

Hello everyone we are ready with:-

- Summary Notes
- With Charts / Tables & Shortcuts
- Covering all concepts with all points as given in Modules
- Including content from PM & RTP
- SA 200 / 300 / 400 / 500 / 600 / 700 Series
- Total 31 Standards
- 64 Pages

→ NI-IPC are the markings where things are not important for IPCC / IPC, so concerned students can ignore it

→Download from given link

We will be revising SAs in 12 hours in 1 Day revision sessions across 7 cities. We will further enhance content, examples and give printed copies during revision sessions. Summary of other SAs such as 800 / SRE 2400 & 2410 / SAEs 3402 & 3410 / SRSs 4400 & 4410 will be given during revision sessions.

**CA-FINAL & IPC**  
**AUDIT**  
**QUICK REVISION**  
For May'16 Exam

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<b>AHMEDABAD</b>	<b>1<sup>st</sup> April</b>
<b>PUNE</b>	<b>3<sup>rd</sup> April</b>
<b>MUMBAI</b>	<b>5<sup>th</sup> April</b>
<b>DELHI</b>	<b>8<sup>th</sup> April</b>
<b>NAGPUR</b>	<b>11<sup>th</sup> April</b>
<b>RAIPUR</b>	<b>13<sup>th</sup> April</b>
<b>KOLKATA</b>	<b>15<sup>th</sup> April</b>

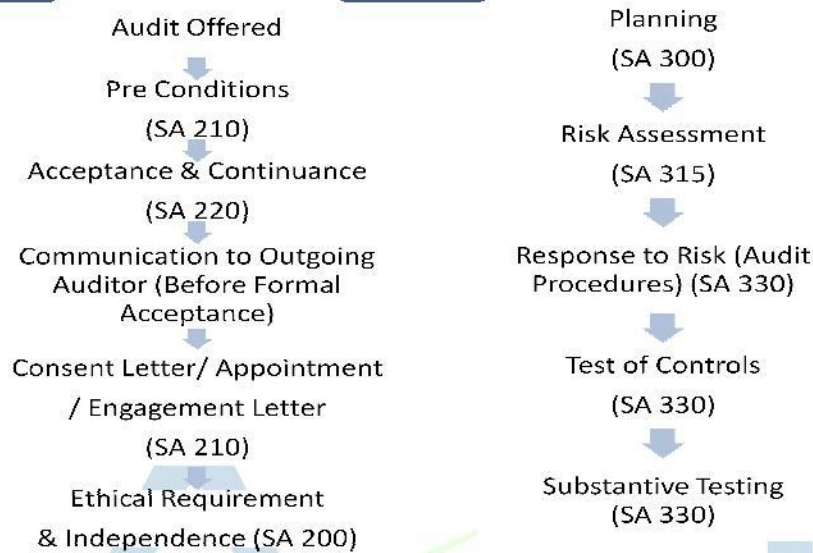
**CA RAVI TAORI**  
(National Level Professor)  
Teaching Since 2007

Time : 8am to 8pm  
Course Coverage with Short Notes  
**Revise SAs +**  
Ques. of PM & 3 RTPs

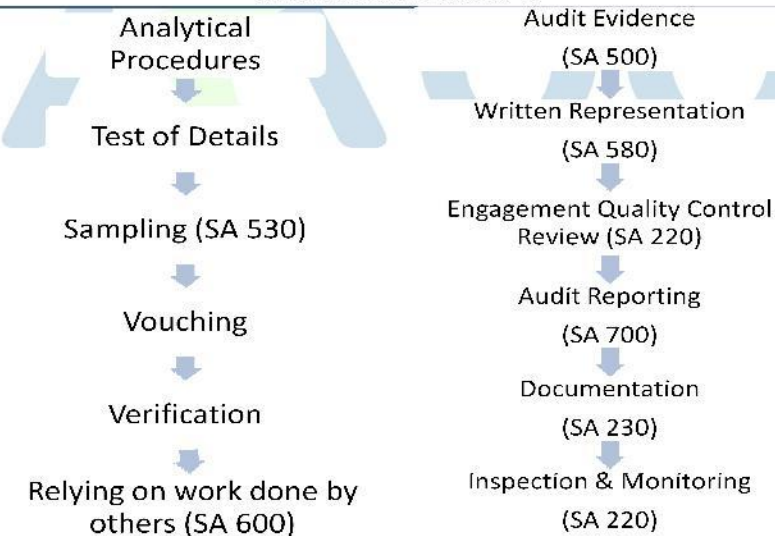
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**Core Audit Process-1**



**Core Audit Process-2**



**INTRODUCTION TO SA**

**1. TYPES OF STANDARDS (5 M)**

a. Standards on Quality Control (1-99)

b. Engagement Standards

1. Assurance Services

a. Standards on Auditing (SAs) (100-999)

b. Standards on Review Engagements (SREs) (2000-2699)

c. Standards on Assurance Engagement (SAEs) (3000-3699)

2. Related Services

Standards on Related Services (SRSs) (4000-4699)

**2. AUDIT V/ S REVIEW (4 M)**

	AUDIT (SAs)	REVIEW (SREs)
<b>Time</b>	More	Less
<b>Audit Procedures</b>	All Types	Inquiry & Analytical Procedure
<b>Level of Assurance</b>	Reasonable(High)	Moderate
<b>Type of Opinion</b>	Positive	Negative
<b>Example</b>	Company Audit	Quarterly Review of Interim, FST

**3. CONTENTS OF SA (2M)**

SAs	CONTENT
100-199	INTRODUCTORY MATTERS
200-299	GENERAL PRINCIPAL & RESPONSIBILITIES
300-399	RISK ASSESMENT & RESPONSE TO RISK
500-599	AUDIT EVIDENCE
600-699	USING WORK OF OTHERS
700-799	AUDIT REPORT
800-999	SPECIALISED AREAS



**4. DRAFTING OF SA (4M)**

DRAFTING OF SA	
Section I	Section II
INTRODUCTION	APPLICATION AND OTHER EXPLANATORY MATERIAL
OBJECTIVES	APPENDICES
DEFINITION	
REQUIREMENTS	

**5. PROCEDURE OF PREPARING AUDITING STANDARDS STATEMENTS/ GENERAL CLARIFICATIONS (5M)**

- a. AASB identifies project/ area where standard is required
- b. Constitutes study Group/ Task Force  
\*Conveyor is appointed who appoints 5-7 members
- c. Study group submits preliminary draft to chairman.
- d. Preliminary Draft is approved by chairman
- e. Draft is hosted on AASB website for minimum 21 Days
- f. Draft considered in meeting & Exposure draft is finalized
- g. Proposed exposure Draft sent to council members, minimum 10 days are provided for comments and changes.
- h. Exposure draft is issued to members & other public bodies and hosted on ICAI website for minimum 60 days.
- i. Comments received up-to 10 days prior to AASB meeting are hosted, AASB meeting is held and drafted is finalized.  
Proposed standard is placed before council & approved & issued

**6. VARIOUS PROFESSIONAL PRONOUNCEMENTS. (4M)**

	ISSUED BY	REMARKS
STANDARDS ON AUDITING/ REVIEW/ OTHER ASSURANCE & RELATED SERVICE	ICAI MANDATORY IN NATURE	ASSURANCE & RELATED SERVICE
STATEMENT ON AUDITING	UNLESS EXEMPTED	CRITICAL MATTERS
GENERAL CLARIFICATION		CLARIFIES ISSUES ARISING IN STANDARD

GUIDANCE NOTES	ICAI RECOMMENDATORY IN NATURE	IF NOT FOLLOWED THERE SHOULD BE JUSTIFICATION
TECHNICAL GUIDES	AASB NO OBLIGATION	BROAD KNOWLEDGE
PRACTICE MANUALS		ADDITIONAL GUIDANCE
STUDIES & OTHER PAPERS		DISCUSSION/ DEBATE/ CREATING AWARENESS.

**7. COMPOSITION OF AASB (2M)**

1. Eminent professionals as appointed by ICAI
2. CO-OPTED MEMBERS
  - 1 EACH FROM SEBI/ RBI/ IRDA
  - 1 FROM IIM OR ANY SUCH INSTITUTION
  - 1 INDUSTRY ASSOCIATION
  - 1 FROM NPO
3. Special Invites but they cannot vote

**8. MANDATORY TO FOLLOW STANDARDS**

**Clause 9 of Part I of the Second Schedule to the CA Act, 1949 holds a member guilty of professional misconduct if he fails to invite attention to material departure from the generally accepted procedures of audit applicable to the circumstances.**

**SA 200 – OBJECTIVES & PRINCIPLES****1. OBJECTIVES OF AN INDEPENDENT AUDITOR (4M)**

- **Primary objective:** whether FST gives true or fair view [free from material misstatement]
- **Secondary (Extended) objective:** If there is suspicion or material misstatement to determine whether it is due to fraud or error.
- **Not an Objective:**
  1. To do **investigation** of fraud and find out truth and get justice.  
To comment on **efficiency/ effectiveness & future viability**

**2. TYPES OF ASSURANCE (2M)****Absolute Assurance:** means 100% assurance**Reasonable Assurance:** means high assurance but not 100% (**Audit**)**Moderate Assurance:** Less than reasonable assurance (**Review**)**3. INHERENT LIMITATION OF AUDIT (5M)**a. Audit evidence is **persuasive** [not confirm] **rather than conclusive**b. Many financial statement items are valued only on the basis of **managements estimates**c. May not be able to detect **intentional misstatement**d. Limited **Time**e. Limited **Cost**f. Use of **sampling**

g. Inherent limitation of internal control system (Human Error / Collusion / Management Override /

**4. REQUIREMENTS OF SA 200 (JES) (6M)**1. Exercise professional **Judgments**2. **Ethical** requirement3. Professional **skepticism**4. Obtain sufficient & appropriate audit **Evidence**5. Follow all **standards** on auditing**5. ETHICAL REQUIREMENTS (4M)****DO-CBI**• **D**-Professional competence & Due care• **O**-Objective• **C**-Confidentiality• **B**-Professional Behavior• **I**-Integrity**6. BASIC PRINCIPLES OF AUDIT****(6M) (As per OLD AAS-1)**

1. Integrity, objectivity and independence

2. Confidentiality

3. Skills and competence

4. Work performed by Others

5. Planning

6. Accounting System and Internal Control

7. Audit Evidence

8. Documentation

9. Audit conclusions and Reporting

**7. SCOPE OF AN AUDIT (4M)****a.** Terms of engagement of the auditor**b.** Requirements of legislation (Law)**c.** Standards on Auditing**d.** Guidance notesTerms of engagement **cannot have an Overriding effect over the scope decided by the legislation or SAs.****8. WORK PERFORMED BY OTHERS (2M)**

Auditor can delegate work but he cannot delegate responsibility.

Only 2 exceptions other auditor and joint auditor.

Work Done by	Auditor's Duties
Assistants	SA-220
Experts	SA-620
Other Auditors	SA-600
Internal Auditor	SA-610
Joint Auditors	SA-299

**SA 210 (R) – AGREEING THE TERMS OF ENGAGEMENT****5 Parts****Part I****1. PRECONDITIONS BEFORE ACCEPTING AUDIT (4M)****a.** AGREEMENT OF MGMT/ TCWG ON ITS RESPONSIBILITIES [“PREMISES OF AUDIT”]



**b.ACCEPTABILITY OF FRF (S<sup>2</sup>R<sup>2</sup>-NU)**

- 1.Suitable
- 2.Sufficient
- 3.Relevance
- 4.Reliability
- 5.Neutrality
- 6.Understandability

**2.LIMITATION ON SCOPE PRIOR TO ACCEPTANCE(2M)**

If Auditor believes the limitations will **result in disclaimer of opinion** on FST, he should **not accept the Audit Engagement unless required by law or regulations**

**Part II****3.ENGAGEMENT LETTER (EL)(5M)**

Compulsory + preferably before commencement of audit

EL'S MANDATORY CLAUSE-

- a.Objective & Scope of Audit
- b.Responsibility of Management
- c.Identify financial reporting framework
- d.Responsibility of Auditor
- e.Reference to expected form & Content of Audit Report

EL'S NON MANDATORY CLAUSE-

- a.Planning regarding audit
- b.Timetable
- c.Reliance on Internal Control
- d.MGT inform auditor about facts that affects FST
- e.Arrangements regarding involvement of internal auditor and other staff
- f.Appointment of other auditor or experts
- g.Expectation of **Written representation**
- h.Inherent **limitations** of Audit
- i.Basis of **Fees**.
- j.Audit report may be subjected to a peer review
- k.Request for acknowledging receipt of EL and terms there in

**4.WHETHER FRESH ENGAGEMENT LETTER IS REQUIRED IN CASE OF RECURRING AUDITS?(5M)**

It depends on whether

- There is change in **circumstances or terms**
- Need to **remind mgmt.**

**FOLLOWING ARE EXAMPLES WHERE REVISION MAY BE REQUIRED**

Any indication that the Entity **misunderstands the objective and scope of the audit.**

- Any revised or **special terms of the audit engagement**
- A **recent change of Senior Management.**
- A significant **change in ownership.**
- A significant **change in nature or size of the Entity's business.**
- A **change in legal or regulatory requirements.**
- A **change in the Financial Reporting Framework** adopted in the preparation of the Financial Statements

**Part III****5.AUDIT TERMS PRESCRIBED BY LAW REGULATION (2M)**

If law or regulation **prescribes in sufficient detail** the terms of the Audit Engagement, **the Auditor need not record** them in a written agreement, **except** for the fact that such **law or regulation applies and that Management acknowledges and understands** its responsibilities as set out in

**6.RESPONSIBILITIES OF MANAGEMENT PRESCRIBED BY LAW(2M)**

If law or regulation prescribes responsibility of management,



Then use word of law for acknowledgment,



If law has not defined the words, then use the word of SA



Get this acknowledgment signed from management

**Part IV**

**7. CHANGE IN TERMS OF ENGAGEMENT (4M)**

Check that whether the changes are **justified or not**, **If justified** than make **new engagement letter**, **If not justified** than **withdraw from engagement + report** to TCWG/ Owners/ Regulators, **if required by law**.

**8. MANAGEMENT REQUEST AUDIT TO REVIEW (2M)**

If management request to change audit to review or to related service because of some reasons for e.g. lack of time

If reason is justified than auditor should continue his work as a review or related service.

If not justified than auditor should withdraw from engagement + report to TCWG/ Owners/ Regulators, if required by law.

**Part V**

**IF THERE IS CONTRADICTION BETWEEN FRF & LAW (4M)**

There are **two** ways for resolving the conflict

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1. Additional Disclosure [do accounting as per AS 11 and give disclosure in notes to accounts for SCH III]

2. Amend Description of FRF [give description that everything is done as per AS except some things]

If any of above is possible then give clean report otherwise give modified report

**9. FRF PRESCRIBED BY LAW & REGULATION (4M)**

NI-IPC

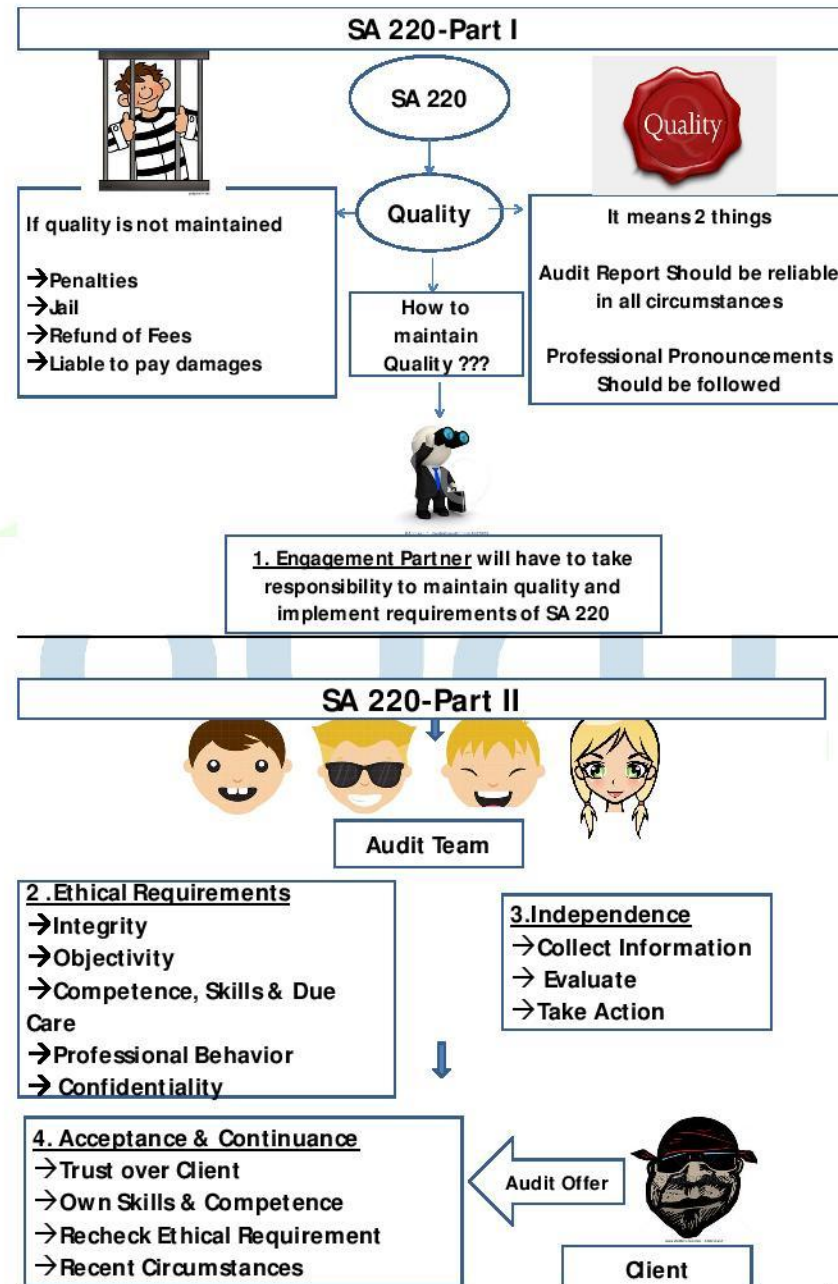
FRF prescribed is unacceptable

Accept only if

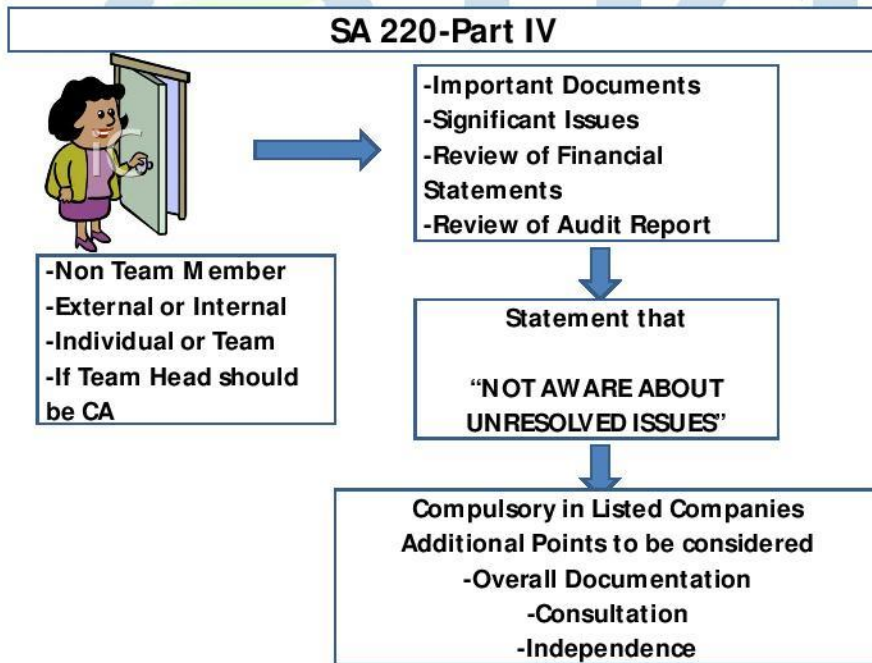
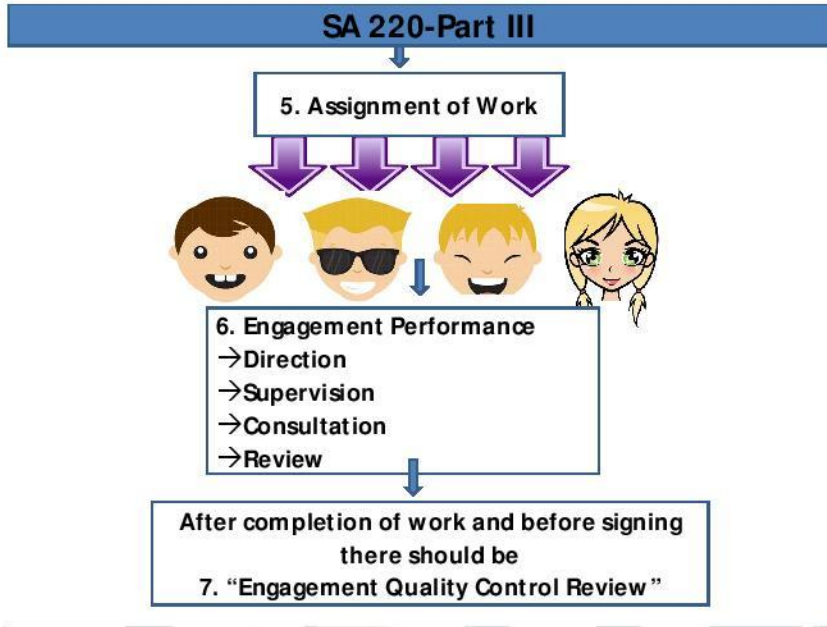
- a. MGMT agrees to additional disclosure &
- b. EMP as per SA 706

Don't use phrases like "present fairly, in all material respects", "give true & fair view"

**SA-220 - QUALITY CONTROL**







**Difference Between SQC 1 & SA 220**

**SQC 1**  
 Applicable to all types of Assignments  
 It talks about how to develop quality system at firm level.  
 It also talks about internal rotation of partner after 7 years & maintenance of documents for 7 years (Internationally 5 years)

**SA 220**  
 Applicable only to audit of Historical Information  
 It talks about how to implement quality policies at assignment level.

**Headings Covered**

- Leadership Responsibility
- Human Resources (Not Included in SA 220)
- Ethical Requirement
- Independence
- Acceptance & Continuance (Included in SA 220)
- Assignment of Engagement Team
- Engagement Performance (Direction, Supervision, Consultation, Review)
- Engagement Quality Control Review
- Engagement Documentation
- Difference of Opinion
- Monitoring
- Complaints & Allegations (Not Included in SA 220)

**SA 230 - AUDIT DOCUMENTATION****1. AUDIT DOCUMENTATION (AD) & CONTENTS OF AD (5M)**

Audit Documentation is prepared by auditor itself or obtained from client. (Terms such as "Working Papers" or "Work Papers" are also sometimes used).

**Examples of Audit Documentation include:**

- Audit Programmes.
- Checklists.
- Letters of confirmation and representation.
- Issues Memoranda.
- Summaries of significant matters
- Correspondence (including e-mail) concerning significant matters

**CONTENT OF AUDIT DOCUMENTS**

- Nature/ timing/ extent of audit procedures
- Results and Audit Evidence obtained:
- Significant Matters and discussion with management and conclusion

**Nature/ timing/ extent of audit procedures is includes:**

1. Identifying Characteristics:
2. Who Performed
3. Date of Completion
4. Who Reviewed
5. Date of Review

**2. PURPOSE OR ADVANTAGES OF WORKING PAPER/ DOCUMENTATION (5M)**

- A. Assist in Planning
- B. Delegation of WORK
- C. Accountability Improves
- D. Supervision
- E. Review
- F. For Quality Control Reviews (SA 220)
- G. Report Finalization
- H. Standardization

- I. Evidence of Proper Planning & Execution
- J. Evidence in COURT
- K. Peer review
- L. Reference in future Audit

**2. MISCELLANEOUS (2M each)**

- I. No Need To Keep Superseded Documents.
- II. Way of Preparing Audit Documentation: Maintain Audit Documentation in Such a Way that any Experienced Auditor should be able to understand it very easily.
- III. Ownership of Audit Documentation: auditor is an owner of audit document irrespective of whether it is made by auditor itself or obtained from client. But principle auditor is not an owner of branch documents because owner of branch documents is Branch Auditor.
- IV. Can auditor exercise lien over clients books or records  
Saxena v/ s Sharma

**3. ASSEMBLY OF AUDIT FILE (2M)**

Within 60 Days from date of Audit Report  
Preserve for minimum 7 years & more in case of litigation.

**4. MATTERS ARISING AFTER AUDIT REPORT (2M)**

Document:-  
Circumstances  
Audit Procedures + Conclusion  
Who made changes + Who reviewed

**5. TYPES OF AUDIT FILE**

- ✓ Permanent Audit File
- ✓ Current Audit File

**6. FACTORS AFFECTING FORM AND CONTENT (5M)**

- (Points are in Sequence of Core Audit Process)
- a. The size and complexity of the entity.
  - b. The identified risks of material misstatement.
  - c. The nature of the audit procedures to be performed.
  - d. The audit methodology and tools used



- e. The significance of the audit evidence obtained.
- f. The nature and extent of exceptions identified.
- g. The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained.

### **7.COMPLETION MEMORANDUM/ SUMMARY OF COMPLETION ( NOT COMPULSORY)(3M)**

1. Good for future Reference to Audit Document.
2. Effective and Efficient review can be made by future auditor
3. Significant matters are again checked

### **9. AUDIT NOTE BOOK (4M)**

Part 1

- Internal info (General Info)

Part 2

- Special Matters

Importance of Audit Note (Similar to Advantages)

- Audit Process Value
- Control value
- Evidence Value
- Report Finalization Value
- Planning Value
- Protection Value

### **SA 240-FRAUD**

Fraud: - Intentional Mis-statement which is Material to Financial Statement

Error : - Unintentional Mis-Statement, by Mistake

### **1.TYPES OF FRAUD(4M)**

- a.Fraudulent Financial Reporting, and
- b.Mis-appropriation of Assets.

*DEFALCATION OF CASH*

- a.By inflating cash payments
- b.By suppressing cash receipts
- c.By casting wrong totals in the cash book

*DEFALCATION OF STOCK*

### **2.CHARACTERISTICS OF FRAUD(4M)**

- a.Intentional Act
- b.Concealed
- c.High Detection Risk
- d.Judgment Areas

### **3.FRAUD TRIANGLE(Reasons)**

Or

### **FRAUD RISK FACTOR (2M)**

1. Pressure / Incentive
- 2.Opportunity
- 3.Rationalization / Attitudes

### **4.REQUIREMENT OF SA-240(6M)**

#### **PART 1(Enquiry)**

- I.Enquiring **TCWG**(Para 20 & 21)
- II.Enquiring **Management and Others** within the Entity(Para 17)
- III.Enquiry with **Internal Auditor**

#### **Part 2(Response) 1**

- IV.**Overall** Responses (Para 28 & 29)
- V.**Responses** at Assertion Level (Para 30)
- VI.Responses to Risks Related to **Management Override of Controls** (Para 31-33)

**Part 3 (Alert)**

VII. Evaluate **Fraud Risk Factors** (Para 24)

VIII. **Unusual or Unexpected Relationships** Identified (Para 22)

IX. **Other Information** (Para 23)

**5. WITHDRAWAL FROM AUDIT**

Where circumstances indicate inability to perform Audit  
Because of fraud or suspected Fraud.  
Inform Mgmt or TCWG

**6. IS AUDITOR RESPONSIBLE FOR FRAUDS DETECTED AFTER SUBMISSION OF AUDIT REPORT?**

Whether auditor has performed audit carefully as per standards on auditing Eg Ethical Requirements & Independence / Planning / Risk Assessment / Response to risk which he can prove with his documents and other evidences then he is not responsible as auditor never give guarantee for detecting all misstatements due to fraud or error, he simply gives reasonable assurance.

