

CA FINAL AUDIT

**ADVANCED AUDITING, ASSURANCE
AND PROFESSIONAL ETHICS**

Theory Notes

4th Edition



By India's Most Dynamic Faculty For Audit

CA Aarti Lahoti

www.aartilahoti.com

MODES OF LEARNING : Pendrive / Google Drive / Face to Face / Livestream

CA FINAL

GROUP - I

ADVANCED AUDITING, ASSURANCE AND PROFESSIONAL ETHICS

(THEORY NOTES)

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CA Aarti N. Lahoti

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Dear Students,

IT'S ALL ABOUT AUDIT!

It gives me immense pleasure to present before you the 4th Edition of Advanced Auditing, Assurance & Professional Ethics – Theory Notes & Q – A Scanner – for CA Final.

I have made an humble attempt to include all theory, Q & A & Amendments released by ICAI through its different mediums viz. Latest Study Material, Suggested Answers, Mock Test Papers & Revision Test Papers in this book.

Any constructive criticism is always welcome. @ aartilahoti9@gmail.com

The greatest strength of this book is its wholistic approach towards the subject – a one stop solution for the entire subject of CA Final Auditing. It covers each & every topic of the syllabus in a tabular & pointwise format & also the myriad varieties of questions in relation to the same.

*Having **CONCEPTUAL CLARITY** about the topics is half the battle won!!! To complete it you need to do a lot of **WRITING PRACTICE**. As a general problem faced by students is that though they understand the concepts but they are not able to put it in words & this happens merely due to lack of writing practice. So never forget that!*

*And one final piece of advice would be to do **CUMULATIVE REVISIONS** of the subject so that you are able to retain the subject better.*

Wishing you all the very best for your exams and for a brightful future!

Happy Auditing!

