and stamp duty payable to MCA.

II. SHARES ISSUED AT PREMIUM (ICAI SM)

If Co. issues shares at a premium, Co. shall transfer premium amount to securities premium a/c & state purpose for which amount can be applied. No restriction for issue of shares at premium.

Application of securities premium a/c for following purposes:

a) towards issue of unissued shares of Co. to members of Co. as fully paid bonus shares
b) for purchase of its own shares or other securities under Section 68. (Buyback)
c) in writing off preliminary expenses of Co.
d) in providing for premium payable of redemption of any redeemable preference shares or debentures of Co.
e) in writing off expenses, or commission paid or discount allowed on, any issue of shares or debentures of Co.

Auditor needs to verify:

a) whether premium received is transferred to a "securities premium a/c"

b) whether application of "securities premium a/c" is only for purposes mentioned above.

III. SHARES ISSUED AT A DISCOUNT (MAY'24)

As per Section 53 of Companies Act,2013:

a) Co. shall NOT issue shares at discount, except sweat equity shares u/s 54 of Companies Act,2013.

b) any share issued by a Co. at a discounted price shall be void.

Exception:

Co. may issue shares at a discount to its creditors when its debt is converted into shares in pursuance of any statutory resolution plan or debt restricting scheme as per any RBI guidelines.

Penalty:

Co. & every officer in default liable to a penalty

- Amount raised through issue of shares at discount or Rs. 5 lakh, whichever is less, &
- Co. also liable to refund all monies received with interest @ 12% p.a. from date of issue of such shares to persons to whom such shares have been issued.

Auditor needs to check:

a) movement in SC during year and wherever there is any issue.

b) Verify that Co. hasn't issued any shares at discount by reading minutes of meeting of directors & SH authorizing issue of SC & issue price.

c) Also verify whether Co. has issued shares at a discount to its creditors when debt is converted into shares in pursuance of any statutory resolution plan or debt restricting scheme as per any RBI guidelines.

IV. ISSUE OF SWEAT EQUITY SHARES (SES)

As per Sec. 54 of the Companies Act, 2013, employees may be compensated in form of "Sweat Equity Shares". It means equity shares issued by Co. to employees or directors at a

a) discount or

b) for consideration other than cash for providing know-how or making available right in nature of intellectual property rights or value additions, by whatever name called.

Auditor needs to verify that SEB issued by Co. are of class of shares already issued & following conditions complied:

a) Issue is authorized by SR passed by Co.

b) Resolution specifies no. of shares, CMP, consideration if any, & class or classes of directors or employees to whom such equity shares are to be issued.

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c) omitted

d) where equity shares of Co. are listed on a recognized stock exchange, SES are issued per SEBI regulations & if listed, as per prescribed rules.

e) Further, rights, limitations, restrictions & provisions of SES holders same as equity shareholders.

V. REDUCTION OF CAPITAL

Accumulated business losses, assets of reduced or doubtful value or paid-up capital in excess of requirements of Co. or surplus capital which can't be employed gainfully, require corrective measures to keep financial health of Co. in a reasonably well position. Accordingly, Co. may find necessary to reduce its share capital.

Sec 66 deals with reduction of share capital. Auditor needs to examine whether company has followed requirements of Sec 66.

Auditor shall undertake the following audit procedures: MTP Oct'20

a) Verify the meeting of shareholders to pass SR was properly convened & proposal was circularized in advance to all shareholders

b) Verify that AOA authorizes reduction of capital

c) Verify that MOA of Co. has been suitably altered.

d) Examine that there has been no default w.r.t repayment of deposits accepted by Co. or payment of interest on such deposits. Reduction of capital shall not be affected if such default exists.

e) Examine order of Tribunal confirming reduction & verify that copy of order & minutes registered & filed with ROC

f) Check Registrar's Certificate as regards to reduction of capital

g) Vouch a/c entries recorded to reduce capital & write down assets w.r.t resolution of shareholders & other documentary evidence; also check whether presentation as per Schedule III, Part I

h) Confirm whether revaluation of assets properly disclosed in B.S.

i) Co. may reduce capital by reduction in unpaid capital or cancellation of lost capital or paying off excess paid up capital. Verify adjustment made in members' a/cs in Register of Members & confirm that either paid-up amount shown on old share certificates been altered or new certificates issued in lieu of old, & old ones been cancelled

j) Confirm that words "and reduced", if required by Tribunal order been added to nae of Co. in BS.

k) Check if Co. complied with all T&Cs imposed by tribunal while confirming reduction of SC.

Exemption to Buy-Back: This section doesn't apply to buyback of own securities u/s 68.

VI. DISCLOSURES

For each class of share capital (different classes of preference shares to be treated separately):

a) No. & amount of shares authorized

b) No. of shares issued, subscribed & fully paid, & subscribed but not fully paid

c) par value per share

d) a reconciliation of no. of shares o/s at beginning & end of reporting period

e) rights, preferences & restrictions attaching to each class of shares including restrictions on distribution of dividends & repayment of capital

f) shares in respect of each class in Co. held by its holding Co. or ultimate holding Co. in aggregate

g) shares in Co. held by each shareholder holding more that 5% shares specifying no. of shares held

h) shares reserved for issue under options & contracts/commitments for sale of shares/ disinvestment, including terms & amounts

i) for period of 5 years immediately preceding BS date:

A. Aggregate no. and class of shares allotted as fully paid – up pursuant to contract(s) without payment recd. in cash.

B. Aggregate no. and class of shares allotted as fully paid – up by way of bonus shares.

C. Aggregate no. and class of shares bought back.

j) terms of any securities convertible into equity/preference shares issued along with earliest date of conversion in descending order starting from farthest such date

k) calls unpaid (showing aggregate value of calls unpaid by Directors and officers)

l) forfeited shares (amount originally paid-up)

m) Co. shall disclose Shareholding of Promoters* as below : Nov '22

Shares held by promoters at end of year				% change during yr**	
S.No	Promoter Name	No. of shares	% of total shares**		

**Details shall be given separately for each class of shares

***Percentage change computed w.r.t no. at beginning of year or if issued during year for 1st time then w.r.t the date of issue.

Where securities issued for a specific purpose, whole or part of amount not used for the specific purpose at B.S. date, indicate by way of note how such unutilized amounts have been used or invested.

RESERVES AND SURPLUS

RESERVES & SURPLUS

I. WHAT IS RESERVE? | II. AUDIT PROCEDURES | III. DISCLOSURES

I. WHAT IS RESERVE?

Reserves are amounts appropriated out of profits that are **NOT** intended

- to meet any liability,
- contingency
- commitment or
- diminution in value of assets known to exist at BS Date.

Reserves can be segregated as revenue or capital reserves.

Revenue reserves represent **profits** that are available for distribution to shareholders or below purposes such as:

- to supplement divisible profits in lean years,
- to finance an extension of business,
- to augment working capital of business or
- to generally strengthen Co's financial position.

Capital Reserve represents a reserve not free for distribution. They can be utilized only for certain **limited** purposes. *Eg. Securities premium.* Capital redemption reserve, revaluation reserve on revaluation of assets.

Note: If a Co. appropriates revenue profit for being credited to asset replacement reserve to be used for a capital purpose, such a reserve shall also be in nature of a capital reserve.

II. AUDIT PROCEDURES

Existence: Trace & tally opening balance of reserves and surplus to PY audited FS.

Completeness & Valuation:

- Trace movement to surplus/deficit as per Statement of P&L for year under audit.
- Movement should be traced in Statement of Changes in Equity.
- Verify BOD resolution regarding recommendation of dividend, resolution passed by shareholders declaring dividend.

Note: As per AS-4(Revised) or IND AS 10, **if equity dividends proposed or declared after BS date**, do not recognize those dividends as a liability as at BS date. However, disclose amount of dividends proposed or declared after BS date, but before FS were approved for issue.

- Securities Premium: Obtain & verify BOD resolution passed by BOD for issue of shares at premium.
- Utilisation of securities premium a/c could be done only for limited purposes; auditor needs to ensure the same. (Sec 52 of Cos Act 2013)

III. DISCLOSURES

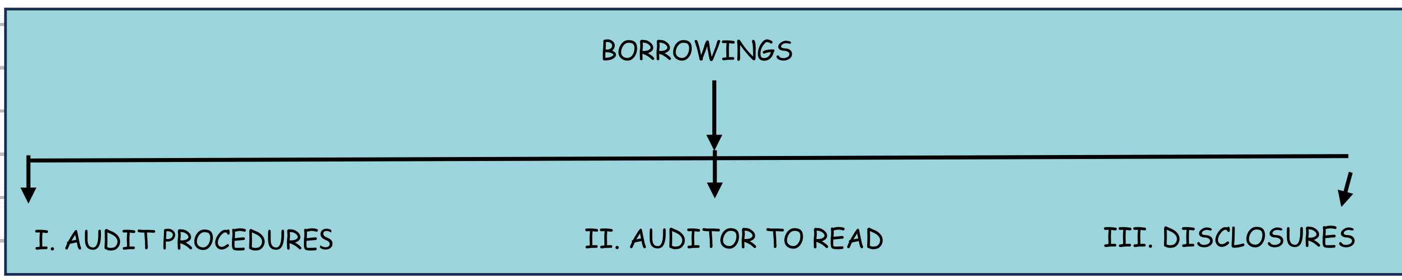
a) Reserves and Surplus shall be classified as:

i. Capital Reserves, Capital Redemption Reserve, Securities Premium, Debenture Redemption Reserve, Revaluation Reserve, Share Options Outstanding a/c, Other Reserves

ii. Surplus i.e., balance in Statement of Profit & Loss disclosing allocations & appropriations such as dividend, bonus shares & transfer to/from reserves, etc.

A reserve specifically represented by earmarked investments shall be termed as a 'fund'.