Examples of Fraud Risk Factors

	Fraudulent Financial Reporting (FFR)	Miss Appropriation of Assets (MAA)
Pressure / Incentive	Pressure 1. "Financial stability or profitability is threatened by economic, industry, or entity operating conditions (Competition / Saturation / Rapid changes / failure in industry or economy / bankruptcy / take over negative cash flows) 2. Excessive pressure exists for management to meet the requirements of expectations of third parties	Pressure 1. Personal financial obligation

	(Analyst / investors / creditors / new debt or equity / SEBI to comply with listing agreement) 3. Pressure from TCWG to achieve targets  Incentive 4. Information available indicates that the personal financial situation of management or those charged with governance" (Significant financial interest / big portion is variable / personal guarantees)	
Opportunities	1. "Significant related party transactions not in ordinary course audited by other or not audited. 2. Ability to dominate in industry (in appropriate or arms length transactions) Many assets & liabilities depend on subjective judgement 3. Significant operations located across international borders 4. Use of business intermediaries with no justification 5. bank accounts & subsidiaries in tax haven 6. The monitoring of management is not effective (Domination by single person	1. "Characteristics a. FA or Inventory small in size / movable / marketable / lacking observable identification of ownership b. Easily convertible investments such as bearer bonds / diamonds / computer chips c. Large amount of cash in hand  2. Inadequate ICS a. Inadequate oversight of senior management b. Lack of understanding in management over IT



	<p>or by small group)                  7.Complex or unstable organisation structure)                  8.Internal control components are deficient"</p>	<p>c.Lack of controls over automated transactions                  d.Inadequate job application screening                  e.No Segregation of duty                  f.Inadequate system of authorisation                  g.Inadequate record keeping of assets                  h.Inadequate physical safeguards                  i.Lack of timely &amp; appropriate reconciliation &amp; documentation                  j.Lack of mandatory leave for employees"</p>
Rationalization / Attitude	<p>"Attitude:-                  1.Communication of Inappropriate values or ethical standards, that are not effective.                  2.Non-financial management's excessive participation in or preoccupation in estimation process                  3.Known history of violations of securities laws or other laws                  4.Excessive interest in increasing or maintain earning trend / stock price                  Rationalisation                  1.Low morale among senior</p>	<p>"Attitude:-                  (Management)                  a.Intolerance to petty theft                  Disregard to monitor / reduce risk of MAA                  b.Disregard to ICS over MAA                  (Employee)                  c.Changes in behaviour or lifestyle                  Rationalization:-                  (Employee)                  a.Behaviour indicating displeasure / dissatisfaction                  b.Adverse relationship between entity &amp;</p>

	<p>management.                  2.Dispute between shareholders in a closely held entity.                  3.The relationship between management and the current or predecessor auditor is strained"                  5.Omitting to achieve aggressive or unrealistic forecasts                  6.Inappropriate means to minimize Reported earnings for tax-motivated reasons.</p>	<p>employees (Anticipated / known layoffs or change in compensation or promotion etc)"</p>
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**SA- 250 Laws and Regulations in an Audit**

**1.MANAGEMENT'S RESPONSIBILITIES (4M)**

- Prevention & Detection of non-compliance*
- Monitoring Legal requirements*
- Establishing IC.*
- Developing Code of conduct.*
- Training*
- Engaging Legal Advisors.*

**2.AUDITOR RESPONSIBILITIES (4M)**

- 1.Obtain general understanding** of legal & Regulatory Framework
- 2.Obtain Evidence for:-**
  - A.**Compliance if it has Direct Effect
  - B.**Non – compliance if it has No Direct Effect
- 3.Remain alert (Professional Skepticism)**
- 4.WR from mgmt.**

**3. CLASSIFICATION OF LAWS (4M)****Direct effect** on determination of amount & disclosures of FST

Eg. Tax laws/ Depreciation/ Schedule VI/ POGA/ POBA

Obtain **sufficient & appropriate evidence** about compliance[In case of direct effect auditor have to check in detail and obtain evidence about **compliance**]**No direct** effect on financial statements but affects

- Continuity of business
- Can result in material penalties  
Eg. Environment Act/ Labour Laws

Obtain evidence about non-compliance

Perform only specified audit procedure like enquiry from management, TCWG, **about non-compliance & check correspondence with authorities****4. NON COMPLIANCE (4M)****When non-compliance is identified as suspected**

Obtain understanding of Act

Circumstances

Effect on financial statements

Litigation/ Penalty / Going Concern/ Disclosure Requirement

Discuss with Mgmt &amp; TCWG

**Obtain legal advice if requirement****5. INDICATORS FOR NON COMPLIANCE (4M)**

Investigations/ Fines &amp; Penalties/ Unexplained payments to consultants/ Adverse Media Comment etc

**6. REPORTING REQUIREMENTS (4M)**

- Reporting responsibilities – To Mgmt.
- Reporting responsibilities – To TCWG
- Audit Report
- Reporting responsibilities – To Regulatory & Enforcement Authorities

**SA 260 COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE (TCWG)****1. DEFINITIONS & MATTER TO BE COMMUNICATED (5M)****Those charged with governance –**

- The person(s) or organization(s) (e.g., a corporate trustee) with **responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity.**

*Matters to be communicated*

- The Auditor's **R**esponsibilities in Relation to the Financial Statement Audit:
- **P**lanned Scope and Timing of the Audit
- **S**ignificant Findings from the Audit
- Auditor **I**ndependence (Only in Listed Co)

*Communication process (writing or oral & on timely basis)***Factors Affect (Writing V/ S Oral)**

- Legal requirements.
- Expectations of TCWG
- Size, operating structure, control environment, and legal structure of the entity.
- Special purpose or General purpose financial statements.
- Significant changes in the membership of a governing body.

**LEGAL OR REGULATORY RESTRICTIONS ON COMMUNICATING WITH TCWG (2M)**

That might prejudice an investigation



**SA 265 DEFICIENCIES IN INTERNAL CONTROL****1. MEANING OF DEFICIENCIES & SIGNIFICANT DEFICIENCY IN I.C & COMMUNICATION (6M)***Deficiencies in I.C*

Absence of control or Inability of I.C to prevent detects & corrects misstatement.

*Significant Deficiency*

Means deficiency either material misstatement already occurred or likelihood [very much chance] that material misstatement could occur.

**2. Requirements**

- a) Perform audit procedures as per SA 315 & SA 330
- b) Is there a deficiency?
- c) Is it a significant deficiency?
- d) Inform TCWG all significant deficiency in writing.
- e) Inform to Management about significant deficiencies and other deficiency unless inappropriate.
- f) Content of Communication  
Description & Clarification

**3. INDICATORS OF SIGNIFICANT DEFICIENCIES (4M)**

Evidence of **ineffective aspects of control environment**

Entity's Risk assessment process- **Absent/ ineffective**

**Ineffective response** to identified significant Risks

**Correction of prior period misstatements** arising due to fraud/ error

Management **inability to oversee** F.S. Preparation

Misstatements detected by the auditor's procedures were not **prevented, or detected and corrected by the entity internal control.**

**4. CONTINUOUS DEFICIENCY (2M)**

Report in CARO

Significant Deficiency: - Repeat Communication

Other Deficiency:- No need to repeat

**SA-299 JOINT AUDITORS****1. JOINT AUDIT ADVANTAGES & DISADVANTAGES (4M)**

When **two or more practicing units** are appointed to. Conduct audit of an entity it is called joint audit.

**Advantages**

- **Pooling and sharing of resources** [like equipment, experts, team member]
- Better **quality of work** performance; [improves quality of work]
- Advantage of **mutual consultation**;
- Everyone has **Expertise in different area**
- If one auditor leave the audit than other will continue
- Improved **services to Client Company**;
- **Lower costs** to carry out the audit work.

**Disadvantages**

- **Co-ordination** problems in **conduct of work**;
- **Sharing of fees.**
- Areas of **common concern** being neglected;
- Lack of clear definition in case of **joint responsibility**;
- Problems when Firms of different standing are associated

**2. BASIS OF DIVISION & DOCUMENTATION (2M)**

Joint Auditor should divide work among them on basis of-

**I. Period;**

II. Functional **areas**;

III. **Components** of financial statement; or

IV. Geographical **location. etc.**

**Documentation**

Such division should be adequately documented.

**3. CO-ORDINATION (3M)**

If one auditor comes to know a matter relevant/ related to area of audit of other joint auditor, he should communicate it in writing immediately or before submission of report or at the time of report to other joint auditor.

**4. RESPONSIBILITY (4M)**Separate responsibility of each Joint Auditor

- For **work** allocated to him
- For drafting his own audit **program and planning**
- For **understanding the ICS** of area for which work is allocated
- For **execution** of audit program
- For **fraud, error, negligence**.
- For keeping appropriate **documentation**
- **For components** allocated to him in case of large entities having many components. [Means branch, joint venture etc.]

Joint and several responsibility of all Joint Auditors

- General planning audit strategy like nature, timing, extent of audit
- Audit work not divided
- New Matters brought to knowledge of all by any one of them and on which they all agree to do audit jointly.
- Presentation & Disclosure requirements in financial statement [e.g. disclosure as per Sch. VI]

Compliance of Audit Report with statutory requirement.

**5. RELIANCE ON OTHER JOINT AUDITOR'S WORK (2M)**

Generally Each joint auditor is entitled to assume that the other joint auditors have carried out their part of the audit work in accordance with the generally accepted audit procedure. And there is no need to review work done by other Joint Auditor.

If fraud is detected in any area then respective joint auditor is responsible, not all.

**6. DIFFERENCE OF OPINION (2M)**

(Separate Report)

Generally all arrive at unanimous opinion. However, any joint auditor is not bound by majority opinion. Those disagreeing with others may provide their own opinion through a separate report.

## CA-FINAL & IPC **AUDIT** QUICK REVISION

For May'16 Exam




<b>AHMEDABAD</b>	<b>1<sup>st</sup> April</b>
<b>PUNE</b>	<b>3<sup>rd</sup> April</b>
<b>MUMBAI</b>	<b>5<sup>th</sup> April</b>
<b>DELHI</b>	<b>8<sup>th</sup> April</b>
<b>NAGPUR</b>	<b>11<sup>th</sup> April</b>
<b>RAIPUR</b>	<b>13<sup>th</sup> April</b>
<b>KOLKATA</b>	<b>15<sup>th</sup> April</b>



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 Course Coverage with Short Notes  
**Revise SAs + Ques. of PM & 3 RTPs**









**SA 300 PLANNING AN AUDIT OF FINANCIAL STATEMENTS****SA-MAP****1. Preliminary Engagement Activities (PEA)**

(Conducted before planning starts)

**2. Establishing Overall Audit Strategy**

(Overall plan, first step in planning)

**3. Develop an Audit Plan**

(It is a detailed step by step instruction for 3 areas)

**4. Planning Direction / Supervision / Review (DSR)**

(This plan is important for execution of Audit Plan)

## Miscellaneous Points

**5.** Involvement of key engagement team members (Seniors should be involved)

**6.** Updates to Overall Strategy (Changes should be made as and when new information is received)

**7.** Additional Considerations in Initial Audit Engagements (2 extra points in first audit)

& Finally

**8.** Advantages & Disadvantages of planning & How to overcome them.

**1. Preliminary Engagement Activities (PEA)**

(Conducted before planning starts)

a. Acceptance (If initial audit engagement covered in latter point) / Continuance (If it is recurring audit) -> 4 Points to be covered are given in SA 220

b. Understanding the terms of engagement (once it is signed study it and take steps for implementation)

c. Compliance with Ethical Requirements & Independence Requirement (Appropriate decisions to ensure that team is ethical & independent)

When we perform above activities it helps in planning. Below are the examples for the same.

i. Acceptance / Continuance :- Integrity of Management :- Information from legal head is not reliable as it is filtered and manipulated hence such information should be always corroborated with external evidence

ii. Engagement Letter: - New branches should be audited always by Principle Auditor for first 2 years, so make appropriate arrangement in consultation with management.

iii. Independence :- Our team has past employees from northern office of company so they should not be sent to audit of northern region otherwise there will be Conflict of Interest.

**2. Establishing Overall Audit Strategy (Overall plan, first step in planning)****(R-CRPF)**

**R-** Resources (Nature / Timing & Extent)

**C-** Characteristics of Assignment

**R-** Reporting & Communication

**P-** Preliminary Engagement Activities Results

**F-** Significant Factors

Resources

a. Engagement Budgeting (Estimated time required for overall audit and specific areas, depending on RMM)

b. Selection of Engagement Team

c. Assignment of work, experienced members for higher RMM / Complex areas / where expert is involved

d. Assignment of resources for inventory counting, review of other auditors, dealing with service organisation etc

e. Determining time & team for interim audit

f. Who will manage and how much time will be invested:- direct / supervise / review work of team

Characteristics of Assignment

a. Industry-specific reporting requirements (Banking / Insurance etc)

b. Financial reporting framework (AS / IFRS)

c. Only audit or audit + Review of Interim Financial Statements

d. Audit of standalone or consolidation or both

- e.Number and locations of components to be included.
- f.Components are audited by other auditors.
- g.The nature of the control relationships between a parent and its components
- h.The nature of the business segments
- i.The reporting currency to be used,
- j.The effect of information technology & use of CAAT
- k.The availability of the work & extent on reliance on work of internal auditors
- l.Audit evidence obtained in previous audits
- m.Use of service organizations
- n.Availability of client personnel and data.

### Significant Factors & Preliminary Engagement Activities (CRIM)

#### Changes

- a.Significant business developments: - Acquisitions / Mergers / Divestments, Changes in industry regulations / new reporting requirements / business processes / key management / information technology / FRF / Legal Environment

#### Risk

- b.Preliminary identification of *areas where there may be a higher risk of material misstatement*.
- c.The *impact of the assessed RMM* at the overall financial statement level on *DSR*
- d.Emphasizes on exercising *professional scepticism*

#### Internal Control System

- e.Results of previous audits on operating effectiveness of internal control /deficiencies & action taken
- f.Experience of performing other services to the entity.
- g.Commitment to the design, implementation, maintenance & documentation of ICS
- h.Importance attached to ICS
- i.Volume of transactions affects decision to rely more on ICS

#### Materiality

- j.Determination of *materiality*  
(Materiality for *components* & communication thereof to component auditors)
- k.Significant components and *material classes of transactions, account balances* and disclosures

### 3.Develop an Audit Plan

(It is a detailed step by step instruction for 3 areas)

- a.NTE of planned risk assessment procedures
- b.NTE of planned further audit procedures at the assertion level (Test of Controls & Substantive Procedures)
- c.Plan other audit procedures to comply with specific SAs (SA 550 / SA 560)

### 4.Planning Direction / Supervision / Review (DSR)

(This plan is important for execution of Audit Plan)

- NTE of such planning depends on  
Size / Complexity of Business (Ship Manufacturing Vs Trading) / Assessed RMM / Area of Audit (Inventory Vs Share Capital) / Competence & Capability of Team Members

### 5. Involvement of key engagement team members (Seniors should be involved)

Engagement Partners & Other Key Members should be involved. Their experience and insight, thereby enhancing the effectiveness and efficiency of the planning process.

### 6.Updates to Overall Strategy (Changes should be made as and when new information is received)

- a.Significant changes in the accounting organisation, procedures and personnel subsequent to the audit procedures.
- b.Volume of transactions increased substantially post planning
- c.Suspicion is aroused regarding misappropriation or other frauds
- d.Extra Ordinary Increase in closing amount of Inventory & Debtors as compared to previous years



7. Additional Considerations in Initial Audit Engagements (2 extra points in first audit)

1<sup>st</sup> Carefully determine Acceptance & 2<sup>nd</sup> Communicate with previous auditor.

Auditor may consider following matters also

- a. Discussion of major issues identified during acceptance procedures with management & TCWG (Bribing practices in company & its impact on audit team)
- b. Arrangement with previous auditor like discussion / review of working papers if client agree.
- c. Evidence regarding opening balance
- d. Compliance with firm's policy w.r.t initial audit engagements (For Example requirement that audit strategy of first audit should be reviewed by another partner or senior individual)

8. Advantages & Disadvantages of planning & How to overcome them.

Advantages:- appropriate selection & assignment of work / responsibility & accountability of work delegated improves / clear set of instructions to juniors / systematic plan with proper emphasis on important areas / less chances of overlooking eg EPS checking omitted / identify & resolve potential problems eg need of expert in inventory determination & valuation / helps in co-ordination with other auditors / helps in controlling / supervising audit work / serves as guide in succeeding years / serves as evidence in case of charge against negligence

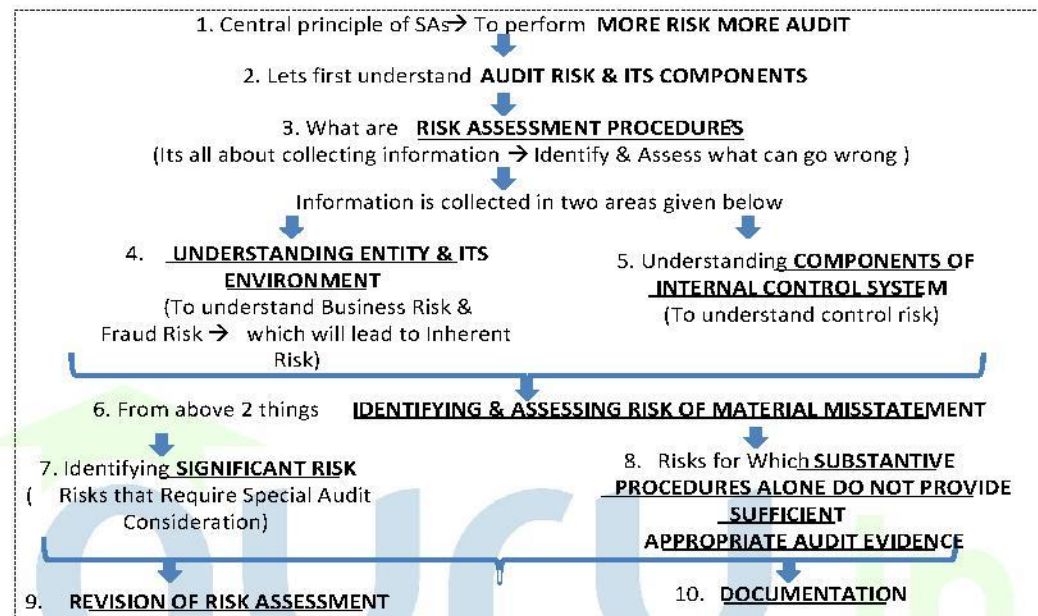
Disadvantages:- Fixed Pattern Not Applicable/ Rigid/ Mechanical / Good for inefficient assistants / Bad for efficient assistants

Measures to overcome disadvantages of audit programme

Suitability/ Review Internal Controls / Changes in Business / Participative / Flexibility / Minimum Requirement

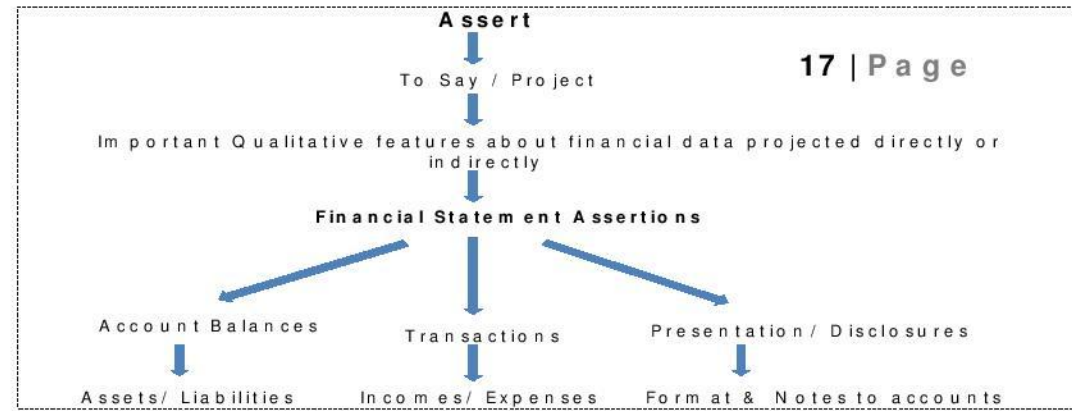
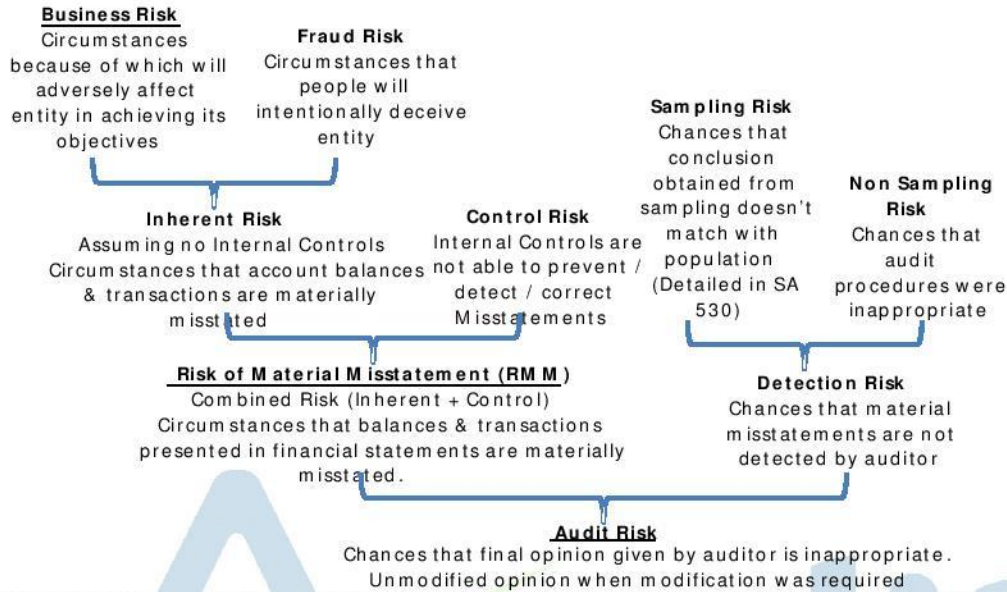
**SA 315:- IDENTIFYING AND ASSESSING THE RISK OF MATERIAL MISSTATEMENT THROUGH UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT**

**SA MAP**



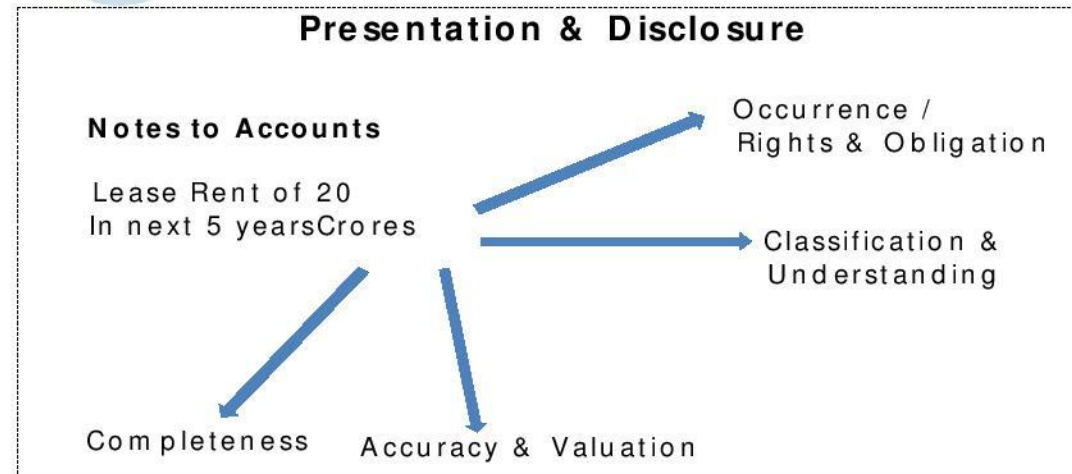
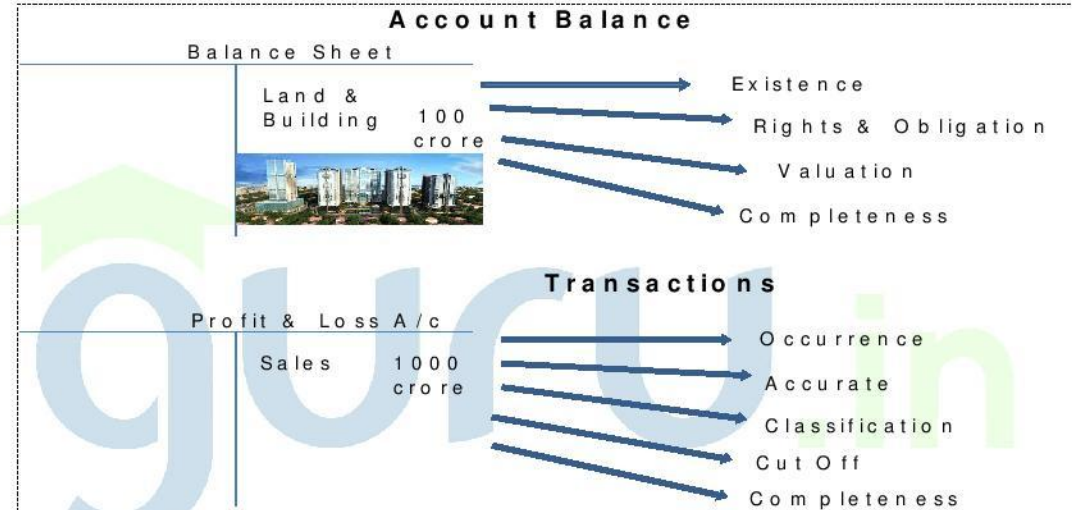
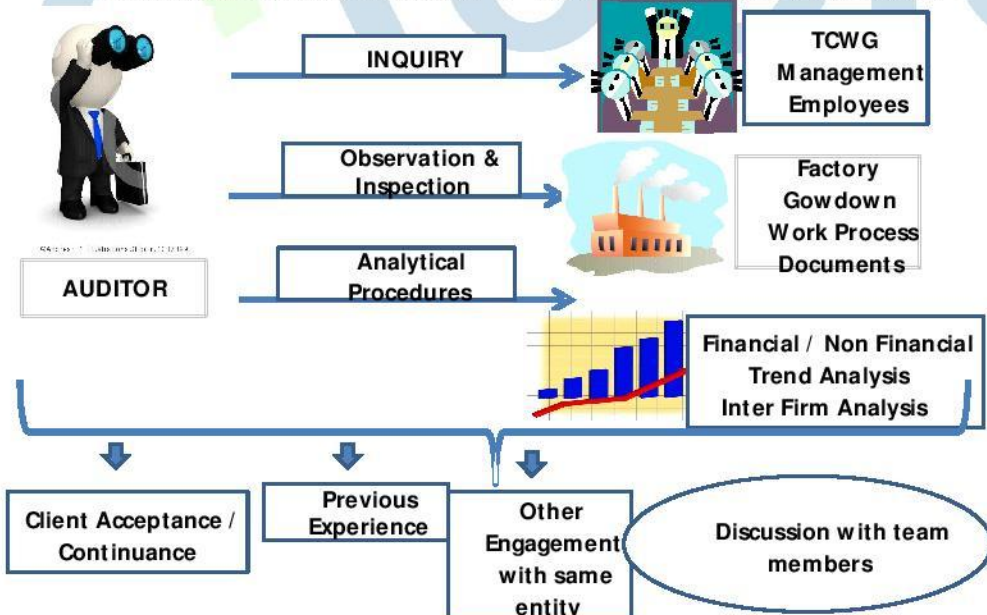
1. Central principle of SAs -> To perform "MORE RISK MORE AUDIT"

Risk	Salary Checking
No Risk	Random selection & checking of 100 Salary Slips + Analytical Procedures
Risk of Material Misstatement (Complex Pension & Gratuity)	+ Appointment of Actuary as Expert
Significant Risk (Fake Employees)	+ Head Count at all locations + Photo & Address Identity



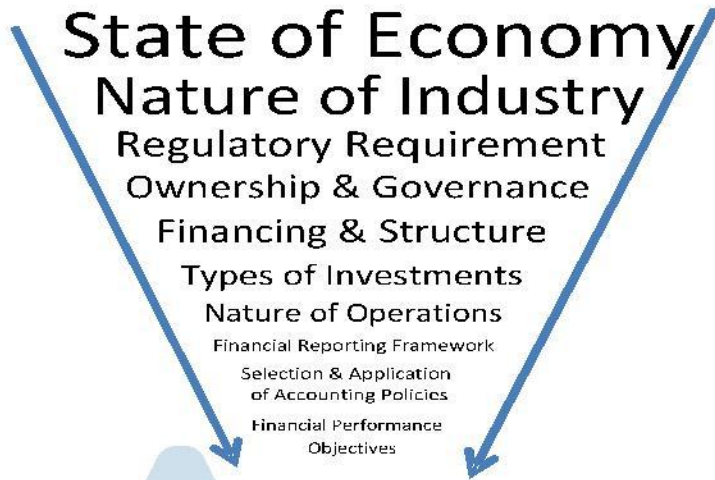
3. RISK ASSESSMENT PROCEDURES

(Its all about collecting information → Identify & Assess what can go wrong)





4. UNDERSTANDING OF THE ENTITY AND ITS ENVIRONMENT



Experience / Stature / Independence from Management / Extent of Involvement / Information received by them / Scrutiny of activities / Degree of difficult questions raised & pursued by management / Interaction with internal & external auditors

c.Management

Philosophy & Operating Style:- Taking & Managing Business Risks / Attitude & Action towards FRF , Information Processing , Accounting Functions & Personnel

d.Commitment to competence

e.Human resource policies and practices

f.Assignment of authority and responsibility

g.Organisation Structure :- To plan , execute , control and review activities

5. COMPONENTS OF INTERNAL CONTROL



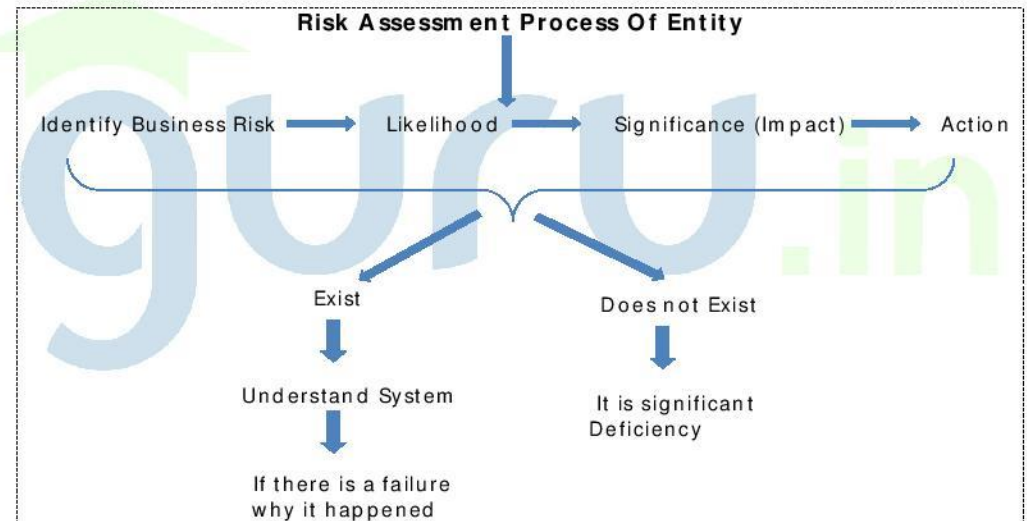
1.Control environment (Base for all other elements)

It is attitudes, awareness, and actions of TCWG & Management towards ICS also whether culture of organisation has honesty & ethical behaviour.

