

Chapter 1 Quality Control

Question 1

PQR & Associates are statutory auditors of a listed company. There arose an issue during the course of audit relating to related party transactions. The engagement partner wants to consult engagement quality control reviewer on this matter during the course of audit process itself. Can he consult with engagement quality control reviewer? Discuss.

Answer

It is necessary to maintain objectivity of 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 and eligibility to perform the role.

Question 2

Beta Private Limited has approached a firm of Chartered accountants to assist them in preparation of financial statements and issue a compilation report in this regard. Does CA firm have responsibility in relation to quality control for above said engagement? Discuss with reasons.

Answer

Such kind of services fall in category of “**related services**”. **SQC 1** is applicable to all type of engagements including engagement pertaining to “related services”.

Question 3

Ramanujan, a CA final student, feels that engagement file in audit engagement should be ready prior to issue of audit report. Discuss whether Ramanujan’s view is in order.

Answer

The firm should establish policies and 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. Thus, view of Ramanujam is **not in order**.

Question 4

BNE & Co. are in midst of audit process of a listed company. During the course of audit, an issue arose relating to revenues from contracts with customers in terms of Ind AS 115. The engagement partner took a certain stand. However, engagement quality control reviewer recommended otherwise after review. The engagement partner is not willing to accept recommendations of reviewer. How can the stalemate be ended?

Answer

In case, recommendations of engagement quality control reviewer are not accepted by engagement partner and 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. The audit report should be issued **only after resolution of matter**.

Question 5

MB & Associates is a partnership firm of Chartered Accountants which was established seven years back. The firm is getting new clients and has also, been offered new engagement services with existing clients. The firm is concerned about obtaining such information as it considers necessary in the circumstances before accepting an engagement with a new client and acceptance of a new engagement with an existing client. The firm is looking to work with only select clients to adhere to the Quality Control Standards. Guide MB & Associates about the matters to be considered with regard to the integrity of a client, as per the requirements of SQC 1.

Answer

As per SQC 1, 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, and when considering acceptance of a new engagement with an **existing client**. Where issues have been identified, and the firm decides to accept or continue the client relationship or a specific engagement, it should document how the issues were resolved.

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

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

The 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.

Question 6

Discuss the Auditor's responsibility to provide access to his audit working papers to Regulators and third parties.

Answer

- The auditor should not provide access to working papers to **any third party** without specific authority or unless there is a **legal** or professional duty to disclose. **Clause (1) of Part I of Second Schedule to the Chartered Accountants Act, 1949** states that a

Chartered Accountant in practice shall be deemed to be guilty of professional misconduct if he discloses information acquired in the course of his professional engagement to any person other than his client, without the consent of his client or otherwise than as required by law for the time being in force. SA 200 on “**Overall Objectives** of the Independent Auditor and the conduct of an audit in accordance with Standards on Auditing” also reiterates that, “the auditor should respect the confidentiality of the information obtained and should not disclose any such information to any third party without specific authority or unless there is a legal or professional duty to disclose”.

- If there is a request to provide access by the regulator based on the legal requirement, the same has to be **complied** with after informing the client about the same.
- Further, Standard on **Quality Control (SQC) 1**, “Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements”, provides that, unless otherwise specified by law or regulation, audit documentation is the property of the auditor. He may at his discretion, make portions of, or extracts from, audit 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 auditor or of his personnel.
- As per SA 230, Audit documentation serves a number of additional purposes, including the enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements.
- Therefore, it is auditor's responsibility to provide access to his audit working papers to Regulators whereas it's at **auditor's discretion**, to make portions of, or extract from his working paper to third parties.

Question 7

M/s NK & Co., Chartered Accountants were appointed as Statutory Auditors of Fresh Juice Limited for the F.Y 2019-2020. The previous year's audit was conducted by M/s. LP & Associates. After the audit was completed and report submitted, it was found that closing balances of last financial year i.e., 2018-19 were incorrectly brought forward. It was found that M/s NK & Co. did not apply any audit procedures to ensure that correct opening balances have been brought forward to the current period.

Accordingly, a complaint was filed against NK & Co. in relation to this matter.

You are required to inform what policies are required to be implemented by NK & Co. for dealing with such complaints and allegations as required by Standard on Quality Control (SQC).

Answer

In the given question, NK & Co. did not apply audit procedures to ensure that opening balances had been **correctly brought forward**. A complaint was filed against the auditors in this context. As per Standard on Quality Control (SQC) 1 “Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements”,

- 1) The firm should establish policies and procedures designed to provide it with

reasonable assurance that it deals **appropriately** with:

- a. Complaints and allegations that the work performed by the firm fails to comply with professional standards and regulatory and legal requirements; and
- b. Allegations of **non-compliance** with the firm's system of quality control.

- 2) Complaints and allegations (which do not include those that are **clearly frivolous**) may originate from within or outside the firm. They may be made by firm personnel, clients or other third parties. They may be received by engagement team members or other firm personnel.
- 3) As part of this process, the firm establishes clearly defined channels for firm personnel to raise any concerns in a manner that enables them to come forward **without fear of reprisals**.
- 4) The firm investigates such complaints and allegations in accordance with established policies and procedures. The investigation is supervised by a partner with **sufficient** and **appropriate experience** and authority within the firm but who is not otherwise involved in the engagement, and includes involving legal counsel as necessary. **Small firms** and **sole practitioners** may use the services of a suitably qualified external person or another firm to carry out the investigation. Complaints, allegations and the responses to them are documented.
- 5) Where the results of the investigations indicate deficiencies in the design or operation of the firm's quality control policies and procedures, or non-compliance with the firm's system of quality control by an individual or individuals, the firm takes **appropriate action**.

