



Peer Review Board

Quality Control Framework

General Controls & Specific Controls

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TWO DAYS TRAINING PROGRAMME FOR PEER REVIEWERS

Organized by:

Peer Review Board,

The Institute of Chartered Accountants of India,

New Delhi

31st December 2022 at Pune Branch of WIRC

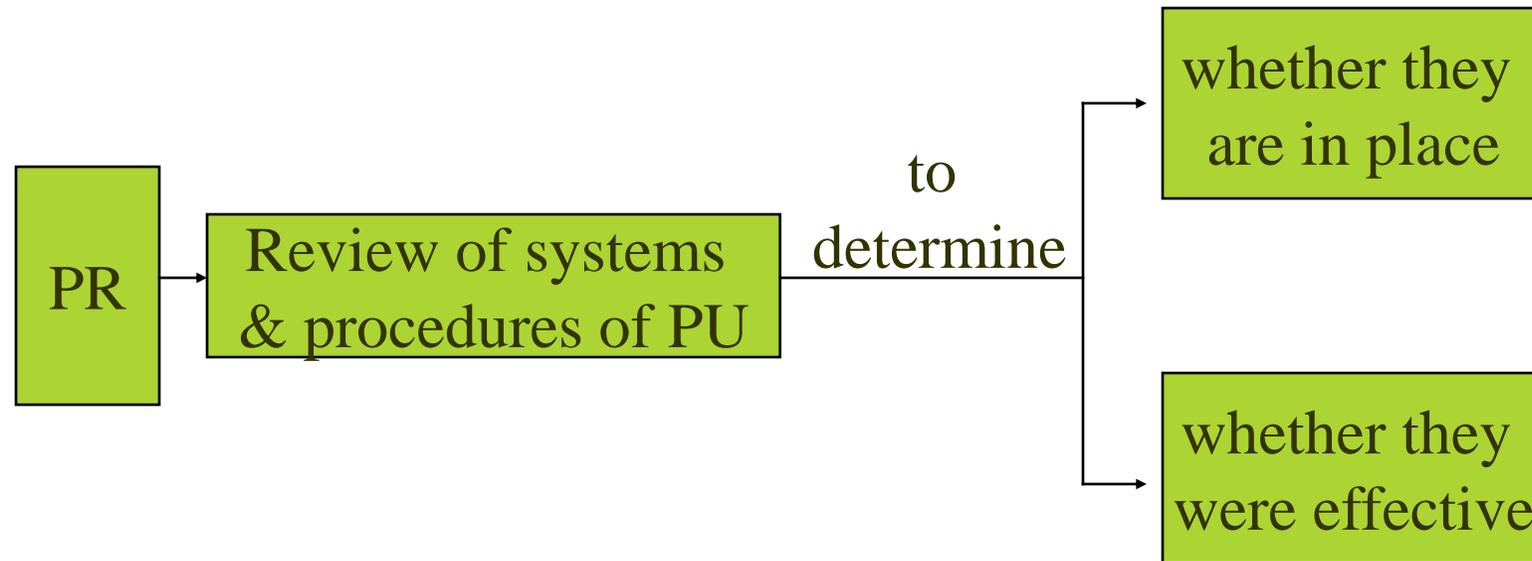
**Session 4 Compliance With Framework of Quality
Control General & Specific Controls**

CA Dr Dilip V Satbhai

Former Chairman Pune Branch of WIRC



What is Peer Review



**To ensure Quality in Assurance Services
as mandated by Technical Standards**

Identify weakness in engagements rather than
failure in engagements



Scope of Peer Review

■ Assurance Services

“Peer Review period” means **3 years preceding the year** in which the Practice Unit is selected or such other period or any period as may be prescribed by the Peer Review Board for conducting a Peer Review.

■ Focus

- Compliance with **Technical, Professional and Ethical Standards**
- Quality of Reporting
- Office Systems and Procedures
- Training Programme for Staff



Tips

- Nothing is achieved without labour – we need to unlearn the old and relearn the new: **at any age, a CA is always a student**
- To be a peer reviewer is a greater challenge than being a reviewee – **you need to know before you can challenge!**
- Dream is not the one that we see in sleep but it is the one that **does not allow us to sleep to acquire knowledge which brings wisdom**



Role of controls testing

- What are controls? -
Preventive,
Detective
- Their importance
 - COSO framework: Control environment, risk assessment, control activities, information and communication, monitoring