Elements of Control Environment

a.Communication and enforcement of integrity and ethical values

b.TCWG



2. Risk Assessment Process of Entity

3.Control activities relevant to audit

Understanding of only those control activities related to significant class of transactions, account balance, and disclosure in the financial statements and the assertions which the auditor finds relevant in his risk assessment process. (Segregation of Duties / Authorization / Performance Reviews / Physical Verifications)

**4. Monitoring of controls**

(Supervision Activities / Internal Audit / External Inspection Reports / Customer Complaints / Suggestions for Improvements)

**5. Information System & Information Technology**

Significant Classes of Transactions / IT & Manual systems to initiate, record, process & report transaction / Controls surrounding journal entries, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments / financial reporting process / information system captures events and conditions, other than transactions, that are significant to the financial statements;

**6. Identifying and Assessing the Risks of Material Misstatement**

Financial Statement Level & Assertion Level

I. These risks can be identified while understanding entity & its environment and relevant controls

II. Considers likelihood of misstatement & its magnitude

III. Evaluate whether it relates more pervasively to the FTS and potentially affect many assertions

**7. Risks that Require Special Audit Consideration (Indicators of Significant Risk)**

The auditor shall exclude the effects of identified controls related to the risk while making judgement of significant risk.

CFO-CSR

C- Significant **C**hanges in economic, regulatory, accounting

F- Is it a **F**raud Risk

O- **O**utside the normal course of business

C- **C**omplexity of Transactions

S- **S**ubjectivity in measurement

R- **R**elated Parties involved

**8. Risks for Which Substantive Procedures Alone Do Not Provide Sufficient Appropriate Audit Evidence**

NI-IPC

→ Highly automated processing with little or no manual intervention.

→ Controls are automated and initiation, processing, accuracy depends on system

→ Audit evidence may be available only in electronic form

**9. Revision of Risk Assessment**

Where the auditor obtains audit evidence from performing further audit procedures, or if new information is obtained, either of which is inconsistent with the audit evidence on which the auditor originally based the assessment, the auditor shall revise the assessment and modify the further planned audit procedures accordingly.

**10. Documentation**

→ Key elements in understanding entity & its environment and components of internal control system

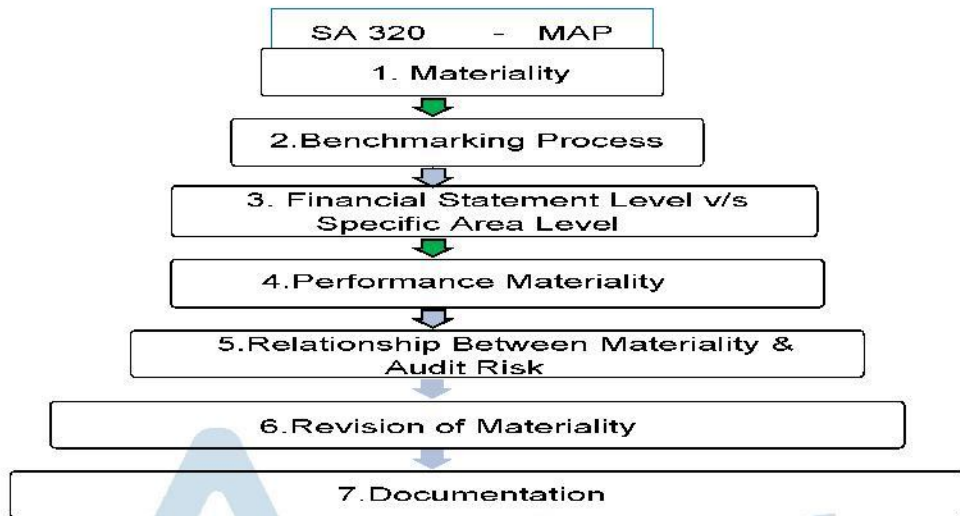
→ Discussion among the engagement team

→ Identified risk at financial statement & assertion level

→ Relevant controls which cover identified risk



**SA 320 MATERIALITY IN PLANNING AND PERFORMING AN AUDIT**



1. Materiality

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;

Materiality depends on factors given below (It is matter of Judgment)

Quantity:- Size

Quality:- User Needs / Nature / Circumstances (As explained ahead)

2. Benchmarking

A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole.

Benchmark (Base) x Percentage = Materiality

Eg

Profit	x	5%
Total Assets	x	1%
Total Turnover	x	0.5%

Step 1:- Decide Benchmark (Base)

Apple LOVE

A- Attention of the users (PVT Sector-Profit/ PSUs -Turnover/ Charity- Corpus)

L-Life Cycle & Industry & Economic Environment (Flipkart Vs Reliance)

O-Ownership Structure & Financing (Big Vs Small Shareholder / Debt Vs Equity)

V-Volatility (Volatility may lead to big changes in materiality & all audit procedures, hence less volatile is more preferred)

E-Elements of Financial Statements

Step 2:- Normalization (Adjusting Base)

Adjust for following factors

Time Period:- Previous Financial Period was 9 months which should be proportionately increased to 12 months

Changes in Business Entity:- Acquisitions / Mergers / Demergers

Economic Environment:- If Boom → Increase / Recession → Decrease

Abnormal Items:- Should be excluded

Step 3:- Determine Percentage

Generally as benchmark quantum increases lower percentages are used, for example percentage keeps reducing if we change base from Profits to Total Assets to Total Turnover

3. Financial Statement Level v/s Specific Area Level

Materiality is generally determined at financial statement level, if circumstances require we can have LOWER materiality for specific area not higher, if users can get influenced even with relatively smaller amounts.

a.Law / Regulation / FRF prescribes disclosure requirements and limits hence user carefully analyses them hence lower specific materiality is required (Eg Related party transactions / Managerial Remuneration/ CSR Expenditure)

b.Key Disclosures Related to the Industry (Eg Research & Development Expense in Pharmaceuticals or Recall costs in Automobile Industry)

c.Attention is focused on particular aspect of business (New acquired business or discontinuing operations as per AS24)

#### 4. Performance Materiality

Auditor is aware that some misstatements remain uncorrected and some are undetected. Hence there should be some margin for such misstatements while planning audit. Hence auditor shall determine performance materiality which is less than materiality (50% to 90%) of materiality at financial statement level or specific area level. It is used determining RMM, and NTE of further audit procedures.

Performance materiality is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in the financial statements exceeds materiality for the financial statements as a whole.

#### 5. Relationship Between Materiality & Audit Risk

Materiality and audit risk are considered throughout the audit, in particular, when:

- Identifying and assessing the risks of material misstatement;
- Determining the nature, timing and extent of further audit procedures; and
- Evaluating the effect of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report.

Not given in SA 320 but important

Further there is inverse relationship between materiality and audit risk, if materiality is more we do more audit procedures which reduces audit risk.

#### 6. Revision of Materiality

If auditor gets additional information then he should revise materiality, for example

- Change in base → Anticipated profit was taken as benchmark but actual profits were significantly higher so base was revised which lead to change in materiality
- New discourse requirement of law / regulation / FRF Eg Salient Features of Subsidiary
- New aspect of business Eg New acquisition or disposal

#### 7. Documentation

Materiality for the financial statements as a whole. / Specific Area Level Materiality / Performance materiality / any revisions.

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**Ques. of PM & 3 RTPs**









**1. (4M) Risk at Financial Statement Level is identified**  
 → So we give for overall response to such risk

1. More Experienced Staff
2. Involve Expert
3. Increase Supervision
4. Audit Procedures should be unpredictable
5. Change audit procedures to get more persuasive evidence

SA 330  
 Response to Risk (Audit Procedures)

Before applying 330, SA 315 is applied and risks are identified at 2 levels

Risk at Assertion Level  
 For this risk we can use combination of

NI-IPC, Refer  
 Ch:- ICS

7. Substantive Procedures

Irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure.

The auditor shall consider whether external confirmation procedures are to be performed as substantive audit procedures. (Most Reliable and takes time)

2. Test of Controls

NI-IPC, Refer  
 Ch:- ICS

All controls are not checked, only those controls are checked which are

1. Marked relevant at the time of risk assessment, which are compensating risks.
2. Where substantive procedures alone cannot sufficient audit evidence

Design & Perform audit procedures to understand:- Who applied controls / By what means / Consistency of application / during the relevant times during the year

**Indirect Controls:-** Controls may be affected by performance of other controls, for example software based automated controls depends on general IT Controls.

**Nature and Extent**  
 Auditor may determine that:

- (a) Performing only substantive analytical
- (b) Only tests of details are appropriate.
- (c) A combination of substantive analytical procedures and tests of details

**Interim Date (Timing)**  
 Cover the remaining period by performing:

- a) Substantive procedures, combined with tests of controls for the intervening period; or
- b) If the auditor determines that it is sufficient, further substantive procedures only; that provide a reasonable basis for extending the audit conclusions from the interim date to the period end.

**Nature**  
 Inquiry is one of the most important procedures but other like Observation, Inspection, Recalculation, and Reperformance should be used depending on circumstances

**(4M) Extent**

1. Frequency of Performance
2. Length of time
3. Expected rate of deviation
4. Relevance & Reliability of Audit Evidence
5. Other test of controls

**3. (4M) Interim Period (Timing)**  
 We can use audit evidence obtained during interim period provided he gets evidence for

1. Significant Changes to those controls
2. Effectiveness over remaining period

L-CARDS  
 L-Length of Remaining Period | C-Control Environment | Assessed RMM | Reduction in Substantive Procedure Intended | Degree of AE obtained | Significant Changes

↓

#### 4. Using audit evidence from previous audits

LG ki M ERC

- 1. Lack of a change
- 2. Effectiveness of General IT-controls
- 3. Risks arising from the characteristics of the control (Manual Vs Automated or Internal Staff Vs External or Documents Available)
- 4. Effectiveness of the control and its application by the entity (SAP Vs Tally)
- 5. RMM (Stock Vs Share Capital)
- 6. Effectiveness of Control Environment / RAP / Monitoring Controls

The auditor shall test the controls at least once in every third audit

NI-IPC, Refer  
Ch:- ICS

NI-IPC, Refer  
Ch:- ICS

#### 6. Evaluating the Operating Effectiveness of Controls

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 tests of controls that have been performed provide an appropriate basis for reliance on the controls; (Signature by Junior, Occasional or Regular)
- (b) Additional tests of controls are necessary; or (Software Failure)
- (c) The potential risks of misstatement need to be addressed using substantive procedures.

↓

#### 5. Controls over significant risks

When the auditor plans to rely on controls over a risk the auditor has determined to be a significant risk, **the auditor shall test those controls in the current period.**

↓

#### 8. Substantive Procedures Related to the Financial Statement Closing Process

The auditor's substantive procedures shall include the following audit procedures related to the financial statement closing process:

- (a) Agreeing or reconciling the financial statements with the underlying accounting records; and
- (b) Examining material journal entries and other adjustments made during the course of preparing the financial statements

↓

#### 9. Substantive Procedures Responsive to Significant Risks

When the auditor has determined that an assessed risk of material misstatement at the assertion level is a significant risk, the auditor shall perform substantive procedures that are specifically responsive to that risk. When the approach to a significant risk consists only of substantive procedures, those procedures shall include tests of details

NI-IPC, Refer  
Ch:- ICS

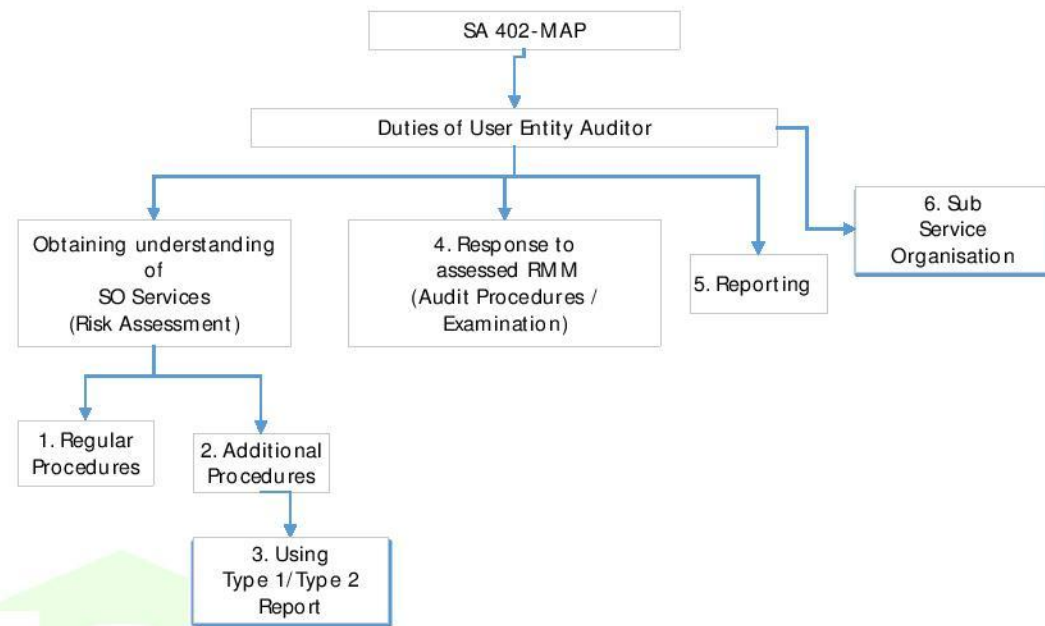
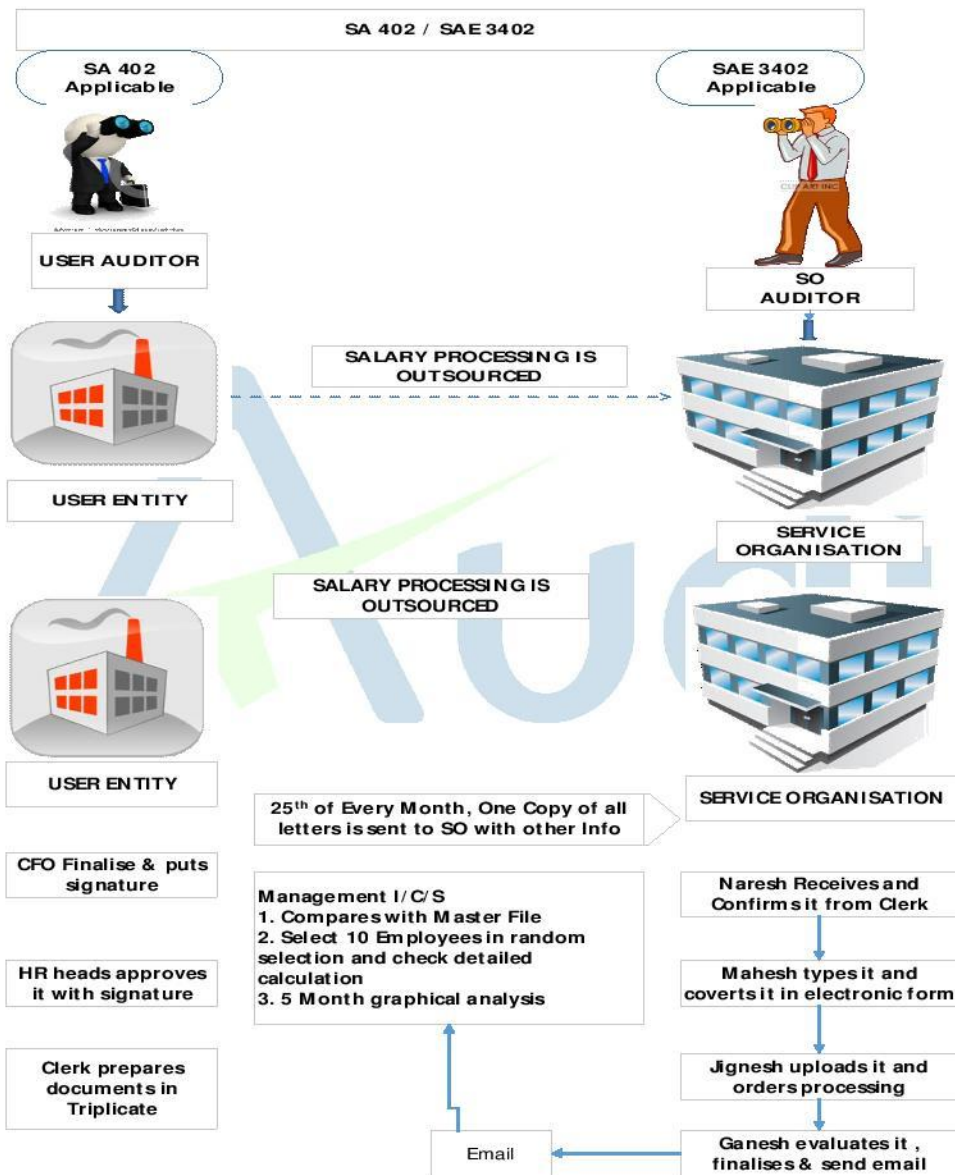
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#### 10. Adequacy of Presentation and Disclosure

The auditor shall perform audit procedures to evaluate whether the overall presentation of the financial statements, including the related disclosures, is in accordance with the applicable financial reporting framework.



**SA 402 AUDIT CONSIDERATIONS RELATING TO AN ENTITY USING A SERVICE ORGANISATION**



**OBTAINING AN UNDERSTANDING OF THE SERVICES PROVIDED BY A SERVICE ORGANISATION, INCLUDING INTERNAL CONTROL:-**

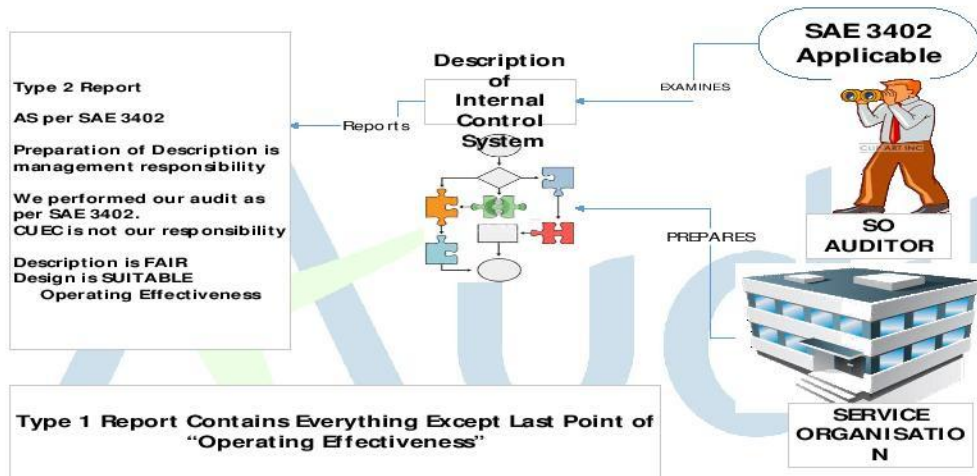
1. Regular Audit Procedures (Which information should be collected)
  - a. Nature of the services
  - b. Significance of those services (production & revenue are more significant than salary processing or advertisement management)
  - c. Effect thereof on the user entity's internal control (Old procedures which are dumped & new procedures which are incorporated, for example now actuary is appointed by SO but we need to high security data transfer & communication)
  - d. Nature and materiality of the transactions
  - e. Nature of the relationship (Subsidiary / BPO / KPO / Independent Party etc) between the user entity and the service organisation, including the relevant contractual terms for the activities undertaken by the service organisation. (MOU / Agreement)
  - f. Auditor shall evaluate the design and implementation of "relevant controls" at the user entity
  - g. Degree of interaction

Sources of Information for above matters.

Contract or Agreement / System overviews / User manuals / Technical manuals / Documents from SO / Report of SO auditor / Internal Auditor

2. Additional Procedures

- a. Contacting the service organisation
- b. Visiting the service organisation
- c. Using another auditor to perform procedures
- d. Obtaining a Type 1 or Type 2 report, if available



3. Using a Type 1 or Type 2 Report to Support the User Auditor Understands of the Service Organisation:-

Whether to rely on Type 1 / Type 2 report depends on 2 things 1<sup>st</sup> Service Auditors Professional Competence & his independence from SO (If he is a CA from ICAI then it is assumed that he is competent) and 2<sup>nd</sup> Which standard he is using to prepare his report Eg SAE 3402

He should be able to understand and evaluate 3 types of controls after reading these reports

- a. Complementary User Entity Controls
- b. Controls at Service Organisation
- c. Relevant Controls at User Entity over services of SO

4. Responding to the Assessed Risks of Material Misstatement:-

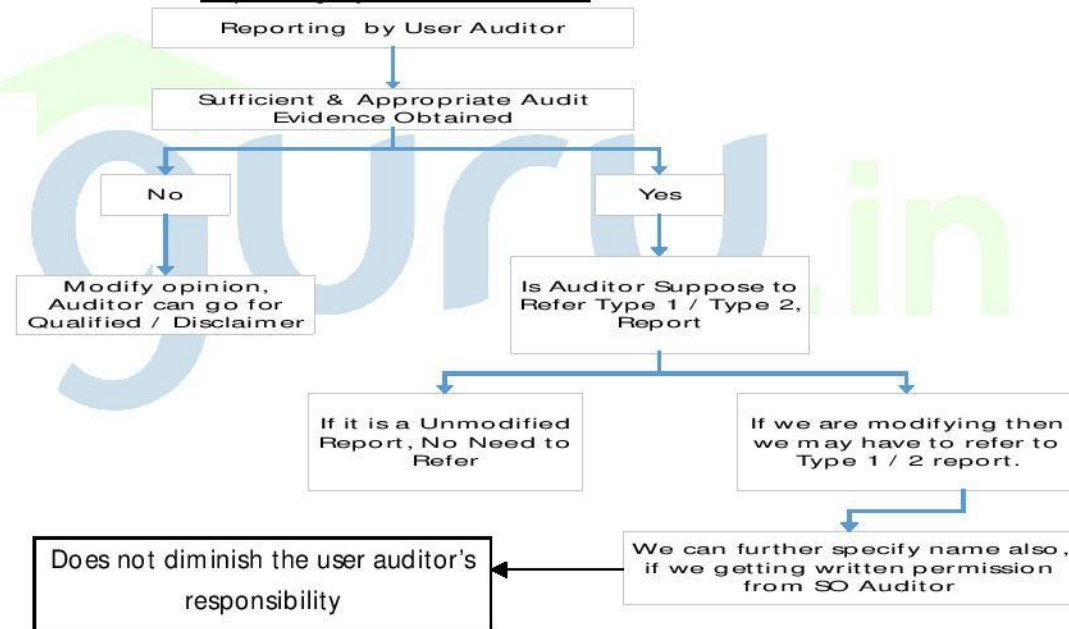
First Test of Controls

- Performing appropriate tests of controls at the service organisation; or
- Using another auditor to perform tests of controls
- Obtaining a Type 2 report, if available;

Then Substantive Procedures

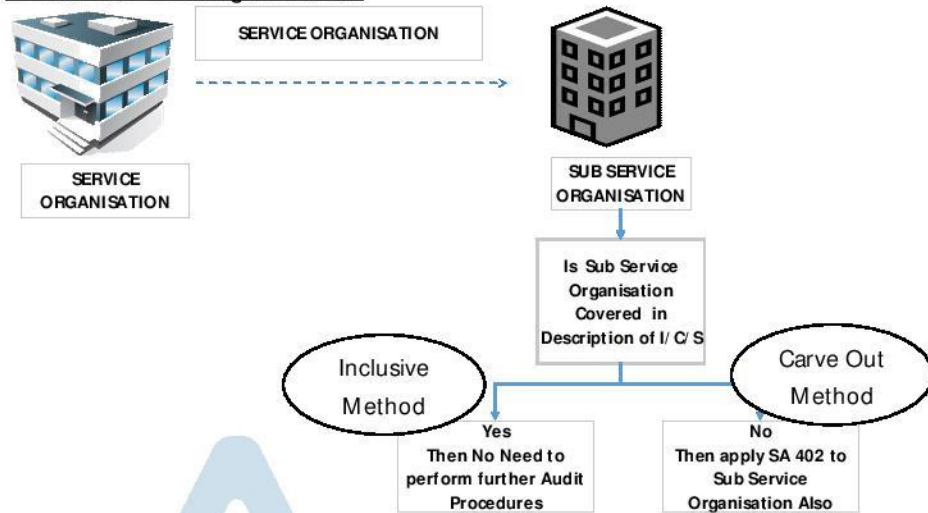
- Inspecting records and documents held by the user entity
- Inspecting records and documents held by the service organisation:
- Obtaining confirmations of balances and transactions from SO
- Performing analytical procedures on the records maintained by the user entity or on the reports received from the service organisation

a. Reporting by the User Auditor





## 6. Sub-Service Organisation



## SA 450

## EVALUATION OF MISSTATEMENTS IDENTIFIED DURING THE AUDIT

SA 450-MAP:-

- 1.Misstatement & Sources
- 2.Types of Misstatement
- 3.What to do when misstatements are detected (Evaluation)?
- 4.Documentation

1.Misstatement & Sources

Difference in what is done and what is expected as per FRF in amounts, classification, presentation, or disclosure.

- a.Omission:- (Supplier didn't send purchase bills on time so some year end bills were omitted)
- b.Inaccuracy in gathering or processing data:- (batch number & expiry details were not properly recorded leading to error in determining expired goods)
- c.Selection or Application of accounting policies inappropriate. (LIFO is selected which is not as per AS 2)

- d.Incorrect accounting estimate (Declaring damaged just looking at outer packing), or clear misinterpretation of, facts(just referred height of WIP & considered stage of completion without looking at weight & dimensions)
- e.estimates that the auditor considers unreasonable.(Inventory will be sold at 0% selling cost)

## 2. Types of Misstatement

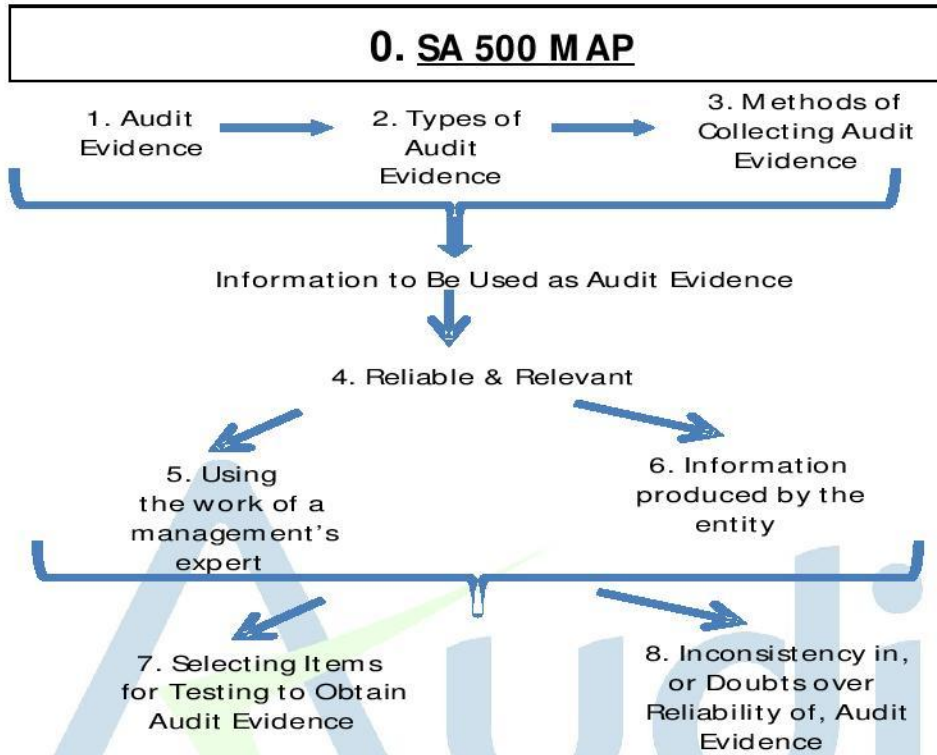
Factual misstatements:- (Number of units in godown with records)

Judgmental misstatements:- (Auditor feels useful life is only 5 years and WDV is proper, management is taking 10 years as life and SLM as method)

Projected misstatements:- (Auditor projects after sampling that discounts in purchases to the tune of 50 lakhs are not properly recorded)

3. What to do when misstatements are detected (Evaluation)?

- Step 1:- Accumulate misstatements unless they are "Clearly Trivial"
- Step 2:- Communicate on timely basis to management and ask them to correct.
- Step 3:- Shall perform additional audit procedures to determine whether misstatements remain.
- Step 4:- if management refuses understand reasons for not making the corrections
- Step 5:- Auditor shall determine whether the overall audit strategy and audit plan need to be revised if: 1<sup>st</sup> It indicates that other misstatements may exist and effect could be material 2<sup>nd</sup> Aggregate of misstatements accumulated during the audit approaches materiality
- Step 6:- The auditor shall reassess materiality
- Step 7:- Determine whether uncorrected misstatements are material, individually or in aggregate.
- Step 8:- Shall communicate with TCWG uncorrected misstatements & request them to correct it (CY & PY)
- Step 9:- Request a written representation from management where effect will be immaterial.
- Step 10:- Consider effect of uncorrected misstatements on Audit Opinion as per SA 705. (Qualify / Adverse)



**1. Audit Evidence**

Anything which gives information to form an opinion (Obtained from client or Prepared by Auditor)

It includes

i. Accounting Records:- Which are prepared specifically for accounting process or output of accounting process. For Example Working for depreciation / Interest / Cost Allocation / Voucher / Primary Books / Secondary Books

ii. Other Information:- Which are prepared for various purposes but which can be used to verify accounting records. For Example Legal Records such as AOA / MOA / BOD Minutes etc, Production Records such as number of units produced & scrap generation or Employee Records such as their personal & professional details.