BORROWINGS



I. AUDIT PROCEDURES

I. BORROWINGS – AUDIT PROCEDURES	
All borrowings on BS represent valid claims by banks or other 3rd parties **(EXISTENCE)**	All borrowings have been accounted for in books of Co. in a timely basis. **(COMPLETENESS)**
1.Review board minutes for approval of lending agreements. Ensure loan agreements or bond issuances were authorized. 2.Agree details of loans recorded (intt rate, nature & repayment terms) to loan agreement. 3.Roll out & obtain independent balance confirmations (SA 505) for all borrowings from lender. 4.Agree details of leases & hire purchase creditors recorded to underlying contracts/agreements. 5.In case of debentures, examine trust deed for terms & dates of redemption, borrowing restrictions & compliance with covenants. 6.When debt is retired, ensure discharge is received on assets securing debt. 7.Obtain WR that all liabilities recorded represent a valid claim by lenders (SA 580).	1. Obtain schedule of ST&LT borrowings (including debts o/s at end of PY & any new debt or renewal of debt) showing beginning & ending balances & borrowings taken & repaid during the year & perform following: a) Consider evidence of additional debt obtained by examining minutes of BOD, significant contracts, confirmations b) Trace closing balances as per schedules to GL. 2. Review subsequent transactions after period end to check if there are unrecorded liabilities at year end & transactions are recorded in correct period. (Eg: Fresh loan taken near BS date. 3. **Direct confirmation procedures** Roll out & obtain independent balance confirmations for all borrowings from lender (banks/ FI etc.) perform: - a) Ask for all relevant info. Related to debt & intt. Balances (e.g., applicable intt. Rates, due dates, collateral & security interests). b) Send reminders for non-replies. c) Compare balances as per confirmations to books of a/c. Ask for reconciliations, if any differences & test supporting documents for reconciling items on test check basis.

Liability is recorded at **correct amount**. **(VALUATION)**

- Determine that a/c policies & methods & methods are appropriate & applied consistently.
- Agree loan balance & loan payables to loan agreement,
- Recompute intt & discount or premium on redemption, if any.
- Check computation of amortization of premium or discount, if any.
- For foreign currency loans, check closing exchange rate(s) used & verify restatements of foreign currency balances o/s at year end. (As per AS 11)

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II. AUDITOR TO READ

Read provisions in loan & debt agreements and perform following:

a) Test Compliance with loan covenants & other significant provisions of agreements.
b) If any provisions with which entity is NOT in compliance, determine if debt should be classified as current.
c) Examine due dates on loans for proper classification between long-term & short-term.
d) Where instalments of LT loans due within next 12 months have been disclosed in FS
e) Examine debt agreements for restrictive covenants. Review RC & provisions vrt. default & ensure discl. in FS.
f) Examine important terms in loan agreements & documents
g) If value of security falls < amount of loan o/s, whether loan is secured only to extent of MV of security.
h) Examine hire purchase agreements for purchase of assets by entity
i) Review borrowings from related parties & ensure compliance with AS18 or Ind AS24.
j) Verify whether liabilities towards bank in respect of bills discounted, bills negotiated, cheques discounted, etc. are correctly reflected & disclosed in FS.
k) Also verify amount borrowed is within borrowing powers laid down by AOA & MOA.
l) Where entity has accepted deposits, examine whether directives issued by RBI complied with.

III. DISCLOSURES

Long-Term Borrowings:

i. Long-term borrowings shall be classified as: Bonds/debentures
a. Term loans: from banks., from other parties.
b. Deferred payment liabilities
c. Deposits
d. Loans and advances from related parties
e. long term maturities of finance lease obligations
f. other loans and advances (specify nature)

Other Long-term Liabilities:

Other Long-term Liabilities shall be classified as:
a. Trade Payables;
b. Others

Short Term Borrowings

i. Short-term borrowings shall be classified as:
   a. Loans repayable on demand; from banks, from other parties.
   b. Loans and advances from RPs
   c. Deposits
   d. Other loans and advances (specify nature).

ii. Borrowings shall further be sub-classified as secured and unsecured.

iii. Loans have been guaranteed by directors or others, agg. amt of such loans under each head shall be disclosed.

iv. Period & amount of default as on B.S. date in repayment of loans and interest, shall be specified separately in each case.

v. Current maturities of Long-term borrowings shall be disclosed separately.

TRADE PAYABLES & OTHER CURRENT LIABILITIES

TRADE PAYABLES

I. AUDIT PROCEDURE

II. DISCLOSURES

I. AUDIT PROCEDURES

Existence

1. Check whether controls are in place to ensure that any purchase/expense invoice NOT recorded more than once
2. Obtain a/c payable ageing report & trace its balances to GL.
3. **Perform Direct Confirmation Procedure [SA 505]**

- **Consent**: Employs direct confirmation procedure with consent of entity.
- **Date:** Trade crs may be requested to confirm bal either at BS date or as at any other date close to BS date..
- **Form** of requesting confirmation may be either
  - Form **with balance**
  - Form **with no balance**.
- **Method** of selection of creditors should not be revealed to the Co.
- Entity should be asked to investigate & reconcile the discrepancies.

4. Where **no reply** is received perform additional testing regarding the balances. This testing could include
   - o Testing of subsequent payments for trade payables but no replies received
   - o Agreeing details of respective balance to underlying vendor invoices
   - o Preparing a detailed analysis of balance, ensuring it consists of identifiable transactions & confirming that purchases/ expense transactions actually occurred(examination in depth)
5. If there are any related party payables, review whether they were properly authorized & value of such transactions were reasonable & at arm's length.
6. Review a trend line of purchases/expenses & a/c payable, or a comparison of two overtime, to see if there are any unusual trends. Make enquiries about reasons for changes in trends from management

Completeness

Trade payables and Liabilities Balances that was supposed to be recorded have been recognized in FS.

1. Auditor needs to perform following cut off procedures:
   - For the last 5 invoices included in the trade payables; the goods should have been received/ risk and rewards of ownership in goods should be in favour of the entity.
   - All goods received prior to period/year end should have been booked in the form of purchases & included in trade creditors.
2. Test purchases/expenses on a sample basis selecting same from a/c payable ledgers.
3. Match purchase invoice dates to gate entry(inward) dates to check whether pur recorded in correct a/c period.
4. Review subsequent expense vouchers.
5. For advance received from customers/revenue received in advance, obtain customer wise listing along with its ageing and nature.
6. In relation to statutory dues liability like withholding tax (TDS) payable, GST payable, PF & ESI payable, etc, prepare a reasonability w.r.t sales/purchases/employee benefit expenses.

   Example: GST liability, PF liability, challans for deposits. He shall prepare a complete list of all statutory dues & consider his reporting requirements under CARO, 2020.

Valuation:

1. Review process followed by Co to identify if any old creditor balance/liability needs to be written back.
2. Obtain ageing of payable balances, & list of vendors with whom Co. has disputes and claims from customers, under litigation & compare with PY.
3. Check write backs in liability balances assessed as no longer payable approved by senior management (CEO/MD)
4. Check restatement of foreign currency trade payables done properly as per AS 11.

II. DISCLOSURES

Details relating to micro and small enterprises:

1. Principal amount and interest due thereon (to be shown separately) remaining unpaid to any supplier
2. Amount of interest paid by buyer in terms of sec 16 of MSME Development Act.2006, along with amount of payment made to supplier beyond appointed day during each a/c year.
3. Amount of interest due and payable for period of delay in making payment (which have been paid but beyond the appointed day during the year) but without adding interest specified under MSME Development Act,2006
4. Amount of interest accrued and remaining unpaid at end of each a/c year.

Trade Payables Ageing Schedule

Particulars	O/s for following periods from due date of payment		Total
< 1 year	1-2 years	2-3 years	> 3 years
i) MSME			
ii) Others			
iii) Disputed dues-MSME			
iv) Disputed dues-Others			

similar info shall be given where no due date of payment is specified in that case disclosure shall be from date of transaction.

Unbilled dues shall be disclosed separately

Other current liabilities

Whether amount disclosed under OCL are classified as below:

1. Current maturities of finance lease obligations
2. Interest accrued but no due on borrowings
3. Interest accrued and due on borrowings
4. Income received in advance
5. Unpaid dividends
6. Application money received for allotment of securities & due for refund, and interest accrued thereon.
7. Unpaid matured deposits/debentures and interest accrued thereon
8. Unpaid matured debentures and interest accrued thereon Others (specify nature)

PROVISIONS & CONTINGENT LIABILITIES

BORROWINGS

I. PROVISION & CONTINGEMENT LIABILITY

II. AUDIT PROCEDURE

III. DISCLOSURES

I. WHAT IS PROVISION & CONTINGEMENT LIABILITY ?

Provision is a liability which can be measured only by using a substantial degree of estimation. A provision is recognized when:

- An entity has a present obligation (legal or constructive) as a result of past event
- Probable that & outflow of resources embodying economic benefits ll be required to settle the obligation
- Reliable estimate can be made of amount of obligation
- If above conditions are not met, no provision is recognized

Example: Provision may include provision for litigation, provision for warranties, etc.