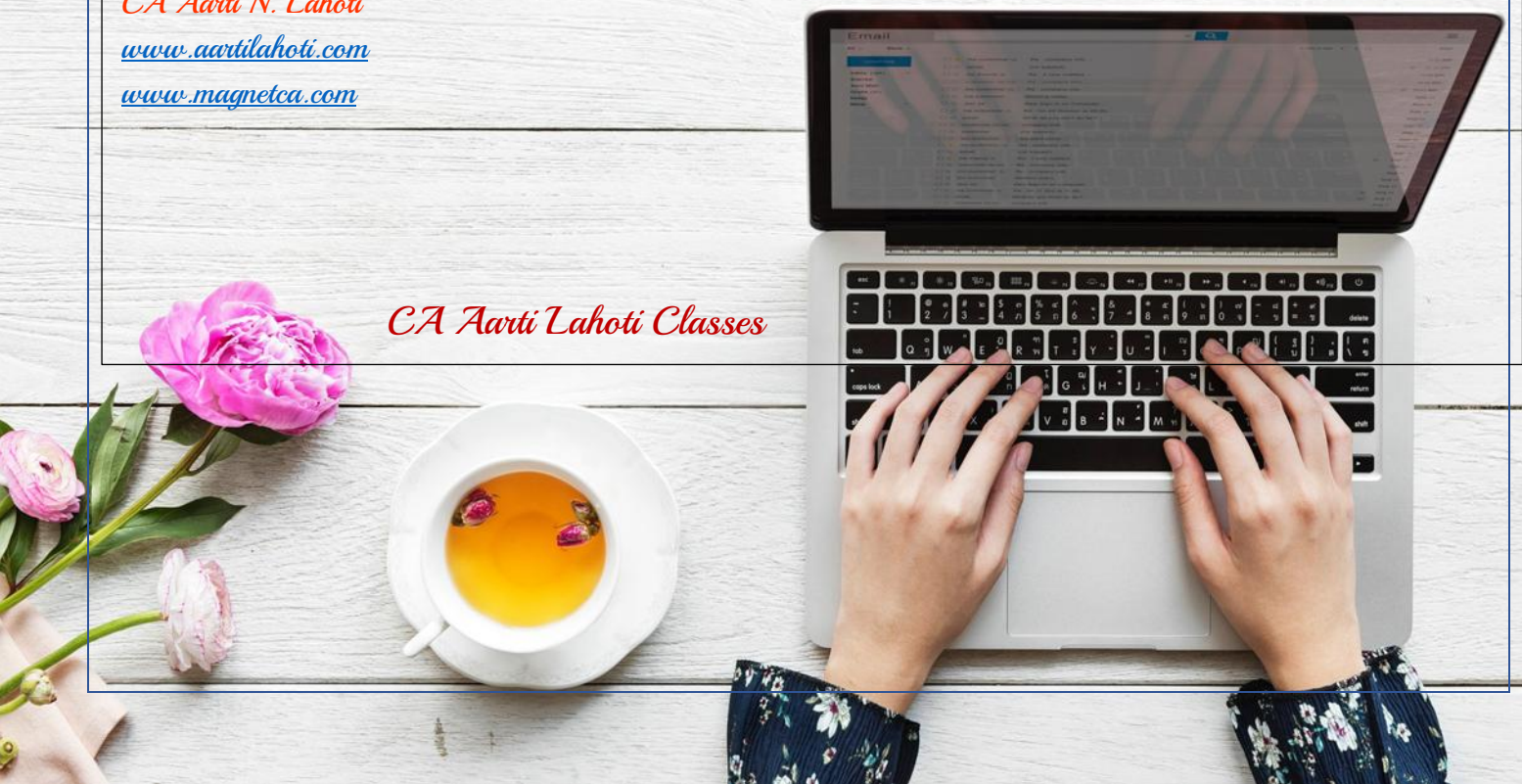
Regards,

CA Aarti N. Lahoti

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CHAPTER

0

INTRODUCTION & QUICK RECAP

1

LIST OF QUALITY CONTROL & ENGAGEMENT STANDARDS

Std. No.	Title of the Standard	Effective Date
1 – 99	STANDARDS ON QUALITY CONTROL (SQC)	
SQC 1	Quality Control for Firms that Perform Audits & Reviews of Historical Financial Information, & Other Assurance & Related Services Engagements	01.04.2009
100 – 899	AUDITS & REVIEWS OF HISTORICAL FINANCIAL INFORMATION (SA)	
100 – 199	INTRODUCTORY MATTERS	
200 – 299	GENERAL PRINCIPLES & RESPONSIBILITY	
SA 200	Overall Objectives of the Independent Auditor & the Conduct of an Audit in Accordance with Standards on Auditing	01.04.2010
SA 210	Agreeing the Terms of Audit Engagements	01.04.2010
SA 220	Quality Control for an Audit of Financial Statements	01.04.2010
SA 230	Audit Documentation	01.04.2009
SA 240	The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements	01.04.2009
SA 250	Consideration of Laws & Regulation in an Audit of Financial Statements	01.04.2009
SA 260	Communications with Those Charged With Governance	01.04.2017
SA 265	Communicating Deficiencies in Internal Control to Those Charged with Governance & Management	01.04.2010
SA 299	Joint Audit of Financial Statements	01.04.2018
300 – 499	RISK ASSESSMENT & RESPONSE TO ASSESSED RISKS	
SA 300	Planning an Audit of Financial Statements	01.04.2008
SA 315	Identifying & assessing the Risks of Material Misstatements through understanding the Entity & Its Environment	01.04.2008
SA 320	Materiality in Planning & Performing an Audit	01.04.2010
SA 330	Auditor's Responses to Assessed Risks	01.04.2008
SA 402	Audit Considerations Relating to an Entity Using a Service Organisation	01.04.2010
SA 450	Evaluation of Misstatements Identified During the Audit	01.04.2010
500 – 599	AUDIT EVIDENCE	
SA 500	Audit Evidence	01.04.2009
SA 501	Audit Evidence – Specific Considerations for Selected Items	01.04.2010
SA 505	External Confirmations	01.04.2010
SA 510	Initial Audit Engagements - Opening Balances	01.04.2010
SA 520	Analytical Procedures	01.04.2010
SA 530	Audit Sampling	01.04.2009
SA 540	Auditing of Accounting Estimates, including Fair Value Accounting Estimates & Related Disclosures	01.04.2009
SA 550	Related Parties	01.04.2010
SA 560	Subsequent Events	01.04.2009
SA 570	Going Concern	01.04.2017
SA 580	Written Representations	01.04.2009
600 – 699	USING WORK OF OTHERS	
SA 600	Using the Work of Another Auditor	01.04.2002

SA 610	Using the work of Internal Auditors	01.04.2016
SA 620	Using the Work of an Auditor's Expert	01.04.2010
700 – 799	AUDIT CONCLUSIONS & REPORTING	
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SA 701	Communicating Key Audit Matters in the Independent Auditor's Report	01.04.2018
SA 705	Modifications to the Opinion in the Independent Auditor's Report	01.04.2018
SA 706	Emphasis of Matter Paragraphs & Other Matter Paragraphs in the Independent Auditor's Report	01.04.2018
SA 710	Comparative Information – Corresponding Figures & Comparative Financial Statements	01.04.2011
SA 720	The Auditor's Responsibilities Relating to Other Information	01.04.2018
800 – 899	SPECIALISED AREAS	
SA 800	Special Considerations - Audits of Financial Statements Prepared in Accordance with Special Purpose Framework	01.04.2011
SA 805	Special Considerations - Audits of Single Financial Statements & Specific Elements, Accounts or Items of a Financial Statement	01.04.2011
SA 810	Engagements to Report on Summary Financial Statements	01.04.2011
2000 – 2699	STANDARDS ON REVIEW ENGAGEMENTS (SRE)	
SRE 2400	Engagements to Review Historical Financial Statements	01.04.2016
SRE 2410	Review of Interim Financial Information Performed by the Independent Auditor of the Entity	01.04.2010
3000 – 3699	STANDARDS ON ASSURANCE ENGAGEMENTS (SAE)	
SAE 3400	The Examination of Prospective Financial Information	01.04.2007
SAE 3402	Assurance Report on Controls at a Service Organisation	01.04.2011
SAE 3420	Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus	01.04.2016
4000 – 4699	STANDARDS ON RELATED SERVICES (SRS)	
SRS 4400	Engagements to Perform Agreed-upon Procedures Regarding Financial Information	01.04.2004
SRS 4410	Compilation Engagements	01.04.2016