COSO

- The **Committee of Sponsoring Organizations of the Treadway Commission (COSO)** is a joint initiative to combat corporate fraud. It was established in the United States by five private sector organizations, **dedicated to guide executive management and governance entities** on relevant aspects of organizational governance, business ethics, internal control, enterprise risk management, fraud, and financial reporting. COSO has established a common internal control model against which companies and organizations may assess their control systems



Key concepts of the COSO framework

- Internal control is a *process*. It is a means to an end, not an end in itself.
- Internal control is affected by *people*. It's not merely policy, manuals, and forms, but people at every level of an organization.
- Internal control can be expected to provide only *reasonable assurance*, not *absolute assurance*, to an entity's management and board.
- Internal control is geared to the achievement of *objectives* in one or more *separate but overlapping categories*.



Key concepts

- Controls testing (compliance approach) vs substantive testing (substantive approach)
- Tests of design, implementation and operating effectiveness
- **Controls testing methods in peer review**
 - Inquiry, corroborated by inspection of documents



COMPLIANCE TEST SUBSTANTIVE TEST

- **Compliance test** determines controls are being applied that complies with management policies and procedures. **Substantive test** determines the integrity of actual processing.
- In **compliance testing** we gather evidence with the objective of testing an organization's compliance with control procedures **Substantive procedures** are tests designed to obtain evidence to ensure the completeness, accuracy and validity of the data.



COMPLIANCE TEST SUBSTANTIVE TEST

- **Compliance testing** checks for the presence of controls
Ex: Verification of Access rights controls, Presence of procedures for Program Change control management, incident management, problem management, review of existing network controls **Substantive testing** checks the integrity of contents. Review of transactions/ numbers/ values. Eg: Inventory validation, record matching, balance checks
- **Compliance testing** will be performed first **Substantive testing** is always performed after compliance testing



COMPLIANCE TEST SUBSTANTIVE TEST

- **Compliance testing** is independent of Substantive testing. However, the results of compliance testing are used to determine if **Substantive testing** is required.
- If **compliance testing** indicates strong internal control, **substantive testing** may be waived off or reduced.
- In case **compliance testing** indicates weak internal controls then **substantive testing** to be more rigorous

Structure of standards issued by AASB under the authority of ICAI.



Standards on
Quality Control

The Chartered
Accountants
Act, 1949, Code of
Ethics and other
relevant
pronouncements of
ICAI.



SQC - Services covered by AASB

Assurance Services

Related Services

Audit and Review of Historical Fin. Info.