Contingent liability is:

- A possible obligation that arises from past events and whose existence will be confirmed only by occurrence or non-occurrence of one or more uncertain future events not wholly within the control of entity; or
- A present obligation that arises from past events but is not recognized because:
  - It is not probable that an outflow of resources embodying economic benefits will be required to settle the obligations or
  - The amount of the obligation cannot be measured with sufficient reliability

II. AUDIT PROCEDURE

1. Obtain a list of all provisions and compare with balances in the ledger
2. Inspect underlying agreements like agreement with customers to assess warranty commitments, any legal & other claims on the entity i.e. Litigations
3. Obtain underlying working and basis for each of the provisions made, from management & verify whether same is complete and accurate.
4. Wherever required, obtain experts' report, calculation & underlying working for provision amount
5. Obtain WR as per SA 580

Examples: For warranty involving complex calculations, entities get that valued through an actuary. Request management to share actuarial valuation report

As per SA 500, when using work of a management expert, audit evidence should include: Sep'24

1. Evaluate competence, capabilities and objectivity of that expert:
   - Whether expert is employed by entity or outside party
   - Whether expert is independent in respect of the entity
   - Auditor's previous experience of the work of expert
   - Knowledge of expert, his qualification, membership of professional body or industry association
2. Obtain an understanding of work of that expert:
   - Whether auditor has expertise to evaluate work of expert
   - Evaluate assumptions and methods used by the management
   - Evaluate nature of internal or external data used by expert
3. Evaluate appropriateness of his work as audit evidence for the relevant assertion
   - Relevance & reasonableness of expert findings or conclusions
   - Evaluating relevance, completeness and accuracy of the source data used by the expert

III DISCLOSURES

Long term provisions

Amount shall be classified as:

a) Provision for employee benefit

b) Others (specify nature)

Short term provisions

Amount shall be classified as:

a) Provision for employee benefits

b) Others (specify nature)

Contingent liabilities shall be classified as

a) Claims against the company not acknowledged as debt

b) Guarantees

c) Other money for which the Co. is contingently liable

Commitments shall be classified as:

a) Estimated amount of contracts remaining to be executed on Capital a/c and not provided for

b) Uncalled liability on shares and other investments partly paid

c) Other commitments (specify nature)

In terms of AS 29, ensure following disclosures are made:

- For each class of provision, disclose [movement]:
  - Carrying amount at beginning & end of period
  - Additional provisions made in period, including increases to existing provisions
  - Amounts used (i.e. incurred and charged against provisions) during period
  - Unused amounts reversed during period
- Disclose following for each class of provision [details of nature & timing of outflows]:
  - Brief description of nature of obligation and expected timing of outflows of economic benefits.
  - Indication of uncertainties about amount or timing of outflows. Where necessary, disclose major assumptions concerning future events &
  - Amount of any expected reimbursement, stating amount of any asset that has been recognised for that expected reimbursement.
- Unless possibility of outflow is remote, disclose for each class of contingent liability at BS date
  - A brief description of nature of contingent liability & where practicable
  - Estimate of its financial effect
  - Indication of uncertainties relating to any outflow &
  - Possibility of any reimbursement MTP Mar'21

PROPERTY, PLANT AND EQUIPMENT

\PROPERTY, PLANT & EQUIPMENT

- I. RECOGNITION CRITERIA
- II. ELEMENTS OF COST
- III. COST THAT ARE NOT PPE
- IV. AUDIT PROCEDURE
- V. DISCLOSURES

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I. RECOGNITION CRITERIA FOR PPE (COST OF AN ITEM OF AN ITEM OF PPE SHOULD BE RECOGNIZED AS ASSET ONLY IF)

1. It is probable that future economic benefits associated with item will flow to enterprise, and
2. Cost of item can be measured reliably.

These costs include costs incurred:

a) initially to acquire or construct PPE &

b) subsequently to add to, replace part of, or service it.

Measurement at Recognition: Item of PPE that qualifies for recognition as asset should be measured at its cost

II. ELEMENTS OF COST

Cost of PPE comprises:

a) its purchase price, including import duties & non-refundable purchase taxes, after deducting trade discounts and rebates

b) any cost directly attributable to bringing asset to location and condition

c) initial estimate of cost of dismantling, removing the item & restoring the site on which it is located, referred to as decommissioning, restoration & similar liabilities,

Examples of directly attributable costs are:

a) Costs of employee benefits (as defined in AS 15, Employee Benefits) arising directly from construction or acquisition of item of PPE

b) Cost of site preparation

c) Initial delivery and handling costs

d) Installation and assembly costs

e) Cost of testing whether asset is functioning properly, after deducting net proceeds from selling any items produced while bringing asset to that location and condition (example: Samples produced when testing equipment) &

f) Professional fees

III. EXAMPLES OF COSTS THAT ARE NOT COST OF PPE ARE: [ICAI SM + MAY'24]

Examples of costs that are not cost of PPE are: [ICAI SM + May'24]

a) Cost of opening a new facility or business such as inauguration cost

b) Cost of introducing a new product or service (including cost of advertising and promotional activities)

c) Cost of conducting business in a new location or with a new class of customers (including staff training costs)

d) Administration and other general overhead costs

IV. AUDIT PROCEDURES

Existence:

1. Review entities plan for physical verification of PPE
2. Evidence of appropriate supervision of those performing physical verification of PPE should be examined
3. Obtain PPE physical verification report backed by working sheets from entity and perform following procedures:
   - Assess if all items are properly tagged & carry identification marks
   - Reconciliation of items physically verified with fixed asset register maintained by entity.
   - Verify discrepancies based on physical verification & manner in which discrepancies dealt in books & FS

For e.g., Any identified shortages/assets not in working condition & /or active use should be accounted as deletions, post approvals by entities mgmt & dep should cease to be charged after date of deletion

Completeness:

[Additions to PPE during period under audit have been recorded in FS & don't include any PPE that belong to 3rd parties but does include PPE owned and controlled by entity although lying with a 3rd party]

1. Verify movement in PPE schedule [asset class-wise like building, plant & machinery, etc] compiled by management i.e. opening balances + additions during period -deletions during period = closing balance. Tally closing balance to entities books of accounts
2. Check arithmetical accuracy of movement in PPE schedule
3. Tally opening balances to PY audited FS
4. For additions obtain listings of all additions from management and perform following procedures:
   - For all material additions verify if expenditure meets criteria of PPE as per AS 10. These costs include costs incurred initially to acquire or construct PPE & subsequently to add, replace part of, or service it.
   - Items such as spare parts, standby equipment & servicing equipment are recognised as per AS 10 when they meet the definition of PPE.
   - Test purchase invoice, installation certificate or report or other similar documentation maintained by entity to verify date of addition, for all additions, samples of PPE
   - Verify PPE additions have been approved by authorised personnel.
5. Verify proper internal process and procedures like inviting competitive quotations/floating tenders, etc.
6. In relation to deletions to PPE,
   - Understand from management reason and rational for deletion
   - Obtain management approval and discard note authorising disposal of asset from active use
   - Verify process followed for sale of discarded PPE
   - Verify that management has accurately recorded the deletion of PPE

Valuation: MTP Sep'24

Value of fixed assets or PPE depreciates due to efflux of time, use and obsolescence.

P&L would not be correctly ascertained & values of PPE would be shown at higher amounts.

The auditor should:

1. Verify that entity has charged depreciation on all items of PPE unless an item is non-dep like free hold land.

2. Assess that depreciation method reflects pattern in which asset's future economic benefits to be consumed by entity. E.g. Straight-line method, diminishing value method, unit of production method, as applicable
3. Auditor should also verify whether management has done an impairment assessment to determine whether an item of PPE is impaired as per AS 28-impairment of assets

Rights: MTP Sep'24

1. Verify that all PPE purchase invoices are in the name of the entity
2. For all additions to L&B , check conveyance deed/sale deed to verify entity is a legal and valid owner or not
3. Verify original title deeds for all immovable properties held as at BS date.
4. In case entity has given such immovable property as security for any borrowings & original title deeds are not available with entity, request entity's management for obtaining confirmation from respective lenders that they are holding original title deeds of immovable property as security
5. Also verify register of charges, available with entity to assess any charge created against PPE

V. DISCLOSURES

i. Classification shall be given as:
   a. Land , Buildings, Plant & equipment, Furniture & fixtures, Vehicles, Office equipment, Others

ii. Assets under lease shall be separately specified under each class of asset

iii. A reconciliation of gross and net carrying amounts of each class of asset at beginning & end of reporting period showing additions, disposals, acquisitions through business combinations, amount of change due to revaluation (if changes 10% or more in aggregate of net carrying value of each class of PPE) & other adjustments & related depreciation & impairment losses/reversals shall be disclosed separately.

iv. Where sums have been written off on a reduction of capital or revaluation of assets or where sums have been added on revaluation of assets, every subsequent BS shall show reduced or increased figures as applicable & shall by way of a note also show amount of reduction or increase as applicable together with date thereof for first five years subsequent to date of such reduction or increase.

INTANGIBLE ASSETS (COMPRISING GOODWILL, BRAND/TRADE MARK, COMPUTER SOFTWARE, ETC.)

INTANGIBLE ASSETS

I. WHAT IS INTANGIBLE ASSET ?

II. AUDIT PROCEDURE

III. DISCLOSURES

I. WHAT IS INTANGIBLE ASSET?

It is an identifiable non-monetary asset,
- Without physical substance,
- Held for use in the production or supply of goods or services, for rental or administrative purposes

Notes:
- As per AS 26, internally generated goodwill should not be recognised as an asset
- Some IAs may be contained in /on a physical substance such as compact disc (for computer software), legal documentation (for license or patent) or film (for motion pictures).

II. AUDIT PROCEDURES

Existence:

1. Since IA is identifiable non-monetary asset, without physical substance
   - IA is in active in production or supply of goods/ for rental/for administrative purposes
- Example: For verifying existence of software, verify whether such software is in active use by entity & for purpose
2. In case IA not in active use, deletion recorded in books of accounts post approval by entities management & amortization charge cease beyond date of deletion

Completeness MTP Jan'25+ Sep'22

1. Verify movement in IAs schedule i.e. opening + addition – deletions = closing.
2. Check arithmetical accuracy of movement in IA schedule.

For Additions:

3. For all material additions verify whether such expenditure needs recognition criteria as per AS 26
4. Ensure that no intangible asset arising from research is recognised.
5. Check certificate or report maintained by entity to verify date of use of IA
6. Verify whether additions (acquisitions) are approved by appropriate entities personnel
7. Verify whether proper internal processes like inviting competitive quotations/ proper tenders, etc.

For Deletions:

- Understand from management reason and rationale for deletion & manner of disposal
- Obtain management approval & disposal note authorising disposal of asset from active use,
- Verify process for sale of discarded asset, example: inviting quotes, tender & calculation of sales proceeds

Valuation July'21

Value of IAs may diminish due to efflux of time, use and/or obsolescence. Diminution of value is cost to entity for earning revenue during the given period. Unless amortization is charged to P&L account, P&L would not be correctly ascertained & values of IA would be shown at higher amounts.