Question 8

J.A.C.K. & Co., a Chartered Accountant firm was appointed as the statutory auditor of Falcon Ltd. after ensuring the compliance with relevant provisions of the Companies Act, 2013. Mr. Jay was the engagement partner for the aforesaid audit and prior to commencement of the audit, Mr. Jay had called for a meeting of the engagement team in order to direct them and assign them their responsibilities. At the end of meeting, Mr. Jay assigned review responsibilities to two of the engagement team members who were the most experienced amongst all, for reviewing the work performed by the less experienced team members. While reviewing the work performed by the less experienced members of the engagement team, what shall be the considerations of the reviewers?

Answer

As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements", review responsibilities are determined on the basis that **more experienced** team members, including the engagement partner, review work performed by **less experienced** team members.

In the given situation, Mr. Jay, engagement partner assigned review responsibilities to two of the engagement team members who were the most experienced team members.

While reviewing the work performed by less experienced members of the engagement team, both the **more experienced** Reviewers should consider whether:

- (i) The work has been performed in accordance with professional standards and regulatory and **legal requirements**.
- (ii) Significant matters have been raised for further consideration.
- (iii) Appropriate consultations have taken place and the resulting conclusions have been documented and implemented.
- (iv) There is a **need to revise** the nature, timing and extent of work performed.
- (v) The work performed supports the conclusions reached and is appropriately documented.
- (vi) The evidence obtained is sufficient and appropriate to support the report; and
- (vii) The objectives of the engagement procedures **have been achieved**.

Question 9

HK & Co. Chartered Accountants have been auditors of SAT Ltd (a listed entity) for the last 8 financial years. CA. H, partner of the firm, has been handling the audit assignment very well since the appointment. The audit work of CA. H and her team is reviewed by a senior partner CA. K to assure that audit is performed in accordance with professional standards and regulatory and legal requirements. CA. K was out of India for some personal reasons, so this year CA. G has been asked to review the audit work. In your opinion, what areas CA. G should consider at the time of review. List any four areas and also comment whether firm is complying with Standard on Quality Control or not.

Answer

As per SQC 1, an engagement quality control review for audits of financial statements of listed entities includes considering the following:

- (i) The work has been performed in accordance with professional standards and regulatory and legal requirements;
- (ii) Significant matters have been raised for further consideration;
- (iii) Appropriate consultations have taken place and the resulting conclusions have been **documented** and **implemented**;
- (iv) There is a need to revise the nature, timing and extent of work performed;
- (v) The work performed supports the conclusions reached and is appropriately documented;
- (vi) The evidence obtained is sufficient and appropriate to support the report; and
- (vii) The objectives of the engagement procedures have been achieved.

The firm should establish **policies and procedures**:

- (i) Setting out criteria for determining the need for **safeguards** to reduce the familiarity **threat** to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and
- (ii) For all audits of financial statements of listed entities, requiring the rotation of the engagement partner after a specified period in compliance with the **Code**.

The familiarity threat is particularly relevant in the context of financial statement audits of listed entities. For these audits, the engagement partner should be rotated after a **pre-defined period**, normally not more than seven years.

From the facts given in the question and from the above stated paras of SQC 1, it can be concluded that firm is not complying with SQC 1 as Engagement Partner H is continuing for more than 7 years.

Question 10

AP & Associates, Chartered Accountants, are Statutory Auditors of XP Limited for the last four years. XP Limited is engaged in the manufacture and marketing of FMCG Goods in India. During 2021-22, the Company has diversified and commenced providing software solutions in the area of "e-commerce" in India as well as in certain European countries. AP & Associates, while carrying out the audit for the current financial year, came to know that the company has expanded its operations into a new segment as well as new geography. AP & Associates does not possess necessary expertise and infrastructure to carry out the audit of this diversified business activities and accordingly wishes to withdraw from the engagement and client relationship. Discuss the issues that need to be addressed before deciding to withdraw.

Answer

As per SQC 1, "Quality Control for Firms that Perform Audit and Reviews of Historical Financial Information, and other Assurance and Related Services Engagements", the firm should establish policies and procedures for the acceptance and continuance of client relationships and specific engagements, designed to provide it with reasonable assurance that it **will undertake or continue relationships** and engagements only where it is competent to perform the engagement and has the capabilities, time and resources to do so.

In the given case, AP & Associates, Chartered Accountants, statutory auditors of XP Limited for the **last four years**, came to know that the company has expanded its operations into a new segment as well as new geography. AP & Associates does not possess necessary expertise for the same, therefore, AP & Associates wish to withdraw from the engagement and client relationship. Policies and procedures on withdrawal from an engagement or from both the engagement and the client relationship **address issues** that include the following:

- Discussing with the appropriate level of the client's management and those charged with its governance regarding the appropriate action that the firm might take based on the **relevant facts and circumstances**.
- If the firm determines that it is appropriate to withdraw, discussing with the appropriate level of the client's management and those charged with its governance withdrawal from the engagement or from both the engagement and the client relationship, and 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 and the client relationship, together with the reasons for the withdrawal, to regulatory authorities.
- Documenting **significant issues, consultations, conclusions** and the basis for the conclusions.