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LIST OF IMPORTANT ABBREVIATIONS

AFRF (SA 200)	APPLICABLE FINANCIAL REPORTING FRAMEWORK
FRF	FINANCIAL REPORTING FRAMEWORK
GPF	GENERAL PURPOSE FRAMEWORK
SPF (SA 800)	SPECIAL PURPOSE FRAMEWORK
RMM (SA 200)	RISKS OF MATERIAL MISSTATEMENT
SAAE (SA 200)	SUFFICIENT APPROPRIATE AUDIT EVIDENCE
TCWG (SA 260)	THOSE CHARGED WITH GOVERNANCE
MGMT	MANAGEMENT
WR (SA 580)	WRITTEN REPRESENTATIONS
FI	FINANCIAL INFORMATION
HFI	HISTORICAL FINANCIAL INFORMATION
IFI (SRE 2410)	INTERIM FINANCIAL INFORMATION
PFI (SAE 3400)	PROSPECTIVE FINANCIAL INFORMATION
PFFI (SAE 3420)	PRO FORMA FINANCIAL INFORMATION
FS	FINANCIAL STATEMENTS
AFS	AUDITED FINANCIAL STATEMENTS
CFS	CONSOLIDATED FINANCIAL STATEMENTS
SFS (SA 810)	SUMMARY FINANCIAL STATEMENTS
SGFS	SINGLE FINANCIAL STATEMENT

CG	CENTRAL GOVERNMENT
NTE	NATURE, TIMING & EXTENT
EP (SQC 1 & SA 220)	ENGAGEMENT PARTNER
EQCR (SQC 1 & SA 220)	ENGAGEMENT QUALITY CONTROL REVIEW
KAM (SA 701)	KEY AUDIT MATTERS
EOM (SA 706)	EMPHASIS OF MATTER
OM (SA 706)	OTHER MATTER

3

IMPORTANT TERMS

1.	Historical financial information	<p>➤ Information expressed in financial terms in relation to a particular entity, derived primarily from that entity's accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.</p>
2.	Financial Statements	<p>➤ A structured representation of historical financial information, including related notes, intended to communicate an entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework.</p> <p>➤ The related notes ordinarily comprise a summary of significant accounting policies & other explanatory information. The term "financial statements" ordinarily refers to a complete set of FS as determined by the requirements of the AFRF, but can also refer to a single financial statement.</p>
3.	Applicable Financial Reporting Framework	<p>➤ The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation & presentation of the FS that is acceptable in view of the nature of the entity & the objective of the FS, or that is required by law or regulation.</p> <p>➤ The term "fair presentation framework" is used to refer to a financial reporting framework that requires compliance with the requirements of the framework &:</p> <ol style="list-style-type: none"> Acknowledges explicitly or implicitly that, to achieve fair presentation of the FS, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the FS. Such departures are expected to be necessary only in extremely rare circumstances. <p>➤ The term "compliance framework" is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (i) or (ii) above.</p>
4.	Auditor	<p>➤ "Auditor" is used to refer to the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm. Where an SA expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term "engagement partner" rather than "auditor" is used. "Engagement partner" & "firm" are to be read as referring to their public sector equivalents where relevant.</p>
5.	Management	<p>➤ The person(s) with executive responsibility for the conduct of the entity's operations.</p> <p>➤ For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.</p>
6.	Those Charged With Governance	<p>➤ The persons or organisations (e.g., a corporate trustee) with responsibility for overseeing the strategic direction of the entity & obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.</p>

