PAPER – 5:
AUDITING AND ETHICS

QUESTIONS

PART – I: Multiple Choice Questions based on Case Scenarios

Case Scenario

ABC Limited is a mid-sized manufacturing company engaged in the production of electrical components and spare parts. The company maintains significant inventory across multiple warehouses. During the audit of the financial statements for the year ended 31st March 2025, the auditor noted that inventory prices were highly volatile during the year and that discrepancies in inventory records had been reported in earlier audits. Certain inventory items were also identified as slow-moving and required significant management judgement for valuation. Based on these factors, the auditor assessed the risk of material misstatement in inventory valuation as high.

In the course of the audit, the auditor performed inquiries with the stores manager, production head, and finance personnel to understand the process for identification of obsolete inventory and valuation adjustments. While management represented that adequate provisions had been made for obsolete inventory, the stores manager indicated during inquiry that certain obsolete items were still carried at cost due to pressure to meet profitability targets. This inconsistency prompted the auditor to reassess audit procedures.

Considering the high risk assessment and contradictory responses obtained during inquiry, the auditor decided to perform tests of controls relating to approval of inventory write-downs and review of inventory ageing reports. Based on the results, the auditor concluded that controls over identification and valuation of obsolete inventory were not operating effectively throughout the period.

Accordingly, the auditor designed and performed substantive procedures, including detailed testing of inventory valuation, examination of subsequent sales prices, physical inspection of slow-moving items, and substantive analytical procedures. While designing these procedures, the auditor identified conditions that would constitute a misstatement in the relevant assertions relating to inventory.

While evaluating the audit evidence obtained, the auditor considered the management assertions made in representing that the financial statements are prepared in accordance with the applicable financial reporting framework, particularly assertions relating to existence, valuation, completeness, and presentation and disclosure of inventory.

Based on above, answer the following MCQs:

1. In the audit of ABC Limited, which combination of circumstances primarily justified the auditor's decision to obtain additional audit evidence for inventory valuation?

   (a) Existence of slow-moving inventory requiring management judgement

   (b) Prior period discrepancies, price volatility and contradictory inquiry responses regarding obsolete inventory

   (c) Materiality of inventory balance and availability of ageing reports

   (d) Physical dispersion of inventory across multiple warehouses

2. The stores manager's statement that obsolete items were carried at cost due to pressure to meet profitability targets most appropriately implies that the auditor should:

   (a) Conclude that the issue relates only to operational inefficiency and does not affect financial reporting

   (b) Accept management's representation regarding adequate provisioning

   (c) Treat the information as an indicator of potential management bias and modify audit procedures accordingly

(d) Consider the inquiry response as sufficient appropriate audit evidence

3. In the audit of ABC Limited, after obtaining contradictory responses during inquiry and before designing substantive procedures, the auditor decided to test controls specifically over approval of inventory write-downs and review of ageing reports.

This decision was primarily to determine whether:

(a) Controls existed and operated effectively to prevent management from deferring write-downs of obsolete inventory to meet profitability targets

(b) Inventory quantities recorded in the system matched the physical stock across warehouses

(c) Substantive testing of inventory valuation could be restricted to analytical procedures only

(d) Management representations regarding obsolete inventory could be accepted without further corroboration

4. After concluding that controls over identification and valuation of obsolete inventory were not operating effectively throughout the period, the auditor performed procedures such as examining subsequent sales prices, physically inspecting slow-moving items, and performing substantive analytical procedures.

These procedures were primarily designed to:

(a) Determine whether inventory write-downs had been formally approved in accordance with internal policies

(b) Obtain direct audit evidence to evaluate whether inventory was overstated due to delayed or inadequate write-downs

(c) Re-assess the design of internal controls over inventory management

(d) Corroborate management's representations regarding profitability targets

5. The auditor identified that certain slow-moving and obsolete inventory items continued to be carried at cost due to pressure to meet profitability targets.

This situation most directly affects which management assertion, thereby requiring focused audit procedures in response to the identified risk?