AP & Associates should address the above issues before **deciding to withdraw**.

Question 11

PQR & Associates, Chartered Accountants, is a partnership firm having 3 partners CA P, CA Q and CA R. PQR & Associates are appointed as Statutory Auditors of ABC Limited, a listed entity for the financial year 2021-22 and CA P is appointed as Engagement Partner for the audit of ABC Limited. Before issuing the Audit Report of ABC Limited, CA P asked CA R to perform Engagement Quality Control Review and is of the view that his responsibility will be reduced after review by CA R. Whether the contention of CA P is correct? What are the aspects that need to be considered by CA R while performing Engagement Quality Control Review for audit of financial

statements of ABC Limited?

Answer

As per SQC 1, "Quality Control for Firms that Perform Audit and Reviews of Historical Financial Information, and other Assurance and Related Services Engagements", the review does not reduce the responsibilities of the engagement partner. Hence, contention of CA. P that after engagement quality control review by CA. R, his responsibility will be reduced, **is not correct**.

However, CA. R needs to consider the following aspect while performing Engagement Quality Control Review for audit of financial statements of a listed entity ABC Ltd.:

1. The engagement team's evaluation of the firm's independence in relation to the specific engagement.
2. Significant risks identified during the engagement and the responses to those **risks**.
3. Judgments made, particularly with respect to **materiality** and **significant risks**.
4. Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations.
5. The significance and disposition of corrected and uncorrected misstatements identified during the engagement.
6. The matters to be communicated to management and those charged with governance and, where applicable, other parties such as regulatory bodies.
7. Whether working papers selected for review **reflect** the work performed in relation to the significant judgments and support the conclusions reached.
8. The appropriateness of the report to be issued.

Engagement quality control reviews for engagements other than audits of financial statements of **listed entities** may, depending on the circumstances, include some or all of these considerations.

Question 12

SPS & Associates, Chartered Accountants, are statutory auditors of Grec Limited for the last two years. Grec Limited is engaged in the manufacturing and marketing of pharmaceutical goods in India. During the year 2023-24, the company has diversified and commenced providing software solutions in "e-commerce" in India as well as in certain African countries. SPS & Associates, while carrying out the audit, noticed that the company has expanded its operations into a new segment as well as in a new country. SPS & Associates does not possess the necessary expertise and infrastructure to carry out the audit of these diversified business activities and accordingly wishes to withdraw from the engagement and client relationship. Discuss the issues that need to be addressed before deciding to withdraw.

Answer

As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements", the firm should establish policies and procedures for the acceptance and continuance of client relationships and specific engagements, **designed** to provide it with reasonable assurance that it will undertake or continue relationships and engagements only where it is competent to perform the engagement and has the **capabilities, time and resources to do so**.

In the given case, SPS & Associates, Chartered Accountants, statutory auditors of Grec Limited for the last two years, came to know that the company has **expanded** its operations into a new segment as well as in new country. SPS & Associates does not possess the necessary **expertise** for the same, therefore, SPS & Associates wish to withdraw from the engagement and client relationship. Policies and procedures on withdrawal from an engagement or from both the engagement and the client relationship address issues that include the following:

Discussing with the appropriate level of the client's management and those charged with its governance regarding the appropriate action that the firm might take based on the relevant facts and circumstances.

If the firm determines that it is appropriate to withdraw, discussing with the appropriate level of the client's management and those charged with governance withdrawal from the engagement or from both the engagement and the client relationship, and 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 and the client relationship, **together with the reasons** for the withdrawal, to regulatory authorities.

Documenting significant issues, consultations, conclusions, and the basis for the conclusions.

SPS & Associates should address the above issues before **deciding to withdraw**.

Question 13

TPX & Co., Chartered Accountants is a large audit firm. It maintains audit documentation both electronically and in physical form (hard files). The physical files are neither scanned and incorporated into electronic files nor cross-referenced to the electronic files. Further, there are many instances where audit working papers do not contain details as to whether information was obtained from client or prepared by engagement team. How do you view above situation from point of view of quality control system in audit firm? Analyse.

Answer

In accordance with SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information and Other Assurance and Related Services Engagements" the firm should establish policies and procedures designed to maintain **confidentiality, safe custody, integrity, accessibility and retrievability** of engagement documentation.

In the given situation, the physical files are neither scanned and incorporated in the electronic files nor cross-referenced to the electronic files. Inability to do so shows that firm has not established policies and procedures to maintain integrity of engagement documentation. Lack of ensuring the same makes it difficult to demonstrate completeness of audit files and whether these were assembled **within 60 days** timeframe stipulated in SQC 1. Where engagement documentation is in paper, electronic, or other media, the integrity, accessibility or retrievability of the **underlying data** may be compromised if the documentation could be altered, added to or deleted without the firm's knowledge, or if it could be **permanently lost or damaged**. One of the reasons for designing and implementing appropriate controls for engagement documentation in this regard is the protection of the integrity of information at all stages of engagement.

For the practical reasons, original paper documentation may be electronically scanned for inclusion in engagement files. In that case, the firm implements appropriate procedures requiring engagement teams to:

- (a) Generate **scanned copies** that reflect the entire content of the original paper documentation, including manual signatures, **cross- references** and **annotations**;
- (b) Integrate the scanned copies into the engagement files, including indexing and signing off on the scanned copies as necessary; and
- (c) Enable the scanned copies to be retrieved and **printed as necessary**.