7.	Internal Control System	<ul style="list-style-type: none"> ➤ The process designed, implemented & maintained by TCWG, management & other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness & efficiency of operations, safeguarding of assets, & compliance with applicable laws & regulations. ➤ "Internal Control System" means all the policies & procedures (internal controls) adopted by the management of an entity to assist in achieving management's objective of ensuring, as far as practicable, the orderly & efficient conduct of its business, including adherence to management policies, the safeguarding of assets, the prevention & detection of fraud & error, the accuracy & completeness of the accounting records, & the timely preparation of reliable financial information.
8.	Premise	<ul style="list-style-type: none"> ➤ Premise, relating to the responsibilities of management &, where appropriate, those charged with governance, on which an audit is conducted – That management &, where appropriate, TCWG have the following responsibilities that are fundamental to the conduct of an audit in accordance with SAs. That is, responsibility: <ol style="list-style-type: none"> For the preparation & presentation of the FS in accordance with the AFRF; this includes the design, implementation & maintenance of internal control relevant to the preparation & presentation of FS that are free from material misstatement, whether due to fraud or error; & To provide the auditor with: <ol style="list-style-type: none"> All information, such as records & documentation, & other matters that are relevant to the preparation & presentation of the FS; Any additional information that the auditor may request from management &, where appropriate, TCWG; & Unrestricted access to those within the entity from whom the auditor determines it necessary to obtain audit evidence. ➤ In the case of a fair presentation framework, the responsibility is for the preparation & fair presentation of the FS in accordance with the financial reporting framework; or the preparation of FS that give a true & fair view in accordance with the financial reporting framework. This applies to all references to "preparation & presentation of the FS" in the SAs. ➤ The "premise, relating to the responsibilities of management &, where appropriate, TCWG, on which an audit is conducted" may also be referred to as the "premise".
9.	Overall Objectives of the Auditor	<ul style="list-style-type: none"> ➤ In conducting an audit of FS, the overall objectives of the auditor are: <ol style="list-style-type: none"> To obtain reasonable assurance about whether the FS as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the FS are prepared, in all material respects, in accordance with an Applicable Financial Reporting Framework; & To report on the FS, & communicate as required by the SAs, in accordance with the auditor's findings.
10.	Reasonable assurance	<ul style="list-style-type: none"> ➤ In the context of an audit of financial statements, a high, but not absolute, level of assurance.
11.	Professional judgment	<ul style="list-style-type: none"> ➤ The application of relevant training, knowledge & experience, within the context provided by auditing, accounting & ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.
12.	Professional skepticism	<ul style="list-style-type: none"> ➤ An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, & a critical assessment of audit evidence.
13.	Assertions	<ul style="list-style-type: none"> ➤ Representations by management, explicit or otherwise, that are embodied in the financial statements, as used by the auditor to consider the different types of potential misstatements that may occur.

14.	Misstatement	<ul style="list-style-type: none">➤ A difference between the amount, classification, presentation, or disclosure of a reported financial statement item & the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the AFRF.➤ Misstatements can arise from error or fraud.➤ When the auditor expresses an opinion on whether the FS are presented fairly, in all material respects, or give a true & fair view, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the auditor's judgment, are necessary for the FS to be presented fairly, in all material respects, or to give a true & fair view.								
15.	Business Risk	<ul style="list-style-type: none">➤ A risk resulting from significant conditions, events, circumstances, actions or inactions that could adversely affect an entity's ability to achieve its objectives & execute its strategies, or from the setting of inappropriate objectives & strategies.								
16.	Audit Risk	<ul style="list-style-type: none">➤ The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated.➤ Audit risk is a function of the risks of material misstatement & detection risk.								
17.	Risk of Material Misstatement	<ul style="list-style-type: none">➤ The risk that the financial statements are materially misstated prior to audit. This consists of two components, described as follows at the assertion level: Inherent Risk & Control Risk.								
18.	Significant Risk	<ul style="list-style-type: none">➤ An identified & assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration.								
19.	Inherent Risk	<ul style="list-style-type: none">➤ The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.								
20.	Control Risk	<ul style="list-style-type: none">➤ The risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure & that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected & corrected, on a timely basis by the entity's internal control.								
21.	Detection Risk	<ul style="list-style-type: none">➤ The risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists & that could be material, either individually or when aggregated with other misstatements.								
22.	Audit Evidence	<ul style="list-style-type: none">➤ Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the FS & other information. For purposes of the SAs:<ul style="list-style-type: none">(i) Sufficiency of audit evidence is the measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement & also by the quality of such audit evidence.(ii) Appropriateness of audit evidence is the measure of the quality of audit evidence; that is, its relevance & its reliability in providing support for the conclusions on which the auditor's opinion is based.								
23.	7 Methods of Obtaining Audit Evidence	<table><tr><td>Inspection</td><td><ul style="list-style-type: none">➤ Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset.</td></tr><tr><td>External Confirmations</td><td><ul style="list-style-type: none">➤ An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium. (SA 505)</td></tr><tr><td>Analytical Procedures</td><td><ul style="list-style-type: none">➤ Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial & non-financial data. (SA 520)</td></tr><tr><td>Inquiry</td><td><ul style="list-style-type: none">➤ Inquiry consists of seeking information of knowledgeable persons, both financial & non- financial, within the entity or</td></tr></table>	Inspection	<ul style="list-style-type: none">➤ Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset.	External Confirmations	<ul style="list-style-type: none">➤ An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium. (SA 505)	Analytical Procedures	<ul style="list-style-type: none">➤ Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial & non-financial data. (SA 520)	Inquiry	<ul style="list-style-type: none">➤ Inquiry consists of seeking information of knowledgeable persons, both financial & non- financial, within the entity or
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Inquiry	<ul style="list-style-type: none">➤ Inquiry consists of seeking information of knowledgeable persons, both financial & non- financial, within the entity or									