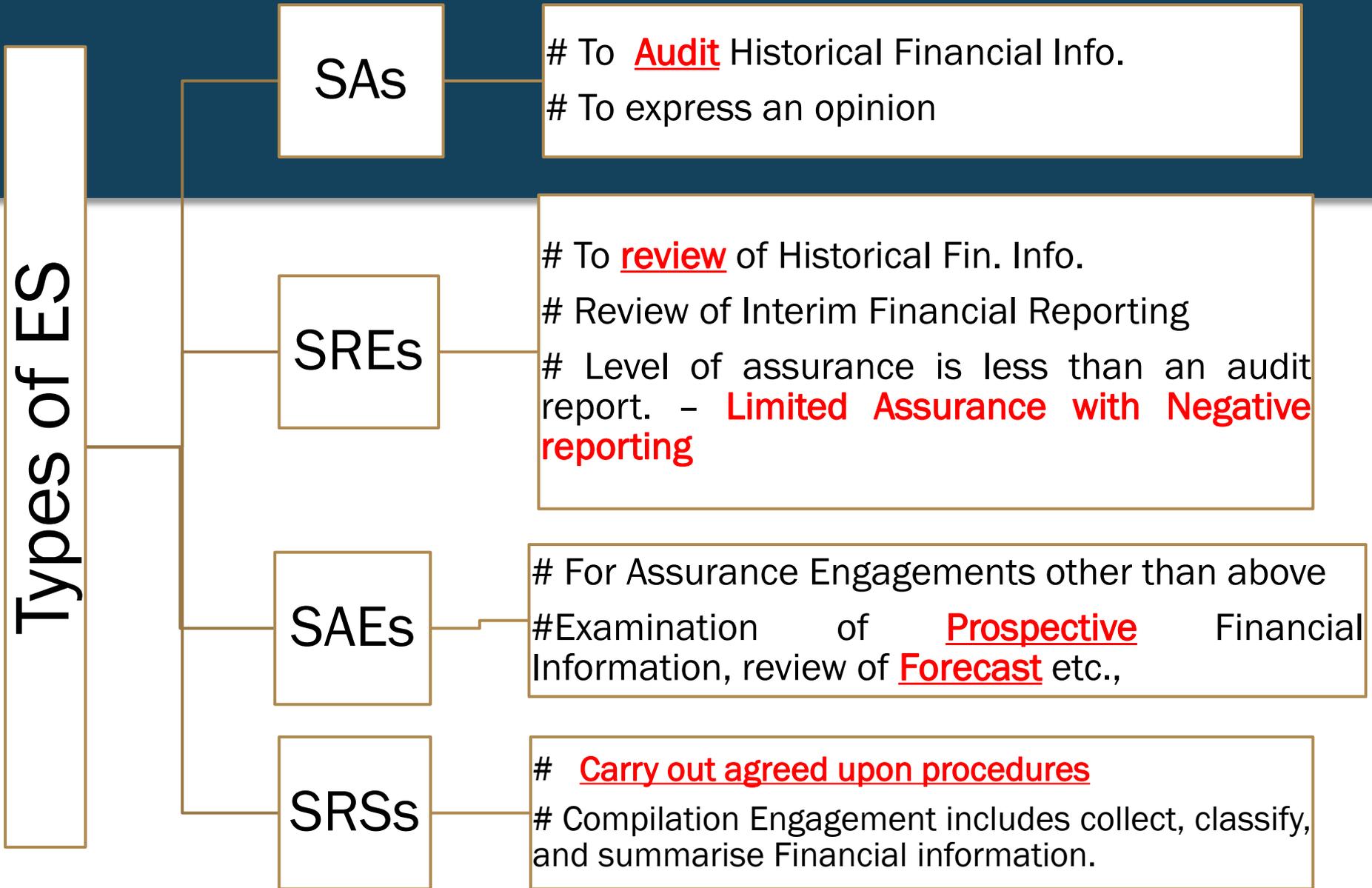
Assurance Engagements other than Audit and review of Historical Fin. Info

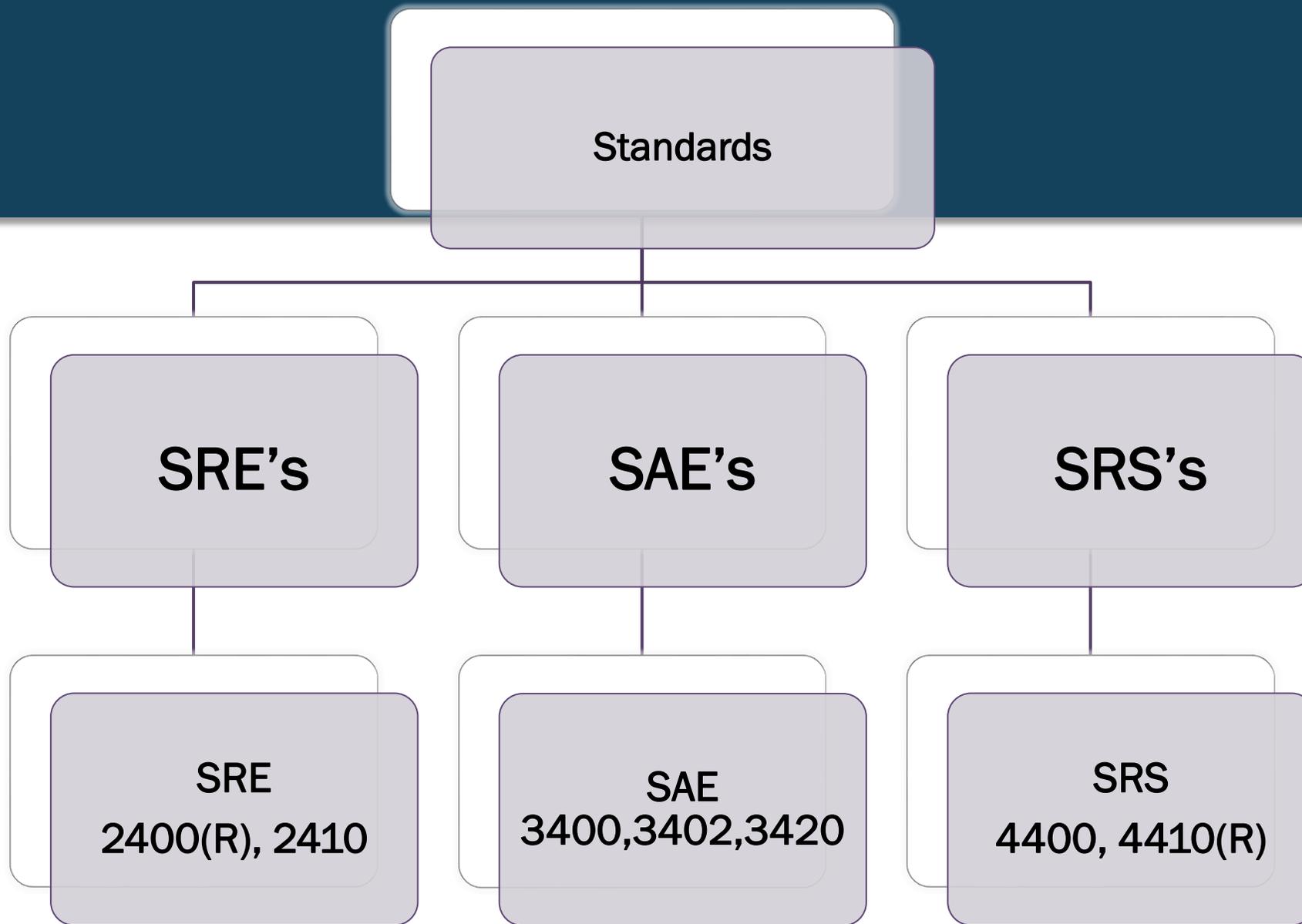
Standards on Auditing
[100-999]