(a) Existence – because slow-moving inventory may no longer physically exist

(b) Completeness – because obsolete inventory may not have been recorded in the inventory records

(c) Presentation and disclosure – because obsolete inventory requires separate classification in the financial statements

(d) Valuation – because inventory may be overstated as net realisable value has not been appropriately considered

General MCQs

6. During the audit of QRS Ltd. for the year ended 31 March 2025, the auditor observed that management had changed the method of depreciation from Written Down Value Method to Straight Line Method. The change was applied in the current year and disclosed in the notes to accounts. The auditor also reviewed whether the financial statements appropriately summarised the transactions and events recorded and evaluated the judgments made by management in selecting and applying accounting policies consistently.

   In the above case, which of the following represents the auditor's responsibility while evaluating the financial statements?

   (a) To select the most appropriate accounting policies for the entity.

   (b) To prepare and present the financial statements in accordance with applicable statutory requirements.

   (c) To change the accounting policies where they do not reflect true and fair view.

   (d) To ensure that accounting policies selected by management are evaluated for appropriateness and consistent application and that relevant information is properly disclosed.

7. P & Co., Chartered Accountants, were appointed as statutory auditors of LMN Ltd. for the year ended 31 March 2025. Soon after completing the audit for the previous year, the engagement team began discussions for

the current year's audit. Before identifying and assessing the risks of material misstatement, the auditor planned the timing of certain activities such as applying analytical procedures, obtaining an understanding of the applicable legal and regulatory framework, determining materiality and considering the need for involvement of experts.

Which of the following statements best explains the nature of audit planning as per the Standards on Auditing in the above case?

(a) Audit planning is a separate phase that begins only after the identification of risks of material misstatement.

(b) Audit planning is a continual and iterative process that includes consideration of analytical procedures, materiality, legal and regulatory framework and involvement of experts prior to performing further audit procedures.

(c) Audit planning is restricted to preparation of the audit programme and allocation of audit staff.

(d) Audit planning is required only in case of initial audit engagements.

8. While auditing a charitable trust for the year ended 31 March 2025, the auditor obtained a list of books and records maintained by the trust and verified them with the mandatory records prescribed. Based on his evaluation of internal controls, he applied test checks, complied with the applicable Accounting Standards and Standards on Auditing, considered materiality while performing audit procedures and maintained detailed working papers documenting the audit evidence relied upon for forming his opinion.

Which of the following actions of the auditor in the above case is most appropriate as per generally accepted auditing practices?

(a) Using professional judgment to determine audit tests, applying test checks based on internal control evaluation, considering materiality and maintaining working papers to support the audit opinion.

(b) Applying test checks irrespective of internal control evaluation, since trust audits are not governed by internal control considerations.

(c) Restricting compliance to Accounting Standards only, as Standards on Auditing are recommendatory in case of trust audits.

(d) Maintaining working papers only for material items, as immaterial matters do not require audit documentation.

PART II – Descriptive Questions

Chapter 1 - Nature, Objective and Scope of Audit

9. You are appointed as statutory auditor of Zebra Industries Ltd. for FY 2024–25. During the course of audit, you observe that the company's management frequently delays in providing certain documents and explanations requested by you. A portion of the accounting records related to "special procurement" is supported only by basic acknowledgements without proper vendor details. You also notice that some transactions appear to be with entities that may be related to the company, but management denies the existence of any such relationships. Further, during verification, you find that some documents produced as evidence appear unusually uniform and lack standard commercial markings, raising concerns about their authenticity. Since your audit is conducted on a test-check basis, you are unable to verify all such transactions individually.

   Based on the above, explain the inherent limitations of an audit that restrict the auditor from obtaining absolute assurance that the financial statements of Zebra Industries Ltd. are free from material misstatement.

Chapter 2 - Audit Strategy, Audit Planning and Audit Programme

10. You are the Engagement Partner for the statutory audit of Strong Engineering Ltd. for FY 2024–25. While planning the audit, you observe the following practical issues:

    (i) Two newly recruited audit assistants inform you that they are unsure about the exact audit procedures expected from them for different areas of the audit.

    (ii) The audit this year is a major assignment involving multiple units, and your team seems unable to visualise the full scope of procedures to be performed.

(iii) Because the audit work has not been formally planned, defined and segregated, you are unable to allocate tasks to assistants on the basis of their individual capabilities.

(iv) Last year, in the absence of a written programme, the then audit team followed a "mental plan", as a result of which certain subsidiary records were overlooked.