It has also been stated that there are many instances where audit working papers do not contain details as to whether information was obtained from the client or prepared by the engagement team. It is important to identify the source of the document and the information used as audit evidence to ensure its reliability. It could have **potential risks** of non-compliance with standards on auditing.

Question 14

Pine & Associates is the statutory auditor of BB Ltd., a listed company and started its operations 6 years ago. The fieldwork during the audit of the financial statements of the company for the year ended 31st March, 2023 was completed on 1st May, 2023. The auditor's report was dated 15th May, 2023. During the documentation review of the engagement, it was observed that the engagement quality control review was completed on 18th May, 2023. The engagement partner had completed his reviews in entirety by 12th May, 2023. Comment

Answer

As per SA 220, "Quality Control for an Audit of Financial Statement", the engagement partner shall take responsibility for reviews being performed in accordance with the firm's review policies and procedures. For audits of financial statements of listed entities, the engagement partner shall:

- Determine that an engagement quality control reviewer has been **appointed**;
- Discuss significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer; and
- **Not date** the auditor's report until the completion of the engagement quality control review.

Further, **SA 700**, "Forming an Opinion and Reporting on Financial Statements", requires the auditor's report to be dated not earlier than the date on which the auditor has obtained sufficient appropriate evidence on which to base the auditor's opinion on the financial statements. In cases of an audit of financial statements of listed entities where the engagement meets the **criteria** for an engagement quality control review, such a review assists the auditor in determining whether sufficient appropriate evidence has been obtained.

Conducting the engagement quality control review in a timely manner at appropriate stages during the engagement allows significant matters to be promptly resolved to the engagement quality control reviewer's satisfaction on or before the date of the auditor's report.

In this case, the audit of BB Ltd. for the year ending on **31st March 2023** was conducted by Pine & Associates and was completed on 1st May, 2023. Subsequently, the engagement partner reviewed the audit by 12th May, 2023. The audit report issued by Pine and Associates was dated **15th May, 2023**. However, the engagement quality control review was finalized on

18th May, 2023, which is **later** than the date of the audit report. In view of above, the date of auditors' report before the completion of the engagement quality control review, is not correct.

Question 15

PQR Associates are the statutory auditors of a large un-listed company, which is engaged in manufacturing of auto components. Subsequent to re-appointment of auditors in the Annual General Meeting, the Company shared the appointment letter with PQR Associates, seeking acknowledgement and acceptance letter. CA. R is the engagement partner and is planning to issue the acceptance letter. During the current financial year, there was a search by the Income-tax Authorities on the company, and certain accounting records were seized for verification. Based on the information available on social media, CA. R noted that the promoters' brother, is contemplating to contest in the ensuing elections, under the banner of a political party. One of the current senior engagement team manager, who has been doing the audit engagement till last year, has left PQR Associates and is planning to provide some accounting services to one of the associate companies. PQR Associates are yet to recruit another senior manager having adequate experience in the audits of clients engaged in automotive sector.

Elaborate the matters to be considered by PQR Associates with respect to acceptance & continuance of client relationships considering the above issues.

Answer

Acceptance and Continuance of Client Relationships: As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements," 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, and key managerial personnel.
- Competence (including **capabilities, time, and resources**) to perform engagement.
- Compliance with ethical requirements.

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, and when considering acceptance of a new engagement with an existing client. Where issues have been identified, and the firm decides to accept or continue the client relationship or a specific engagement, it should document how the issues were resolved.

Further, as per SA 220, "Quality Control for an Audit of Financial Statements", the engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall obtain relevant information from the firm and, where applicable, **network firms**, to identify and evaluate circumstances and relationships that **create threats** to independence.

In view of the above, PQR Associates should:

- ✓ Follow their firm's policies and procedures for client acceptance and continuance. This includes evaluating the integrity of the client, assessing potential risks associated with the engagement, and ensuring the firm has the necessary resources and expertise to perform the engagement effectively. The engagement team, should assess, whether the company is involved in any **funding activities**, to the **political parties**, and if so enquire and assess the risks related to such transactions.
- ✓ Communicate clearly with the client regarding the scope of the engagement, the

responsibilities of both parties, and any limitations on the services to be provided. This helps manage expectations and ensures alignment between the firm and the client. independence and objectivity throughout the engagement. Any potential threats to independence, such as relationships with the client's affiliates or involvement in political activities by related parties, should be evaluated and mitigated appropriately. Since the senior manager who was on this engagement is providing certain accounting services, to one of the group companies, the engagement partner, should assess, whether it would have any impact on the audit and examine the relevant ethical/independence requirements.

- ✓ Continually monitor the client relationship for any changes or developments that may impact the firm's ability to provide services effectively. This includes staying informed about significant events such as the Income-tax search, changes in client management, or potential conflicts of interest. Since there was an income-tax raid on the organisation, the engagement partner should evaluate the risks of material misstatements, and non-disclosure of tax disputes and liabilities.
- ✓ Ensure that their engagement team possesses the necessary competence and capabilities to perform the audit effectively. The departure of a senior manager and the need to recruit a replacement with specific industry experience should be addressed promptly to maintain audit quality. Since one of the senior engagement team members has left PQR Associates, the engagement partner should assess, whether he would be in a position to devote adequate time on the engagement or whether to recruit another resource, before commencement of the audit.