Auditor uses combination of both to support his opinion. Further it should be Sufficient (Quantity) & Appropriate (Quality:- Reliable & Relevant)

Factors affecting sufficiency & appropriateness

PR<sup>2</sup>IMA

Previous Audit Experience:- No Exp, More Q&Q

Risk of Material Misstatement:- High Risk, More Q&Q (Big Size Company / Complicated Business / Weak Internal Controls/ Weak Financial Position / Situations exerting unusual influence on management)

Results of work:- Many frauds / errors detected during the course of audit, More Q&Q

Information available:- If xerox copies are available, More Q&Q

Materiality:- Higher Materiality, More Q&Q

Analytical Reviews:- If there is fluctuating trends, More Q&Q

2. Types of Audit Evidence

Depending upon NATURE

Visual | Oral | Documentary

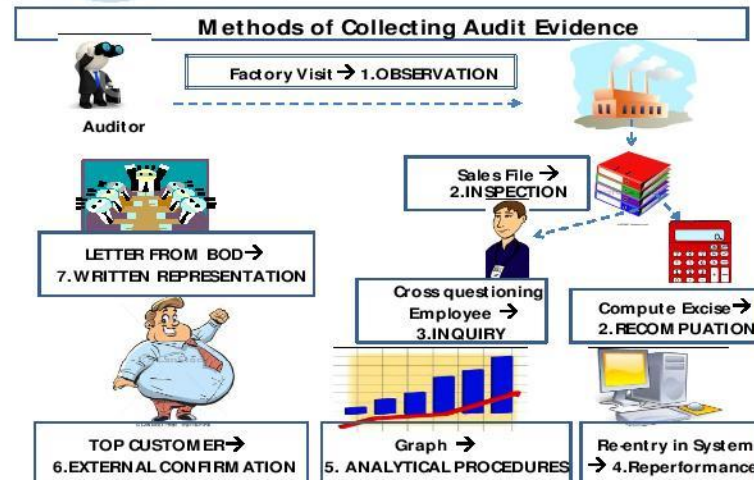
Depending upon IMPACT

Persuasive | Conclusive

Depending upon SOURCE

External | External-Internal

Internal- External | Internal





**4. Reliable & Relevant**

When designing and performing audit procedures, the auditor shall consider the reliability & relevance of the information to be used as audit evidence.

Factors affecting reliability

- i. Evidence from independent source outside entity is more reliable.
- ii. Obtained directly by auditor is more reliable
- iii. Evidence in documentary form is more reliable
- iv. Evidence provided by original documents is more reliable
- v. If internal controls related to preparation & maintenance is strong evidence is more reliable.

Factors affecting relevance

- i. It should cover the purpose of audit procedure. (For Example AE depends on direction of testing, if there is risk of understatement of creditors then we focus on information other than existing creditors i.e last year creditors not in list, new suppliers not in list, unrecorded purchase invoices but if risk of overstatement of creditors we check parties covered in list, take confirmation from them etc
- ii. It should cover relevant all assertions as described in SA 315
- iii. It should cover test of controls
- iv. It should cover substantive procedures

**5. Using the work of a management's expert(1.89)**

Before relying on work done by managements expert, check following things (Similar to SA 620)

- Competence
  - Capable
  - Objectivity
  - Obtain required understanding of the field & experts work
  - Appropriateness of experts work
- (Data used / Methods used / Assumptions / Professional Standards / Legal requirements / Whether expert has area of speciality relevant for audit)

**7. Inconsistency in, or Doubts over Reliability of, Audit Evidence(1.90)**

If: a) Audit evidence is inconsistent or has doubts over the reliability  
Modifications or additions to should be done to audit procedures

**8. Selecting Items for Testing to Obtain Audit Evidence**

i. Selecting all items(100%)

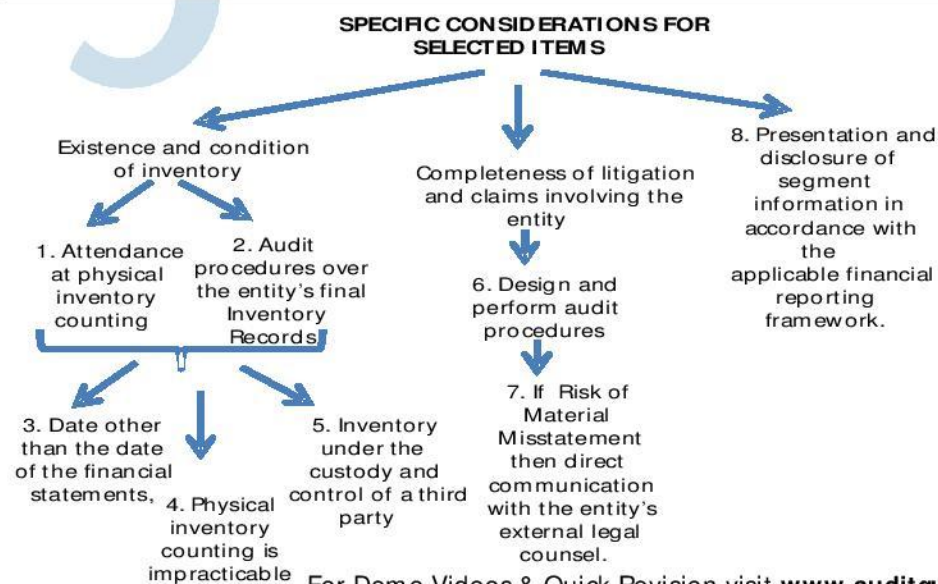
- a. Small number of large value items; (20 Export Sales)
- b. Significant risk  
(In absence of remuneration committee, fixed policy and agreements for remuneration to directors it is significant riskà100% selection)
- c. Cost Effective  
(Depreciation Calculation / Loose Tools Weighing)

ii. Selecting Specific Items

- a. High value or key items  
(Top 5 Customers in Software Industry)
- b. All items over a certain amount.  
(Sale above 10,00,000)
- c. Items to obtain information.  
(All transaction related to Australian branch)

iii. Audit Sampling

**0. SA 501 MAP**





Existence & Condition of Inventory1. Attendance at physical inventory count

\*Perform unless impracticable

- i. Evaluate management's instructions and procedures
- ii. Observe management's count procedures
- iii. Inspect the inventory
- iv. Perform test counts

2. Audit procedures over the entity's final inventory records to determine whether they accurately reflect actual inventory count results.Evaluate Management's Instructions and Procedures

- i. Control over the movement of inventory
- ii. Application of appropriate control activities
- iii. Accurate identification of the stage of completion of work in progress, of slow moving, obsolete or damaged items and of inventory owned by a third party
- iv. Procedures used to estimate physical quantities

Matters relevant in planning attendance at physical inventory counting

- i. The locations at which inventory is held
- ii. Nature of inventory. (Solid / Liquid / Gaseous)
- iii. The nature of the internal control related to inventory. (Strong / Weak)
- iv. Whether the entity maintains a perpetual inventory system.
- v. The risks of material misstatement related to inventory. (Low:- Unsalable/ High:- Saleable)
- vi. Stages of completion of work in progress. (100% Complete / In-complete)
- vii. Whether adequate procedures are expected to be established and proper instructions issued for physical inventory counting. (Adequate / Inadequate)
- vi. The timing of physical inventory counting. (Year End / Latter)
- vi. Whether the assistance of an auditor's expert is needed.

3. Physical Inventory counting is conducted at a date other than the date of the Financial Statements

→ Obtain audit evidence about whether changes in inventory between the count date and the date of the financial statements are properly recorded.

Considerations while checking above

- i. Reliability of the entity's perpetual inventory records.
- ii. Reasons for significant differences
- iii. Whether the perpetual inventory records are properly adjusted.

4. Physical inventory counting is impracticable (1.94)

The auditor shall perform alternative audit procedures to obtain sufficient appropriate audit evidence regarding the existence and condition of inventory. If it is not possible to do so, the auditor shall modify the opinion in the auditor's report in accordance with SA 705

5. Custody and control of a third party

- i. Request confirmation from the third party
  - ii. Inspection or Other Audit Procedures
    - a. Attending, or arranging for another auditor to attend,
    - b. Another auditor's report, or a service auditor's report, on the adequacy of the third party's internal control
- Inspecting documentation regarding inventory held by third parties

6. Design and perform audit procedures for completeness Litigation and Claims.Step 1:- Internal Evidence

- a. Inquiry of management
- b. Reviewing minutes of meetings
- c. Correspondence between the entity and its external legal counsel
- d. Reviewing legal expense accounts.

Step 2:- Written Representations

That all known actual or possible litigation and claims have been disclosed to the auditor and appropriately accounted

Step 3:- Direct Communication with External Legal Counsel



7. If Risk of Material Misstatement then direct communication with the entity's external legal counsel.

→ The auditor shall do so through a letter of inquiry, prepared by management and sent by the auditor, requesting the entity's external legal counsel to communicate directly with the auditor.

(List of litigation and claims / management's assessment of the outcome / A request that the entity's external legal counsel confirm the reasonableness)

→ In certain circumstances, the auditor also may judge it necessary to meet with the entity's external legal counsel (Significant Risk / Complex Matter / Disagreement between management & external legal counsel)

8. Segment Information

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i. Understanding of the methods used by management (Sales, transfers and charges between segments, and elimination of intersegment amounts / Allocation of assets and costs among segments)

ii. Compliance with applicable FRF (AS 17)

iii. Testing the application of such methods;

iv. Performing analytical procedures

v. Consistency with prior periods, and the adequacy of the disclosures with respect to inconsistencies.

vi. Comparisons with budgets and other expected results

1. What is External Confirmation ?

Direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.

It is more reliable because

- a. It comes from independent outside party
- b. It is from parties selected by auditor
- c. It is documentary form
- d. It comes directly to auditor

Situations where external confirmations can be obtained  
(In sequence of balance sheet)

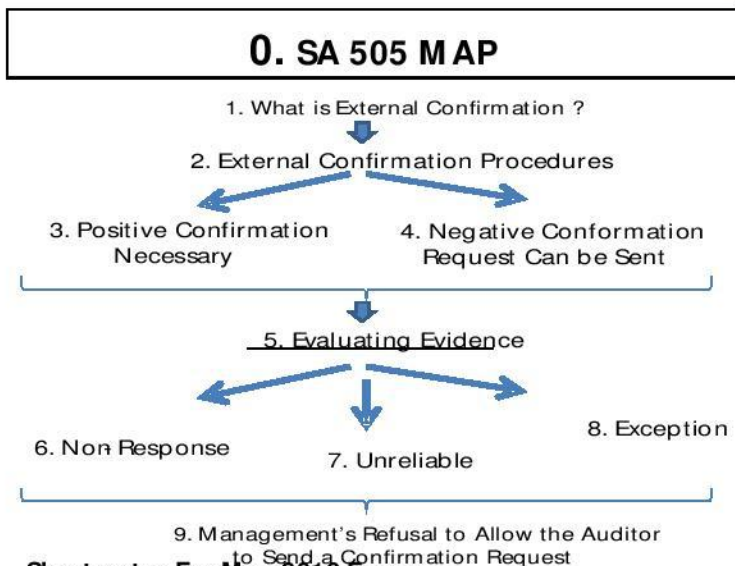
Property title deeds held by third parties | Investments purchased but delivery not taken | Stock held by third parties | Debtor balances | Bank Balance and other information from bankers | Bank loans | Creditor balances | Transactions & related details | Terms of agreement or transactions with third parties

2. External Confirmation Procedures

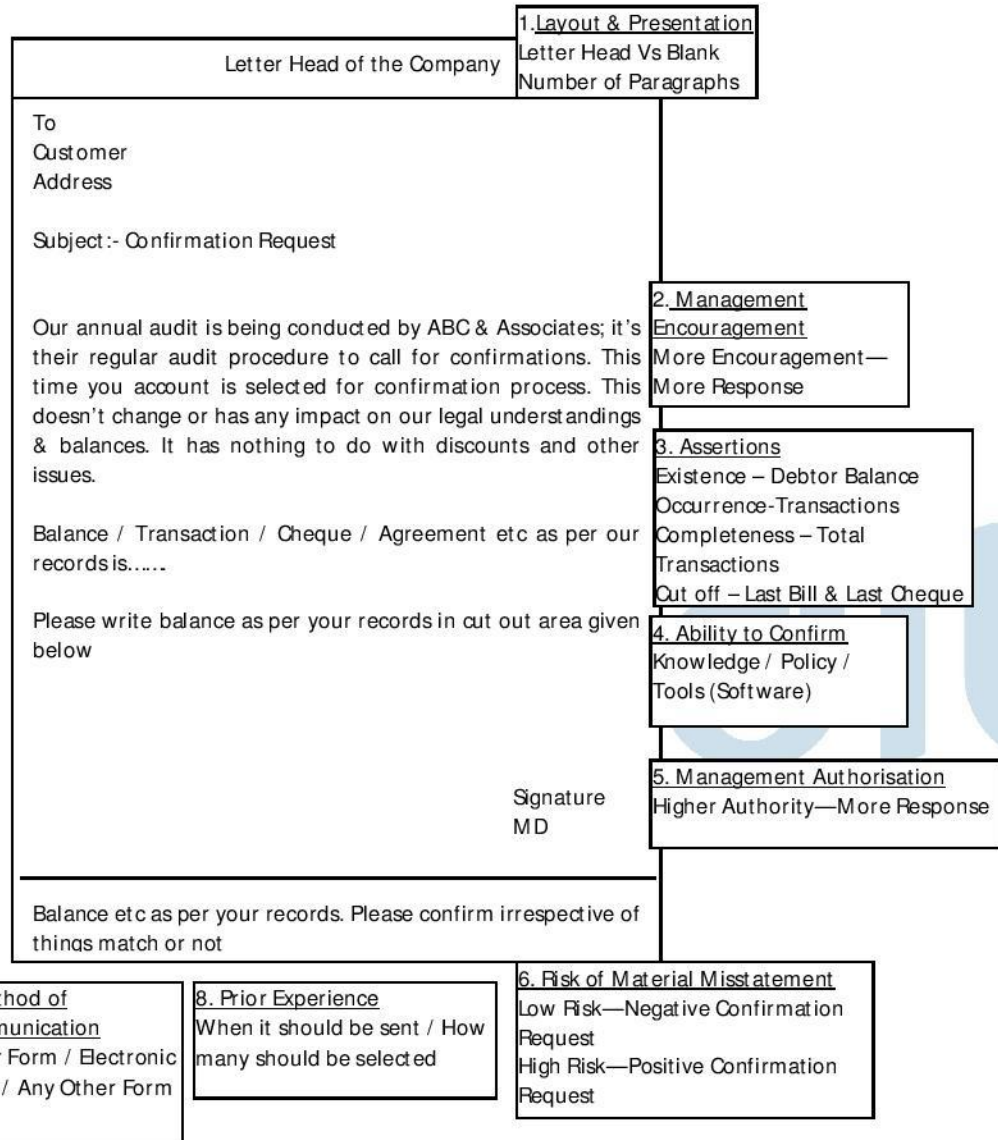
- a. Determining the information to be confirmed or requested;
- b. Selecting the appropriate confirming party;
- c. Designing the confirmation requests, including determining that requests are properly addressed and contain return information for responses to be sent directly to the auditor; and
- d. Sending the requests, including follow-up requests when applicable, to the confirming party.

Designing Confirmation Requests

Directly affect the confirmation response rate, and the reliability and the nature of the audit evidence.



Factors to consider when designing confirmation requests include:



3. Positive Confirmation Request

Positive confirmation request – Party has to indicate whether they agree or disagree with the information in the request, or they have to provide information. (any either case reply is requested)

Positive confirmation request is necessary, alternative audit procedures will not provide sufficient evidence. (Risk of management override controls (Cheques issued / loan taken from bank) / Risk of collusion (Purchase Manager & Store keeper & Supplier) / Only outside evidence is available (Goods sent to Consignee, no records at stores)

If the auditor does not obtain such confirmation, the auditor shall determine the implications for the audit and the auditor's opinion in accordance with SA 705.

4. 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.

Situation where it should be used

- a. Assessed the RMM is low (cash balances with agents)
- b. Controls relevant to assertion are operating effectively (Proper records & daily reporting)
- c. Comprises a large number of small, homogeneous items (all cash balances)
- d. Very low exception rate is expected (mismatch)
- e. Not aware of circumstances or conditions that would cause recipients of negative confirmation to disregard request (reliable & old)

5. Evaluating the Evidence Obtained

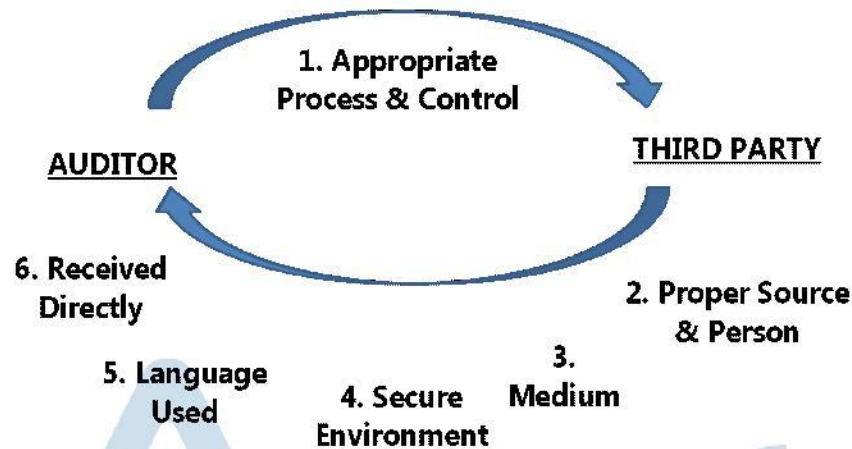
- i. Non-response
- ii. Response deemed unreliable
- iii. Response indicating an exception
- iv. Response by the appropriate party which is in agreement

6. Non-Responses:-

A failure of the confirming party to respond or confirmation request returned undelivered.

- Perform alternative audit procedures
- May indicate a previously unidentified risk of material misstatement.
- May need to revise the assessed risk of material misstatement



7. Reliability of Responses to Confirmation Requests

→Modify planned audit procedures

When the auditor concludes that a response is unreliable, the auditor may need to revise the assessment of the risks of material misstatement at the assertion level and modify planned audit procedures accordingly.

8. Exceptions

→Shall investigate exceptions

→May indicate misstatements or potential misstatements

→ May indicate a deficiency, or deficiencies

→Some exceptions do not represent misstatements

→May provide a guide to the quality of responses

9. Refusal to send a Confirmation Request

→Inquire as to management's reasons

→Seek audit evidence as to their validity

→ Evaluate the implications (RMM / ROF)

→ Perform alternative audit procedures

→Refusal is unreasonable & unable to obtain relevant and reliable audit evidence

→Modify opinion as per SA 705

**SA 510**

Contents

1. Applicability & Objectives of SA 510
2. Audit Procedures to examine Opening Balances
3. Factor affecting Nature & Extent of Audit Procedures regarding Opening Balance
4. Audit Conclusions and Reporting
5. Other matter paragraph

**1. Applicability & Objectives of SA 510**

Applicability:- Initial audit engagement.

Initial audit engagement –

- 1.Last year financial statements not audited; or
- 2.Audited by a predecessor auditor.

Objective:-

- 1.Misstatements that materially affect CY financial statements
- 2.Consistency of Accounting Policy & Disclosures if there are changes

**2. Audit Procedures to examine Opening Balances**

- 1.Check whether closing balances have been correctly brought forward from last year ledger.
- 2.Agree opening balance with the most recent financial statements
- 3.Read predecessor audit report if any.
- 4.Read accounting policies of LY and determine whether they are consistently applied in CY
- 5.If any adjustment is shown as prior period item, trace to previous period documents.
- 6.Whether audit procedures performed in the current period provide evidence relevant to the opening balances

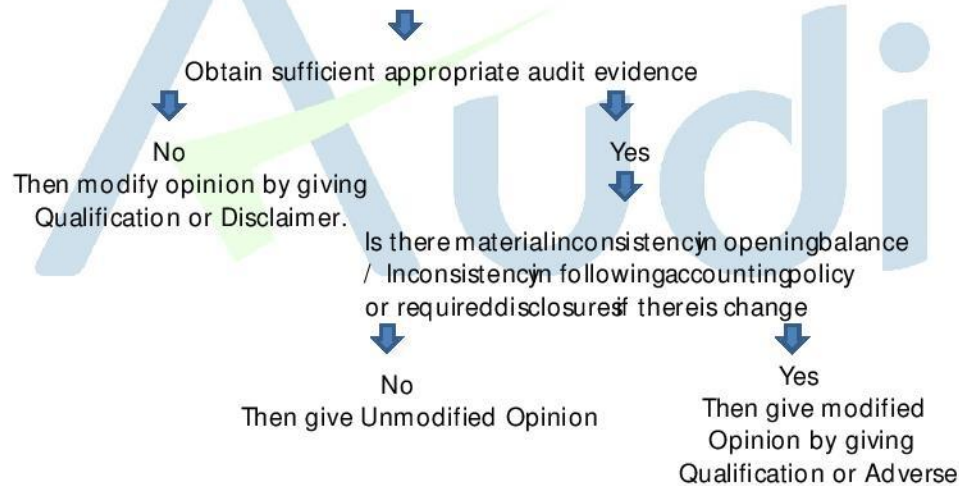
(While physical verification of fixed assets, we can see date of acquisition to find out whether they existed in opening, same thing can be done for investments, ask for confirmation for closing as well as opening balances for debtors ,Collection opening debtors & creditors while doing ledger scrutiny)

7. Performing specific audit procedures to obtain evidence regarding the opening balances. (Reconciliation of inventory Op (Bal fig) + Purchase – Sale = Closing / Checking inventory valuation of opening inventory / Re computing last year depreciation)

**3. Factor affecting Nature & Extent of Audit Procedures regarding Opening Balance**

1. Significance of the opening balances
2. Nature of the account balances, classes of transactions
3. Whether the prior period's financial statements were audited
4. The accounting policies followed by the entity (Changes).
5. Whether the predecessor auditor's opinion was modified.

**4. Audit Conclusions and Reporting**



**5. Other matter paragraph**

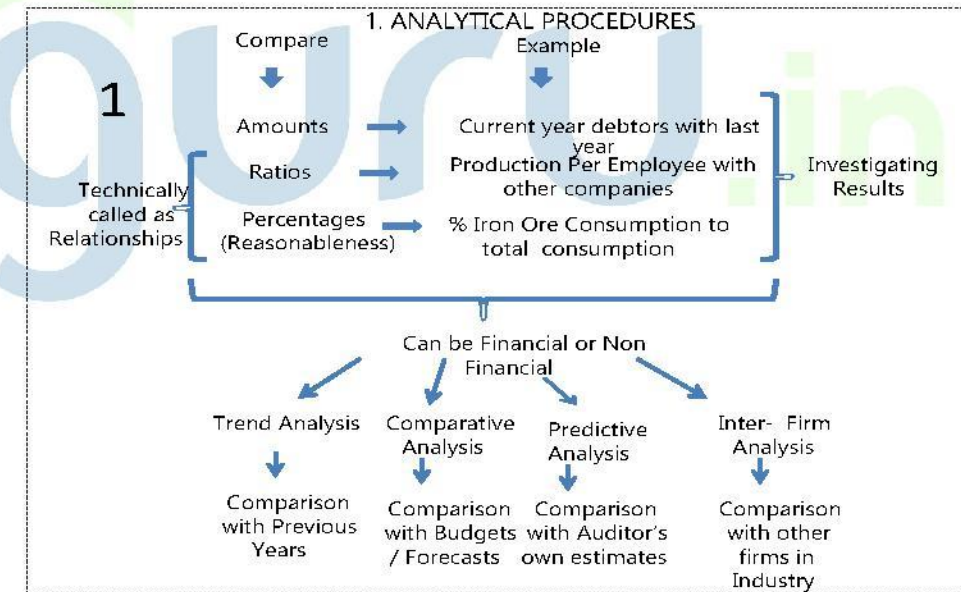
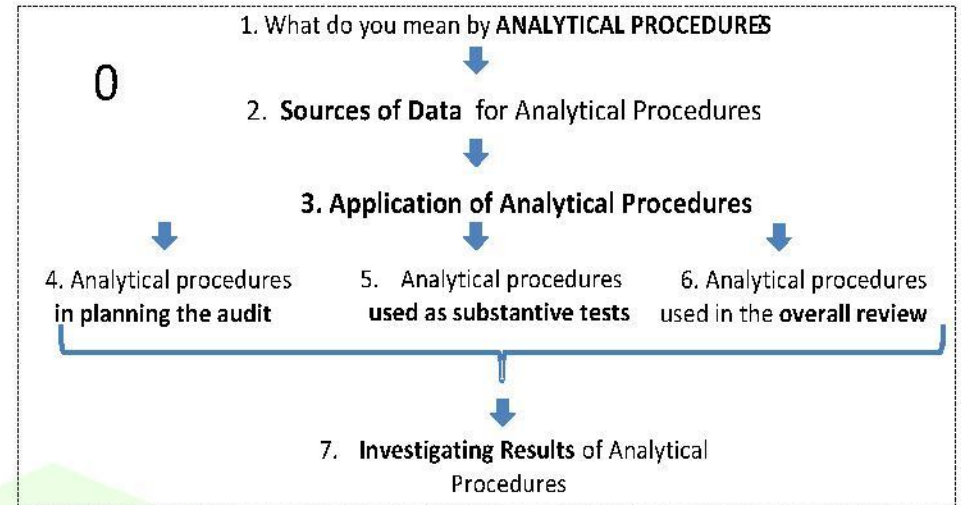
When we have to insert OMP:

1. If no audit is performed in last year
2. If audit is by done someone else in last year than we have to give

- Name of auditor
- Date of report
- Type of opinion given by him

These two points are reference to SA 710.