(v) During review, you notice that assistants have not signed off on procedures performed, making it difficult to trace work back to the responsible individual.

(vi) As the principal auditor, you find it difficult to track the progress of different audit areas because no written audit programme has been initiated by assistants.

(vii) Your firm wishes to use this year's audit documentation as a reference for planning next year's audit of Strong Engineering Ltd. (viii) The firm is also facing a negligence allegation on another audit, and you are concerned about having adequate evidence of exercising reasonable skill and care in this assignment.

Based on above facts, analyse why preparing a written audit programme is advantageous for the audit of Strong Engineering Ltd.

Chapter 3 - Risk Assessment and Internal Control

11. ABC Limited is a medium-sized manufacturing company having multiple departments and large volume of transactions. The management claims that the company has a well-designed internal control system and an internal audit department in place.

While planning the statutory audit, the auditor decides to evaluate the internal control system of the company before determining the nature, timing and extent of audit procedures. During the review, the auditor focuses not only on accounting controls but also on administrative controls and their impact on financial reporting. Based on the above facts, explain how evaluation of the internal control system would benefit the auditor in planning and conducting the statutory audit of ABC Limited.

Chapter 4 - Audit Evidence

12. XYZ Limited is engaged in infrastructure development and has significant balances relating to valuation of long-term assets and environmental provisions. Environmental provisions are amounts recognised for future obligations like site restoration, environmental clean-up, or compliance with environmental laws, which also involve technical and judgmental estimates. For this purpose, the management has engaged independent experts to determine fair values and technical estimates which have been incorporated in the financial statements.

    While conducting the statutory audit, the auditor considers whether and to what extent he can rely on the work performed by the management's expert for obtaining audit evidence and forming his audit opinion.

    State the condition and procedures to be followed by the auditor while relying on the work of management's expert.

Chapter 5 - Audit of Items of Financial Statements

13. PQR Limited is engaged in trading and manufacturing activities and reports a substantial amount of inventories in its financial statements as at 31st March 2025. A portion of the inventories is held at the company's own warehouses, while some inventories are held on consignment and with third parties.

    While conducting the audit, the auditor is required to obtain sufficient and appropriate audit evidence to establish the legal ownership rights over the inventories claimed to be held by the entity and recorded in the financial statements.

    State the audit procedures to establish the legal ownership rights over the inventories claimed to be held by the entity.

14. TUV Ltd. is engaged in the business of manufacturing and sale of electronic appliances. During the audit of the company for the year ended 31st March 2025, the auditor observed a significant increase in revenue in the last month of the financial year as compared to previous months.

    Further, it was noticed that:

    - Some sales invoices near year-end were cancelled subsequently.

- The sales return ratio for the current year showed wide fluctuation compared to the previous year.
- Management was under pressure to meet revenue targets to comply with loan covenants.
- Certain customers had not made payments even after an extended credit period.

The auditor is concerned about the risk of overstatement of revenue and wants to verify whether the recorded sales genuinely represent goods shipped or services performed during the period.

As an auditor, explain the audit procedures you would perform to verify the Occurrence assertion in respect of revenue transactions of TUV Ltd.

Chapter 6 - Audit Documentation

15. ABC & Co., Chartered Accountants is conducting the statutory audit of a listed company having multiple locations and a large engagement team. The audit involves extensive planning, supervision, review of work performed by assistants and is also subject to quality control review by the firm as well as possible inspection by regulatory authorities.

During the audit, the engagement partner emphasises the need for proper and comprehensive audit documentation.

With reference to above, explain the purpose served by audit documentation for the auditor and the engagement team.

Chapter 7 - Completion and Review

16. During the audit of LMN Limited, the auditor identified certain significant deficiencies in the internal control system which could adversely affect the reliability of financial reporting. The auditor is required to communicate such deficiencies to those charged with governance and also to management on a timely basis.

Further, the auditor is required to ensure that the written communication clearly specifies the nature and implications of such deficiencies.

With reference to above, explain:

(i) the auditor's responsibility for communication of significant deficiencies in internal control to those charged with governance and management; and

(ii) the matters that the auditor shall include in the written communication of such significant deficiencies.