Auditor should:

1. Verify that entity has charged amortization on all IAs
2. Verify that amortization method reflects pattern in which asset's future economic benefits is expected to be consumed by the entity

3. Also verify whether management has done impairment assessment to determine whether IA is impaired. Verify whether entity has applied AS 28

Rights

In addition to procedures for verifying completeness of additions, also verify all expense invoices/ purchase contracts are in name of entity that entitles legal title of ownership to entity

III. DISCLOSURES

i. Classification should be given as:

a. Goodwill, Brand/trademark, Computer software, Mastheads and publishing title, Mining rights, Copy rights, & patents & other intellectual property rights , services and operating rights, Recipes, formulae, models, designs and prototypes, Licenses and franchise, Others.

ii. A reconciliation of gross and net carrying amounts of each class of asset at beginning & end of reporting period showing additions, disposals, acquisitions through business combinations, amount of change due to revaluation (if changes 10% or more in aggregate of net carrying value of each class of IA) & other adjustments & related depreciation & impairment losses/reversals shall be disclosed separately. [SAME AS PPE]

iii. Where sums have been written off on a reduction of capital or revaluation of assets or where sums have been added on revaluation of assets, every subsequent BS shall show reduced or increased figures as applicable & shall by way of a note also show amount of reduction or increase as applicable together with date thereof for first five years subsequent to date of such reduction or increase. [SAME AS PPE]

TRADE RECEIVABLES

TRADE RECEIVABLES

I. TOC FOR IC OVER SALES

II. AUDIT PROCEDURES

III. DISCLOSURES FOR DEBTORS

I. TOC FOR IC OVER SALES

It is important to carry out test of controls for checking effectiveness of internal control over sales as a part of the debtors' audit procedure. What points to consider?

- Only Bonafide sales leads to TR
- All such sales are made to approved customers
- All such sales are properly recorded in BoA
- Once recorded debtors can be settled only by receipt of cash or on authority of a responsible official.

Hello Nanbas & Nanbis

- Segregation of duties at every point in sales transaction (accounting for debtors, collecting payments, sending reminders, etc.)
- Debtors are collected on time

  In case debtors are not collected in time, sending reminders and taking legal action if required

II. AUDIT PROCEDURES

Existence:

1. Check whether controls are in place to ensure that invoices can't be recorded more than once .
2. Ask for period end accounts receivable ageing report & trace balance as per report to GL.
3. Check whether realisation is recorded invoice-wise or not.
4. If not, check that money received from debtors is adjusted chronologically invoice-wise and on FIFO basis.
5. If any large balance is due for long time, ask for reasons and justifications
6. Perform **Direct Confirmation Procedures [DCP] as per SA 505 (same as TP)**
7. Where no reply is received perform alternate procedures regarding balances. This could include:
   - Agreeing balance to cash received subsequently
   - Preparing a detailed analysis of balance, ensuring it consists of identifiable transactions & confirming that these revenue transactions actually occurred. (Examination in depth for those balances)
8. If any related party receivables, review them for collectability & whether they were properly authorised & value of such transactions were reasonable & at arms length
9. Check that receivables for other than sales or services are not included in the list.
10. Review trend line of sales and accounts receivable, or comparison of two over time i.e. perform analytical procedures.

Completeness MTP Sep'24:

All TR balances that were supposed to be recorded have been recognised in FS.

1. **Cut off procedures Nov'2022**

   Auditor needs to satisfy himself of cutoffs. Without a cut off, sales could be under stated or over stated.
   - For invoices issued during last few days (last five days of reporting year) i.e. cut off date
   - Ensure that all goods despatched prior to period/ year end have been invoiced & included in debtors on a test check basis
   - Ensure that no goods despatched after year end have been invoiced
2. **Ageing report:** Test invoices listed in TR report. Select few invoices from TR ageing report and compare to supporting documentation to see if they were build with correct amount, customers, and dates
3. **Shipment:** Match invoices to shipping/despatch log.
4. **Bill & Hold sales:** Assess Bill & Hold sales. If there is a situation where Co. is building customers for sales despite still retaining goods on site (known as Bill & Hold), examine supporting documentation to determine whether sale has actually taken place or not

5. **Receiving Log:** Review receiving log to see if Co. has recorded an inordinately large amounts of customer returns after audit period, which would suggest that Co. may have shipped more goods near period end than what customers had authorised, to inflate profits
6. **Discounts/ Incentives:** Review process of giving discounts/incentives & whether given as per Co. s policy/general industry trends.
7. **Credit Memos:** Review credit memos on a sample basis, issued during audit period to see if they were properly authorised & issued in correct period.

Valuation: MTP Sep'24

1. Review process of Co. to derive allowance for doubtful accounts.
2. Obtain Ageing Report of accounts receivable (both debit and credit balance)
3. Also obtain list of debtors under litigation and compare with PY
4. Scrutinize analysis and identify those debtors which appear doubtful;
5. Check if provisions made at appropriate rates considering recoverability of amounts due
6. Prepare schedule of movements of bad debts -provision accounts & debts written
7. Check that write offs of receivable balances have been approved by appropriate authority i.e. BoDs

III. DISCLOSURES

a) Ageing schedule MTP May'24

Particulars	Os for foll. periods from due dt of paymt. #					Amt(Rs)
	< 6m	6m-1yr	1-2yrs	2-3yrs	>3yrs	
Undisputed T/R-considered good						
Undisputed T/R-considered doubtful						
Disputed T/R-considered good						
Disputed T/R-considered doubtful						

similar info shall be given where no due date of payment is specified, in that case, disclosure shall be from date of transaction. Unbuild dues shall be disclosed separately.

b) Trade Receivables shall be sub classified as:
- Secured, considered good, Unsecured, considered good, Doubtful

c) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately

d) Debts due by
- Directors or other officers of Co. or any of them either severally or jointly with any other person or
- Firms or private companies respectively in which any director is a partner/director/member

LOANS AND ADVANCES & OTHER CURRENT ASSETS

LOANS AND ADVANCES & OTHER CURRENT ASSETS

I. INCLUDES?

II. AUDIT PROCEDURES

III. DISCLOSURES

I. L & A INCLUDES

L&As include L&As to related parties, security deposits, capital advances, amounts recoverable in cash or in kind or for value to be received. Example: rates, taxes and insurance paid in advance or pre-paid.

II. AUDIT PROCEDURES

Existence:

Direct confirmation procedures, similar to a/c receivable with only difference that in addition to principal amount, interest receivable, if any, as per agreed terms between parties, may also be included as part of balance confirmation

Completeness:

1. Obtain list of all advances and other current assets and compare balance with ledger
2. Verify loan agreements and acknowledgements of parties in respect of outstanding loans. L
3. Inspect the minutes of meeting of BoD to confirm if all material L&A were approved by BoD
4. Ascertain if loans are recovered regularly as per agreed installments
5. If any related party L&A review whether authorised & value of such transactions are reasonable & at ALP.
6. In relation to balances with statutory authority like GST input credit prepare a reasonability w.r.t purchases/expenses by applying applicable rate to purchases/expenses & in case of variance with asset recorded, reasons should be requested from entity

Valuation: MTP May'20

1. Assess allowance for doubtful accounts.
2. Review process followed by Co. to derive allowance for doubtful accounts.
3. Obtain ageing report of L&As
4. Also, obtain list of L&As under litigation & compare with PY
5. Scrutinise the analysis & identify those L&As that appear doubtful& discuss with management about reasons
6. Assess bad L&As write offs. Prepare schedule for movements on bad loans/advances
7. Check that write offs & recoverable balances have been approved by authorised & appropriate senior authority
8. Check restatement of foreign currency L&As/OCA are done properly as per AS 11

III. DISCLOSURES

Long term Loans and advances:

i. Long term L&As shall be classified as:
   - **Capital advances** , L&As to related parties (giving details thereof) ,Other L&As (specify nature)

ii. The above shall also be separately sub classified as:
   - Secured, considered good , Unsecured, considered good , Doubtful

iii. Allowance for bad and doubtful L&As shall be disclosed under relevant heads separately

iv. L&As due by

- Directors or other officers of the Co. or any of them either severally or jointly with any other persons or
- Amounts due by firms or private Cos. Respectively in which any director is a partner or a director or a member should be separately stated

Short Term Loans and advances:

i. Short term L&As shall be classified as:

- L&As to related parties (giving details thereof)
- Other L&As (specify nature)

ii. The above shall also be separately sub classified as:

- Secured, considered good , Unsecured, considered good , Doubtful

iii. Allowance for bad and doubtful L&As shall be disclosed under relevant heads separately

To be disclosed as additional regulatory information

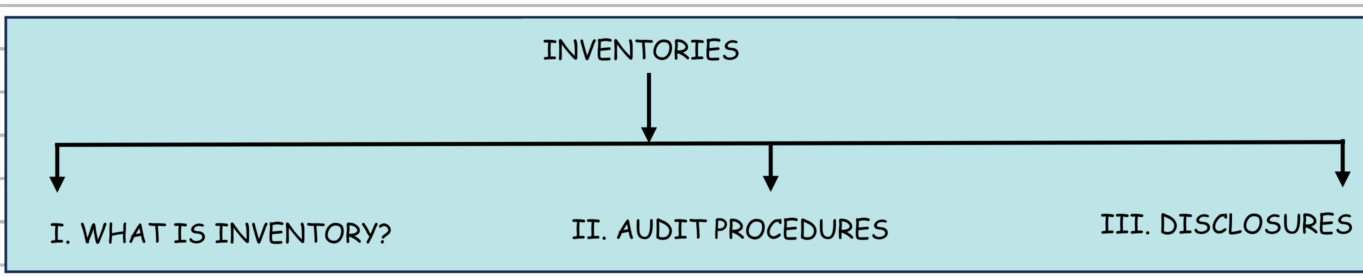
L&As in nature of loans granted to promoters, directors, KMPs & related parties either severally or jointly with any other person, debtor: ICAI SM+May'24

a. Repayable on demand or

b. Without specifying any terms or period of repayment

Type of borrower	Amt of loan/advance in nature of loan o/s	Percentage to total loans &advances
Promoters		
Directors		
KMPs		
Related Parties		

INVENTORIES



I. WHAT IS INVENTORY?

Inventories are assets

a. Held for sale in ordinary course of business

b. In the process of production for such sale or

c. In form of materials or supplies to be consumed in production process or in rendering of service

As per AS 2, valuation of inventory, inventory is valued at lower of cost or net realisable value.