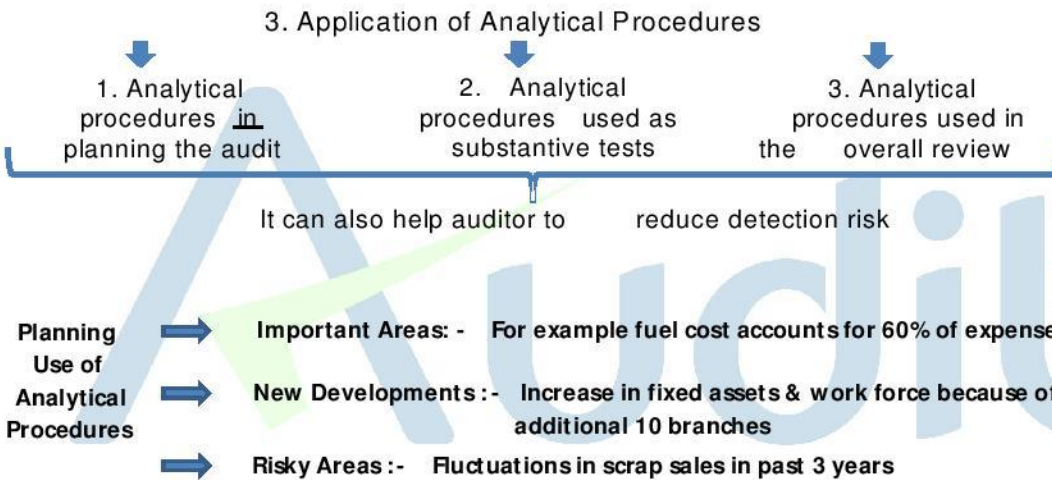
**SA 520**





**3.Sources of Data**

- Budget
- Bank and Cash Records
- Managements Accounts
- Board Minutes
- Interim Financial Information
- VAT Returns
- Discussions or correspondence with Client at year-end
- Non-Financial Information



Factors (Suitability)	Impact	Example
Volume of Transactions	Large:- Suitable Small:- Less Suitable	Interest Earned / Investments Many:- Suitable Few:- Not Suitable (Test of Details)
Predictable Relationship	Yes:- Suitable No:- Not Suitable	Excise Duty / Sales:- Suitable Legal Expense / Sales:- Not Suitable
Level of Assurance	High:- Suitable Low:- Less Suitable	If fixed basic salary:- Average Salary comparison will give more persuasive assurance Gross Profit Margin Comparison will give less persuasive assurance about sales.
Internal Control System of the area.	Strong:- Suitable Weak:- Less Suitable	Strong Sales Process:- Can rely on Average Sales Comparison, perform more test of details
Other Audit Procedures	Yes:- Suitable No:- Less Suitable	Debtors apart from confirmations debtor turnover and ageing analysis is done, gives more persuasive evidence

Factors (Reliability of Data)	Impact	Example
Source of Information	External:- Reliable Internal:- Less Reliable	Data published by Industrial Association:- More Reliable Data given by MIS:- Less Reliable
Control over preparation of Information	Good Controls:- More Reliable Weak Controls:- Less Reliable	Sophisticated ERP :- More Reliable Excel Based :- Less Reliable
Nature & Relevance of Information	Complicated :- Less Reliable	Realistic Budgets:- More Reliable Hypothetical Budgets:- Less

	Simple :- More Reliable	Reliable Number of Employees:- More Reliable Effective Working Hours:- Less Reliable
Comparability	Yes:- More Reliable No:- Less Reliable	Same Products:- More Reliable Specialized Product:- Less Reliable

conclusions formed during the audit of individual components or elements of the financial statements. This assists the auditor to draw reasonable conclusions on which to base the auditor's opinion.

### **8. Investigating Results of Analytical Procedures**

**1. Inquiring of management** and obtaining appropriate **audit evidence relevant to management's responses**; and

**2. Performing other audit procedures** as necessary in the circumstances.

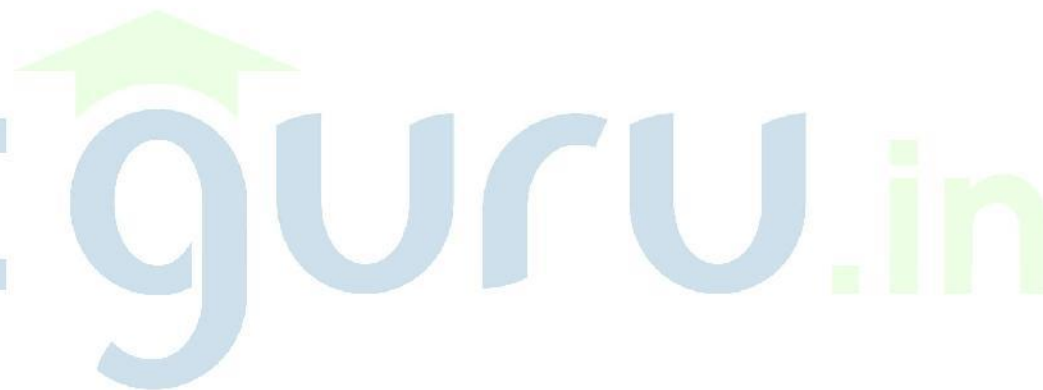
Factors (Developing Expectations)	Impact	Example
Financial as well as Non Financial Available	Yes:- Precision No:- Less Precision	Sales Amount / Quantity / Number of Orders / Dispatches / Number of Sales Executive Available: Precise Analysis
Accuracy of Range	Yes:- Precision No:- Less Precision	Out of past experience we know that Production per hour is 100-105 units :- Precise Analysis
Disaggregation	Yes:- Precision No:- Less Precision	Department wise sales comparison:- Precision Overall Sales Comparison:- Less Precision

Whether to investigate difference obtained while applying analytical procedures depends on Materiality / Risk / Level of Assurance

### **7. Analytical Procedures that Assist When Forming an Overall Conclusion**

The auditor shall design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor's understanding of the entity.

The conclusions drawn from the results of analytical procedures designed and performed in accordance with above paragraph intended to corroborate





SA 530

**Sampling Risk**  
The risk that the auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure.

Sampling risk can lead to two types of erroneous conclusions

**Type I – Error**

In the case of a test of controls, that controls are more effective than they actually are (**Over Reliance on Controls**), or in the case of a test of details, that a material misstatement does not exist when in fact it does (**Incorrect Acceptance**).

The auditor is primarily concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion. (**Reduces Effectiveness of Audit**)

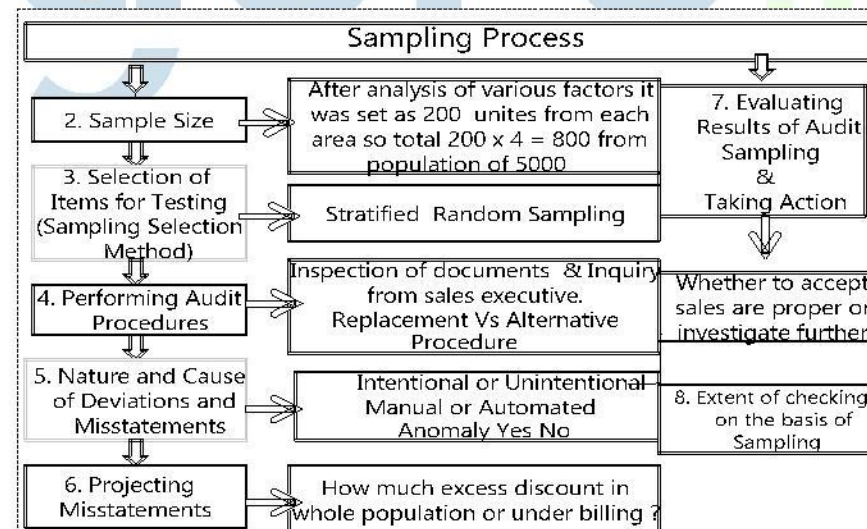
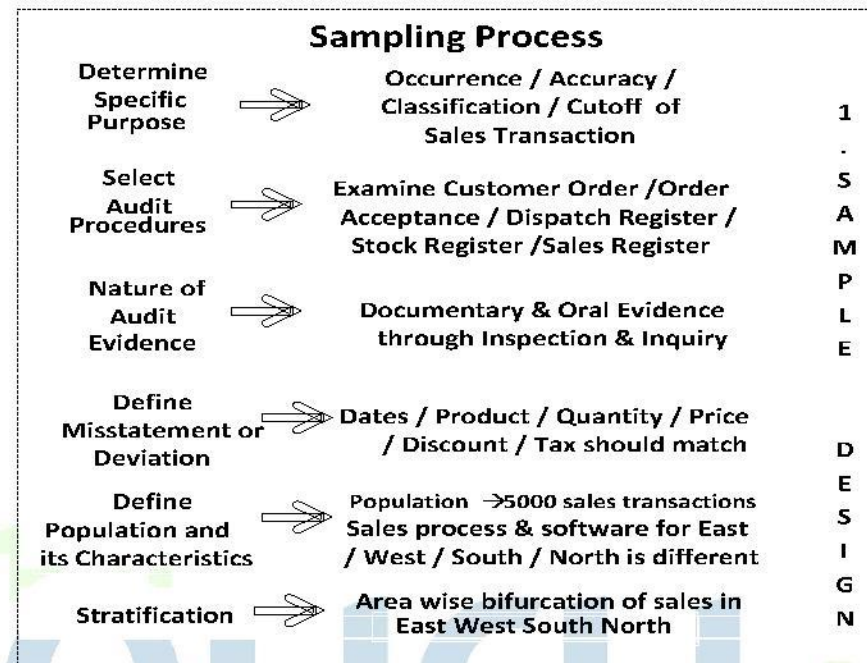
**Type II – Error**

In the case of a test of controls, that controls are less effective than they actually are (**Under Reliance on Controls**), or in the case of a test of details, that a material misstatement exists when in fact it does not. (**Incorrect Rejection**)

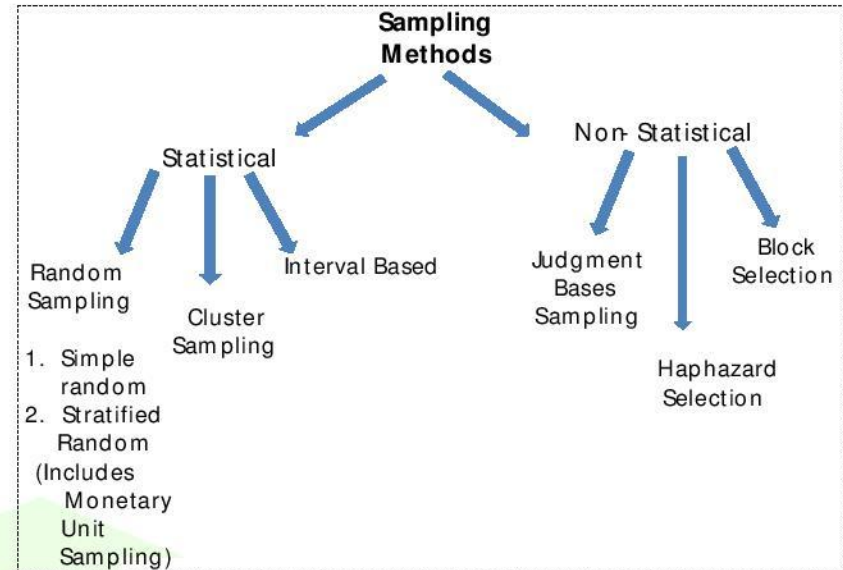
This type of erroneous conclusion affects audit efficiency as it would usually lead to additional work to establish that initial conclusions were incorrect. (**Reduces Efficiency of Audit**)

**Non-Sampling Risk:-** Risk of inappropriate conclusion because of

- Inappropriate Audit Procedure (Risk was that some stock in godown is not covered in stock sheet, auditor selected sample from existing items in stock sheet and traced them to godown)
- Failure to recognize a misstatement or deviation (Failed to recognise that signature on purchase orders were fake or failed to note that rate in PO were more than specified in agreement)
- Misinterpretation of Audit Evidence (Monetary amount of scarp sales to production percentage was increasing drastically, so auditor marked it risky with chances of black money dumped in business but it was simple increase in market price of scrap)



2. Factor affecting Sample Size		
Story	Situation	Impact
Auditor sent to construction company for checking <b>WAGES (Inherent Risk)</b> & preliminary assessment shows no guidance or training for payment staff <b>(Control Risk)</b> .	An <b>increase</b> in the auditor's assessment of the <b>risk of material Misstatement</b>	<b>Larger the sample size</b>
He gets call from colleague that he will not be coming so no analytical procedures and now things will be depending on his checking only.	<b>Decrease</b> in the use of <b>other substantive procedures</b> directed at the same assertion.	<b>Larger the sample size can be.</b>
After performing test of controls he concluded that controls are weak and expected misstatements are higher. Because out of 3 supervisors <b>1 is on leave &amp; 1 is ill for past 9 months.</b>	An <b>increase in the amount of misstatement the auditor expects to find</b> in the population	<b>Larger the sample size can be.</b>
Senior Accountant Says that they cannot generate list of workers area wise or site-wise or month-wise joining <b>so stratification is not possible.</b>	Stratification of the population when appropriate <b>Decrease</b>	<b>Larger the sample size can be.</b>
His senior calls and says he wants higher level of assurance & lower tolerable misstatement	An <b>increase in the auditor's desired level of assurance</b> that tolerable misstatement is not exceeded by actual misstatement in the Population <b>Decrease in tolerable misstatement</b>	<b>Larger the sample size can be.</b>
Further he observes number of workers has increased from 1000 to 3000	<b>Change in the number of sampling units</b> in the Population	<b>Negligible Effect</b>



Advantages of Statistical Sampling

The advantages of statistical sampling may be summarized as follows -

1. Saves Time
2. Saves Cost
3. Improved quality of checking
4. Scientifically Proven
5. Objective (Unbiased)
6. Take pre determined calculated risk
7. There is formula for minimum sample size
8. Does not increase with proportionate increase in population



Non Statistical Sampling (Precautions, This is as per module contains steps similar to sampling process)

The **precautions that should be taken may be the following:**

- i. First check internal control system
- ii. 100% checking in some areas
- iii. Stratification
- iv. Unbiased Selection
- v. Prepare test check plan and train team members
- vi. Carefully decide sample size
- vii. Study some transactions from beginning till end
- viii. Evaluate errors

#### 4. Performing Audit Procedures

The auditor **shall perform audit procedures, appropriate to the purpose, on each item selected.**

##### Replacement

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

##### Alternative Procedures

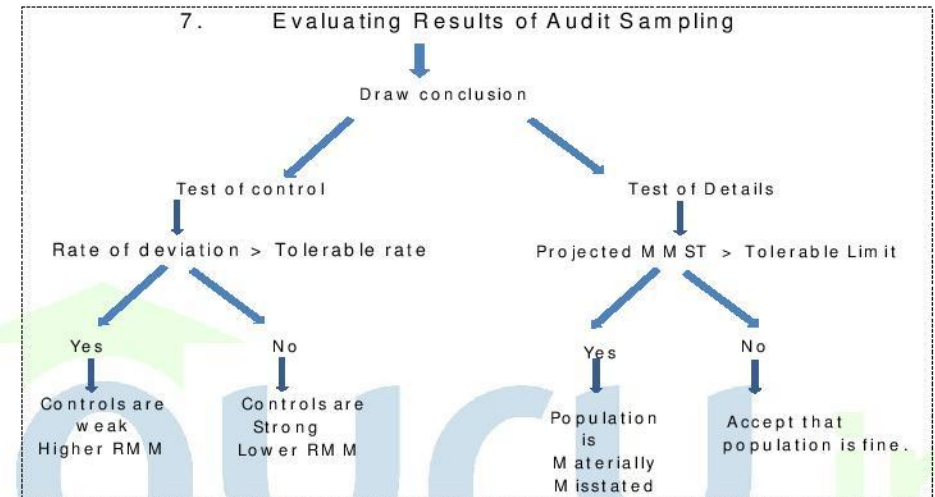
If the auditor is unable to **apply the designed audit procedures, or suitable alternative procedures, to a selected item, the auditor shall treat that item as a deviation from the prescribed control, in the case of tests of controls, or a misstatement, in the case of tests of details.**

#### 5. Nature and Cause of Deviations and Misstatements

In analysing the deviations and misstatements identified, the auditor may observe that many have a common feature, **for example, type of transaction (Sales vs Interest Income), location (Big Branch vs Small Branch), product line (Old product vs New Product) or period of time (Peak Season vs Slack Season).**

#### misstatements.

**For tests of controls, no explicit projection of deviations is necessary since the sample deviation rate is also the projected deviation rate** for the population as a whole. SA 330 provides guidance when deviations from controls upon which the auditor intends to rely are detected.



#### 8. Extent of checking on sampling plan

The factors that should be considered for deciding upon the extent of checking on a sampling plan are following:

- i. **Size of the organisation** under audit. (Big)
- ii. State of the **internal control**. (Strong)
- iii. **Adequacy and reliability** of books and records. (Accurate & Reliable)
- iv. **Tolerable error range**. (Not very small)
- v. Degree of the **desired confidence**. (Not very high)  
(Then higher reliance on sampling)

## SA 540

**AUDITING ACCOUNTING ESTIMATES, INCLUDING FAIR VALUE  
ACCOUNTING ESTIMATES, AND RELATED DISCLOSURES**

1. Accounting Estimates & Types

a. Fair Value Accounting Estimates:- Fair value is a rational and unbiased estimate of the potential market price of a good, service, or asset / liability.

Eg FA held for disposal / For exchange of assets & liabilities / Assets & Liabilities acquired in amalgamation / Investment valuation / NRV of Inventory / Share valuation for share based payments / Complex financial instruments

b. Other Accounting Estimates:- Estimates apart from fair value estimates.

Eg Useful life & depreciation method of FA / Inventory Obsolescence / Provision for doubtful / Provision for compensation in litigation / Warranty Obligations / Probability of contingent liability

2. Risk Assessment Procedures and Related Activities (Which information should be collected with respect to estimates ?)

Relating to all estimates

a. Requirements of applicable FRF (AS 2 / 6 / 13 / 15 / 22 / 26 / 28 / 29)

b. How management identifies whether new estimates will be required or existing estimates need to be revised. (CA for Financial Estimates, CS for Legal Estimates, Engineer for Technical Estimates)

Specific points related to a particular estimate (Lets assume estimate of gratuity / pension / leave encashment etc)

c. Data on which they are based (Employee Data / Salary Data / Mortality & Health Data)

d. Relevant controls (Segregation of Duties, 2 CAs appointed, Monthly Internal Analysis, CFO Presentation, Consultation with Expert)

e. Use of expert (Actuarial Valuation Once in 3 Years)

f. Method, including where applicable the model (Project Unit Method (AS 15) / Corridor Method)

g. Assumptions (Inflation Rate / Salary Rate etc)

h. Assessed the effect of estimation uncertainty Sensitivity to various factors such as Interest Rate / Growth Rate of Salary Etc)

i. Review the outcome of accounting estimates included in the prior period (Whether gratuity / pension payments are as decided in previous years).

2. Identifying and Assessing the Risks of Material Misstatement

RMM in case of estimates depends on

1<sup>st</sup> Estimation Uncertainty & 2<sup>nd</sup> Other Factors

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a. Estimation Uncertainty (High uncertainty High RMM)

b. The outcome of the review of prior period accounting estimates. (Bigger Difference Higher RMM)

c. The recorded amount of the accounting estimate (that is, management's point estimate) in relation to the amount expected by the auditor to be recorded. (Bigger Difference Higher RMM)

d. Whether management has used an expert in making the accounting estimate. (If no expert is used then higher RMM)

e. The actual or expected magnitude of an accounting estimate. (Higher Amount Higher RMM)

Factors on which depends estimation uncertainty (Brand Valuation Vs Construction Contract

JST-OLD

Factor	Brand Valuation (High Uncertainty)	Cost of Construction Contract (Low Uncertainty)
J- Judgement	Depends on how people judge and give importance to brand. *Similarly result of litigations depends a lot on judgement	Here Judgments are prepared as per well established principle so subjectivity is reduced drastically.
S- Sensitivity	It's highly sensitivity to performance and image of other competitive brands.	If prices of cement or still changes as per past data there will not be significant



	As people's perception change brand value changes drastically.	change in overall project cost.
T-Technique	No accounting standard or guidance note on brand valuation.	We have AS 7 which guides on how to compute % completion.
O-Observable Input	There is no proper source of information for customer opinion and preferences and changes happening in them.	There are cement, steel, labour markets from where we can have observable inputs for prices etc.
L-Length of time period	10 years of forecast for brand valuation on the basis of past 10 years of data in technology industry	2 years of forecast in construction contract on the basis of 20 years data
D- Data	Market data collected and maintained by company itself is less reliable.	Market data collected and maintained by industry association or authorities is more reliable.

#### Examples of High Estimation Uncertainty

- Outcome of litigation. (Vodafone Case)
- Fair value of derivative financial instruments not publicly traded. (Maturity more than 3 months)
- Fair value accounting estimates for which a highly specialised entity developed model is used or for which there are assumptions or inputs that cannot be observed in the marketplace. (Share valuation depending on internal assessment of new product and efficiency levels)

#### Examples of Low Estimation Uncertainty

- Business activities that are not complex (Depreciation of furniture in trading entity)
- Accounting estimates that are frequently made and updated (routine) (Inventory Valuation)
- Accounting estimates derived from data that is readily available (Listed Shares)

- Fair value accounting estimates where the method of measurement prescribed by the applicable financial reporting framework is simple (Determining Net Selling Price in AS 28)
- Fair value accounting estimates where the model used to measure the accounting estimate is well-known or generally accepted, provided that the assumptions or inputs to the model are observable. (Share valuation of liquidating company using net asset method)

NI-IPC

#### 4. Responses to the Assessed Risks of Material Misstatement (Points are similar to risk assessment, only difference is risk assessment was information collection & response to risk means examination)

- Test the operating effectiveness of the controls (Segregation of Duties, 2 CAs appointed, Monthly Internal Analysis, CFO Presentation, Consultation with Expert)
- Evaluate Data (Employee Data / Salary Data / Mortality & Health Data)
- Method of measurement used (Project Unit Credit Method)
- requirements of the applicable financial reporting framework (AS 15 Compliance)
- Develop a point estimate or a range to evaluate management's point estimate.

NI-IPC

#### When to use point estimate or range estimate ?

- Review of prior period financial statements suggests process is unlikely to be effective. (Big Difference)
- Alternative sources of relevant data available (Employee attrition, Salary Growth Rate etc)
- Period end and the date of the auditor's report contradict management's point estimate. (Payment of Gratuity)
- Entity's controls not well designed or properly implemented. (No in charge or Expert for Computation)
- Not derived from the routine processing of data (Futuristic Data)



How to develop point estimate or range estimate ?

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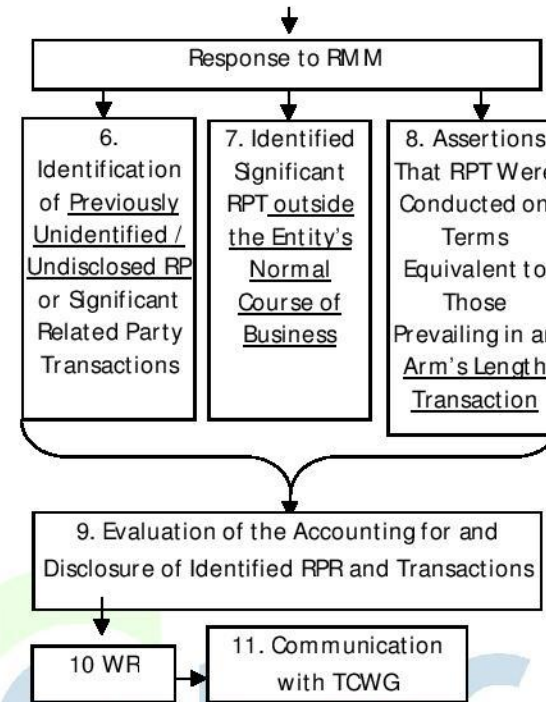
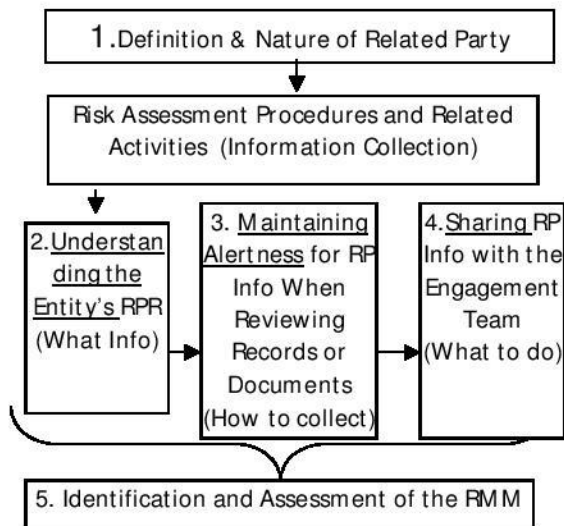
- Using a model, that is commercially available (Popular Software)
- Further developing alternative assumptions or outcomes, (Apply assumptions used by counter parts in industry)
- Employing person with specialised expertise (Auditors Expert)
- Making reference to other comparable conditions, transactions or events, (Compare with markets & others in industry)

### 5. Indicators of Possible Management Bias

Examples of indicators of possible management bias with respect to accounting estimates include:

- Changes in an accounting estimate, or the method for making it, where management has made a subjective assessment that there has been a change in circumstances.
- Use of an entity's own assumptions for fair value accounting estimates when they are inconsistent with observable marketplace assumptions.
- Selection or construction of significant assumptions that yield a point estimate favourable for management objectives.
- Selection of a point estimate that may indicate a pattern of optimism or pessimism.

### SA 550 Related Parties



### 1. Definition of Related Party

a. If FRF defines related party use that definition, Like in India AS 18 defines related party but this need not be the case in all FRFs like Special Purpose FRFs, which may be as per agreement, regulator, holding company etc

b. If there is no definition in FRF then we should use SA 550 definition

i. Any party controlling (More than 50%, ability to decide financial and operating policies) or having significant influence (20% or more, ability to participate in financial and operating policies) over entity (Direct or Indirect through Intermediaries i.e. Subsidiaries)  
(Eg Holding Company, Big Investor, KMP etc)

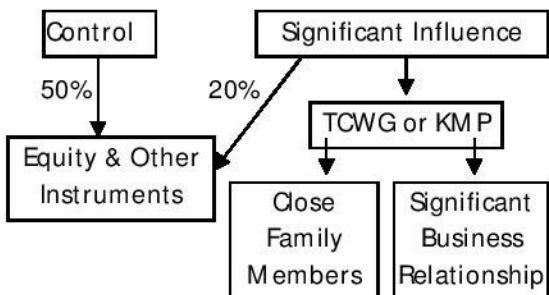
ii. Any party who is under significant influence or control of entity (Direct or Indirect through Intermediaries i.e. Subsidiaries)  
(Eg Subsidiary, Associate, Joint Venture etc)

iii. Parties which are under common control with entity because of common ownership, common KMP or Owners are close friends or relatives.

Exclusion from related party transactions



Entities under control of governments (State or Central) but they will be covered if they have significant transactions or significant resource sharing between them.



### Nature of Related Party / How fraud can take place?

If related party transactions are in normal course of business they are not risky but they will be risky if

**a.** They are not conducted at normal market prices, terms & conditions. (Goods purchased at double the market price from MDs son proprietor firm or goods sold to brother of MD at triple the market price)

**b.** Transactions are conducted through complex related party relationships & structures. (Indian Co pays Technical Consultancy Fees → USA Sub pays Management Consultancy → UK Sub pays Dividend → Canada Holding Co where MD is having major stake)

**c.** Where there are no appropriate employees / register / software (systems) to identify, authorise, record, summarise and disclose related party transactions which may lead to non compliance of AS18.

(Delhi based Company indirectly holds controlling stake in Australian company through its subsidiaries in Mumbai and Chennai but this thing is not disclosed in financial statement as per AS 18, because of lack of expertise in staff managing related party transactions (Non CA / CS/ CWA)

**d.** Unusual or Fictitious terms of transactions which misrepresent business rationale. (On papers sale and repurchase is shown which is actually loan taken and repaid)

### RISK ASSESEMENT PROCEDURES

## 2. Understanding the Entity's Related Party Relationships & Transactions

### a. Inquiry

- i. Identity (Names) of related parties also changes during the year.
- ii. Nature of Relationships (Subsidiary / Associate / Joint Venture/ KMP Etc)

iii. Types and purpose of transactions entered with related parties. (Investment in shares / debentures etc or Sale / Purchase of goods/ services / fixed assets etc)

### b. Understanding the controls (Procedures)

How related party transactions are identified, approved (Specially Significant Transactions & significant transactions & arrangements outside normal course of business), recorded, displayed in notes to accounts as per Financial Reporting Framework (AS18 & Schedule III)

(Audit Committee / BOD authorisation / General meeting resolutions / Related party policies / identification individual / software / register etc)

## 3. Maintaining Alertness

a. Remain alert while inspecting records or documents for identity, nature and transactions of related party.

Following documents should be seen for identity / nature / transactions of related party

- i. AS 18 / Schedule III disclosures of Previous Years
- ii. Shareholders register
- iii. Director's register
- iv. Contracts with TCWG / Directors / KMP
- v. Life insurance policies
- vi. Records of Entity's pension plans
- vii. Statements of Conflict of Interest
- viii. Investment Register
- ix. BOD / Shareholder Meeting Minutes
- x. Sec 189 Register
- xi. Information supplied to Regulatory Authorities
- xii. Filing with SEBI / SEC
- xiii. Tax Returns

xiv. Internal Auditor's Report

xv. Confirmation from Banks / Legal Counsel / Third parties about relationships & transactions

xvi. Invoices & Correspondence with professional advisor

xvii. Contracts not in ordinary course of business

xviii. Contracts re-negotiated



b. If there are transactions outside normal course of business understand their nature and find out whether related party is involved.

Examples of transactions outside normal course of business

- i. Complex Equity transaction, corporate restructuring or acquisitions (Amalgamations, Demerger, Carve Out)
- ii. Leasing Premises or rendering management services to another party without any consideration.
- iii. Unusually large discounts or return on sales.
- iv. Circular arrangements, for example, sales with a commitment to repurchase.
- v. Offshore entities in jurisdictions with weak corporate laws.
- vi. Contracts whose terms are changed before expiry.