Chapter 8 - Audit Report

17. "Using the Work of Another Auditor" is a critical area in the audit of entities having branches or components audited by auditors other than the principal auditor.

With reference to SA 600 – Using the Work of Another Auditor, explain:

1. The need for coordination and proper understanding between the principal auditor and the other auditor; and

2. The procedures to be performed by the principal auditor to evaluate and use the work of the other auditor, including circumstances where the principal auditor may need to visit the component or examine its records.

Chapter 9 - Special Features of Audit of Different Type of Entities

18. Hope Foundation, a registered non-governmental organisation (NGO), is engaged in social welfare activities across multiple states and receives funds from domestic as well as foreign donors. The organisation is governed by a Managing Committee and is required to comply with various statutes and funding agency requirements.

While planning the statutory audit of the NGO, the auditor is required to obtain a thorough understanding of the organisation, its regulatory environment, internal systems and prior audit findings in order to design appropriate audit procedures.

With reference to above, state the matters on which the auditor may concentrate while planning the audit of an NGO.

Chapter 10 - Audit of Banks

19. ABC Bank Limited has a substantial portfolio of advances comprising term loans, cash credit facilities and overdrafts. As at the balance sheet date, significant amounts of advances are outstanding and are required

to be valued, classified and disclosed in accordance with applicable accounting standards, RBI norms and regulatory requirements.

While carrying out the audit of advances, the auditor is required to obtain sufficient and appropriate audit evidence to ensure that the advances reported in the balance sheet are properly recorded, supported, valued and disclosed.

With reference to the above, state the primary matters with respect to which the auditor should obtain audit evidence while carrying out the audit of advances.

Chapter 11 - Ethics and Terms of Audit Engagements

20. ABC & Co., Chartered Accountants, was appointed as the statutory auditor of Kimi Manufacturing Ltd. for the financial year ended 31st March 2025. CA Arjun, a senior partner of the firm, was designated as the Engagement Partner for the audit engagement.

In accordance with SA 220, "Quality Control for an Audit of Financial Statements", CA Arjun took active steps to demonstrate leadership and responsibility for the overall quality of the audit. He communicated to the engagement team the importance of complying with professional standards, regulatory and legal requirements, and adherence to the firm's quality control policies and procedures.

He also emphasised that the auditor's report should be appropriate in the circumstances and should be issued only after obtaining sufficient and appropriate audit evidence. Further, CA Arjun encouraged open communication within the engagement team and assured members that they could raise professional concerns or doubts without fear of reprisals. Throughout the engagement, he consistently highlighted that audit quality is essential in performing audit engagements.

With reference to SA 220, explain how the actions and messages conveyed by the engagement partner demonstrate leadership responsibilities for ensuring overall audit quality on an audit engagement.

SUGGESTED ANSWERS

PART – I: Answers to Multiple Choice Questions

MCQ No.	Answer
1.	(b)
2.	(c)
3.	(a)
4.	(b)
5.	(d)
6.	(d)
7.	(b)
8.	(a)

PART – II: Answers to Descriptive Questions

9. The auditor carries out his work by obtaining audit evidence through performance of audit procedures. However, there are practical and legal limitations on ability of auditor to obtain audit evidence. For example, an auditor does not test all transactions and balances. He forms his opinion only by testing samples. It is an example of practical limitation on auditor's ability to obtain audit evidence.

Management may not provide complete information as requested by auditor. There is no way by which auditor can force management to provide complete information as may be requested by auditor. In case he is not provided with required information, he can only report. It is an example of *legal limitation* on auditor's ability to obtain audit evidence.

The management may consist of dishonest and unscrupulous people and may be, itself, involved in fraud. It may be engaged in concealing fraud by designing sophisticated and carefully organised schemes which may be hard to detect by the auditor. It may produce fabricated documents before auditor to lead him to believe that audit evidence is valid. However, in reality, such documents could be fake or non-genuine.

Auditor is not an expert in authentication of documents. Therefore, he may be led to accept invalid audit evidence on the basis of unauthentic documents.

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

These factors collectively demonstrate that, due to practical constraints, legal boundaries, management fraud risks, and limitations in detecting related party transactions, the auditor can obtain only reasonable assurance and not absolute assurance regarding the accuracy of the financial statements.