Question 16

CA Giri is a senior partner of M/s TSV Associates. M/s TSV Associates is a reputed firm of Chartered Accountants which has been in practice for more than five decades. The firm undertakes statutory audits of large listed companies across various industry sectors and has more than fifty qualified experienced professionals. CA Giri has been assigned as an Engagement Quality Control Reviewer for an audit engagement of a listed company. What are the aspects, which would be looked into by CA Giri as an EQCR in relation to the engagement? Upon completion of the review, CA Giri has identified certain issues, with respect to revenue recognition and adequacy of provisions relating to onerous contracts. The views of CA Giri are not accepted by the Engagement Partner. Suggest the ways of resolving the differences of opinion between CA Giri and the engagement partner

Answer

As per SA 220, "Quality Control for an Audit of Financial Statements", for audits of financial statements of listed entities, CA. Giri, the engagement quality control reviewer, on performing an engagement quality control review, shall also consider the following:

- (i) The engagement team's evaluation of the firm's independence in relation to the audit engagement;
- (ii) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations;
- (iii) Whether audit documentation selected for review reflects the work performed in relation to the significant judgments made and supports the conclusions reached.

As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements," there might be difference of opinion within engagement team, with those consulted and between engagement partner and 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 and 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. In the given situation, under completion of review, CA. Giri, Engagement Quality Control Reviewer has identified certain issues. However, the view of CA Giri, the EQCR are not accepted by the Engagement Partner. This difference of opinion among the CA Giri and Engagement Partner should be resolved with **abovementioned manner** as per SQC 1.

Question 17

STA and Associates, Chartered Accountants, is an upcoming firm and its good professional services are hired by diverse clients for assurance services. With a standing of seven years in practice, the firm has clients in various industries like health care, education, hospitality, manufacturing and many more. With the increasing assignments, changes in regulatory compliances and appointment of new personnel, the senior partner CA T is concerned with the proper functioning of the system of Quality control within the firm. He wants to ensure that policies and procedures relating to the system of quality control of the firm are complied with properly. CA T suggests that a proper monitoring of quality control will be the right approach. Discuss the factors that are to be considered by CA T for monitoring the quality control of engagements to ensure that they comply with SQC.

Answer

Factors considered for Monitoring Quality Control Engagements: As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements," factors to be considered by CA T for monitoring the quality control of engagements to ensure that they comply with SQC:

- Deciding whether the quality control system of the firm has been appropriately designed and effectively implemented.
- **Examining** whether new developments in the professional standards, legal, and 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 and appropriate experience and authority in the firm.
- Dealing with complaints and allegations against the firm or any employees of it of **noncompliance** with professional standards or appropriate regulatory requirements by a person within or outside the firm.
- Taking appropriate **remedial actions** against the personnel who did not conform to quality control policies.
- Taking action when deficiencies in the design or operation of the firm's quality control policies and procedures, or non-compliance with the firm's system of quality control are identified.

Question 18

M/s JinKushal & Co. has been appointed as an auditor of SC Ltd. for the financial year 2023-24. CA Jin, one of the partners of M/s JinKushal & Co., completed entire routine audit work by 19th June, 2024. Unfortunately, on the very next morning, while roving towards office of SC Ltd. to sign final audit report, he met with a road accident and died. CA Kushal, another partner of M/s JinKushal & Co., therefore, signed the accounts of SC Ltd., without reviewing

the work performed by CA Jin. State with reasons whether CA Kushal is right in expressing an opinion on financial statements, the audit of which is performed by another auditor.

Answer

Relying on Work Performed by Another Auditor: As per SA 220 "Quality Control for an Audit of Financial Statements", an engagement partner taking over an audit during the engagement may apply the review procedures such as the work has been performed in accordance with professional standards and regulatory and legal requirements; significant matters have been raised for further consideration; appropriate consultations have taken place and the resulting conclusions have been documented and implemented; there is a need to revise the nature, timing and extent of work performed; the work performed supports the conclusions reached and is appropriately documented; the evidence obtained is sufficient and appropriate to support the auditor's report; and the objectives of the engagement **procedures have been achieved.**

Further, as per the **Code of Ethics** it is the auditor's professional responsibilities and should be complied with that when the auditor delegates work to assistants or uses work performed by other auditors and experts, he will continue to be responsible for forming and expressing his opinion on the financial information. However, he will be entitled to rely on work performed by others, provided he exercises **adequate skill and care** and is not aware of any reason to believe that he should not have so relied.

However, the auditor should **carefully direct**, supervise and review the work delegated. He should obtain reasonable assurance that work performed by other auditors/experts and assistants is adequate for his purpose.

In the given case, all the auditing procedures before the moment of signing of final report have been performed by CA Jin. However, the report **could not be signed by him** due to his **unfortunate death**. Later on, CA Kushal signed the report relying on the work performed by CA Jin. Here, CA Kushal is allowed to sign the audit report, though, will be responsible for expressing the opinion. He may rely on the work performed by CA Jin provided he further exercises adequate skill and due care and review the work performed by him.

Question 19

Rajni Ltd., a listed company, has appointed M/s Amit & Co. as its statutory auditor. CA Sunil, who recently joined the firm, has been appointed as the engagement partner for the first time. While preparing for the audit, he realises the importance of ensuring the audit team's independence, as required by standard audit practices. However, when reviewing the firm's framework, he is unable to find any documented policies or procedures addressing independence compliance. What steps should CA Sunil take to ensure compliance with independence requirements for the audit engagement? Why is it necessary for an audit firm to have well-documented policies and procedures to maintain independence? Discuss with reference to the relevant Standards on Auditing.