Standards on Review Engagements
[2000-2699]

Standards on Assurance Engagements
[3000-3699]

Standards on Related Services
[4000-4699]





Points

Technical and Professional Standards



Standards on Quality Control



Accounting Standards & Standards on Auditing



Ethical Standards



Professional Standards



Statements Issued by ICAI



Notifications/Directions, including those of a self-regulatory nature



Relevant Statutes and Regulations



Guidance Notes

Sec. 143(2) of the Companies Act, 2013



- **Basic Requirements as to Financial Statements**
- The Auditor shall make the Report after taking into account, the following –
 - the provisions of the Act,
 - **the accounting and auditing Standards,**
 - matters which are required to be included in the Audit Report under the provisions of the Act / Rules / Order u/s 143(11)
 - **best of his information and knowledge.**



- Sec. 143(9) – Every Auditor shall **comply** with the Auditing Standards.



Disciplinary Action based on Peer Review:

As per the revised Statement on Peer Review, if the Board is of the opinion that the findings of the subgroup **contains material deficiencies** on the Practicing Unit, then the Board shall revoke the Peer Review Certificate and refer the matter to the Council for considering whether the same may be referred to the Disciplinary Directorate for initiating disciplinary action.



Second Schedule to CA Act 1949 – Part 1

Clause 7

Does not exercise Due Diligence, or is grossly negligent in the conduct of his professional duties.

Clause 9

Fails to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances.

General Controls



- Independence
- Maintenance of Skills
- Outside consultation
- Staff supervision and Development
- Office Administration

Specific Controls – Six Key Controls



Audit Record Administration

Review and Evaluation of System of Internal Controls

Substantive Tests

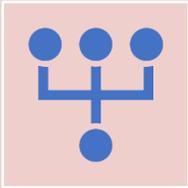
Financial Statement Presentation

Audit Conclusion and

Audit Report



Question 1



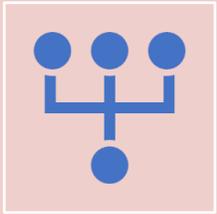
Does the Practicing Unit have a system of quality control for attestation services?



Assess based on completed questionnaire developed by the Peer Review Board and initial meeting with Practicing Unit



Question 2



Does the System of Quality Control is **designed to ensure compliance with Technical Standards** and maintenance of quality in attestation work?



Review of General controls:

Independence

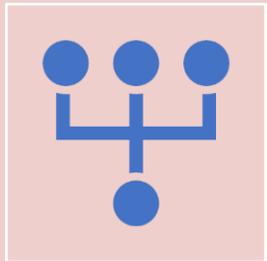
Maintenance of Professional skills and Outside consultation

Staff supervision and development

Office administration



Question 3



Was the Designed Systems and Procedures at Practicing Unit **Effective** during the period of Review?