10. In the present case, the absence of a written audit programme has led to confusion among assistants, ineffective supervision, omission of records and lack of documentary evidence. These issues clearly establish the importance and advantages of preparing a written audit programme. The advantages in the present case may be analysed as follows:

(i) Clear instructions to assistants: The newly recruited assistants are unsure about the audit steps. A written audit programme provides detailed, written instructions regarding the nature, timing and extent of audit procedures regarding the work to be performed.

(ii) Providing a total perspective for a major audit: The current audit is a major, multi-unit assignment. A properly drafted programme gives the team a complete perspective of all audit procedures required.

(iii) Easier selection of assistants based on capability: You find it difficult to allocate work because tasks are not defined. Once the work is rationally planned, defined and segregated, assistants can be assigned roles more effectively depending on their capability.

(iv) Reduces risk of overlooking books/records: Last year some subsidiary records were overlooked due to reliance on a mental plan.

A written and predetermined programme ensures systematic and comprehensive coverage of all books and records and ensures systematic coverage.

(v) Fixation of responsibility through sign-offs: Absence of signatures prevents linking work to individuals. A written programme allows each assistant to sign off, accepting responsibility for work done.

(vi) Enables control and monitoring by the principal: You are unable to track progress without a written programme. When assistants initiate and follow the programme, the principal can control and monitor the audit progress effectively.

(vii) Serves as a guide for next year's audit: The firm wants to use this year's work as reference for next year's planning.

A properly drafted programme acts as a useful guide for future audits.

(viii) Provides evidence against negligence allegations: Since the firm faces negligence allegations elsewhere, proper documentation is critical.

A well-constructed programme provides evidence that the auditor exercised reasonable skill and care.

Considering all facts, preparing a written, structured audit programme will address each challenge directly, enhance audit efficiency, improve accountability, and provide strong defence evidence in case of negligence allegations. Therefore, adopting a comprehensive audit programme is clearly advantageous for the audit of Strong Engineering Ltd.

11. Benefits of Evaluation of Internal Control to the Auditor: The review of internal controls will enable the auditor to know:

(i) whether errors and frauds are likely to be located in the ordinary course of operations of the business

(ii) whether an adequate internal control system is in use and operating as planned by the management

(iii) whether an effective internal auditing department is operating

(iv) whether any administrative control has a bearing on his work (for example, if the control over worker recruitment and enrolment is weak, there is a likelihood of dummy names being included in the wages sheet and this is relevant for the auditor)

(v) whether the controls adequately safeguard the assets

(vi) how far and how adequately the management is discharging its function in so far as correct recording of transactions is concerned

(vii) how reliable the reports, records and the certificates to the management can be

(viii) the extent and the depth of the examination that he needs to carry out in the different areas of accounting

(ix) what would be appropriate audit technique and the audit procedure in the given circumstances

(x) what are the areas where control is weak and where it is excessive and

(xi) whether some worthwhile suggestions can be given to improve the control system.

Thus, evaluation of internal control provides a sound basis for audit planning, helps the auditor assess control risk, and enables him to design appropriate audit procedures while also contributing to improvement of the control system.

12. If the entity has employed or engaged experts, the auditor may rely on the works of experts, provided he is satisfied that sufficient and appropriate audit evidence is obtained with reasonable assurance to form an opinion on the financial statements.

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

(a) Evaluate the competence, capabilities and objectivity of that expert;

(b) Obtain an understanding of the work of that expert; and

(c) Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion.

Thus, reliance on the work of a management's expert does not reduce the auditor's responsibility, and the auditor must exercise professional judgment to ensure that such work provides sufficient and appropriate audit evidence.

13. Audit procedure to establish the legal ownership rights over the Inventories claimed to be held by the entity and recorded in the financial statements:

(i) Vouch recorded purchases to underlying documentation (purchase requisition, purchase order, receiving report, vendor invoice and cancelled cheque or payment file).

(ii) Evaluate the consigned goods.

(iii) Examine client correspondence, sales and receivables records, purchase documents.

(iv) Determine existence of collateral agreements.

(v) Review consignment agreements.

(vi) Review material purchase commitment agreements.