			<p>outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures. Evaluating responses to inquiries is an integral part of the inquiry process.</p>
		Observation	<p>➔ Observation consists of looking at a process or procedure being performed by others, for eg., auditor's observation of inventory counting by entity's personnel.</p>
		Recalculation	<p>➔ Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.</p>
		Reperformance	<p>➔ Re-performance involves the auditor's independent execution of procedures or controls that were performed as part of the entity's internal control.</p>
24.	Risk Assessment Procedures		<p>➔ The audit procedures performed to obtain an understanding of the entity & its environment, including the entity's internal control, to identify & assess the risks of material misstatement, whether due to fraud or error, at the financial statement & assertion levels.</p>
25.	Further Audit Procedures		<p>➔ Further Audit Procedures comprise of:</p> <ul style="list-style-type: none"> (i) Tests of controls, when required by the SAs or when the auditor has chosen to do so; & (ii) Substantive procedures, including tests of details & substantive analytical procedures.
26.	Tests of Control		<p>➔ An audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting & correcting, material misstatements at the assertion level.</p>
27.	Substantive Procedures		<p>➔ An audit procedure designed to detect material misstatements at the assertion level. Substantive procedures comprise:</p> <ul style="list-style-type: none"> (i) Tests of details (of classes of transactions, account balances, & disclosures), & (ii) Substantive analytical procedures.

CHAPTER
1

SQC SERIES

1

AUDIT QUALITY

High Audit
Quality

- **High audit quality** is central to auditing profession. It helps in creating trust in users of financial information. Audit quality requires a rigorous audit process by auditors & quality control procedures that comply with laws, regulations & applicable professional standards.
- **SQC 1- Quality Control for firms that perform audits & reviews of historical financial information, & other assurance & related services engagements & SA-220- Quality Control for an audit of financial statements** deal with issue of establishing quality control systems & responsibilities of auditors in this regard.
- Besides above 2 standards, other Standards on Auditing, Code of Ethics issued by ICAI & certain provisions of Companies Act, 2013 facilitate quality control process. There also exists mechanism for review of quality control through **Peer review Board, Quality review Board & NFRA (National Financial Reporting Authority)**.

2

SQC 1 - QUALITY CONTROL FOR FIRMS THAT PERFORM AUDITS
& REVIEWS OF HISTORICAL FINANCIAL INFORMATION, & OTHER
ASSURANCE & RELATED SERVICES ENGAGEMENTS

Objective

The objective of this SQC is to provide guidance to the audit firm for its auditing practice & describes the elements of control & other matters essential to the effective **design implementation & maintenance of quality control system**.

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

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

Applicability

- This quality control standard applies to all firms irrespective of their constitution.

2.1

Elements of
System of
Quality Control

- The firm's system of quality control should include **policies & procedures** addressing each of the following elements: -
 - Leadership responsibilities for quality within the firm
 - Ethical requirements
 - Acceptance & continuance of client relationships & specific engagements
 - Human resources
 - Engagement performance
 - Monitoring
- Quality control policies & procedures should be **documented & communicated** to the firm's personnel.

2.1.1

Leadership
Responsibilities
for Quality
within the Firm

- SQC 1 requires firms to establish policies & procedures designed to promote an **internal culture** based on the recognition that quality is essential in performing engagements. Such policies & procedures should require the firm's **CEO or the firm's managing partners** to assume ultimate responsibility for the firm's system of quality control.
- Further, persons assigned operational responsibilities for the firm's quality control system should have **sufficient & appropriate experience**, ability, & the necessary authority to assume that responsibility.

Commitment to
achieve Quality

- It has been laid down clearly that firm's business strategy is subject to the overriding requirement for the firm to **achieve quality** in all the engagements that the firm performs.



Essentially, it implies that audit quality is paramount in all engagements. It is **non-negotiable**. In this regard, it should be ensured that: -

- The firm assigns its management responsibilities so that **commercial considerations** do not override the quality of work performed.
- The firm's policies & procedures addressing performance evaluation, compensation, & promotion (including incentive systems) with regard to its personnel are designed to demonstrate the firm's **overriding commitment to quality** &
- The firm devotes **sufficient resources** for the development, documentation & support of its quality control policies & procedures.

2.1.2

Ethical Requirements



- The firm should establish policies & procedures designed to provide it with **reasonable assurance** that the firm & its personnel comply with relevant ethical requirements contained in the Code of ethics issued by ICAI.
- The Code of Ethics establishes the **fundamental principles** which include integrity, objectivity, professional competence & due care, confidentiality & professional behaviour. Fundamental principles should be emphasized by - actions of the leadership of the firm, spreading awareness & training, monitoring & a process for dealing with non-compliance.
- Observance of "Independence"** in all engagements is the founding requirement. The firm should establish policies & procedures designed to provide it with reasonable assurance that the firm, its personnel & (including experts contracted by the firm & network firm personnel) maintain independence where required by the Code. Such policies & procedures should enable the firm to: -
 - Communicate its independence requirements to its personnel
 - Identify & evaluate circumstances & relationships that create threats to independence, & to take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement.
- There should exist a **mechanism** in the firm by which engagement partners provide the firm with relevant information about client engagements & personnel of firm promptly notify firm of circumstances & relationships that create a threat to independence. All breaches of independence should be promptly notified to firm for appropriate action. Its objective is to ensure that independence requirements are satisfied.
- At least annually, obtain **written confirmation** of compliance with its policies & procedures on independence from all firm personnel required to be independent as per the Code.