II. AUDIT PROCEDURES

Existence:

1. Review entities plan for performing inventory count
2. Ensure that consigned goods have been segregated
3. Auditor should participate in the inventory count with management
4. Test counts of inventory by the auditor should include:
   - Observing employees are adhering to the agreed plan
   - Assuring that there is appropriate supervision on the count procedures
   - Assuring that all items are properly tagged
   - Observing that proper amounts are shown on tags
   - Determining that tags and summary sheets are controlled and reconciled
   - If any discrepancy noted in the reconciliation of test counts with tags and summary sheets
   - Staying alert all times and being cautious about empty boxes etc. and obsolete items
   - Performing cut off procedure by documenting last 5 to 10 receiving reports
   - Ensuring exclusion of third-party stock and damaged or obsolete stock
5. When entity uses periodic system for inventory count, it should be undertaken at end of period. If entity uses perpetual system with proper & adequate records, inventory may be counted at interim dates
6. Confirm or investigate any inventory of entity lying with third party

Completeness: MTP Sep'24

1. Only inventories held by entity have been recorded in FS & don't include any inventory that belong to 3rd parties but does include inventory owned by entity & lying with third party
2. Perform analytical procedures (comparison test with industry averages, budgets, prior years, trend analysis, etc.) SA 520
3. Examine non-financial information related to inventory such as weights & other measurements
4. Perform purchase & sales cut off procedures.
5. Verify the clerical & arithmetical accuracy of inventory listings
6. Reconcile physical inventory amounts with perpetual records. Reconcile inventories of client but held with 3rd parties like transporters, warehouses, port authority.

Rights: ICAI SM +MTP Nov'23

1. Entity has valid legal ownership rights over inventories held by entity & recorded in FS
2. Vouch recorded purchases to underlying documentation
3. Examine invoices for evidence of ownership i.e. invoice shall have the name of the client
4. Review material purchase commitment agreement
5. Evaluate the consigned goods
6. Review consignment agreement
7. Examine client correspondence, sales & receivables records, purchase document
8. Determine existence of collateral agreements
9. Auditor shall obtain confirmation for significant items of inventory

Valuation:

1. Depending on how business operates, management may value inventory using FIFO or weighted average basis.
2. For raw materials and consumables:
   - Ascertain what elements of cost are included e.g. Carriage inward, non-refundable duties, etc.
   - If standard costs are used enquire into basis of standards.
   - Test check cost prices with purchase invoices received in months prior to counting
   - Followup valuation of damaged or obsolete inventory noted physical counting to establish a realistic NRV
3. **For WIP** MTP Sep'24+Jan'21
   a. Ascertain how various stages of production/value addition is measured & in case of estimates, understand the basis for such estimates
   b. Ascertain what elements of costs are included. If overheads are included, ascertain basis on which they are included & compare such basis with available costing & financial information maintained by entity
   c. Ensure that material cost exclude any abnormal wastage factors
4. For Finished Goods & Goods for Resale MTP May'20
   - Enquire what costs are included, how are they established & ensure overheads included based on normal costs & reasonable in relation to info in FS
   - Ensure inventories valued at NRV if lower than cost.
   - Follow up for items that are obsolete, damaged, slow moving & ascertain possible realisable value of such items. Carefully examine valuation of obsolete & damaged inventory.
5. Compare recorded cost with replacement cost
6. Examine vendor price list to determine if recorded cost is less than current prices
7. Calculate inventory turnover ratio.
8. In manufacturing environments, test overhead allocation rate & ensure only direct labour, direct material and overheads have been included
9. Verify correct application of lower of cost or NRV principles

III. DISCLOSURES

1) Whether inventory has been classified as
2) Raw materials, WIP, Finished goods, Stock in trade, Stores & spares, Loose Tools, Others
3) Whether goods in transit have been disclosed separately under each sub head of inventories

CASH & CASH EQUIVALENTS

CASH & CASH EQUIVALENTS

I. AUDIT PROCEDURES

II. DISCLOSURES

I. AUDIT PROCEDURES

Existence & Completeness

1. Surprise checks: Unless checked by surprise, there is no certainty that cash produced for inspection was in fact held by custodian. So, cash should be checked not only on the last day of the year, but also after close of the year without giving notice of auditor's visit to entity or staff
2. If more than one cash balances eg. When there is a cashier, petty cashier, branch cashier & in addition impressed balances with employees, all should be **checked simultaneously**.
3. It is desirable for the cashier to be present while cash is counted & sign statement prepared.
4. If any rough cash book or details of daily balances are separately kept, test entries from rough cash book with those in cash book to prove that entries in cash book are correct
5. If auditor finds any slip, chipped, IOU in respect of temporary advances paid to employees
6. Also Perform cash sensitivity analysis by compiling a summary of cash receipts & payments each month & analysing trends to see if there have been variations in any specific month & request brief descriptions from the management
7. Obtain BRS for all bank accounts maintained by the entity as at reporting period & understand client's process & periodicity of making the BRS.
    - Tallying balance as per bank book to bank confirmation or bank statement
    - Checking of all material reconciling items included under checks issued but presented for payment to underlying bank book forming part of BoA.
8. **Perform Direct Confirmation Procedures RTP Nov'20**

- Contact banks or FI directly & ask them to confirm amts held in current, deposit, EEFC, cash credit, restrictive use accounts like dividend, escrow accounts as of end of reporting period.
    - Agreeing balance to bank statement received by the Co. or online login to account in auditor's personal presence
    - Sending audit team member to bank branch with the entity's personnel to obtain balance confirmation from bank directly

Valuation:

In addition to above procedures, ensure that all bank accounts holding foreign currency have been restated at closing exchange rates as per AFRF.

III. DISCLOSURES MTP MAY'24+ICAI SM

i. Cash & cash equivalence shall be classified as :
    - Balances with banks, Checks, drafts on hand, Cash on hand, Others (specify nature)

ii. Earmarked balances with banks (for e.g. For unpaid dividend) shall be separately stated

iii. Balances with banks held as margin money or security against borrowings, guarantees, other commitments shall be disclosed separately

iv. Repatriation restrictions, if any, in respect of cash and bank balances shall be separately stated

v. Bank deposits with more than 12 months maturity shall be disclosed separately

STATEMENT OF PROFIT & LOSS

I. SALE OF PRODUCTS & SERVICES

Sales transactions and ICs to ensure entity is not materially misstating its revenues or a/c receivables.

1. Obtain an understanding of management control (internal control) in respect of sales process:

   E.g. Whether segregation of duties exist
   - Who checks credit limit (if applicable),
   - Who authorises sales orders,
   - Who raises sales invoice,
   - When & how goods are delivered/dispatched or services provided.

2. Test controls for sales cycles to determine how strong & reliable they are. Any deficiency in IC should be communicated as per SA 265.

   E.g. Common ICs over sales cycle include pre numbered sales invoices, proper authority for approval of orders, execution of sales order, customer PO authorisation over a certain limit & authorisation over receivables write off

3. Auditor selects a random sample of transactions & examines related customer invoices & customer statements to ensure that control being tested is a numbered sales invoice. This helps to determine NET of substantive procedures.

   E.g. Auditor ensures all the numbers in a section are accounted for & none are missing

4. Performing substantive audit procedures (SA520) is a must. Substantive analytical procedures will consist of sales trend analysis, comparison with previous account period, category wise sales analysis

   Auditor will need to know sales price of products or services over the year, monthly average sales price per product or service, discount policy.

   Eg. For a manufacturing Co., if average sales price of product X is Rs.10 & 1500 units were sold in that month, expected sales will be Rs.15000. Compare this data with client's data.

OCCURRENCE:

1. Recorded sales represent goods shipped/services performed during the period.
2. Ensure revenue is not over stated by performing following audit procedures MTP May 24
   - Check whether a single invoice is recorded twice or a cancelled sales invoice could also be recorded
   - Test check few invoices with their relevant entries in sales journal
   - Obtain confirmation from few customers to ensure genuineness of sales transaction
   - Whether any fictitious customers & sales have been recorded
   - Whether any shipments done without consent & agreement of customer, especially at year end to inflate sales figures
   - Whether unearned revenue recorded as earned
3. Review sequence of sales invoices

4. Review JE for unusual transactions
5. Calculate ratio of sales return to sales & compare with PY & enquire for reasons for increase/decrease.
6. Check sales return with sales invoice, challan, credit note, stock register, etc.

COMPLETENESS:

All sales made during the period were recorded & no understatement or over statement

1. Perform cut off procedures to ensure revenues are recognised in current a/c period
2. Cut off errors usually arise when Cos recognise revenue based on date on which sales invoices are generated, rather than date on which risks & rewards are transferred to buyer.
3. Also verify credit notes after a/c period. Sometimes sales team can make fictitious sales before year end to meet performance target & cancel out those sales with a post year end credit note
4. Trace from shipping document to sales journal
5. Check whether quantity is appearing in sales register or not & check reconciliation of total sales/goods despatched as per stock records & financial records & statutory records like GST
6. Review GST caps & GST returns & reconcile with revenue reported in P&L a/c.