#### 4. Sharing Related Party Information with the Engagement Team

- a. Identity of related parties.
- b. The nature of the related party relationships and transactions.
- c. Significant or complex related party relationships (Complicated ESOP schemes)

NI-IPC

#### 5. Identification and Assessment of the Risks of Material Misstatement Associated with Related Party Relationships and Transactions

- a. Assess RMM, check likelihood and impact if it is high it becomes Significant Risk. (Brother in law of MD doing renovation of MDs Home & Factory both simultaneously)
- b. Related Party Transaction + Outside Normal Course of Business = Significant Risk (Complex restructuring of whole group in 2 parts, like Mukesh Bhai & Anil Bhai)
- c. Related Party Transaction + Dominant Influence + Other Risk Factors = Significant Risk (Ramalinga Raju was founder & part of current management (DI) and he was sole decision maker without any discussions with others)
- d. Related Party Transactions + Fraud Risk Factors = consider this information while applying SA 240

NI-IPC

#### Dominant Influence

Domination of management by a single person or small group of persons without compensating controls is a fraud risk factor.

Indicators of dominant influence exerted by a related party include:

- a. **Vetoed significant business decisions**
- b. Significant transactions are **referred to the related party for final approval**.

c. There is **little or no debate** regarding business proposals initiated by the related party.

d. Transactions involving the related party are **rarely independently reviewed and approved**.

e. Played a **leading role in founding** the entity and continues to play a leading role in managing the entity.

#### Other Risk Factors

NI-IPC

- a. High turnover of senior management or professional advisors
- b. Use of business intermediaries for significant transactions for which there appears to be no clear business justification (What ruia brothers did in ESSAR)
- c. Evidence of the related party's excessive participation in or preoccupation with the selection of accounting policies or the determination of significant estimates. (What happened in Satyam)

NI-IPC

#### Response to RM M

#### 6. Identification of Previously Unidentified or Undisclosed Related Parties or Significant Related Party Transactions

- a. Confirm the existence
- b. Promptly Communicate to others
- c. Request management identify all transactions with newly identified related party
- d. Inquire why controls failed (Documents received from subsidiary were not checked by CS as per procedure mentioned)
- e. Reconsider risk of other unidentified parties & transactions
- f. If intentional then it is a fraud risk factor.
- g. Perform Substantive Tests

Substantive audit procedures that the auditor may perform relating to newly identified related parties

- a. Inquiries with TCWG / Management / External Legal Counsel / Principal Agents / Consultants / Guarantor
- b. Analysis of Accounting Records
- c. Terms & Conditions of newly identified related party transaction and whether it is appropriately accounted



### 7. Identified Significant Related Party Transactions outside the Entity's Normal Course of Business

For identified significant related party transactions outside the entity's **NI-IPC** of business, the auditor shall: (Sale to subsidiaries in Mauritius and Dubai then export to various countries for tax saving)

- (a) Inspect the underlying contracts or agreements, if any, and evaluate whether:
- The business rationale (or lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets;
  - The terms of the transactions are consistent with management's explanations; and (But goods are not exported but sold to local manufacturer)
  - The transactions have been appropriately accounted for and disclosed in accordance with the applicable financial reporting framework; and
- (b) Obtain audit evidence that the transactions have been appropriately authorised and approved.

### 8. Assertions That Related Party Transactions Were Conducted on Terms Equivalent to Those Prevailing in an Arm's Length Transaction

When management has made an assertion in the financial statements to the effect that a related party transaction was conducted on terms equivalent to those prevailing in an arm's length transaction, the auditor shall obtain sufficient appropriate audit evidence about the assertion. (Toshiba sold high end customised laptops to KMP & relatives; they claim it is at arm's length price)

Management is responsible for the substantiation of an assertion that a related party transaction was conducted on terms equivalent to those prevailing in an arm's length transaction.

Management's support for the assertion may include:

- Comparing the terms of the related party transaction to those of an identical or similar transaction with one or more unrelated parties.
- Comparing the terms of the transaction to known market terms for broadly similar transactions on an open market.
- Engaging an external expert to determine a market value and to confirm market terms and conditions for the transaction.

Evaluating management's support for this assertion may involve one or more of the following:

- Considering the appropriateness of management's process for supporting the assertion.

- Verifying the source of the internal or external data supporting the assertion, and testing the data to determine their accuracy, completeness and relevance.
- Evaluating the reasonableness of any significant assumptions on which the assertion is based.

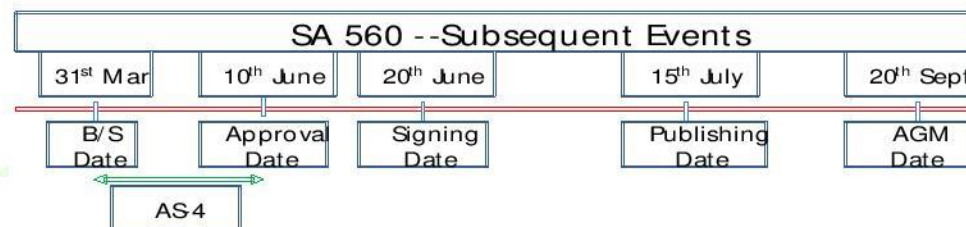
### 9. Evaluation of the Accounting for and Disclosure of Identified Related Party Relationships and Transactions

Compliance of AS18

### 10. Written Representations

### 11. Communication with Those Charged with Governance

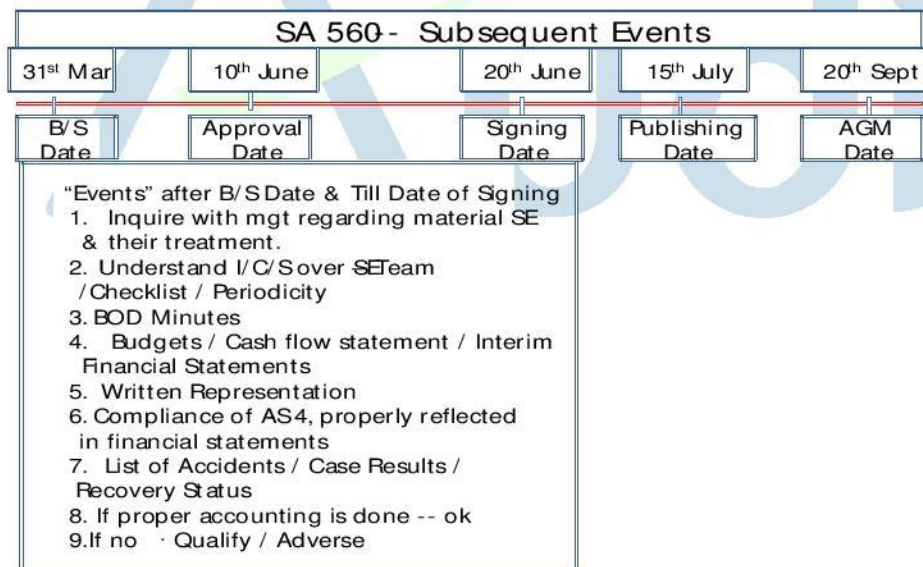
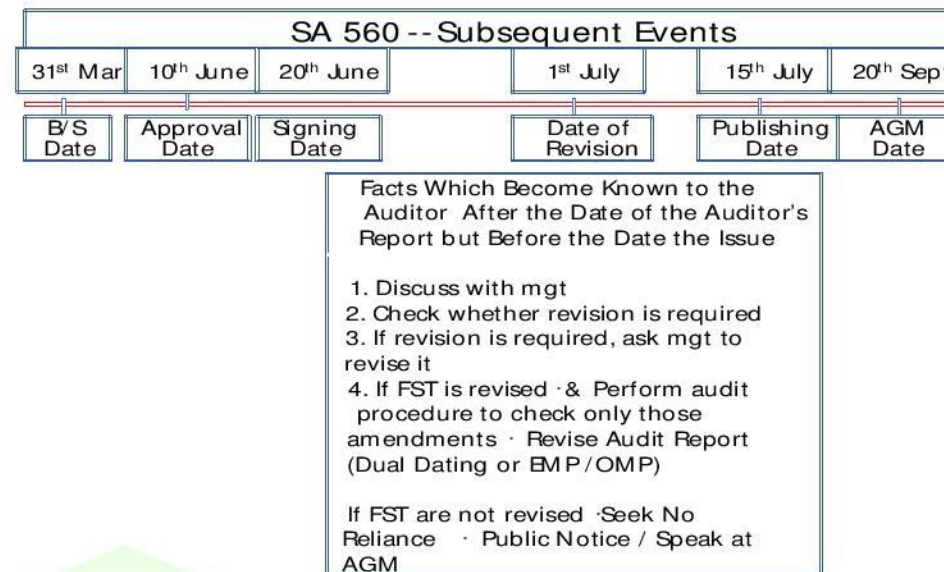
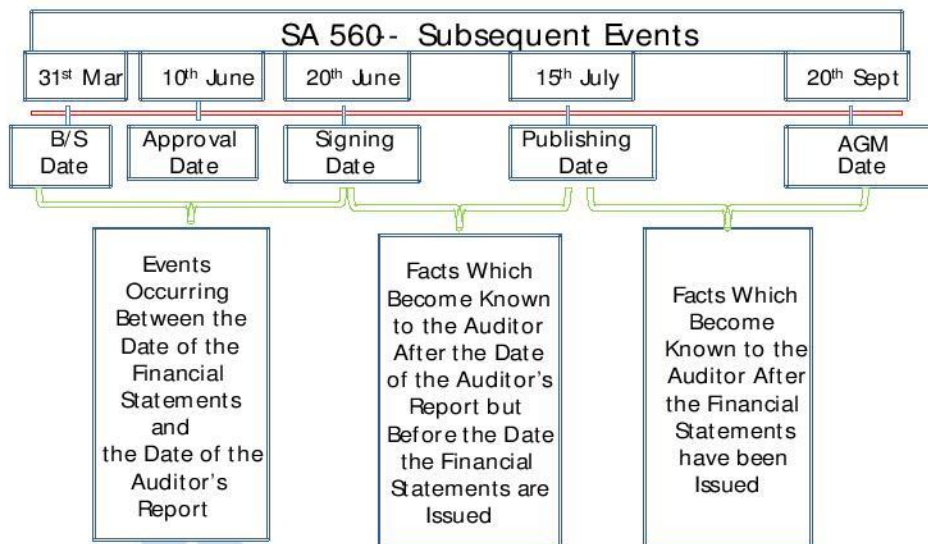
### SA 560 SUBSEQUENT EVENTS



#### AS4

It covers events after Balance Sheet Date & Till Date of Approval.

1. Required by Law or AS  
Eg Proposed Dividend, Impact of Bonus / Right Shares on EPS
2. Affects going concern  
Eg Ban, Accident etc
3. Clarifies contingency on B/S Date  
Eg Pending Case / Doubtful Debtor etc

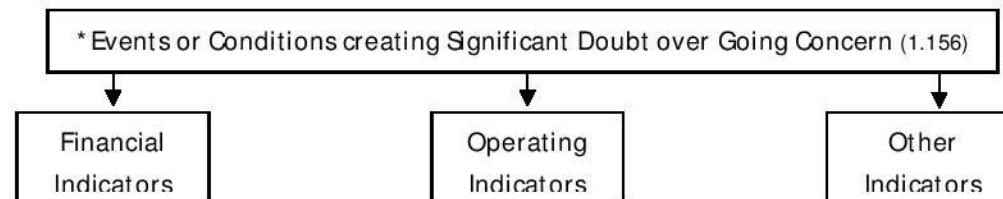
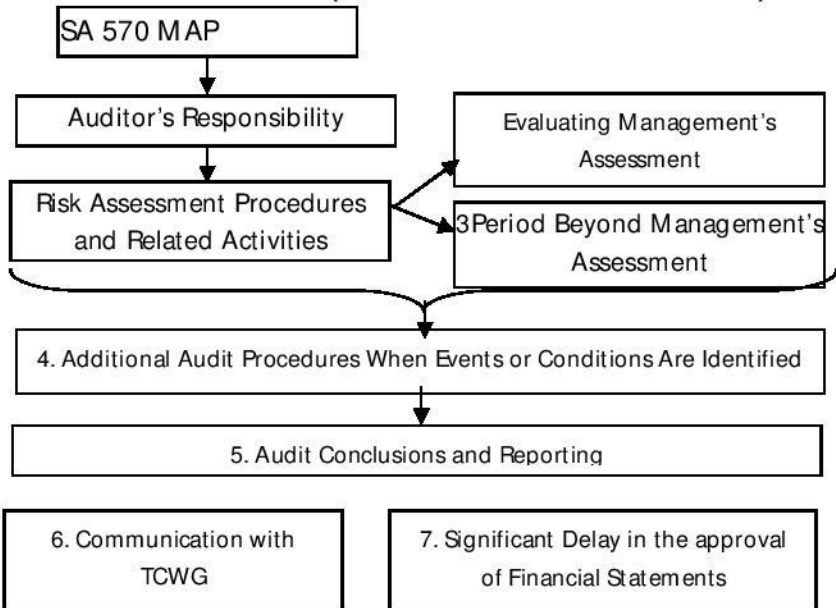


If it is after date of publishing everything remain same only, auditor has to ensure that management has called back and destroyed all old copies or financial statement and audit report to the extent practical.

Points of Inquiry in detail (if specifically asked)

- a. Whether any events have occurred that are relevant to the measurement of estimates or provisions made in the financial statements. (Clarifies uncertainty at B/S date)
- b. Whether any events have occurred that are relevant to the recoverability of assets (Clarifies uncertainty at B/S date)
- c. Whether any events have occurred or are likely to occur which will bring into question the appropriateness of accounting policies used in the financial statements as would be the case, for example, if such events call into question the validity of the going concern assumption. (Clarifies uncertainty at B/S date)
- d. Whether there have been any developments regarding contingencies. (Clarifies uncertainty at B/S date)
- e. Whether there have been increases in capital or issuance of debt instruments, such as the issue of new shares or debentures, or an agreement to merge or liquidate has been made or is planned. (Going Concern)
- f. Whether there have been any developments regarding risk areas and Contingencies. (Clarifies uncertainty at B/S date)
- g. Whether sales or acquisitions of assets have occurred or are planned. (Clarifies uncertainty at B/S date)
- h. Whether new commitments, borrowings or guarantees have been entered into





**2. Evaluating Management's Assessment**

(TAFFL)

I. Time Period to assess going concern should be as per applicable FRF, if law / regulation prescribe longer period then that should be used, in any case it should be minimum 12 months, if it is not auditor should request management to extend it.

III. Assumption used by management (Future sales / expenses / net cash flows etc)

IV. Management's plan for future action (Sale investments / Sale land / borrow money etc)

V. Feasibility of Managements Action Plan (Realistic / Historical evidence supporting action plan)

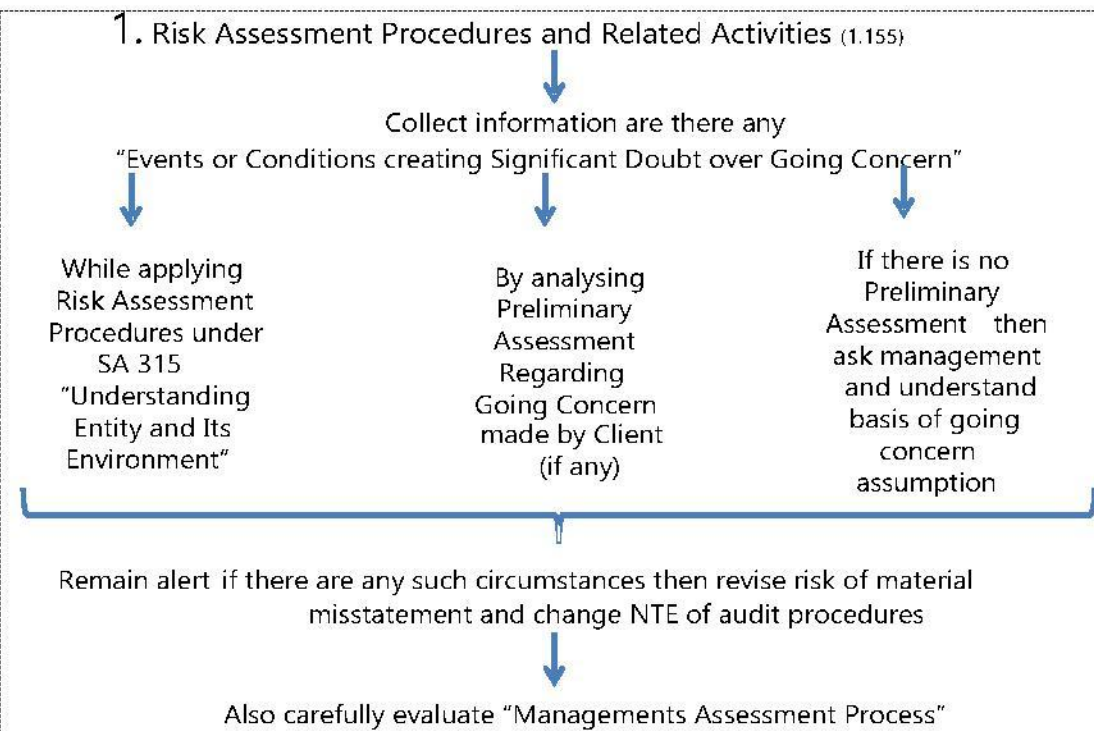
VI. No management's assessment or lack of analysis doesn't mean going concern is in appropriate. It may still be valid if there is evidence to support it (For example past history of profitable operations, good order book of next year etc)

**3. Period Beyond Management's Assessment**

→ Auditor should only inquire from management as to any events or conditions beyond management's assessment creating significant doubt over going concern.

→ Other than inquiry of management, the auditor does not have a responsibility to perform any other audit procedures

→ If there are any indications of going concern issues in above case, they need to be significant before the auditor needs to consider taking further action. In such case additional audit procedures will be applicable.



**4. Additional Audit Procedures When Events or Conditions Are Identified**

→ If there are indications find out whether there is material uncertainty against going concern and is there any mitigating factor

Continued....

1. Ask management to perform assessment of going concern, if they have not prepared yet
2. Cash flow forecast & analysis if prepared by entity then auditor check reliability of underlying data & adequate support for assumptions.
3. To check reliability of forecasts check forecast for prior periods with actual and forecast for current period with actual results as on date.
4. Evaluate management's plan of future action, whether it can really improve situation and is it feasible. (For example, its plans to liquidate assets, borrow money or restructure debt, reduce or delay expenditures, or increase capital.)
5. Any additional information after assessment was prepared
6. Requesting written representation from management
7. Sometimes third party confirmation may be required (Banker / Investor etc)

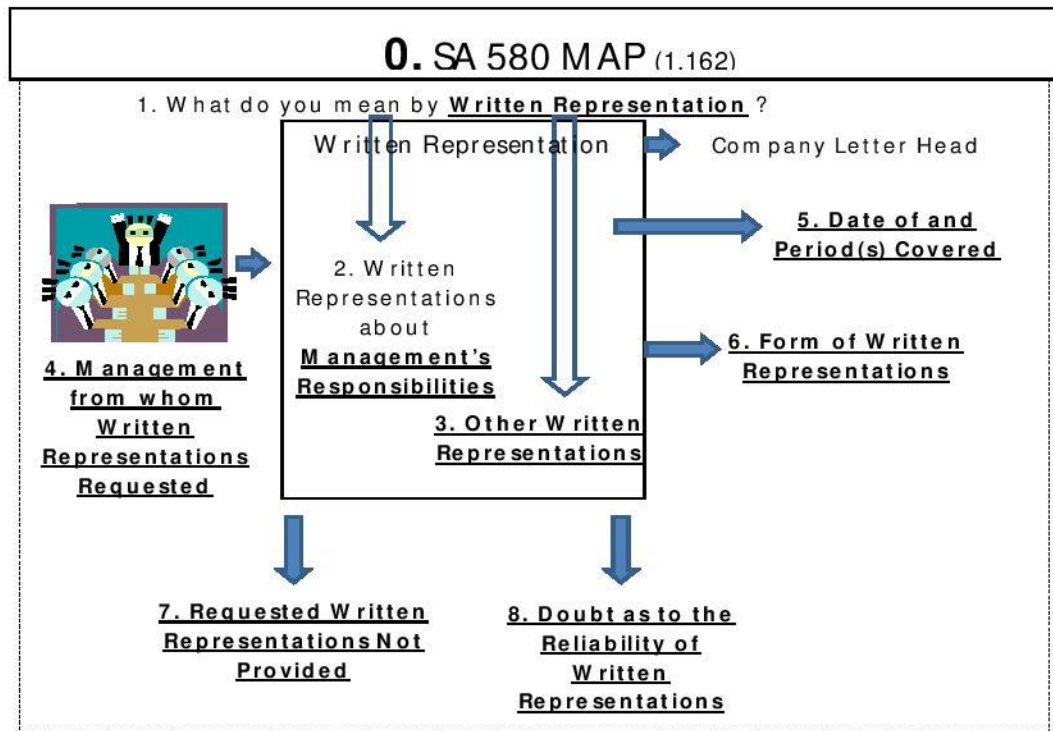
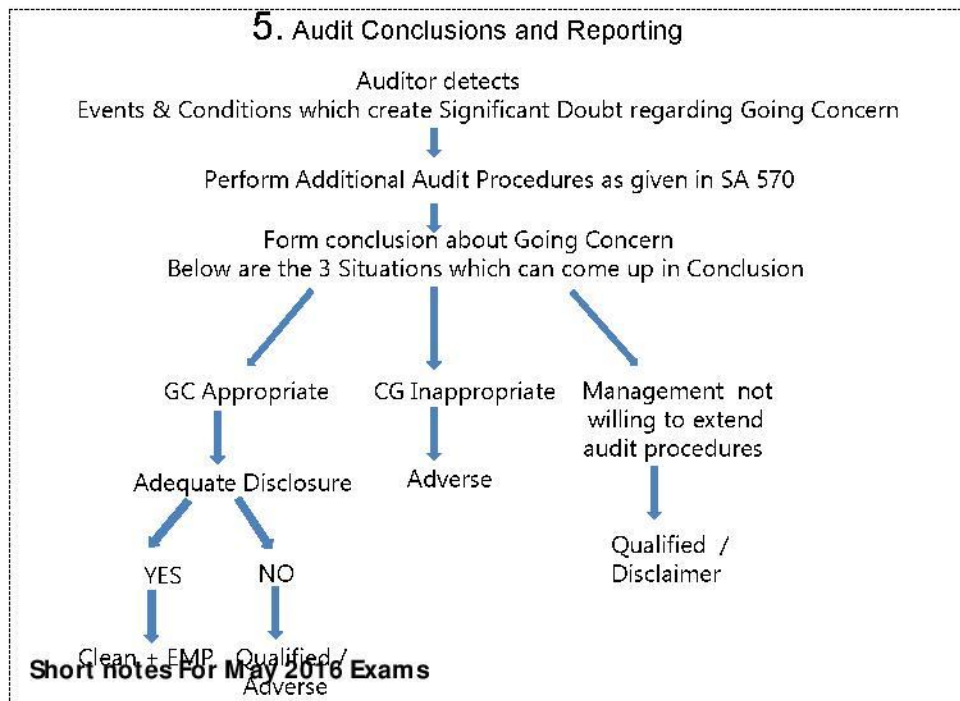
**6. Communication with Those Charged with Governance**

- Constitute a material uncertainty
- Appropriateness of Going Concern
- The adequacy of related disclosures

**7. Significant Delay in the Approval of Financial Statements**

If there is delay in finalising financial statements, auditor should inquire into the reasons.

If auditor believes that it is due to going concern issues, he shall perform additional audit procedures





**1. WRITTEN REPRESENTATION (1.162)**

A written statement by management provided to the auditor to confirm certain matters or to support other audit evidence. "Doesn't include FST / Books / Records (Otherwise nothing else will be required)"

(For example to confirm things which were committed at the start of the audit (preparation of financial statements, inform about all frauds & errors during the audit etc) or to support / corroborate other audit evidences said orally during the audit (Scrap value is Rs 2 lakhs only). Further it is not a primary and only evidence it is corroborative audit evidence, where we are not fully satisfied, for example even after seeing list of all contracts we may take WR to ensure it is complete.)

2 Types of written representations:-

1. Written Representations about Management's Responsibilities (Compulsory) | 2. Other Written Representations (As and when required)

**2. WRITTEN REPRESENTATIONS ABOUT MANAGEMENT'S RESPONSIBILITIES (1.162)**

It is basic pre condition (premises of audit) as per SA 210, it is so important that it should be reconfirmed

→ FST are as per FRF & they give true & fair view (if applicable)

→ All transactions are recorded & reflected in FST.

→ All relevant information & access is provided

\*Reconfirm EL & then take WR if situation demands

**3. Other Written Representation (1.163)**

(Apart from required as per other SAs)

**I. ADDITIONAL WR ABOUT THE FST (General) (Judgement Involved)**

→ Selection and application of accounting policies are appropriate.

**Proper Accounting of the following**

a. Title to, or control over, assets, the liens or encumbrances on assets, and assets pledged as collateral. (Eg Finance Lease)

b. Carrying value or classification of assets and liabilities; (Long Term Vs Short Term)

c. Liabilities, both actual and contingent;

d. Aspects of laws, regulations and contractual agreements, including Non Compliance (Restoration cost in contract)

**II. ADDITIONAL WR ABOUT INFORMATION PROVIDED**

→ That it has communicated to the auditor all deficiencies in internal control of which management is aware.

**III. WR ABOUT SPECIFIC ASSERTIONS**

"Strong **CCI**"

→ The entity's ability to pursue a specific course of action. (Will entity generate adequate CASH Flow in future to support its operations, when going concern is doubtful)

→ The entity's past history in carrying out its stated intentions. (Investments are always sold as per strategy set out by CFO, hence his WR should be taken as basis for Long term / Current Classification)

→ The entity's reasons for choosing a particular course of action. (Selected SLM, as decrease will be even / Booked DTA, as there is reasonable uncertainty)

→ Inconsistency with management's judgment or intent. (Some machines were scrapped earlier as compared to their useful life)

determined useful life / some investments were sold early as against intentions stated earlier, they are rare justified & will not occur again.

#### 4. Management from whom Written Representations is Requested (1.164)

→ From management with appropriate responsibility and knowledge (Eg CFO / CEO / MD etc)

→ It can be conditional, like as per information provided or after inquiry from actuary / engineer / legal counsel

#### 5. Date of & Period(s) Covered

→ Date shall be as near as practicable to, but not after, the date of the auditor's report. The written representations shall be for all financial statements and period(s) referred to in the auditor's report.

→ Take WR for last year again even if it was taken last year

→ Even if management has changed still they will have to provide WR for last year as whole FST is there responsibility irrespective of change

#### 6. Form of Written Representations

→ It should be in the form of letter addressed to auditor (It is not a agreement or MOU)

→ Mere expression of responsibility in law or regulation is not sufficient, written representation is must.

→ If management has made written public statements about its responsibility as per law (Covers responsibilities, From Proper authority & copy is made available to auditor) then no need to get such statements again in WR

### 7. Requested WR Not Provided (1.166)

Auditor requests written representation

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Management does not provide WR

Reevaluate Integrity & Reliability of any Representation

Take Appropriate Action

Offer to prepare WR / Just get BOD resolution

IF still No withdraw / Disclaimer / Qualify.

### 8. Doubt as to the Reliability of Written Representations (1.167)

Concern over  
Ethical Value/ Integrity  
/Competence /Diligence /  
Commitment  
[Eg → Illiterate/ Inexperience /  
Family son – MD ]

Inconsistency of WRwith  
other audit evidence  
[ **WR** → Intention to sale  
investment in long-term.  
**Media** -> Negotiation are  
going on.]

NI-IPC

Reassess RMM / Reconfirm EV / I / C / D / COM

Perform Further Audit Procedures

Clarify Concern / Resolve Inconsistency

Clarified / Resolved value

OK

Not clarified/ Resolved

May withdrawal  
Qualify / Disclaimer

It is a significant Matter all details & Conclusion should be documented.