Familiarity Threat

- SQC 1 lays special emphasis on familiarity threat.** Using the same senior personnel on assurance engagements over a prolonged period may impair the quality of performance of the engagement. Therefore, the firm should establish criteria for determining the need for safeguards to address this threat. In determining appropriate criteria, the firm considers such matters as-
 - the nature of the engagement, including the extent to which it involves a matter of public interest &
 - the length of service of the senior personnel on the engagement.
- Examples of **safeguards** include **rotating the senior personnel** or requiring an EQCR. The **familiarity threat** is particularly relevant in the context of FS audits of listed entities. For these audits, the engagement partner should be rotated after a predefined period, normally not more than **7 years** (except in cases where audit of listed entities is conducted by a sole practitioner). However, to ensure quality control exists in such firms & appropriate reports are issued, there is a process for **mandatory peer review** of such firms.

2.1.3

Acceptance & Continuance of Client Relationships &

- A firm before accepting an engagement should acquire vital information about the client. Such an **information** should help firm to decide about: -
 - ➔ **Integrity** of Client, promoters & key managerial personnel.
 - ➔ **Competence** (including capabilities, time & resources) to perform engagement.
 - ➔ Compliance with **ethical requirements**.

<p>Specific Engagements</p> 	<ul style="list-style-type: none"> ■ The firm should obtain such information as it considers necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, & when considering acceptance of a new engagement with an existing client. Where issues have been identified, & the firm decides to accept or continue the client relationship or a specific engagement, it should document how the issues were resolved.
<p>Integrity of a Client</p> 	<p>With regard to the integrity of a client, matters that the firm considers include, for example:</p> <ul style="list-style-type: none"> ■ Identity & business reputation of the client's principal owners, key management, related parties & TCWG. ■ Nature of the client's operations, including its business practices. ■ Information concerning the attitude of client's principal owners, key management & TCWG towards such matters as aggressive interpretation of AS & internal control environment. ■ Whether client is aggressively concerned with maintaining firm's fees as low as possible. ■ Indications of an inappropriate limitation in the scope of work. ■ Indications that client might be involved in money laundering or other criminal activities. ■ Reasons for proposed appointment of the firm & non-reappointment of previous firm. ■ Extent of knowledge a firm will have regarding the integrity of a client will generally grow within the context of an ongoing relationship with that client.
<p>Competence & Capabilities</p> 	<p>In considering whether the firm has the capabilities, competence, time & resources to undertake an engagement, following matters have to be taken into consideration: -</p> <ul style="list-style-type: none"> ■ Firm personnel have knowledge of relevant industries or subject matters; ■ Firm personnel have experience with relevant regulatory or reporting requirements, or the ability to gain the necessary skills & knowledge effectively; ■ Firm has sufficient personnel with necessary capabilities & competence; ■ Experts are available, if needed; ■ Individuals meeting the criteria & eligibility requirements to perform EQCR are available, where applicable; & ■ Firm would be able to complete the engagement within the reporting deadline.
<p>Conflict of Interest</p> 	<ul style="list-style-type: none"> ■ If there is any conflict of interest between the firm & client, it should be properly resolved before accepting the engagement. Where the firm obtains information that would have caused it to decline an engagement if that information had been obtainable earlier, policies & procedures on the continuance of the engagement & the client relationship should include consideration of: <ol style="list-style-type: none"> a) The professional & legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities; & b) The possibility of withdrawing from the engagement or from both the engagement & the client relationship.
<p>Withdrawal from Engagement</p> 	<ul style="list-style-type: none"> ■ Policies & procedures on withdrawal from engagement or from both engagement & client relationship, addresses following issues: <ul style="list-style-type: none"> ➤ Discussing with the appropriate level of client's management & TCWG regarding the appropriate action that the firm might take based on relevant facts & circumstances. ➤ If the firm determines that it is appropriate to withdraw, discussing with the appropriate level of client's management & TCWG withdrawal from the engagement or from both the engagement & client relationship, & the reasons for the withdrawal. ➤ Considering whether there is a professional, regulatory or legal requirement for the firm to remain in place, or for the firm to report the withdrawal from the engagement, or from both the engagement & the client relationship, together with the reasons for the withdrawal, to regulatory authorities. ➤ Documenting significant issues, consultations, conclusions & the basis for the conclusions.

2.1.4

Human Resources



- The firm should establish policies & procedures designed to provide it with reasonable assurance that it has **sufficient personnel** with the capabilities, competence, & commitment to ethical principles necessary to perform its engagements in accordance with professional standards & regulatory & legal requirements & to enable the firm or engagement partners to issue reports that are appropriate in the circumstances.
- Such **policies & procedures** should address relevant HR issues including recruitment, compensation, training, career development, performance evaluation etc. There should be emphasis on the continuing professional development of firm's personnel.
- The firm should **assign responsibility** for each engagement to an engagement partner.