MEASUREMENT

All sales are accurately measured as per AS & correctly journalised, summarised & posted MTP Nov '22

1. Trace a few transactions from inception to completion (examination in depth) E.g. Take a few sales transactions & checks from receipt of sales order to payment of receivable balance
2. Auditor must understand client's operations & related GAAP issues. E.g. Point of sale revenue recognition vs. percentage of completion.
3. If client engaged in export sales, compliance with AS 11 shall be ensured
4. Compare rate of sales affected with related parties & review for collectability & whether properly authorised & at arm's length

DISCLOSURES MTP March'21

In respect of a Co. other than finance company, revenue from operations shall disclose separately the revenue from –

a) Sale of products, Sale of services, Grants or donations received (relevant in case of sec 8 Co. only), Other operating revenues ,Less: excise duty, In respect of a finance company, revenue from operations shall include revenue from –Interest & Other financial services

Revenue under each of the above heads shall be disclosed separately by way of notes to accounts to the extent applicable

b) Whether brokerage & discount on sales other than usual trade discount has been disclosed.

c) Whether transactions with related parties are appropriately disclosed in notes to a/c

II. OTHER INCOME COMPRISING INT, DIV, G/L ON SALE OF INV

Dividends are recognised in statement of P&L only when:

a) Entities right to receive payment of dividend is established

b) It is probable that economic benefits associated with dividend will flow to entity &

c) Amount of dividend can be measured reliably

Gain/loss on sale of investment in mutual funds is recorded as other income on transfer of title from entity & is determined as difference between redemption price & carrying value of investments Jan'21

OCCURRENCE/COMPLETENESS/MEASUREMENT:

1. Obtain listing of FDs opened during period with intt. rate & no. of days for which deposit was o/s durin period
2. Verify arithmetical accuracy of interest calculation made by entity by recomputing i.e. Deposit amount * no. of days * interest rate
3. For deposits still outstanding as at period end, trace same to direct confirmations obtained from respective banks/FIs
4. Obtain a confirmation of interest income from bank & verify that interest income as per bank reconciles to calculation shared by entity
5. For dividends, verify its recognised in P&L only when entity's right to receive payment of dividend is established
6. Verify that gain/loss on sale of investment is recorded as "other income" only on
   - Transfer of title from entity AND
   - Is determined as difference between redemption price & carrying value. Obtain MF statement & trace gain/loss recorded in books to gain/loss recorded in statements

DISCLOSURE:

a) Interest income (in case of a Co. other than finance Co.)

b) Dividend income

c) Net gain/loss on sale of investments

d) Other non-operating income (net of expenses directly attributable to such income)

Undisclosed income: Co. shall give details of

Any transaction not recorded in BoA

That has been surrendered or disclosed as income in tax assessments under Income Tax Act, 1961 unless there is immunity for disclosure under any scheme &

III. PURCHASES

Obtain a clear understanding about organisation & its production centres e.g. Type of services or products they procure used in production/rendering of services, sources of procurement whether domestic or overseas, major vendors, credit period, quality checks, purchase terms (credit/cash purchase) etc.

1. Identify control points over purchases

Eg. Whether segregation of duties exist, whether competitive quotes invited, issues & authorises POs, when and how goods are received & acknowledged, who checks quality, quantity & specifications of goods received & prepares GRN, who approves vendor invoice, whether a 2/3-way match process exists. Auditor tests controls entity has set up for purchase cycle to determine whether they are effective or not. If controls are effective, reduce extent of substantive testing.

E.g. Common ICs over purchase cycle include inviting competitive quotations for short listing vendors, numbered POs, Generation of GRN on receipt of goods, quality inspection of goods, 2/3-way match, authorisation of purchase invoices.

2. Select a rendom sample of transactions & examine related POs, GRN, purchase invoices, inward gate entry register & vendor reconciliation/statements
3. Perform substantive audit procedures (SA 520) like analytical procedures consisting of purchase trend analysis, comparison with previous periods, category wise purchases, E.g. If purchase price is 100 & 15000 units are received during the year, auditor expects purchases to be Rs.15 lacs.

OCCURRENCE:

1. Ensure purchases are not under stated or over stated by performing following audit procedures:
2. Whether any fictitious vendors booked or purchases recorded by reviewing vendor selection process followed by entity & also ensure existence of vendors
3. Whether goods received at factory gate & there exists entry in security gate inward register
4. Whether a goods receipt note was prepared & signed by appropriate client personnel
5. Whether quality inspection of goods was done
6. Whether purchase invoice approved as per delegation of authority & whether a 2 or 3 way matches done
7. Whether stock record updated by stores personnel

Special considerations during audit of purchases:

1. Purchase invoice received should be original copy (& not photocopy/carbon copy) against which entity has recorded purchase in BoAs.
2. Purchase invoice to be booked only when risk & rewards have been transferred to the entity. Specific considerations where delivery terms agreed with vendor are F.O.B, C.I.F, etc.
3. Purchase invoice should be in the name of entity.
4. Input tax component should be booked in input tax ledger. Obtain tax returns filed with authorities & tally input tax reflected in books to amount disclosed in returns.
5. For purchases from related parties or allied & associated concerns, verify if approval from BoDs obtained & verify selected samples (SA 530) & perform analytical procedures (SA 520) to confirm arms length price
6. Review whether purchases are capitalised or expensed of in P&L as per his professional judgement
7. Review journal entry for unusual transactions.

COMPLETENESS & MEASUREMENT:

1. Perform cut off test to ensure purchases are recognised in correct accounting period.
2. Ensure correct a/c treatment of goods in transit as per agreed terms with vendor regarding transfer of risk & reward of ownership in goods

3. Obtain written representation from management that all purchases during the year have been properly recorded in books (SA 580)
4. Perform analytical procedures (SA 520) to obtain audit evidence as to overall reasonableness of purchase quantity & price which may include:
   - **Consumption analysis**: Scrutinize raw material consumed as per manufacturing account & compare with PYs
   - **Stock composition analysis**: Collect reports from management for composition of stock i.e. Raw materials as a % of total stock & compare with PY & ask for reasons from mgmt in case of significant variations
   - **Ratios**: Compare creditors turnover & stock turnover ratios of CY with PYs
   - Auditor should review quantitative reconciliation of clg. stocks with opg. stock, purchases & consumption

DISCLOSURES:

a. Whether purchases of stock in trade have been specifically disclosed
b. Whether changes in inventories of finished goods, stock in trade & WIP has been specifically disclosed
c. Whether transactions with related parties are appropriately disclosed in notes to accounts

IV. EMPLOYEE BENEFIT EXPENSES

Obtain clear understanding about organisation & its hiring, appraisal & retirement process in following manner:

1. Auditor test controls around employee benefit payment process to determine how effective they are. Eg. Maintenance of attendance records, employee master, authorisation & approval of monthly payroll processing & disbursement, computation of employee deductions like payroll taxes, other benefits like gratuity, leave encashment, bonus, etc.
2. Select a random sample of transactions & examine related appointment letters, appraisal letters, attendance records, HR policies, employee master, etc.
3. Performing substantive audit procedures is must. Substantive analytical procedures will consist of monthly expense reasonability, comparison with previous periods (SA 520)

AUDIT PROCEDURES [OCCURRENCE, COMPLETENESS & MEASUREMENT]

1. Obtain understanding of entity's process of capturing employee attendance. There is always a risk that entity could record expense for fictitious employees. To address this risk, auditor may choose to meet employees in person, on a sample basis.
2. Obtain a list of employees as at period end along with monthly movement split between new hires, leavers & continuing employees
3. For a sample selected randomly of new hires, obtain appointment letter & verify whether salary for first month & subsequent months was processed as per the agreed terms
4. For a sample selected randomly of resigned employees, obtain their full & final computation & verify whether all their dues including post-retirement benefits like gratuity, leave encashment have been paid & whether respective employees' acknowledgement on final computation has been obtained
5. Obtain monthly salary register for all 12 months. Compile a monthly payroll reasonability by calculating average salary per employee p.m & compare with PY & preceding month & analyse reasons for variance which could be due to annual increments, employee at senior level joining/leaving, bonus payout, etc.
6. Verify if accrual/provision made for all employee benefits & obligations like bonus, gratuity, etc.

7. Perform analytical procedures to assess overall reasonableness of employee benefit expenses which may include production per employee analysis. (SA 520)

DISCLOSURES:

i. Salaries and wages
ii. Contribution to provident and other funds
iii. Expense on Employee Stock Option Scheme (ESOP) & Employee Stock Purchase Plan(ESPP)
iv. Staff welfare expenses

V. DEPRECIATION

Auditor needs to consider following attributes while verifying depreciation & amortization expenses

1. Obtain understanding of entity's a/c policy
2. Ensure Co. policy for charging depreciation & amortization is as per relevant provisions of Co.s Act/AS
3. A/c policy has been applied consistently year on year. Any change in a/c policy has been adequately disclosed
4. Whether depreciation has been calculated after making adjustment of residual value from cost of assets
5. Whether depreciation & amortization charges are valid
6. Whether depreciation & amortization charges are accurately calculated & recorded
7. Whether each part of PPE with the cost significant in relation to total cost of item is being depreciated separately. E.g. Maybe appropriate to depreciate separately air frame & engines of aircraft
8. Whether most appropriate depreciation method for each separate depreciable component has been used

AUDIT PROCEDURES:

1. Obtain understanding of entity's process of charging depreciation & amortization
2. Obtain fixed asset register (FAR) maintained by entity
   - Always a risk that entity could capitalise revenue expenses to increase its profits or charge capital expenditure directly in P&L to reduce profits.
   - Further, always a risk that fake asset is capitalised in books & to mitigate this risk, physically verify material fixed assets. Obtain list of all additions/deletions with their proper approval from authorised person
3. Select sample of material assets from FAR & verify rates & calculations of depreciation
4. Obtain list of all components identified by management
5. Ensure intangible assets like patents, goodwill, copyrights has been properly amortized
6. Ensure depreciation is charged on assets from the date when it is ready to use & not from date of actual usage. In other words, **depreciation begins when asset is available for use**
7. Ensure depreciation on revalued amount has been properly accounted from revaluation reserve
8. Depreciation computation as per Income Tax Act,1961 – ensure that additions are tallying with as per Co's Act & opening WDV to tax audit schedule for AY preceding the PY under audit
9. Perform analytical procedures(SA 520) to assess overall reasonableness of depreciation & amortization expense- Check arithmetical accuracy of records & perform independent calculations for e.g. recompute depreciation expense

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10. Ensure that residual values have been properly verified as that impacts computation of depreciation.
11. Ensure depreciation & amortization computed prospectively whenever any change in useful life of PPE & intangible assets.