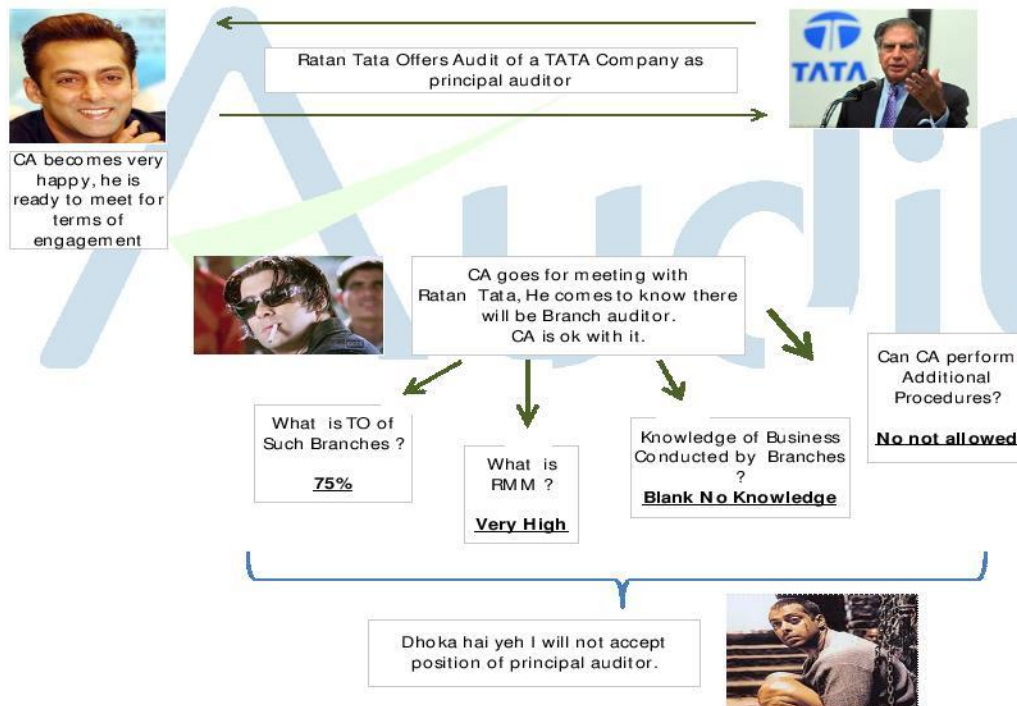


**SA 600 USING THE WORK OF ANOTHER AUDITOR**

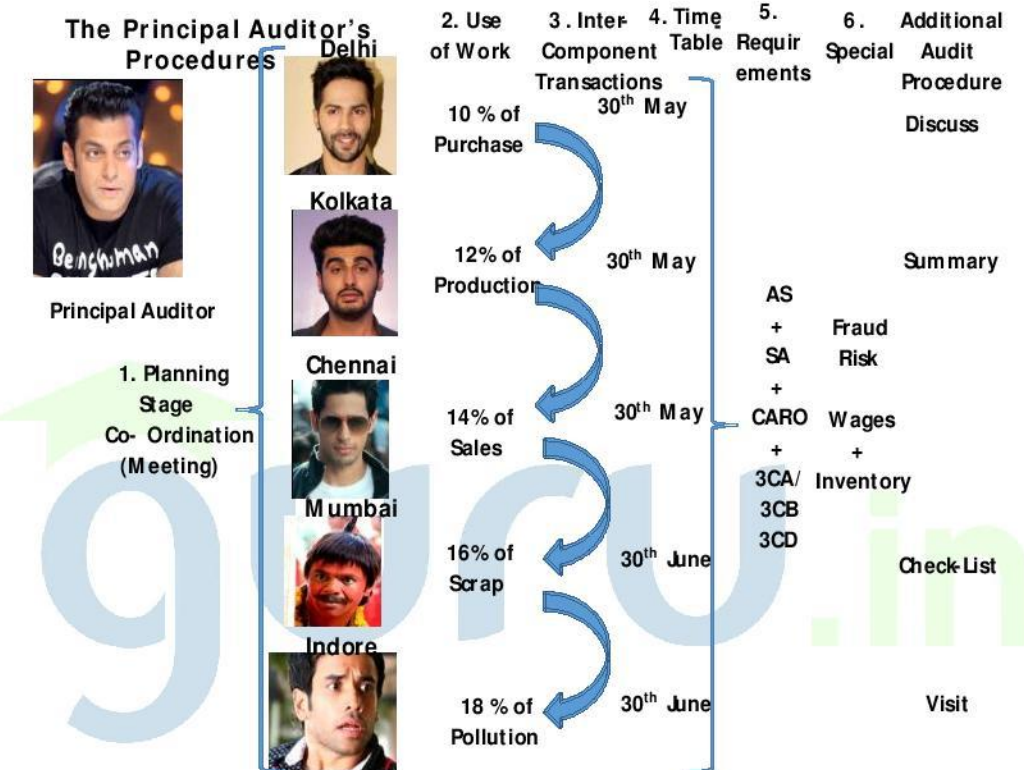
**SA-M AP**

1. Acceptance as Principal Auditor
2. The Principal Auditor's Procedures
3. Co-ordination between Auditors
4. Reporting Considerations
5. Division of Responsibility
6. Documentation

1. Acceptance as Principal Auditor



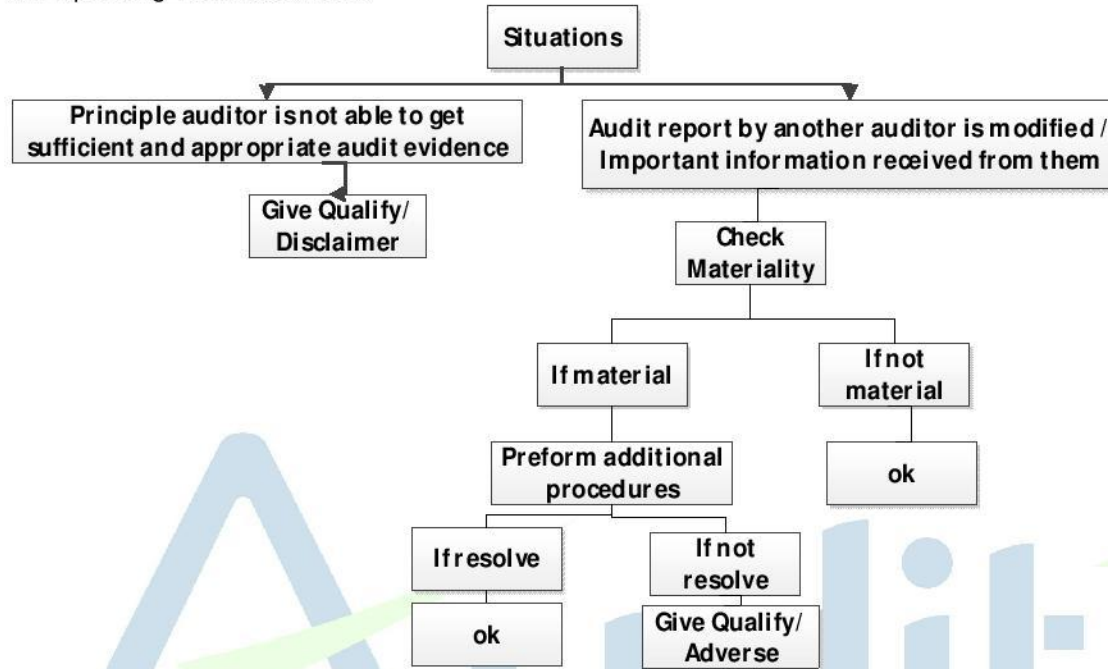
2. The Principal Auditor's Procedures



3. Co-ordination between Auditors (Repetitive)

- a. Sufficient Liaison (Free / Frank communication)
- b. Advice to another auditor (Eg Top management has suspicion over fraud in branch)
- c. Another auditor should communicate immediately any significant matter (Eg Government license norms are broken)
- d. Principal auditor should perform additional procedure if circumstances require (Discuss / Summary / Checklist / Visit)

4. Reporting Considerations



5. Division of Responsibility

Principal auditor should state clearly division of responsibility in his audit report (OMP, Name of Branches (if large only number) their total revenue / cash flows etc)

Principal auditor is not responsible for work entrusted to another auditor (Branch Auditor) unless there was suspicion about reliability of work.

6. Documentation

The principal auditor should document in his working papers

- a. The components audited by other, their significance
- b. The names of the other auditors;
- c. Individual components are not material.
- d. Procedures performed and the conclusions reached (Discussions etc & how he dealt with modified report & other communications)

SA 610 USING THE WORK OF ANOTHER AUDITOR

SA 610-MAP

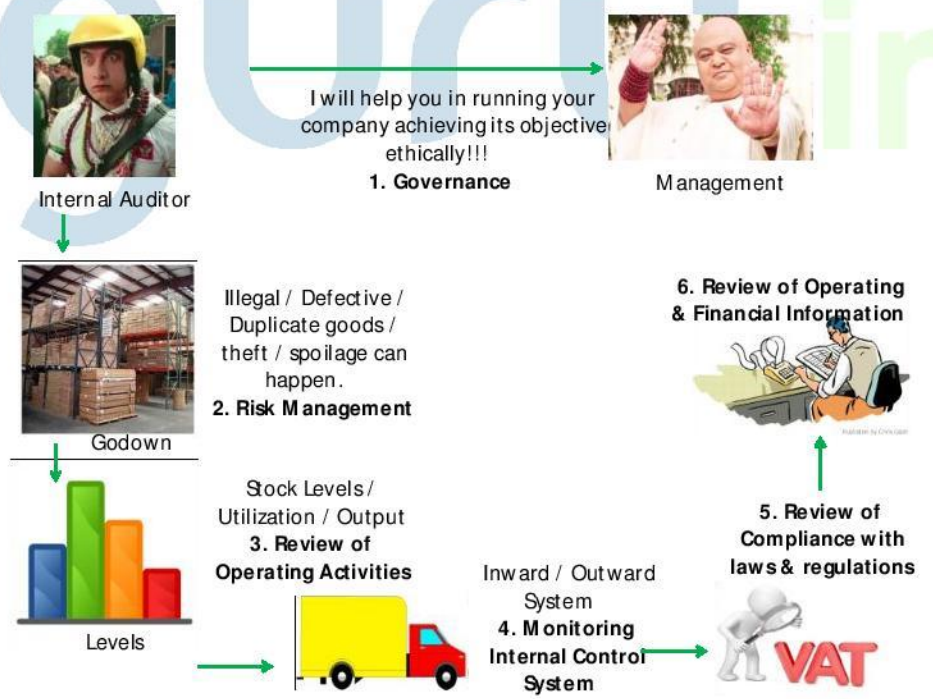
- 1. Scope and Objectives of the Internal Audit Function
- 2. Relationship between the Internal Audit Function and the External Auditor

Step 1:- Whether the work of the internal auditors is likely to be adequate for purposes of the audit (Whether to rely on work on Internal Auditor)

Step 2:- Planned effect of the work of the internal auditors on the nature, timing or extent of the external auditor's procedures (To what areas & extent we can rely)

Step 3:- Using Specific work of the Internal Auditors

1. Scope and Objectives of the Internal Audit Function





2. Relationship between the Internal Audit Function and the External Auditor

		
<b>Particulars</b>	<b>Internal Audit</b>	<b>External Audit</b>
<b>Definition</b>	It is a <b>review of activities, as a service to all levels of Management.</b>	<b>Audit of financial or other quantitative information of any entity</b> with a view to express an opinion thereon.
<b>Objective</b>	<b>Report upon the effectiveness of Internal Controls</b> , financial and others, as a contribution to the efficient use of resources within an organization.	To <b>express an opinion on the true and fair view</b> presented by Financial Statements.
<b>Necessity</b>	It is <b>voluntary. Compulsory to some companies U/ S 138</b>	It is normally <b>compulsory. U/ S 143</b>
<b>Auditor</b>	Generally an <b>employee of the Organization. As per Sec 138 CA / CMA / Other –May or May not be employee</b>	The External or Statutory Auditor is <b>not part of the organization.</b>
<b>Appointment</b>	By the <b>Management (BOD)</b> of the enterprise.	By the <b>owners (Shareholders)</b> of the enterprise.
<b>Scope of work</b>	It is <b>determined by the Management</b> and ranges from the pure review of accounting functions to the review of various operational services in the organization.	It <b>arises from the</b> responsibilities placed on him by the statute or the terms of engagement.

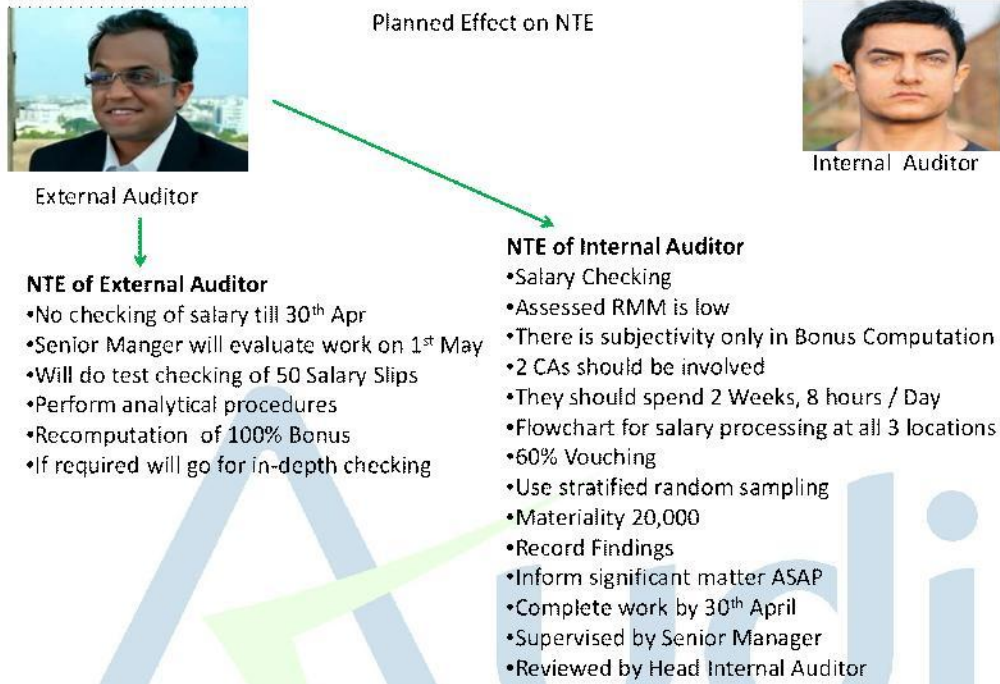
<b>Submission of Report</b>	To the <b>Management.</b>	To the <b>Shareholders.</b>
<b>Format of Report</b>	<b>No format</b> is prescribed. Guidelines in SIA 4	The aspects to be covered in the <b>Report are prescribed by law. SA 700</b>
<b>Orientation</b>	<b>Management Oriented.</b>	Oriented to the <b>needs of the users of Financial Statements</b> and also Management.

Step 1:- Whether the work of the internal auditors is likely to be adequate for purposes of the audit

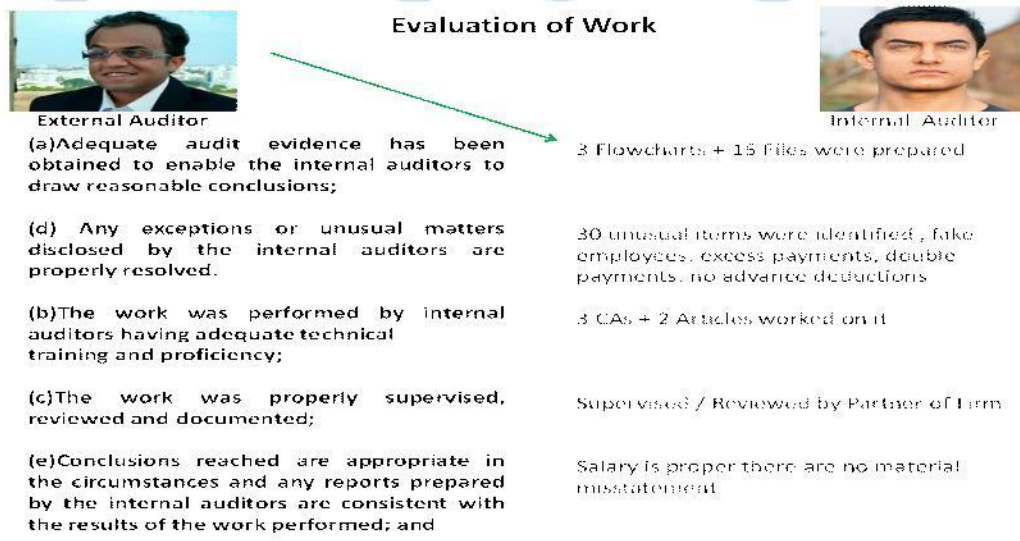
	Qualification Training & Exp → 10 Yrs each in PWC/ EY/ KPM G Team	CA / CPA / CMA / CIA All qualified & trained	
External Auditor	2. <b>Objectivity</b> Conflict of Interest Appointment & Reporting Scope Status Staff Appointments Recommendations	No Conflict of Interest TCWG No Restrictions Below Directors TCWG Supervises Full compliance	Internal Auditor
	3. <b>Due Professional Care</b> →	Systematic plan / supervised / Reviewed / Documented	
	4. <b>Communication</b> →	Team Members have internal control manual / Charts / Checklist etc No Restrictions Weekly emails & letters Monthly Meetings Important Matters are discussed ASAP	

**I am happy I will rely on work done by you**

Step 2-Planned Effect of the Work of the Internal Auditors on the Nature, Timing or Extent of the External Auditor's Procedures



STEP 3:- USING SPECIFIC WORK OF THE INTERNAL AUDITORS



**SA 620 USING THE WORK OF AN AUDITOR'S EXPERT**

**MAP**

**Expertise & Types of Experts**

- Step 1:- Determining the Need for an Auditor's Expert
- Step 2:- The Competence, Capabilities and Objectivity of the Auditor's Expert
- Step 3:- Obtaining an Understanding of the Field of Expertise of the Auditor's Expert
- Step 4:- Agreement with the Auditor's Expert
- Step 5:- Evaluating the Adequacy of the Auditor's Expert's Work
- Step 6:- Reference to the Auditor's Expert in the Auditor's Report

Expertise & Types of Experts

Expertise – Skills, knowledge and experience in a particular field, in a field other than accounts and audit





Step 1:- Determining the Need for an Auditor's Expert

400% change as compared to last year, there is policy / system on how to value oil well.


**2. Risk of Material Misstatement** Team only knows "Car needs petrol", some of them vomit with excess odor of oil." Always had experience of Bank Audits

Valuation depends on depth / width / density / viscosity / salt levels / surface / drilling cost / oil burning

**2. Complexity**

Oil Well Valuation Rs8000 Core  
Total Assets 10,000 Crore  
It accounts for 80% of B/S

**1. Material / Significant**



**3. Auditor's knowledge & experience**


1<sup>st</sup> Management Expert met with accident.  
2<sup>nd</sup> resigned  
3<sup>rd</sup> was removed  
4<sup>th</sup> is not yet appointed

**4. Management Expert**

Step 2:- The Competence, Capabilities and Objectivity of the Auditor's Expert


Engineer from Nepal University  
Training attendant @ petrol pump  
Experience: 8<sup>th</sup> Year Complete  
This is 1<sup>st</sup> Appointment (Not Complete)

**1. Competence**




Time: 2 din hai mere pass  
Equipment: kabaadi se loke aaya hon  
Team: 2 year dropouts: behail & vivek  
Do you know odissi: No (I know sign language)

**2. Capability**



Aditya: MD of Company Bhaiya Hai Mere  
I am 25% shareholders  
Saarein kharche isi dividend se nikaltein hai  
Mein sab aacha hi bolunga

**3. Objectivity**



**Auditor**

**Expert**

**Short notes For May 2016 Exams**

Step 3:- Obtaining an Understanding of the Field of Expertise of the Auditor's Expert

- a. Experience in auditing entities that require such expertise
- b. Education or professional development in the particular field. (Eg formal courses or trainings or discussion with experts)
- c. Discussion with auditors who have performed similar engagements.

**Step 4:- Agreement with the Auditor's Expert**

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

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

**3. Objective**

- Width
- Depth
- Quality
- Valuation

**4. Role of Expert**

- To arrange equipment
- To arrange team
- To follow time limits

**5. Role of Auditor**

- To get permissions to access & use oil well from management
- Request Management to send drilling data (source data)
- To arrange satellite images

**2. Scope**

- Only oil wells in Orissa
- Without considering climate change



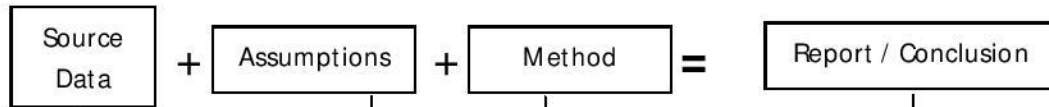
**1. Nature of work**

- Analysing company drilling data of past 2 years
- Satellite Images Evaluation
- 10 Samples from different spots for lab testing
- Drilling 5000 ft

**7. Confidentiality**

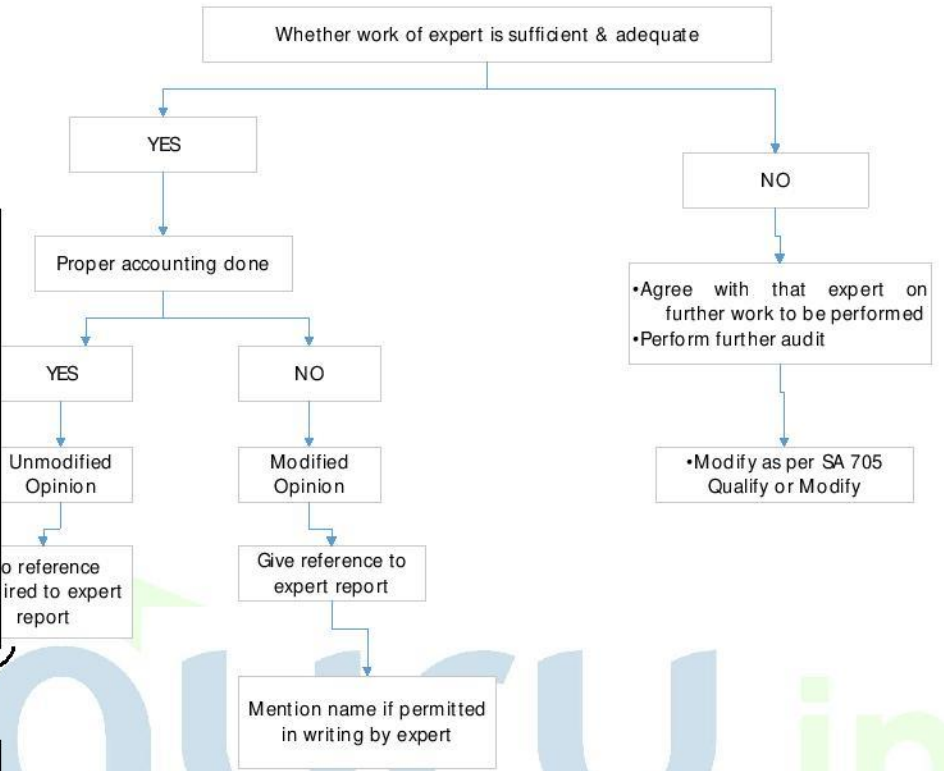
Declaration from each team member of expert  
Penalty of Rs 25 lakhs if there is a breach + damages

Step 5:- Evaluating the Adequacy of the Auditor's Expert's Work



- |  |  |  |
|--|--|--|
| <ul style="list-style-type: none"> <li>a. Origin (External / Internal)</li> <li>b. ICS (Internally Generated)</li> <li>c. Transmission to expert</li> <li>d. Complete &amp; Consistent</li> <li>e. Test source data</li> </ul> | <ul style="list-style-type: none"> <li>a. Generally Accepted</li> <li>b. As per FRF</li> <li>c. Consistent with Mgt</li> <li>d. Any specialised model (Internally developed Method)</li> </ul> | <p><b>Relevant</b></p> <ul style="list-style-type: none"> <li>a. Clearly expressed (no ambiguity) as per objectives &amp; scope agreed</li> <li>b. Presented in manner consistent with FRF</li> <li>c. Appropriate time period &amp; subsequent events</li> </ul> <p><b>Reasonable</b></p> <ul style="list-style-type: none"> <li>a. Errors / Deviations encountered</li> <li>b. Reservations / Limitations / Restrictions on use</li> </ul> |
|--|--|--|

If auditor concludes that experts work is not adequate, he should perform additional audit procedures like assigning further work to same expert or appointing new expert or performing work himself → if he is still not able to obtain sufficient & appropriate evidence then modify opinion as per SA 705 (Quality / Disclaimer)



Step 6:- Reference to the Auditor's Expert in the Auditor's Report

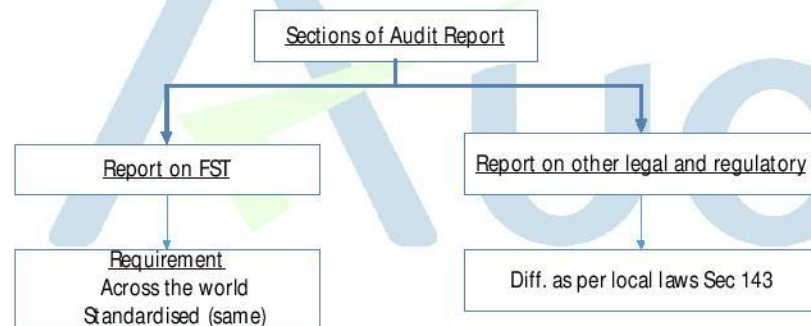


**SA 700 FORMING AN OPINION AND REPORTING ON FINANCIAL STATEMENTS**

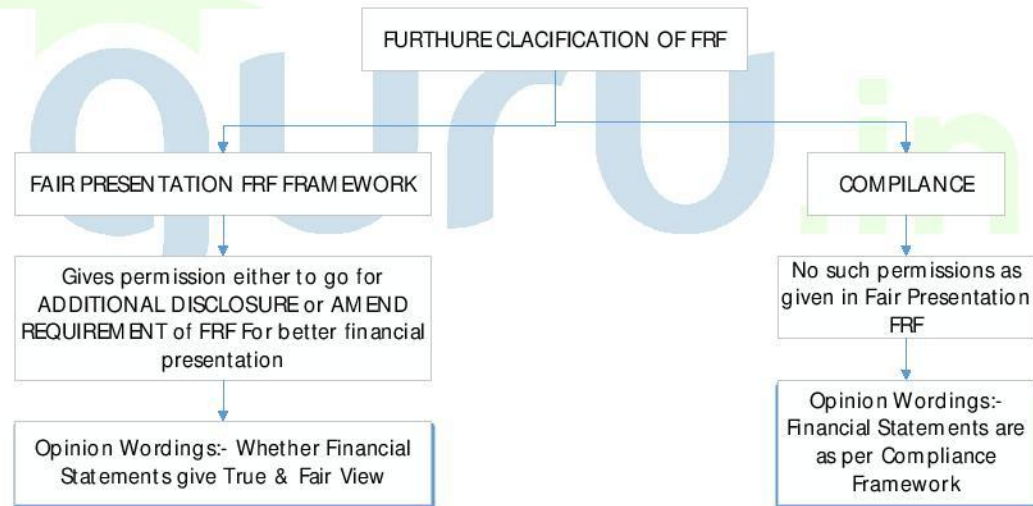
MAP

1. Basic Elements of Audit Report
2. Types of FRF & Its Impact on Audit Report
- 3.2 FRFs & 2 Standards on Auditing in one Audit Report
4. Format of Audit report Prescribed by LAW
5. Supplementary Information
6. True & Fair
7. Forming opinion on Financial Statements Topics related to SA 700
8. Report Vs Certificate
9. Reporting to Shareholders Vs Reporting to TCWG

1. Basic Elements of the Auditor Report



1. Title
2. Addressee:- 2 Parts of Audit Report  
Report on FST (1st Part)
3. Intro Paragraph
4. Management Responsibility
5. Auditor Responsibility
6. Opinion Para  
Report on Other Legal & Regulatory Requirement (2nd Part)
7. Signature / 8. Date / 9. Place



3. 2FRFs & 2 Standards in one Audit Report

2 FRFs

a. Reference to More than One Financial Reporting Framework Entity may decide to present financial statement as per 2 FRF, for example as per AS & IFRS.

b. So description will contain both FRFs provided both the FRFs should be fully complied (i.e. can't use particular FRF only for one or two item of FST) & no need for reconciliation between both.