To Decide the Effectiveness

Review of Controls

Compliance Approach

Substantive Approach

Six Key Controls to be reviewed

Audit Record Administration

- Review & Evaluation of System of Internal Controls
- Substantive Tests
- Financial Statement Presentation
- Audit Conclusion and
- Audit Report





**Peer Review
Manual
[Paragraph 8]**

**Illustrative
Checklist of the
Practice Unit**

**Appendix X
Compliance
according to SQC 1**

**SA Wise Points for
Verification**

**AS & IndAS wise
Points for
Verification**

Types of controls in peer review

- **General controls (SQC)**

- These are quality controls at the firm level, designed to provide it with reasonable assurance that the firm and its personnel **comply** with *professional standards* and *regulatory and legal requirements* **and** that reports issued by the firm or engagement partner are appropriate in the circumstances

Types of controls in peer review

- **Specific controls:**

- These are controls at the **engagement level**, designed to ensure that the PU **plans** and **performs** an assurance engagement in **compliance with the standards on auditing or review** and other **regulatory and legal requirements**



General Controls -

**Compliance
Review of
General
Controls**



1. Independence



Concept of Independence

Independence of Mind-

- The state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgement, allowing an individual to act with integrity, and exercise objectivity and professional skepticism

Independence in appearance–

- The **avoidance of facts and circumstances** that are so significant, that a reasonable and informed third party, having knowledge of all relevant information, including safeguards applied, would reasonably conclude a firm's, or a member of the audit team's, integrity, objectivity or professional skepticism had been compromised



What are “threats” to independence?

- **Self-interest threat**
 - Auditor could benefit from an interest
- **Self-review threat**
 - Auditor audits his own work
- **Advocacy threat**
 - Auditor promotes client’s position/ opinion
- **Familiarity threat**
 - Relationship buys auditor’s sympathy
- **Intimidation threat**
 - Auditor succumbs to client’s threats



Illustrative “safeguards”

- Involving an additional advisory or reviewing partner or manager
- Rotation of partner/ manager
- Discussion of independence matters with audit committee or board
- Independence confirmations from engagement team
- Removing individuals who might cause a threat – eg those with financial/ business interests or having employment relationships

Disqualifications [Sec.141(3)]

Basic Disqualification



- **(a) Body Corporate (other than LLP)**
- **(b) An Officer or Employee of the Company**
- **(c) Partner or Employee of an Officer or employee of the Company,**
- **(d) A Person or a Firm having Business Relationship (directly or indirectly) with the Company or its Holding / Subsidiary/Associate**
- **(e) Relative of Director or KMP**
- **(f) Person in Full time employment or a person or a partner of a Firm holding audits of more than 20 Companies on the date of appointment [Exclusions – One Person Companies, Dormant Companies, Small Companies, and Private Ltd Companies having paid up capital less than Rs. 100 Crores - Notification dt 05-06-2015]**
- **(g) Person convicted by court for an offence involving Fraud and 10 years has not elapsed from such conviction**
- **(h) a person who, directly or indirectly, renders any service referred in Sec.144 to the Company or its Holding Company or its Subsidiary Company.**



Basic Disqualification

- **(h) a person who, directly or indirectly, renders any service referred in Sec.144**



Basic Disqualification

- a Person who, or his Relative or Partner (involved in the following aspects with the Company or its Subsidiary, Holding or Associate or a Subsidiary of such Holding Company –
- is holding **any security** of or interest.
- Is **Indebted in excess** of Rs. 5,00,000, or
- has given a **guarantee or provided any security** in connection with the indebtedness of any third person, in excess of Rs. 1,00,000.
- A Relative may hold security or interest in the Company of Face Value not exceeding Rs. 1,00,000. (No disqualification if corrective action taken within 60 days in case of subsequent acquisition)