DISCLOSURES

- Accounting policy for depreciation & amortization
- Useful life of assets as per schedule III of the Companies Act, 2013
- Residual value of assets
- Depreciation method.

VI. OTHER EXPENSES

ATTRIBUTES: Dec'21 + MTP Oct'21 + Nov'22

While auditor may choose to analyse monthly trends for **expenses like rent, power & fuel** auditor generally prefers to vouch for other expenses to verify following attributes:

1. Whether the expenditure was in relation to entity's business & not a personal expenditure
2. Whether expenditure had valid supporting documents like travel ticket, insurance policy, 3rd party invoice, etc.
3. Whether expenditure has been classified under correct expense head
4. Whether expenditure qualified as a revenue & not a capital expenditure
5. Whether expenditure pertained to current period under audit
6. Whether expenditure was authorised as per delegation of authority matrix

RENT EXPENSE MTP Nov'22

1. Obtain a month wise expense schedule with rent agreements
2. Verify if expense is recorded for all 12 months & whether rent amount is as per underlying agreement
3. Specific consideration should be given to escalation clause in agreement to verify if rent was required to recorded on a straight-line basis during period under audit
4. Also, verify if agreement is in name of the entity & premises used for business operations of entity

POWER & FUEL EXPENSE MTP Nov'21

1. Obtain a month wise expense schedule with power bills
2. Verify if expense has been recorded for all the 12 months
3. Also, compile a month wise summary of power units consumed & applicable rate & check arithmetical accuracy of bills raised on monthly basis
4. In relation to units consumed, analyse monthly power units consumed by linking it to units of finished goods produced & investigate reasons for variance in monthly trends

INSURANCE EXPENSE

1. Obtain a summary of insurance policies with their validity period
2. Verify whether expense correctly classified between prepaid & expense for the period based on no. of days

LEGAL & PROFESSIONAL EXPENSES: MTP Mar'23

1. Obtain a month wise & consultant wise summary
2. In case of monthly retainership agreements, verify whether expenditure for all 12 months recorded correctly
3. For non recurring expenses, select a sample & vouch for attributes discussed above
4. Be cautious while vouching legal expenses as some may highlight a dispute for which entity may not have made any provision & matter may also not have been discussed/highlighted to auditor

TRAVEL, REPAIRS & MAINTENANCE, PRINTING & STATIONARY, MISC. EXPENSES:

1. Auditor should select a sample & vouch for attributes discussed above
2. Wherever possible, prepare summary of expenditure on monthly basis & then analytically compare the trends
3. Perform analytical procedures (SA 520) to assess overall reasonableness of the other expense
4. Auditor should analyse expense per unit produced & compare with PY & present industry trends & ask for reasons from mgmt if any significant variations are found

OTHER TOPICS

a. Goods sent out on sale or return basis

i. Check whether separate memoranda record of goods sent out on sale or return basis is maintained.

ii. Verify that prices of such goods is unloaded from sales a/c & debtors record. **Check memoranda record to confirm that on receipt of acceptance from each party, his a/c has been debited & sales a/c correspondingly credited**

iii. Ensure that goods in respect of which period of approval has expired at the end of the year, have either been received back or customer a/cs been debited

iv. Confirm that inventory of goods sent out on approval, period of approval had not expired till end of the year lying with party, has been included in closing inventory

b. Goods sent on borrowings: Maybe in form of overdraft limits of terms

i. Reconcile balances in overdrafts or loan accounts with pass books & confirm last mentioned balance by obtaining a certificate from bank showing balance in a/cs at the end of the year

ii. Obtain independent balance confirmation from bank showing balances, securities deposited with bank as security for loans/charge created on asset & confirm the same has been correctly disclosed & duly registered with registrar of Co.s & recorded in register of charges

iii. Verify authority under which loan or draft has been raised. In case of a Co., only board directors are authorised to raise a loan or borrow from bank.

iv. Confirm in case of a Co., that restraint contained in sec 180 of Co.s Act, 2013 as regards maximum amount of loan that Co. can raise has not been contravened.

c. Goods sent on consignment:

i. Verify accounts sales submitted by consignee showing goods sold & in hand

ii. Reconcile figure of goods on hand, as given in the last a/cs sale, with proforma invoices & accounts sales received during the year.

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iii. If any consignment inventory was in the hands of consignee at the beginning of the year, same should be taken into account in reconciliation

iv. Obtain confirmation from consignee for goods held on consignment on b/s date. Verify terms of agreement between consigner and consignee to check commission & other expenses debited to consignment a/c and credited to consignee's a/c. Account sales also must be checked

v. Ensure that quantity of goods in hand with consignee has been valued at cost + proportionate non-recurring expenses eg. Freight, dock dues, customs due, etc. unless value is lower. In case NRV is lower, inventory in hand of consignee should be valued at NRV.

vi. See that goods in hand with consignee have been shown separately under the head inventories

d. Foreign travel expenses:

i. Examine travelling allowance bills submitted by employees stating details of tour, expenses, etc.

ii. Verify that tour program of properly authorised by competent authority

iii. Check TA bills along with accompanying supporting documents such as air tickets, travel agent bills & hote bills w.r.t internal rules for employees & also make sure that bills are properly passed

iv. See that tour report accompanies TA bill. Tour report will show purpose of tour.Satisfy that purpose of tour as shown by tour report conforms to authorisation of tour

v. Check RBI's permission, if necessary, for withdrawing foreign exchange. For a Co. amt of forex spent is to be disclosed separately in a/cs as per requirement of schedule III to Companies Act, 2013 & AS 11 "the effects of changes in foreign exchange rates"

e. Receipt of Capital Subsidy:

i. Check application for claim of subsidy to ascertain purpose & scheme of subsidy

ii. Examine documents for grant of subsidy & note conditions attached relating to its use, etc.

iii. Ensure that conditions to be fulfilled & other terms especially whether it is for a specific asset or for setting up a factory at a specific location

iv. Check relevant entries for receipt of subsidy

v. Check compliance with AS 12 on "Accounting for Govt. grants" i.e. whether it relates to specific amount or in form of promoter's contribution & accordingly accounted & disclosed

f. Provision for Income Tax:

i. Obtain computation of income & income tax & whether it is as per Income Tax Act, 1961 & Rules

ii. Review adjustments, expenses disallowed, special rebates, etc. w.r.t last available assessment

iii. Examine relevant records & documents of advance tax, self assessment tax & other demands

iv. Compute tax payable as per latest applicable rates in finance act

v. Ensure that overall provisions on b/s date is adequate w.r.t CY provision, advance tax paid, assessment orders, etc.

vi. Ensure that requirements of AS 22 on accounting for taxes on income are appropriately followed

g. **Payment of Income Tax:**

i. Payment of Income Tax & other taxes upon a regular assessment should be verified by reference to copy of assessment order, assessment form, notice of demand & receipted challan

ii. Payments are advance payments of Income Tax should also be verified with notice of demand & receipted challan acknowledging amount paid

iii. Interest allowed on advance payments of Income Tax should be included as income & penal interest charged for non payment should be debited to interest account

iv. Nowadays, electronic payment of taxes is in trend. It means payment of taxes by way of internet banking facility /credit/debit cards

v. Entity can make electronic payment of taxes also from account of any other person. However, challan for such payment must clearly indicate PAN of assessee on whose behalf payment is made. This should be checked by the auditor

vi. It is not necessary for entity to make payment of taxes from his own account in authorised bank. While vouching such e-payment, cross verify such challan with PAN/TAN no. etc.

h. **Sales proceeds of scrap material:**

i. Review internal control on scrap materials, as regards its generation, storage & disposal

ii. Ascertain whether entity is maintaining reasonable records for sale & disposal of the scrap

iii. Review production & cost records for determining scrap materials that may arise in a period

iv. Compare income from sale of scrap materials with corresponding figures of preceding 3 years

v. Check rates at which different types of scrap materials are sold & compare with preceding year

vi. See that scrap material sold have been billed & check calculations on invoices

vii. Ensure there is proper procedure to identify scrap & good quality material is not mixed with it & sold as scrap

viii. Make overall assessment of realisation from sale of scrap materials for its reasonableness

i. **Advertisement**:

i. Verify bills/invoices from advertising agency to ensure rates charged for different types of advertisement as per contract

ii. See that advt relates to client's business

iii. Inspect receipt issued by agency

iv. Ascertain nature of expenditure-revenue or capital expenditure & see if recorded properly

v. Ascertain period for which payment made & see that prepaid amount, if any is carried to b/s

vi. See that all outstanding advt bills have been provided for

IMPORTANT DISCLOSURES

CORPORATE SOCIAL RESPONSIBILITY(CSR) MTP May'24+ May'22

For Co's covered u/s 135 of Co's Act:

a) Amount required to be spent by the Co. during the year
b) Amount of expenditure incurred
c) Shortfall at the end of the year
d) Total of PY's shortfall
e) Reason for shortfall
f) Nature of CSR activities
g) Details of related party transactions eg. Contribution to a Trust controlled by the company in relation to CSR expenditure as per relevant a/cing standards
h) Where a provision is made w.r.t a liability by entering into a contractual obligation, the movements in the provision during the year should be shown separately

ROUND OFF

Depending upon total income of Co., figures appearing in the FS shall be rounded off as:

Total income	Rounding off
a) less than Rs.100 cr	To nearest hundreds, thousands, lakhs or millions, decimals thereof.
b) Rs.100 cr or more	To the nearest lakhs, millions or crores, or decimals thereof

Once a unit of measurement is used, it should be used uniformly in the FS

DETAILS OF BENAMI PROPERTY HELD May'22 + RTP May'24

Where any proceedings have been initiated or pending against Co. for holding any benami property under Benami Transactions (Prohibition) Act, 1988 & rules made thereunder, Co. shall disclose the following:

a) Details of such property, including year of acquisition,
b) Amount thereof
c) Details of beneficiaries
d) If property is in books, then reference to item in B/S
e) If property is **not** in books, the fact shall be stated with reasons
f) Where proceedings against Co. under this law as an abetter of transaction or as transferor then details shall be provided
g) Nature of proceedings, status of same & Co's view on same

RELATIONSHIP WITH STRUCK OFF COMPANIES

WHERE Co.s has any transactions with Co.s struck off u/s 248 of Companies Act,2013 Co. shall disclose following details:

Name of struck off Co.	Nature of transactions with struck off Co.	Balance o/s	Relationship w/struck off Co., if any, to be disclosed
	Investments in securities		
	Receivables		
	Payables		
	Shares held by struck off Co.		
	Other o/s balances		

RATIOS TO BE DISCLOSED Sep'24 + RTP May'24

a) Current ratio
b) Debt Equity ratio
c) Debt service coverage ratio
d) Return on equity ratio
e) Inventory turnover ratio
f) Trade receivables turnover ratio
g) Trade payables turnover ratio
h) Net capital turnover ratio
i) Net profit ratio
j) Return on capital employed
k) Return on investment

Co. shall explain items included in numerator & denominator for computing above ratios. Further explanation should be provided for any change in ratio MORE THAN 25% as compared to preceding year.