The firm should establish policies & procedures requiring that:

- a) The identity & role of the engagement partner are communicated to key members of the client's management & TCWG;
- b) The engagement partner has the appropriate capabilities, competence, authority & time to perform the role; &
- c) The responsibilities of the engagement partner are clearly defined & communicated to that partner

- Each **engagement team** should be able to carry out its responsibilities with necessary competence & skill. Therefore, the firm should ensure suitable people are available & also groom them for their role. The firm should assess performance of their partners & team members keeping in mind their commitment towards quality.

2.1.5

Engagement Performance

- **Consistency in quality** of engagement performance is achieved through briefing of engagement teams of their objectives, processes for complying with engagement standards, processes of engagement supervision & training, methods of reviewing performance of work, appropriate documentation of work performed.




Consultation in difficult or contentious matters:



- Consultation should take place in **difficult or contentious matters** pertaining to an engagement. Consultation includes discussion, at the appropriate professional level, with individuals **within or outside** the firm who have specialized expertise. It helps to promote quality & improves the application of professional judgment.
- Consultation procedures require consultation with those having **appropriate knowledge**, seniority & experience within the firm (or outside the firm) on significant technical, ethical & other matters & appropriate documentation & implementation of conclusions resulting from consultations.
- A firm needing to **consult externally**, for example, a firm without appropriate internal resources, may take advantage of advisory services provided by other firms or professional & regulatory bodies. Complete & proper documentation should be maintained on issues involved & results of consultation.

Engagement Quality Control Review

- **Significant judgments** made in an engagement should be reviewed by an engagement quality control reviewer for taking an objective view before the report is issued.
- The extent of the review depends on the **complexity of the engagement** & the risk that the report might not be appropriate in the circumstances. The review **does not reduce** the responsibilities of the engagement partner.
- Engagement quality control reviewer is a **partner, other person** in the firm (who should be member of ICAI), **suitably qualified external person**, or a team made up of such individuals. In this regard, suitably qualified external person refers to an individual outside the firm with the capabilities & competence to act as an engagement partner, for example a partner or an employee (with appropriate experience) of **another firm**.
- In addition, the engagement quality control reviewer for an audit of the FS of a listed entity is an individual with **sufficient & appropriate experience** & authority to act as an audit engagement partner on audits of FS of listed entities. It is necessary to maintain **objectivity** of such reviewer. Therefore, participation in engagement or making decisions for engagement team is to be avoided at all costs. However, engagement partner may consult engagement quality control reviewer during the engagement so as not to compromise his objectivity & eligibility to perform the role.

	<ul style="list-style-type: none"> EQCR is mandatory for all audits of FS of listed entities. In respect of other engagements, firm should devise criteria to determine cases requiring performance of EQCR.
	<p>An EQCR for audits of FS of listed entities includes considering the following: -</p> <ul style="list-style-type: none"> Engagement team's evaluation of firm's independence in relation to specific eng. Significant risks identified during the engagement & the responses to those risks. Judgments made, particularly with respect to materiality & significant risks. Whether consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, & conclusions arising from those consultations. Significance & disposition of corrected & uncorrected misstatements identified during the engagement. Matters to be communicated to management & TCWG & where applicable, other parties such as regulatory bodies. Whether working papers selected for review reflect the work performed in relation to the significant judgments & support the conclusions reached. The appropriateness of the report to be issued.
<p>Differences of Opinion</p> 	<ul style="list-style-type: none"> There might be difference of opinion within engagement team, with those consulted & between engagement partner & engagement quality control reviewer. The report should only be issued after resolution of such differences. In case, recommendations of engagement quality control reviewer are not accepted by engagement partner & matter is not resolved to reviewer's satisfaction, the matter should be resolved by following established procedures of firm like by consulting with another practitioner or firm, or a professional or regulatory body.
<p>Engagement Documentation:</p> 	<ul style="list-style-type: none"> Policies & procedures should be designed to maintain confidentiality, safe custody, integrity, accessibility & retrievability of engagement documentation. Care should be taken that policies & procedures on documentation of the EQCR should require documentation that: - <ol style="list-style-type: none"> The procedures required by the firm's policies on EQCR have been performed. The EQCR has been completed before the report is issued & The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made & the conclusions they reached were not appropriate. Unless otherwise specified by law or regulation, engagement documentation is the property of the firm. The firm may, at its discretion, make portions of, or extracts from, engagement documentation available to clients, provided such disclosure does not undermine the validity of the work performed, or, in the case of assurance engagements, the independence of the firm or its personnel. The retention period should not be shorter than 7 years from the date of the auditor's report, or, if later, the date of the group auditor's report. The firm should establish policies & procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized. Engagement files should be completed in not more than 60 days after date of auditor's report in case of audit engagements & in other cases within the limits appropriate to engagements.
<p>2.1.6</p> <p>Monitoring</p> 	<ul style="list-style-type: none"> The firm should ensure that policies & procedures relating to the system of quality control are relevant, adequate, operating effectively & complied with in practice. Such policies & procedures should include an ongoing consideration & evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements. Quality control of engagements has to be monitored taking into account following factors: <ul style="list-style-type: none"> Deciding whether quality control system of firm has been appropriately designed & effectively implemented.