Answer

As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements," the firm should establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, others subject to independence requirements (including

experts contracted by the firm and network firm personnel), maintain independence where required by the Code. Such policies and procedures should enable the firm to:

- (i) Communicate its independence requirements to its **personnel** and, where applicable, to others subject to them; and
- (ii) Identify and evaluate circumstances and relationships that create threats to independence, and 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.

Further, as per SA 220, "Quality Control for an Audit of Financial Statements", the engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement.

In doing so, the engagement partner shall:

- (iii) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate circumstances and relationships that create threats to independence;
- (iv) Evaluate information on identified **breaches**, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for the audit engagement; and
- (v) Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is **permitted by law or regulation**. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action.

Question 20

KSN and Co., Chartered Accountants, have been appointed by Nature Ltd. to assist management in the preparation and presentation of financial information in accordance with an applicable financial reporting framework and issuing a report. CA L has been appointed as the engagement partner for the assignment.

What are the responsibilities of CA L and which documentation requirements related to Engagement Level Quality Control should CA L ensure compliance with in such an engagement?

Answer

The engagement partner shall take responsibility for: -

- (i) The **overall quality** of each compilation engagement to which that partner is assigned and
- (ii) The engagement being performed in accordance with the firm's quality control policies and procedures.

The practitioner shall include in the engagement documentation: -

- (i) Significant matters **arising** during the compilation engagement and how those matters were addressed by the practitioner.
- (ii) A record of how the compiled financial information **reconciles** with the underlying records, documents, explanations and other information, provided by management and
- (iii) A copy of the final version of the compiled financial information for which management or those charged with governance, as appropriate, has **acknowledged** their responsibility, and the practitioner's report. The practitioner may consider also including in the engagement documentation a copy of the entity's **trial balance**, summary of significant accounting records or other information that the practitioner used to perform the compilation.

Question 21

SDC & Associates, a medium-sized audit firm, is appointed as an auditor of Neuronix Ltd., a listed pharmaceutical company engaged in extensive R&D with complex global operations. CA Rashi an engagement partner of SDC & Associates is leading the audit team for the audit of the same. Neuronix Ltd. was earlier audited by a Big 4 firm that withdrew from the engagement citing scope limitations. During the audit planning, CA Rashi realises that while her team is skilled in standard manufacturing audits, they lack experience in pharma R&D and associated regulatory frameworks. The firm is under pressure to complete the audit in time to meet the listing obligations of Neuronix Ltd. The Managing Partner insists on continuing the audit and advises CA Rashi to rely on the firm's standard procedures to ensure timely delivery. In light of SQC 1 and SA 220, analyse the quality control considerations CA Rashi must evaluate before continuing with the engagement. What actions should she take to uphold audit quality and professional standards?

Answer

As per **SQC 1, "Quality Control for firms that perform audits and reviews of historical financial information, and other assurance and related services engagements"**, CA Rashi, as the engagement partner, is required to evaluate whether the firm has the capabilities, competence, time and resources to undertake an engagement, following matters have to be taken into consideration: -

- 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 and knowledge effectively;
- The firm has sufficient **personnel with the** necessary capabilities and competence;
- Experts are available, if needed;
- Individuals meeting the **criteria and eligibility** requirements to perform engagement quality control review are available, where applicable; and
- The firm would be able to complete the engagement within the reporting deadline.

Under **SA 220, "Quality Control for an audit of financial statements"**, the responsibility of an engagement partner in this regard in an audit engagement is on lines of SQC 1 which requires 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, and when considering acceptance of a new engagement with an existing client.

Information like integrity of principal owners, competence of engagement team and consideration of necessary capabilities including time and resources, compliance with relevant ethical requirements and significant **matters arisen during current or previous audit engagement and their implications** assist the engagement partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate.

In the given case:

Under **SA 220, "Quality Control for an audit of financial statements"**, the responsibility of an engagement partner in this regard in an audit engagement is on lines of SQC 1 which requires 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, and when considering acceptance of a new engagement with an existing client.

Information like **integrity of principal owners, competence of engagement team** and consideration of necessary capabilities including time and resources, compliance with relevant ethical requirements and significant matters arisen during current or previous audit engagement and their **implications assist the engagement** partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate.

In the given case:

- SDC & Associates lacks experience in pharmaceutical R&D audits, a highly regulated and technical field.
- The previous auditor's withdrawal citing scope limitations is a warning sign that must be evaluated.
- The engagement team lacks relevant expertise, and there is pressure from the managing partner to proceed regardless.
- Proceeding without addressing these issues would violate the requirements of SQC 1 and SA 220.

CA Rashi must not proceed with the engagement unless satisfied that all conditions under SQC 1 and SA 220 are met. **She should:**

- **Assess the firm's capability and consider engaging external experts.**
- **Understand the reason for previous auditor's withdrawal.**
- **Ensure that a qualified EQCR reviewer is appointed and review is completed before issuing the audit report.**

This will help maintain audit quality, ensure compliance with professional standards, and protect the firm from regulatory repercussions.