DETAILS OF CRYPTO OR VIRTUAL CURRENCY Nov'22

Where Co. has traded or invested in Crypto or virtual currency during FY, following shall be disclosed

a) Profit or loss on transactions involving Crypto currency or virtual currency
b) Amount of currency held as at reporting date
c) Deposits or advances from any person for trading or investing in Crypto/virtual currency

UTILISATION OF BORROWED FUNDS & SHARE PREMIUM

Where Co. has advanced or loaned or invested funds (either borrowed funds or share premium or any other sources or kind of funds) to any other persons/entities including foreign entities (intermediaries) with an understanding (whether recorded in writing/other wise) that intermediary shall

a) Directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the Co. (ultimate beneficiaries) or

b) Provide any guarantee, security, or the like on behalf of the ultimate beneficiary

Co. shall disclose the following:

- Date & amount of fund advanced or loaned or invested in intermediaries with complete details of each intermediary
- Date & amount of fund further advanced or loaned or invested by such intermediaries to other intermediaries or UBs along with complete details of UBs
- Date & amount of guarantee, security or like provided to or on behalf of UBs
- Declaration that relevant provisions of FEMA, 1999 & Companies Act has been complied with for such transactions & transactions are not violative of PMLA, 2002

Where a Co. has received any fund from any persons or entities including foreign entities (funding parties) with an understanding (whether recorded in writing/otherwise) that Co. shall

a) Directly or indirectly lend or invest in other persons or entity identified in any manner whatsoever by or on behalf of the funding party (ultimate beneficiaries) or

b) Provide any guarantee, security or on the like on behalf of the UBs

Co. shall disclose the following

- Date and amount of fund received from FPs with complete detail of each FP
- Date and amount of fund further advanced/loaned/invested other intermediaries or UBs along with complete details of other intermediaries or UBs
- Date and amount of guarantee, security or the like provided to or on behalf of UBs
- Declaration that relevant provisions of FEMA,1999 & Companies Act has been complied with for such transactions & transactions are not violative of PMLA 2002

WILFUL DEFAULTER

Wilful defaulter means a person or an issuer who or which is categorised as a wilful defaulter by any bank or FI as per the RBI guidelines on wilful defaulters

Where a Co.is declared wilful defaulter by any bank/FI or other lender, following details be given:

a) Date of declaration as wilful defaulter

b) Details of defaults (amount & nature of default)

REGISTRATION OF CHARGES OR SATISFACTION WITH REGISTRAR OF COMPANIES

Where any charges or satisfaction yet to be registered with ROC beyond statutory period, details & reasons shall be disclosed

TITLE DEEDS OF IMMOVABLE PROPERTY NOT HELD IN NAME OF THE COMPANY

Co. shall provide details of all immovable property (other than properties where Co. is lessee & lease agreements are duly executed in favour of lessee) whose title deeds are not held in name of Co. & where such immovable property is jointly held with others, details to be given to the extent of Companies' share.

Relevant line item in BS	Description of property	Gross carrying value	Title deeds held in name of	Whether title deed holder is a promoter, director or relative of promoter/director or employee of promoter/director	Property held since which date	Reason for not being held in name of Co.
						Indicate if any dispute

Where Co.has revalued its PPE, it shall disclose as to whether revaluation is based on valuation by a regd valuer.

CAPITAL WORK-IN-PROGRESS (CWIP)

a) For CWIP, following ageing schedule shall be given:

CWIP ageing schedule

CWIP	<1 year	1-2 years	2-3 years	>3 years	Total
Projects in progress					
Projects temporarily suspended					

b) For CWIP, whose completion is overdue or exceeded its cost compared to original plan, following CWIP completion schedule shall be given:

	To be completed in				Total
	< 1 year	1-2 years	2-3 years	>3 years	
Project 1					
Project 2					

(Details of projects where activity has been suspended to be given separately)

Similar schedules are to be given for Intangible assets under development.

P6 – AUDITING & ETHICS
MNEMONICS

SA 230 – Audit Documentation

Audit Documentation includes

CCLAAIMS

C ***C***hecklist
C ***C***orrespondence
L ***L***etters (Letter of confirmation and Management Representation Letter)
A ***A***udit program
A ***A***nalysis
IM ***I***ssue ***M***emoranda
S ***S***ummary of significant transactions

SA 315 – Identifying and assessing the Risk of Material Misstatement through understanding the entity and its environment

Risk Assessment Procedures

AIIO

A ***A***nalytical procedures
I ***I***nspection
I ***I***nquiry
O ***O***bservation

INTERNAL CONTROL

Study of various aspects of IC:

Controls Relevant to the Audit

SLM NCC DRS

S ***S***ize of the entity
L ***L***egal & regulatory requirements
M ***M***ateriality
N ***N***ature of the Business
C ***C***ircumstances & components of Internal control
C ***C***omplexity & nature of Information Systems
D ***D***iversity & complexity of the entity's operations
R ***R***elated risks
S any ***S***pecific control is there for preventing, detecting & correcting material misstatements

Components of Internal Controls

CRIME

C ***C***ontrol Activity
R ***R***isk Assessment Process
I ***I***nformation Systems
M ***M***onitoring
E control ***E***nvironment

Control Activity – Policies and Procedures

ISPPA

I ***I***nformation Processing
S ***S***egregation of Duties
P ***P***erformance Review
P ***P***hysical Controls
A ***A***uthorization

Entity's Risk Assessment Procedure

ISPA

I ***I***dentifying risk
S Estimating ***S***ignificant risk
P ***P***robability – likelihood of happening or not
A ***A***ction to be taken for the risk

Control Environment

SHAPE PC

S Organizational ***S***tructure
H ***H***R Policies and Practices / Procedures
A ***A***ssignment of authority & Responsibility
P ***P***hilosophy and operating style of Management
E ***E***thical Values & communication and enforcement of Integrity
P ***P***articipation of TCWG
C ***C***ommitment to competence

Testing of IC

IIO + TR

I ***I***nspection
I ***I***nquiry
O ***O***bservation
T ***T***esting
R ***R***e-performance

Audit Procedure in Automated Environment

IIO + R

I ***I***nspection
I ***I***nquiry
O ***O***bservation
R ***R***e-performance

SA 500 – Audit Evidence

Audit Procedures

EII ROAR

E ***E***xternal Conformation
I ***I***nspection
I ***I***nquiry
R ***R***e-performance
O ***O***bservation
A ***A***nalytical Procedure
R ***R***ecalculation

SA 501 – Audit Evidence – Specific considerations for Selected Items

Other Audit Procedures for inventory - custody of 3rd parties

ACID

A ***A***nother Auditor
C ***C***onfirmation - Pledged
I ***I***nternal Control
D ***D***ocument Inspection

Matter relevant in Planning for Physical verification

TWIN LIP

T ***T***iming of inventory
W ***W***ork in progress
X ***I***nternal Control
N ***N***ature of inventory
L ***L***ocation of inventory
I ***I***nstructions given for inventory counting
P ***P***erpetual inventory system

Litigation & Claims

Audit Procedures

MILE

M ***M***inutes
I ***I***n house legal team
L ***L***egal expenses account
E ***E***xternal legal council

SA 520 – Analytical Procedures

When performing Analytical procedures Auditor shall:

DRESS

D **D**ifference
R ***R***eliability
E ***E***valuate
S ***S***uitability

SA 530 – Audit Sampling

Characteristics of Population

CAR

C **C**ompleteness
A ***A***ppropriateness
R ***R***eliability

SA 550 – Related Parties

Existence of related party relationship & transactions

SHORT LIPSTICK

SH ***S***hare ***H***olders Register
O not in ***O***rdinary Course (contracts & agreements)
R ***R***egulatory Authority (Documents submitted to)
T ***T***ax Returns (Income Tax Returns)
L ***L***ife Insurance Policies
I ***I***nvestments made
P ***P***rofessional Advisors
S ***S***EBI – Docs filed with Securities Regulators
T ***T***CWG – contracts/ agreements with Key management / TCWG
I ***I***nternal Audit Functions
C ***C***onflicts of Interest reports
C ***C***ontracts – Significant contracts negotiated.

SA 560 – Subsequent Events

How the Auditor make Inquiry with the Management & TCWG to ascertain what are all the subsequent events

AAABCD

A ***A***ccounting Policies
A ***A***cquisition of Assets
A ***A***ccounting Adjustments
B ***B***orrowings
C ***C***ontingencies
D ***D***estroyed

ETHICS

Fundamental principles of professional ethics

COPPI

C ***C***onfidentiality
O ***O***bjectivity – not compromise on professional judgment
P ***P***rofessional behaviour – not discredit the profession
P ***P***rofessional knowledge & skill / competence & due care
I ***I***ntegrity – truthfulness / honest