2 Auditing Standards

Audits Conducted in Accordance with Both Auditing Standard issued by ICAI and International Standard on Auditing · Refer both provided:-

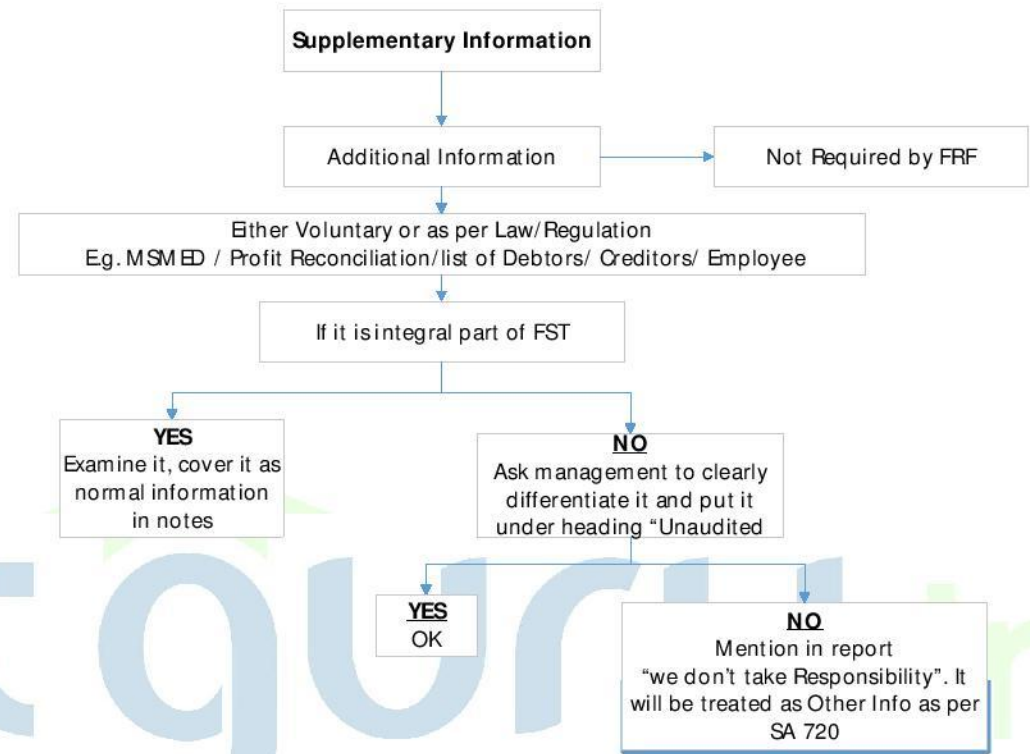
- A) THERE IS NO CONFLICT i) to form a different opinion, or (ii) not to include an Emphasis of Matter paragraph that and
- B) The auditor's report includes, at a MINIMUM ELEMENTS.

4. Auditor Report Prescribed by Law or Regulation

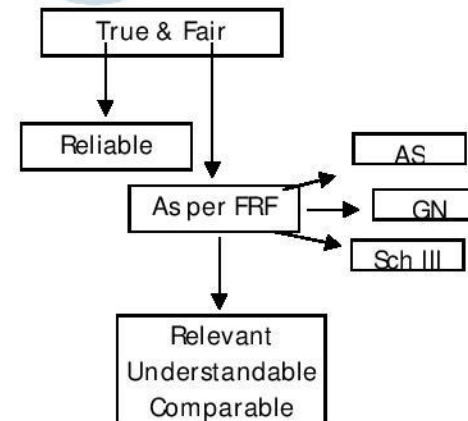
{Ex: Format of tax audit report prescribed by law}

Refers to Standards on Auditing only if the auditor's report includes, at a minimum, each of 9 Basic Elements of Audit Report. In India we don't refer to SA 700 while preparing tax audit report because it is not having management responsibility & auditor responsibility paragraph.

5. Supplementary Information



6. True & Fair





7. Forming an Opinion on the Financial Statements

- Summary of detailed theory, in easy to remember sequence
- No Omissions / Authorized / Accuracy
- Quality Accounting Policy
- As per Accounting Standards
- Followed Consistently
- Displayed in Financial Statements
- Effect of Management Bias in Estimates
- Estimates are reasonable
- Presentation as per Schedule III
- Disclosure as per AS & SCH III
- Major transactions & events are disclosed
- No material misstatement whether due to fraud or error
- Misstatements are corrected and uncorrected as immaterial
- Sufficient & Appropriate Evidence is Obtained
- Presents real financial position of entity
- Relevant / Reliable / Comparable / Understandable

8. Report Vs Certificate

A certificate is a written confirmation of the accuracy of the facts stated therein and does not involve any estimate or opinion. The term 'certificate' is, therefore, used where the auditor verifies the accuracy of facts.

The 'report' involves expression of opinion which may differ from one professional to another. There is no question of exactitude in case of a report since the information contained therein is based on estimates and involves judgement element.

9. Reporting to Shareholders V/s Reporting to TCWG

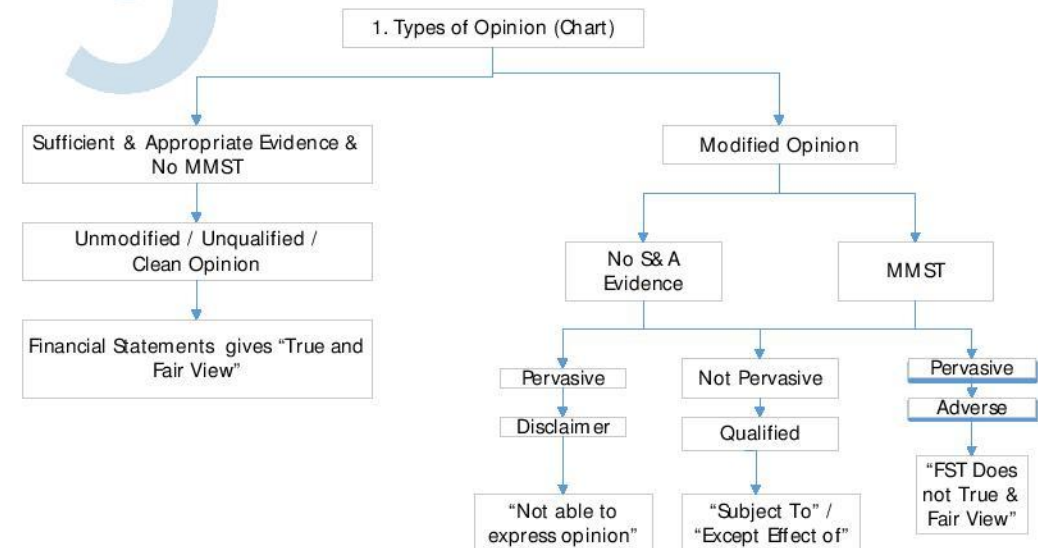
Reporting to Shareholders	Reporting to Those Charged with Governance.
Section 143 of the Companies Act, 2013 deals with the provisions relating to reporting to Shareholders. Thus, it	SA 260 deals with the provisions relating to reporting to those Charged with Governance.

is a Statutory Audit Report which is addressed to the members.	
Statutory Audit Report is on true and fair view and as per prescribed Format.	It is a reporting on matters those charged with governance like scope of audit, audit procedures, audit modifications, etc.
Statutory Audit Reports are in public domain.	Reporting to those Charged with Governance is an internal document i.e. private report.

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

- 1.Types of Opinion
- 2.Analysis of Reasons for Modification
- 3.Effect of Modification
- 4.Limitation of Scope after accepting engagement
- 5.Difference Between Various Types of Report
- 6.Can 1 Audit Report have all Qualified / Adverse / Disclaimer together?

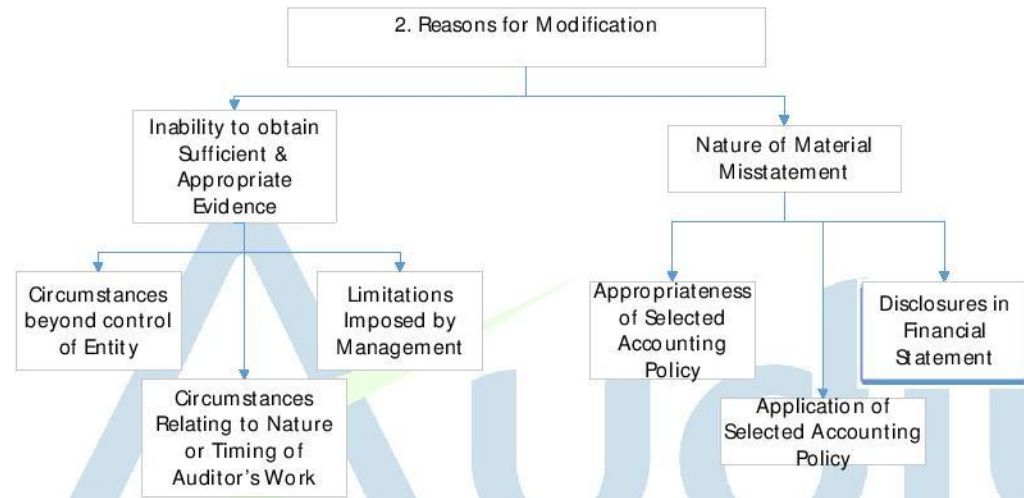
1.Types of Opinion



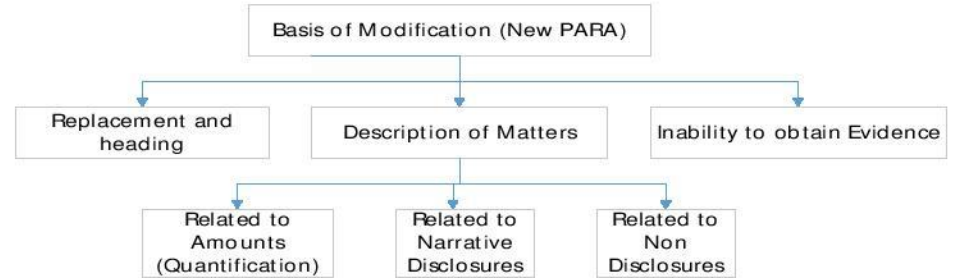
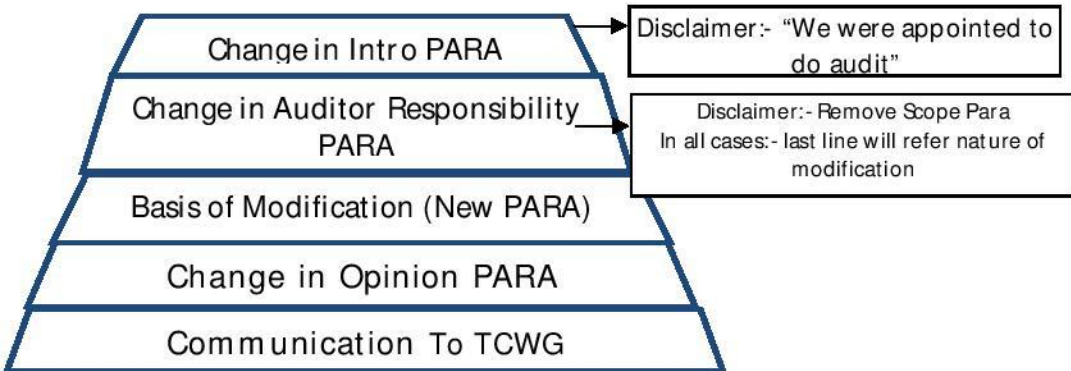
Pervasive

- a. Affects many items in financial statements
- b. Affects specific element but it is substantial part of financial statement
- c. Related to disclosures which are fundamental to users of financial statement

2. Analysis of Reasons for Modification



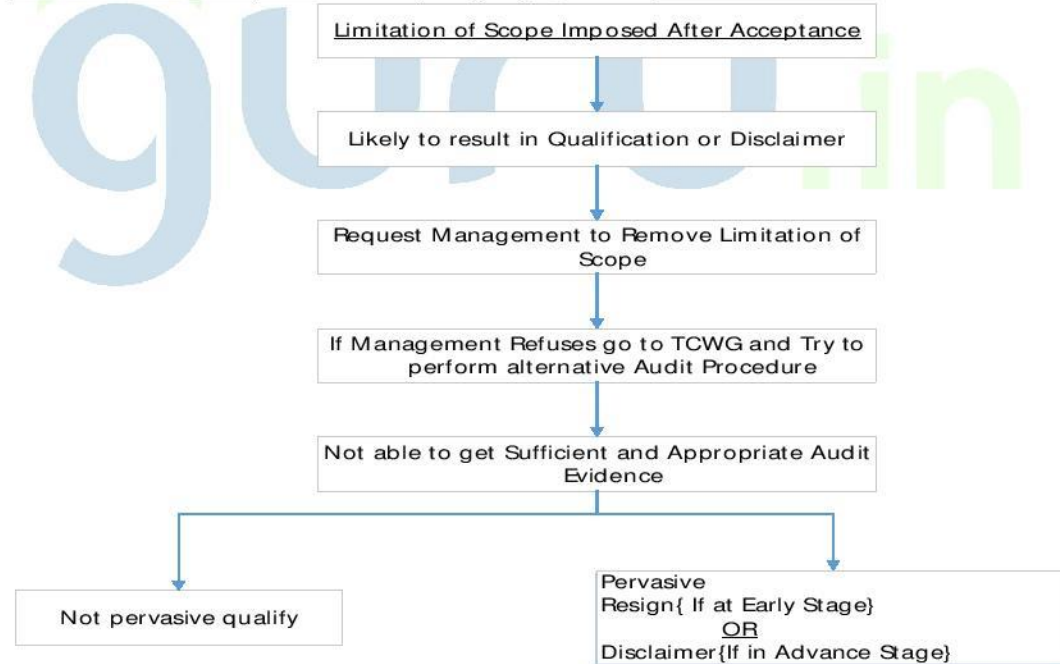
3. Effect of Modification



COMMUNICATION TO TCWG:-

When the Auditor expects to modify the Opinion in the Auditor's Report, the Auditor shall communicate with Those Charged with Governance, the circumstances that led to the expected modification, and the proposed wording of the modification.

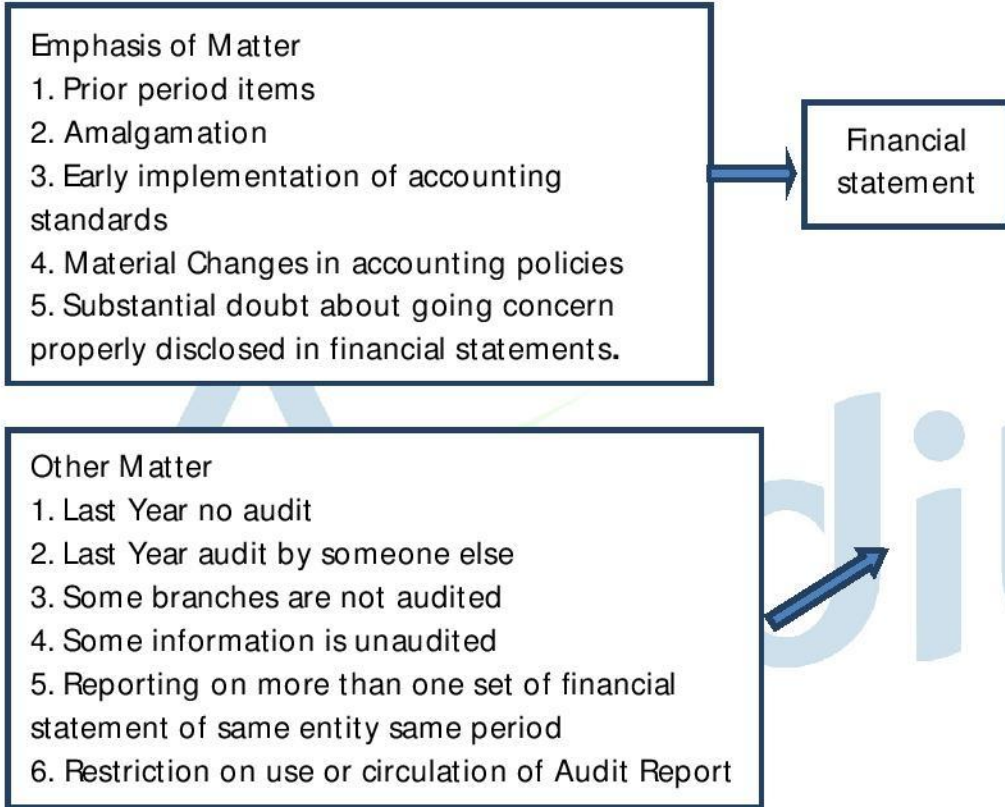
4. Limitation of Scope after accepting engagement





SA 706

EMPHASIS OF MATTER PARAGRAPHS & OTHER MATTER PARAGRAPHS  
IN THE INDEPENDENT AUDITOR'S REPORT



		<b>report.</b>
In audit report	Places immediately <b>after the opinion paragraph</b> in auditor's report.	After the " <b>opinion "para&amp; "emphasis of matter " para</b>
Heading	"emphasis of matter"	"other matter "
It includes	<ul style="list-style-type: none"> <li>• Clear reference to the matter being <b>emphasized.</b></li> <li>• Where <b>exactly it can be found</b> in the financial statement.</li> </ul>	Other <b>reporting responsibilities</b> in case of audit of a company.
Examples	<ul style="list-style-type: none"> <li>• Prior period items</li> <li>• Material Changes in accounting policies</li> <li>• Amalgamation</li> <li>• Substantial <b>doubt about going concern properly disclosed</b> in financial statements.</li> </ul>	<ul style="list-style-type: none"> <li>• Last Year no audit</li> <li>• Last Year audit by someone else</li> <li>• Some branches are not audited</li> <li>• Some information is unaudited</li> </ul>

COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE

If the auditor expects to include an Emphasis of Matter or an Other Matter paragraph in the auditor's report, the auditor shall communicate with those charged with governance regarding this expectation and the proposed wording of this paragraph.

	<b>Emphasis of matter paragraph</b>	<b>Other matter paragraph</b>
Meaning	Para refer to a matter <b>appropriately incorporated statement.</b>	Para relating to matter, other than those in financial statements, which is relevant to users <b>understanding or auditors responsibility or his</b>

**SA 710  
COMPARATIVE INFORMATION CORRESPONDING FIGURES AND  
COMPARATIVE FINANCIAL STATEMENTS**

SA-MAP

1. Comparatives & Audit Procedures
2. Approaches to Comparative Information
3. Corresponding Figure Vs Comparative Financial Statements
4. Requirement of OMP
5. Misstatements in Comparatives

1. Comparatives & Audit Procedures

Comparative information– The amounts and disclosures respect of one or more prior periods.

Audit procedures

I. Basic Evaluation of comparative information (Must / Compulsory)

- a. Understand requirement of applicable FRF
- b. Check whether requirements of FRF is fulfilled
- c. Compare amounts with previous year financial statements / closing ledger balances of last year
- d. Examine consistency of accounting policy as compared to previous year
- e. If there changes then they should be disclosed appropriately as per AS 5

II. Additional procedures in case of Material Misstatement:

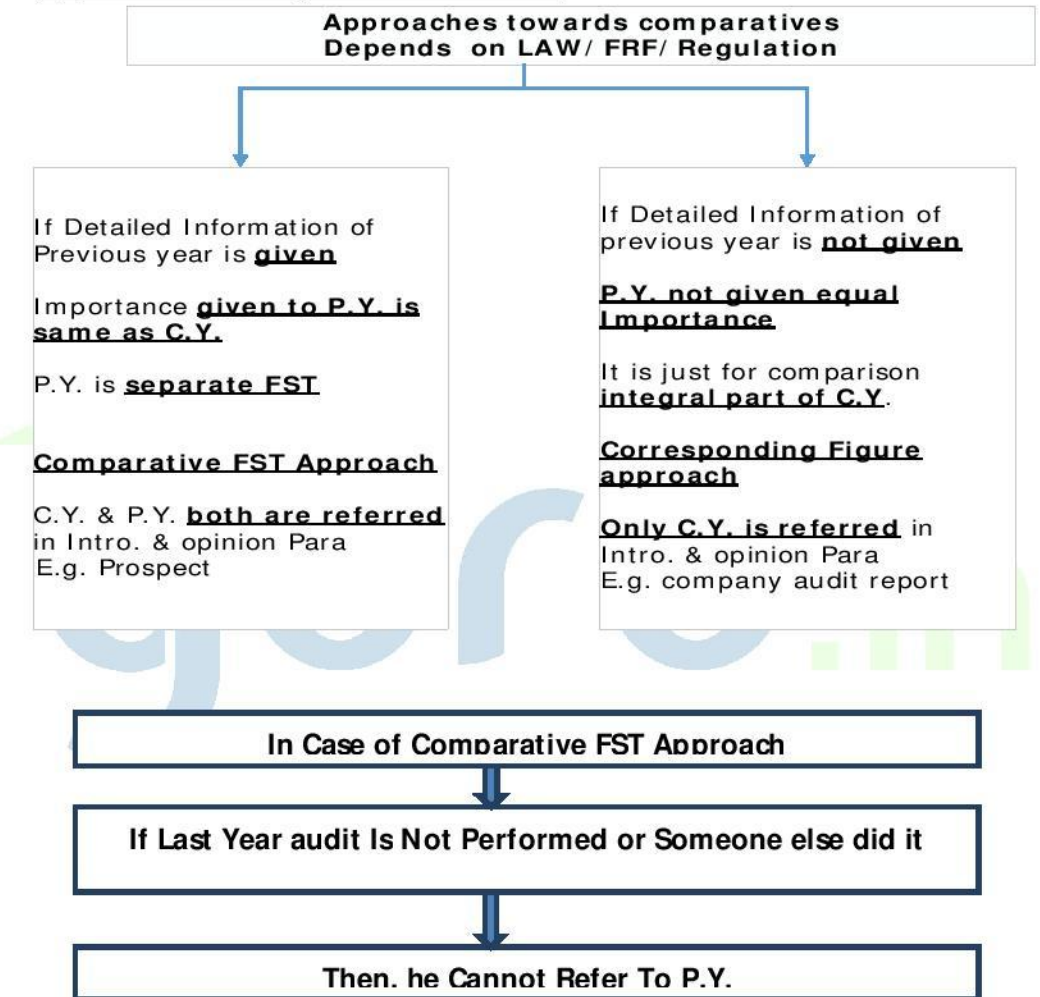
If auditor becomes aware of possible misstatement or misstatement then he shall perform additional audit procedures as per circumstances. Asking for previous year workings etc  
If he was himself auditor then it is a subsequent event as per SA 560 (if before AGM in Indian context) then revision of financial statements may be required.

III. Written Representations:

- a. Request Written Representations for all periods referred to in the opinion.

Also Obtain a specific Written Representation regarding any Prior Period Item that is separately disclosed in the current year's Statement of Profit and Loss.

2. Approaches to Comparative Information



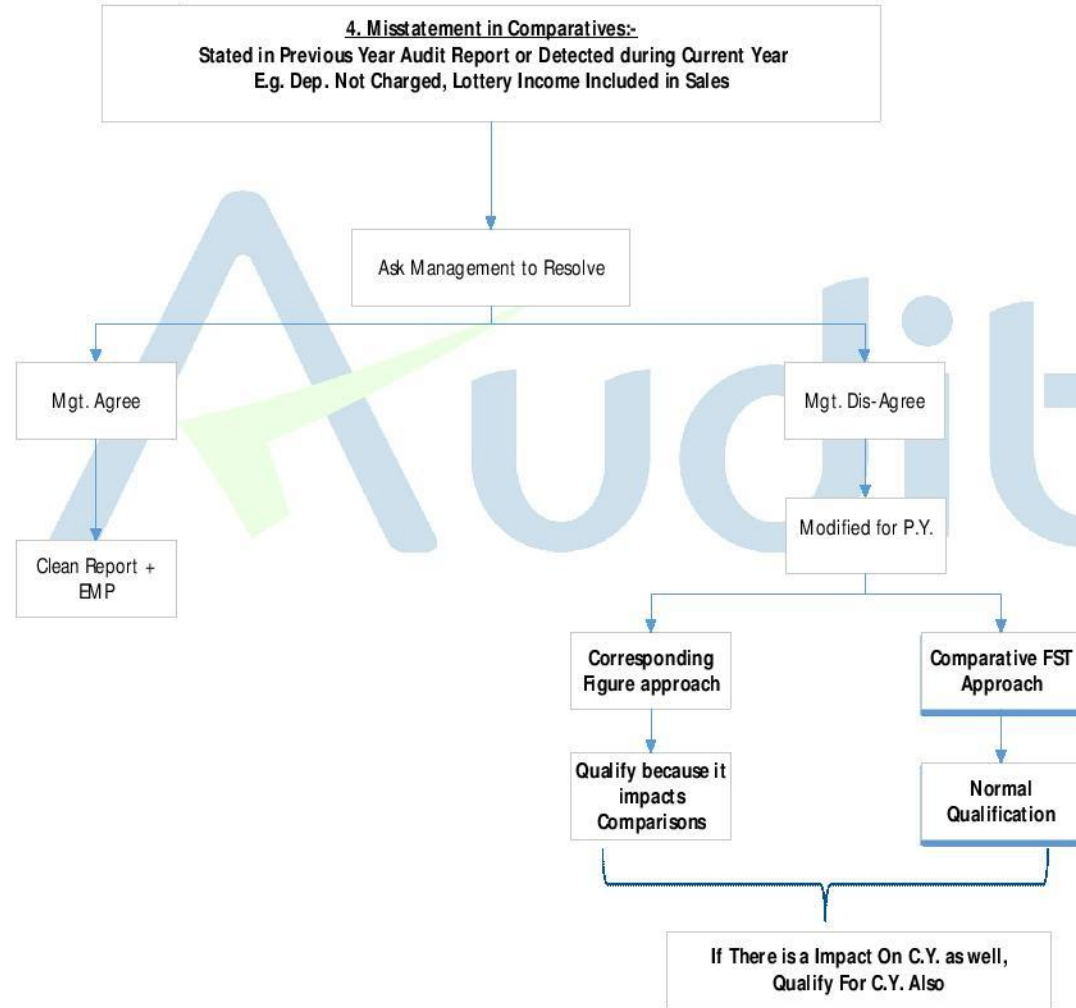


**3. Requirement of OMP**

OMP should be given if previous audit is done by someone else or audit has not been conducted both approaches.

Details such as

1. Name of the auditor
2. Type of opinion, if modified then the reason for the same should be given
3. Date of Report

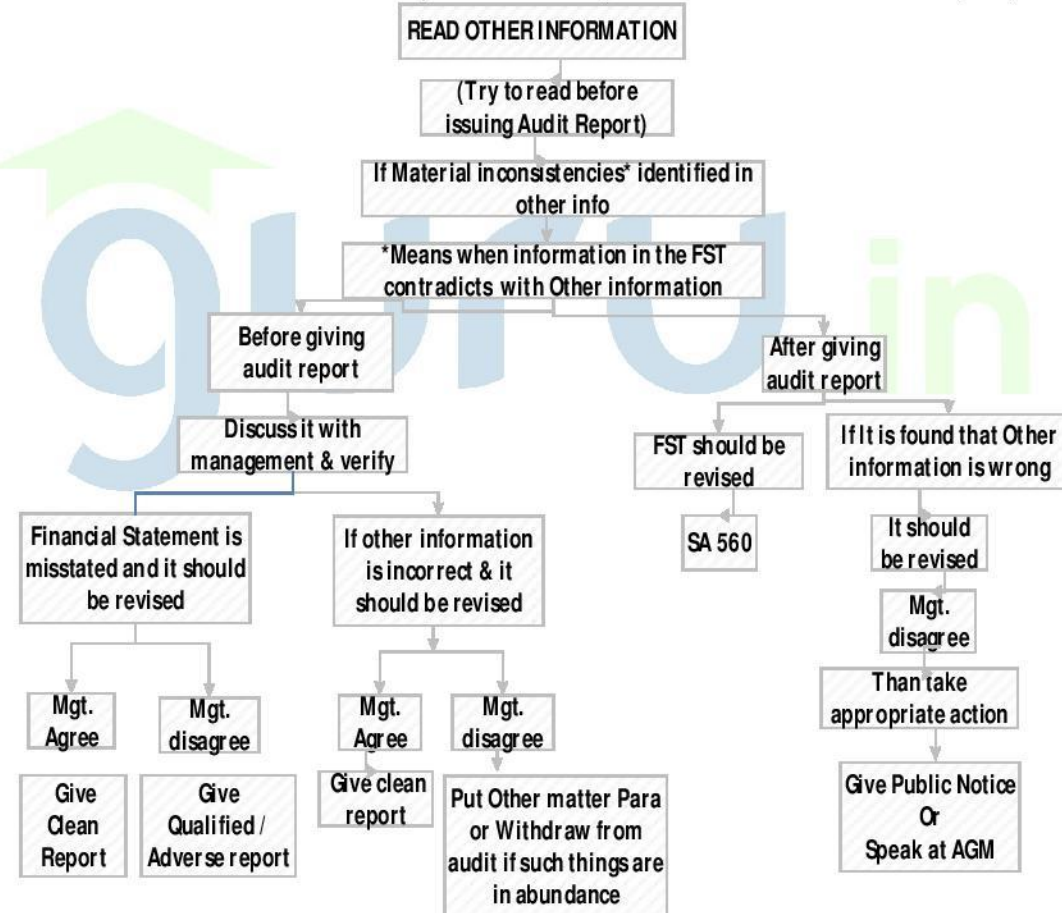


5. If Auditor is Changes his Opinion regarding P.Y. as Report Earlier then in such case appropriate OMP should be put explaining how opinion of auditor about previous year in last year report has changes in current year report.

**SA 720**

**THE AUDITOR'S RESPONSIBILITY IN RELATION TO OTHER INFORMATION IN DOCUMENTS CONTAINING AUDITED FINANCIAL STATEMENTS**

Other information – Financial and non-financial information (other than the financial statements and the auditor's report thereon) which is included, either by law, regulation or custom, in a document containing audited financial statements and the auditor's report thereon. (All documents in annual report)





Audit

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# AUDIT

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<b>NAGPUR</b>	<b>11<sup>th</sup> April</b>
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Course Coverage with Short Notes

**Revise SAs +**  
Ques. of PM & 3 RTPs