(vii) Examine invoices for evidence of ownership i.e. the invoices shall be in the name of the client.

(viii) Auditor shall obtain confirmation for significant items of inventory.

(ix) For instances of inventory held by third party, the auditor should insist on obtaining declaration from the third party on its business letterhead and signed by authorised personnel of that third party confirming that the items of inventory belong to the entity and are being held by such third party on behalf of and for the benefit of the entity under audit.

Thus, by performing the above procedures, the auditor can obtain sufficient and appropriate audit evidence regarding the entity's legal ownership rights over inventories reported in the financial statements.

14. Audit Procedure – Occurrence Assertion: To verify that recorded sales represent goods actually shipped or services actually performed during the period, the auditor should perform the following audit procedures to satisfy the Occurrence assertion and ensure that revenue is not overstated:

1. Ensure revenue is not overstated by performing the following audit procedures:
    - Check whether a single sales invoice has been recorded twice or whether a cancelled sales invoice has also been recorded.
    - Test check a few sales invoices with their relevant entries in the sales journal.
    - Obtain confirmation from a few customers to ensure the genuineness of sales transactions.
    - Verify whether any fictitious customers and fictitious sales have been recorded.
    - Examine whether any shipments were made without the consent and agreement of the customer, especially at the year end, with the intention of inflating sales figures.
    - Check whether any unearned revenue has been incorrectly recorded as earned.
    - Evaluate whether any substantial uncertainty exists regarding the collectability of sales proceeds.
    - Examine whether customer obligations are contingent upon other actions such as financing, resale, etc.
2. Review the sequence of sales invoices to identify any missing, duplicate, or irregular invoices.
3. Review journal entries for unusual or non-routine revenue transactions.
4. Calculate the ratio of sales returns to sales and compare it with the previous year and enquire into the reasons for any significant increase or decrease.

5. Verify sales returns with supporting documents such as sales invoices, challans, credit notes, and stock registers.

Based on above audit procedures, the auditor would be able to conclude whether the sales recorded during the period are genuine, relate to actual shipments or services rendered, and are free from fictitious, duplicate, or premature recognition. These procedures directly address the risks highlighted in the given question regarding overstatement of revenue, particularly at the year end, and provide reasonable assurance on the Occurrence assertion of revenue.

15. The following are the purpose of Audit documentation:

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

Thus, in the given case, audit documentation supports effective audit planning, supervision, accountability, and compliance with quality control and regulatory inspection requirements.

16. The auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis.

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

(a) In writing, significant deficiencies in internal control that the auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances; and

(b) Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties and that, in the auditor's professional judgment, are of sufficient importance to merit management's attention.

The auditor shall include in the written communication of significant deficiencies in internal control:

(a) A description of the deficiencies and an explanation of their potential effects; and

(b) Sufficient information to enable those charged with governance and management to understand the context of the communication.

In particular, the auditor shall explain that:

(i) The purpose of the audit was for the auditor to express an opinion on the financial statements;

(ii) The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control; and

(iii) The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance.

Thus, proper written communication of significant deficiencies along with their implications and context, enables timely corrective action and enhances the effectiveness of governance and internal control systems.

17. Using the Work of another Auditor*:*

1. Need for Coordination and Proper Understanding between the Principal Auditor and the Other Auditor

   When the accounts of the branch are audited by a person other than the company's auditor (principal auditor), there is need for a clear understanding of the role of such other auditor and the company's auditor in relation to the audit of the accounts of the branch and the audit of the company as a whole. There is also great necessity for a proper rapport between these two auditors for the purpose of an effective audit.

In recognition of these needs, SA 600 makes it clear that:

- The principal auditor should advise the other auditor of the use that is to be made of the other auditor's work and report and make sufficient arrangements for coordination of their efforts at the planning stage of the audit.
- The principal auditor would inform the other auditor of matters requiring special consideration, procedures for the identification of inter-component transactions that may require disclosure, and the time-table for completion of audit.
- The principal auditor should advise the other auditor of the significant accounting, auditing and reporting requirements and obtain representation as to compliance with them.

2. Procedures to be Performed by the Principal Auditor to Evaluate and Use the Work of the Other Auditor

   SA 600 requires that the principal auditor should perform procedures to obtain sufficient appropriate audit evidence that the work of the other auditor is adequate for the principal auditor's purposes in the context of the specific assignment.