Question 22

XYZ and Associates, Chartered Accountants, is an audit firm, giving services to the various types of clients in the field of auditing, taxation and management consultancy. It has been doing statutory audit of B Ltd., a listed entity since last seven years. CA X who has been the engagement partner for the company since beginning has a complete idea about the strengths and weaknesses of the internal controls of the company. He maintains good relations with the management and those charged with the governance. Every year audit is completed in a cordial and healthy manner. During current year the quality control reviewer insisted to change the engagement partner for the company saying that continuation of same engagement partner poses certain audit risk and threats to the organization and advises to review the firm's policies and procedures in relation to the engagement partner. The management of the company does not wish to change the engagement partner. How do you view the above situation from the viewpoint of quality control system in audit firm in terms of requirements of SQC 1? Guide the firm in establishing the policies and procedures in respect of an engagement partner.

Answer

SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements," 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

(i) the **nature of the engagement**, including the extent to which it involves a matter of public interest, and

(ii) the **length of service** of the senior personnel on the engagement.

- The familiarity threat is particularly relevant in the context of financial statement audits of listed entities. For these audits, the engagement partner should be rotated after a pre-defined period, normally not more than **seven years (except in cases where audit of listed entities is conducted by a sole practitioner)**. However, to ensure quality control exists in such firms and appropriate reports are issued, there is a process for mandatory peer review of such firms.

In the given situation, XYZ and Associates, Chartered Accountants, has been conducting the statutory audit of B Ltd., a listed company, for the past seven years. CA X served as the engagement partner throughout this period. CA X has developed an in-depth understanding of the company's internal controls and maintains a strong, cordial relationship with the management and those charged with governance. However, during the current year, the firm's quality control reviewer raised concerns about the continued involvement of CA X, citing the continuation of the same engagement partner poses certain audit risk and threats to the organisation, and advised reviewing the firm's policies regarding engagement partner rotation.

In view of SQC 1, the continued involvement of the same engagement partner, CA. X with a listed entity **for an extended period, i.e., more than 7 years**, poses a familiarity threat, potentially impairing audit quality and independence. Therefore, the firm should implement a policy of mandatory **partner rotation and review its quality** control procedures to ensure compliance with professional standards and maintain the integrity of the audit process.

The firm should establish policies and procedures requiring that:

- (I) The identity and role of the engagement partner are communicated to key members of the client's management and those charged with governance;
- (II) The engagement partner has the appropriate capabilities, competence, authority, and time to perform the role; and
- (III) The responsibilities of the engagement partner are clearly defined and communicated to that partner.

Question 23

Munir & Co. is a practicing-chartered accountants' firm having its Head Office at Mumbai. Mr. A, a dedicated and capable article assistant associated with Munir & Co. for the past three years, recently qualified as a Chartered Accountant. Recognizing his strong analytical skills, attention to detail, and in-depth understanding of audit, the firm inducted him as a Partner on 1st February, 2025. On joining the firm, he accepted his first assignment to act as

an Engagement Quality Control Reviewer (EQCR) for J & J Limited, a listed entity, for the financial year 2024-25. Before finalizing the Balance Sheet of the Company for the year 2024-25, CA A signed on few working papers of the engagement team as a token of review performed by him in terms of firm's policies on engagement quality control review without going through the audit file. He made no further documentation, assuming that the team who performed the audit of the company for the year 2024-25, was the same team who performed the audit of the company for the financial year 2023-24.

Comment on the act of CA A in accordance with relevant professional standards.

Answer

As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements", 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 and 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 financial statements of a listed entity is an individual with sufficient and appropriate experience and authority to act as an audit engagement partner on audits of financial statements of listed entities.

In the given case, Munir & Co, admitted Mr. A, who was an articled assistant for 3 years, as a Partner on 1st February **2025 after he qualified** as a Chartered Accountant. He was appointed as Engagement Quality Control Reviewer (EQCR) for J & J Limited, a listed company, for FY 2024-25. It may be considered that CA A has recently qualified as a Chartered Accountant and does not possess the competence **and capability for the work assigned**. Therefore, it was not appropriate for CA A to accept the assignment of Engagement and Quality Control Reviewer.

Further, the engagement quality control reviewer shall document, for the audit engagement reviewed, that:

- (i) The procedures required by the firm's policies on engagement quality control review have been performed.
- (ii) The engagement quality control review has been completed on or before the date of the auditor's report.
- (iii) The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made and the conclusions they reached were not appropriate.

In the given situation, there are no working papers to show that Engagement quality control reviewer has done an evaluation of conclusion reached by the engagement team. Mere signing on some working papers of the engagement team shows that Engagement and Quality Control

Reviewer has made no such evaluation and review of **work performed by the engagement team**. In view of above, act of CA A only signing a few working papers is not correct, and he shall maintain documentation in accordance with the Engagement and Quality Control Standards.

Chapter 2 General Auditing Principles And Auditors Responsibilities

SA 240

Question 1

While auditing accounts of a public limited company for the year ended 31st March 2015, an auditor found out an error in the valuation of inventory, which affects the financial statement materially. Comment as per standards on auditing.

Answer

Errors in Valuation of Inventories and Auditor's Responsibilities: SA 240, "The Auditor's Responsibilities Relating **Fraud** in an Audit of Financial Statements", requires that if circumstances indicate the possible existence of fraud or error, the auditor should consider the potential effect of the **suspected fraud** or error on the financial information.