- Examining whether **new developments** in professional standards, legal & regulatory requirements have been reflected in the quality control policies.
- Conducting monitoring by **entrusting responsibility** of monitoring process to a partner or other persons with sufficient & appropriate experience & authority in the firm.
- Dealing with **complaints & allegations** against the firm or any employees of it of non-compliance with professional standards or appropriate regulatory requirements by a person within or outside the firm.
- Taking appropriate **remedial actions** against personnel who did not conform to quality control policies.
- **Taking action** when deficiencies in design or operation of firm's quality control policies & procedures, or non-compliance with firm's quality control system are identified.

3

SQC 1 VS. SA 220 - KEY DIFFERENCES IN NATURE, SCOPE & APPLICABILITY

S.	SQC 1	SA 220
1	It applies to entire firm & fixes the responsibility of firm to be assumed by CEO or managing partners.	It applies to a particular audit engagement & engagement partner takes responsibility of same.
2	It is applicable to audits, reviews of historical financial Information, & other assurance & related services engagements.	It is applicable to audit engagements only.
3	It relates to setting up of a quality control system consisting of policies & procedures for firm as a whole.	It deals with responsibilities of engagement teams to implement quality control procedures that are applicable to audit engagements.
4	It pertains to establishing a system of quality control designed to provide firm with a reasonable assurance that a firm & its personnel comply with professional standards & regulatory & legal requirements so that reports issued by firm or engagement partners are appropriate in circumstances.	It is premised on the basis that firm is subject to SQC 1. Therefore, SQC 1 is a sine qua non for applicability of SA 220. It is within overall context of a firm's system of quality control, engagement teams implement quality control procedures applicable to audit engagements.

4

MECHANISMS FOR REVIEW OF QUALITY CONTROL

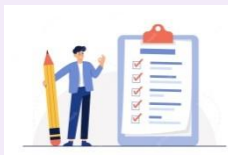
4.1

PEER REVIEW BOARD

- Peer review Board is constituted by Council of ICAI. The main objective of Peer review Board is to ensure that, in carrying out assurance assignments: -
 - **Technical, professional & ethical standards** including regulatory requirements are complied with by members of ICAI.
 - Proper systems are in place including documentation thereof which amply demonstrate **quality of assurance services** provided by members.
 - The peer review is meant for purpose of **enhancing quality** of professional work resulting in more reliable & useful audit reports.
- **Peer review** means an examination & review of the systems & procedures to determine whether the same have been put in place by the **Practice Unit** for ensuring the quality of assurance services as envisaged by the technical, professional & ethical standards or any other regulatory requirements.
- Once a Practice Unit is subjected to Peer review, its assurance engagement records pertaining to Peer review period are subject to examination & review by the Peer Reviewer. On completion of this exercise, a "**peer review certificate**" is issued in case of **unqualified report** issued by Peer Reviewer. In case of a **qualified report**, it is informed to the Practice Unit that same cannot be issued along with the reasons therefor as well as inform about the due date for conducting a **follow-on review** as may be decided by the Board.

4.2

QUALITY REVIEW BOARD



- Quality review Board has been set up by Central Government. It consists of members nominated by Central govt & Council of ICAI. The **functions of QRB** are: -
 - a) To **make recommendations** to the Council regarding the quality of services provided by the members of the Institute;
 - b) To **review the quality of services** provided by the members of the Institute including audit services &
 - c) To **guide the members** of the Institute to improve the quality of services & adherence to the various statutory & other regulatory requirements;
 - d) To **forward cases** of non-compliance with various statutory & regulatory requirements by the members of the Institute or firms, noticed by it during the course of its reviews, to the Disciplinary Directorate for its examination.
- The statutory auditors in respect of the companies are identified for their audit quality review based upon risk-based approach. The review is carried out by technical reviewers who are empanelled by QRB on engagement basis from across the country.

4.3

NATIONAL FINANCIAL REPORTING AUTHORITY(NFRA)



- NFRA has been constituted in terms of Section 132(1) of Companies Act, 2013. **Duties of NFRA** also include the following: -
 - Monitor & enforce compliance with **accounting standards & auditing standards**
 - Oversee the **quality of service** of the professions associated with ensuring compliance with such standards & suggest measures for improvement in the quality of service
- It has power to monitor & enforce compliance with AS & SA & oversee the quality of service u/s 132(2) or undertake investigation u/s 132(4) of the auditors of certain class of companies. Such companies include listed companies, insurance companies, banking companies & other companies as provided for in rule of NFRA Rules, 2018.
- Therefore, overseeing quality of audit services of listed companies falls under the purview of NFRA. QRB can review quality of audit services provided by the members of the Institute only in respect of entities other than those specified under NFRA Rules, 2018 & those referred to QRB by NFRA.