   The principal auditor might:

   - Discuss with the other auditor the audit procedures applied; or
   - Review a written summary of the other auditor's procedures and findings, which may be in the form of a completed questionnaire or checklist.

   The principal auditor may also wish to visit the other auditor. The nature, timing and extent of such procedures will depend on the circumstances of the engagement and the principal auditor's knowledge of the professional competence of the other auditor. This knowledge may have been enhanced from the review of the previous audit work of the other auditor.

Further, in certain situations, the statute governing the entity may confer a right on the principal auditor to visit a component and examine the books of account and other records of the said component, if he thinks it necessary to do so. Where another auditor has been appointed for the component, the principal auditor would normally be entitled to rely upon the work of such auditor unless there are special circumstances making it essential for him to visit the component and/or examine its books of account and other records.

18. While planning the audit, the auditor may concentrate on the following:

(i) Knowledge of the NGO's work, its mission and vision, areas of operations and environment in which it operates.

(ii) Updating knowledge of relevant statutes especially with regard to recent amendments, circulars, judicial decisions viz. Foreign Contribution (Regulation) Act 2010, Societies Registration Act, 1860, Income Tax Act 1961 etc. and the Rules related to the statutes.

(iii) Reviewing the legal form of the Organisation and its Memorandum of Association, Articles of Association, Rules and Regulations.

(iv) Reviewing the NGO's Organisation chart, then Financial and Administrative Manuals, Project and Programme Guidelines, Funding Agencies Requirements and formats, budgetary policies if any.

(v) Examination of minutes of the Board/Managing Committee/ Governing Body/Management and Committees thereof to ascertain the impact of any decisions on the financial records.

(vi) Study the accounting system, procedures, internal controls and internal checks existing for the NGO and verify their applicability.

(vii) Setting of materiality levels for audit purposes.

(viii) The nature and timing of reports or other communications.

(ix) The involvement of experts and their reports.

(x) Review the previous year's Audit Report.

Thus, a comprehensive understanding of the NGO's objectives, regulatory framework, governance structure and internal systems enables the auditor to plan the audit effectively and perform it in accordance with applicable auditing standards.

19. In carrying out audit of advances, the auditor is primarily concerned with obtaining evidence about the following:

(a) Amounts included in balance sheet in respect of advances which are outstanding at the date of the balance sheet.

(b) Advances represent amount due to the bank.

(c) Amounts due to the bank are appropriately supported by loan documents and other documents as applicable to the nature of advances.

(d) There are no unrecorded advances.

(e) The stated basis of valuation of advances is appropriate and properly applied and the recoverability of advances is recognised in their valuation.

(f) The advances are disclosed, classified and described in accordance with recognised accounting policies and practices and relevant statutory and regulatory requirements.

(g) Appropriate provisions towards advances have been made as per the per the RBI norms, Accounting Standards and generally accepted accounting practices.

20. Leadership responsibility of an engagement partner is to take responsibility for the overall quality on each audit engagement. The actions of the engagement partner and appropriate messages to the other members of the engagement team, in taking responsibility for the overall quality on each audit engagement, emphasise:

(a) The importance to audit quality of: -

(i) Performing work that complies with professional standards and regulatory and legal requirements;

(ii) Complying with the firm's quality control policies and procedures as applicable;

(iii) Issuing auditor's reports that are appropriate in the circumstances; and

(iv) The engagement team's ability to raise concerns without fear of reprisals.

(b) The fact that quality is essential in performing audit engagements.

Thus, in line with SA 220 – "Quality Control for an Audit of Financial Statements", the engagement partner, CA Arjun, has demonstrated effective leadership by taking responsibility for the overall quality of the audit engagement. Through his actions and communications, he emphasised the importance of compliance with professional standards, regulatory and legal requirements, adherence to the firm's quality control policies and procedures, issuance of an appropriate auditor's report, and fostering an environment where engagement team members can raise concerns without fear of reprisals. These actions clearly reinforce the fundamental principle that quality is essential in performing audit engagements, thereby fulfilling the leadership responsibilities of the engagement partner as required under SA 220.