- If the auditor believes the suspected fraud or error could have a material effect on the financial information, he should perform such modified or additional procedures as he determines to be appropriate. SA 240 also requires that when the auditor identifies a misstatement, the auditor shall evaluate whether such a **misstatement** is indicative of fraud.
- If there is such an indication, the auditor shall evaluate the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management representations, recognizing that an instance of fraud is unlikely to be an **isolated occurrence**.
- Further, SA 320 Materiality in Planning and Performing an Audit, also requires that in such circumstances, the auditor should consider requesting the management to adjust the financial information or consider extending his audit procedures.
- If the management refuses to adjust the financial information and the results of extended audit procedures do not enable the auditor to conclude that the **aggregate of uncorrected misstatements is not material**, the auditor should express a qualified or adverse opinion, as appropriate.
- In the instant case, the auditor has detected the material errors affecting the financial statements; the auditor should communicate his findings to the management on a **timely basis**, consider the implications on true and fair view and also ensure that appropriate disclosures have been made.

Question 2

M/s Honest Limited has entered into a transaction on 5th March, 2016, near year-end, whereby it has agreed to pay ` 5 lakhs per month to Mr. Y as annual retainer-ship fee for "engineering consultation". No amount was actually paid, but ` 60 lakhs is provided in books of account as on March 31, 2016.

Your inquiry elicits a response that need-based consultation was obtained round the year, but there is no documentary or other evidence of receipt of the service. As the auditor of M/s Honest Limited, what would be your approach?

Answer

As per SA 240 on "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", fraud can be committed by management **overriding controls** using such techniques as Recording fictitious journal entries, particularly close to the end of an accounting period, to manipulate operating results or achieve other objectives.

Keeping in view the above, it is clear that Company has **passed fictitious** journal entries near year end to manipulate the operating results. Also Auditor's enquiry elicited a response that **need-based** consultation was obtained round the year, but there is no documentary or other evidence of receipt of the service, is **not acceptable**.

Accordingly, the auditor would adopt the following approach-

If, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit, the auditor shall:

- (i) Determine the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the audit appointment or, in some cases, to **regulatory authorities**;
- (ii) Consider whether it is appropriate to withdraw from the engagement, where withdrawal from the engagement is legally permitted; and
- (iii) If the auditor withdraws:
 - (1) Discuss with the appropriate level of management and those charged with governance, the auditor's withdrawal from the engagement and the reasons for the withdrawal; and
 - (2) Determine whether there is a professional or legal requirement to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities, the auditor's withdrawal from the engagement and the reasons for the withdrawal.

Further, as per section **143(12)** of the Companies Act, 2013, if an auditor of a company, in the course of the performance of his duties as auditor, has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company, he shall immediately report the matter to the Central Government (in case amount of fraud is **` 1 crore or above**) or Audit Committee or Board in other cases (in case the amount of fraud involved is less than **` 1 crore**) within such time and in such manner as may be prescribed. The auditor is also required to report as per **CARO, 2020**, Whether any fraud by the company or any fraud on the company by its officers or employees has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated.

Question 3

In the course of audit of K Ltd., its auditor Mr. 'N' observed that there was a special audit conducted at the instance of the management on a possible suspicion of a fraud and requested for a copy of the report to enable him to report on the fraud aspects. Despite many reminders it was not provided. In absence of the special audit report, Mr. 'N' insisted that he be provided with at least a written representation in respect of fraud on/by the company. For this request also, the management remained silent. Please guide Mr. 'N'.

Answer

- As per SA 240 on “The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements”, the auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are **free from material misstatement**, whether caused by fraud or error.
- As per SA 580 “Written Representations”, if management modifies or does not provide the requested written representations, it may **alert** the auditor to the possibility that one or more significant issues may exist.
- In the instant case, the auditor observed that there was a special audit conducted at the instance of the management on a possible **suspicion of fraud**. Therefore, the auditor requested for special audit report which was not provided by the management despite of many reminders. The auditor also insisted for written representation in respect of fraud on/by the company. For this request also management remained silent.
- It may be noted that, if management **does not** provide **one or more** of the requested written representations, the auditor shall discuss the matter with management; **re-evaluate** the integrity of management and evaluate the effect that this may have on the reliability of representations (**oral or written**) and audit evidence in general; and take appropriate actions, including determining the possible effect on the opinion in the auditor’s report.
- 143(12).... + CARO...

Key Note:

If, as a result of a misstatement resulting from fraud or suspected fraud, the auditor **encounters** exceptional circumstances that bring into question the auditor’s ability to continue performing the audit, the auditor shall:

- (i) Determine the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the audit appointment or, in **some cases**, to regulatory authorities;
- (ii) Consider whether it is appropriate to withdraw from the engagement, where withdrawal from the engagement is **legally permitted**; and
- (iii) If the auditor withdraws:
 - (1) Discuss with the appropriate level of management and those **charged** with governance, the auditor’s withdrawal from the engagement and the reasons for the withdrawal; and
 - (2) Determine whether there is a professional or legal requirement to report to the person or persons who made the audit appointment or, in **some cases**, to regulatory authorities, the auditor’s withdrawal from the engagement and the reasons for the withdrawal.

Question 4

In the course of audit of A Ltd. you suspect the management has indulged in fraudulent financial reporting. State the possible source of such fraudulent financial reporting.

Answer

Possible Sources of Fraudulent Financial Reporting:

- **Incentives/Pressures**
- **Financial stability or profitability is threatened**
- **Excessive pressure exists for MGT**