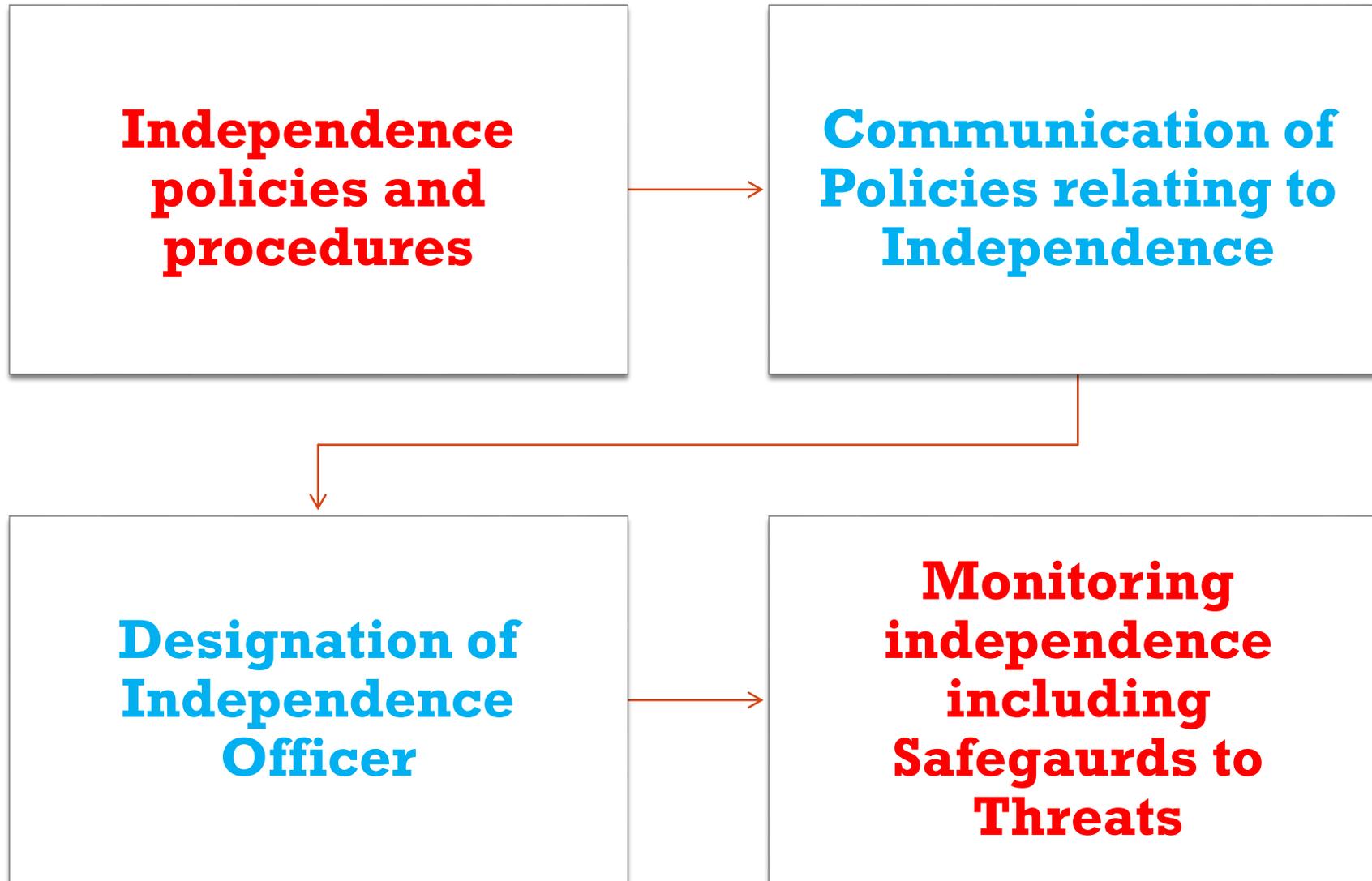
Not to Render Certain Services [Sec.144]



Even if approved by Board, Auditor shall not provide the following Services **Directly or Indirectly**:

- Accounting and Book Keeping Services,
- Internal Audit,
- Design and Implementation of any Financial Information System,
- Actuarial Services,
- Investment Advisory Services,
- Investment Banking Services,
- Rendering of Outsourced Financial Services,
- **Management Services,**
- **Any other kind of Services as may be prescribed.**

Compliance Review of General Controls - Independence



Compliance Review - General Controls



**Maintenance
Skills**

of

- CPE Requirements, Inhouse Discussion, etc.,

**Outside
consultation**

- Experts for Consultation, Use of SA 620, Documenting Differences

**Staff supervision
and Development**

- Orientation & Training, Monitoring Performance & Team Coordination

**Office
Administration**

- Review of Work and Guidance, Communication Aspects etc.,

Staff Supervision:



Assigning progressive work experience to improve abilities of trainees

Designing a study plan to ensure that trainees are fully prepared to take examinations

Ensuring application of practical techniques in the work

Ensuring in-house theoretical training is integrated with practical work experience

Ensuring development of personal and managerial skills through supervision and client contact

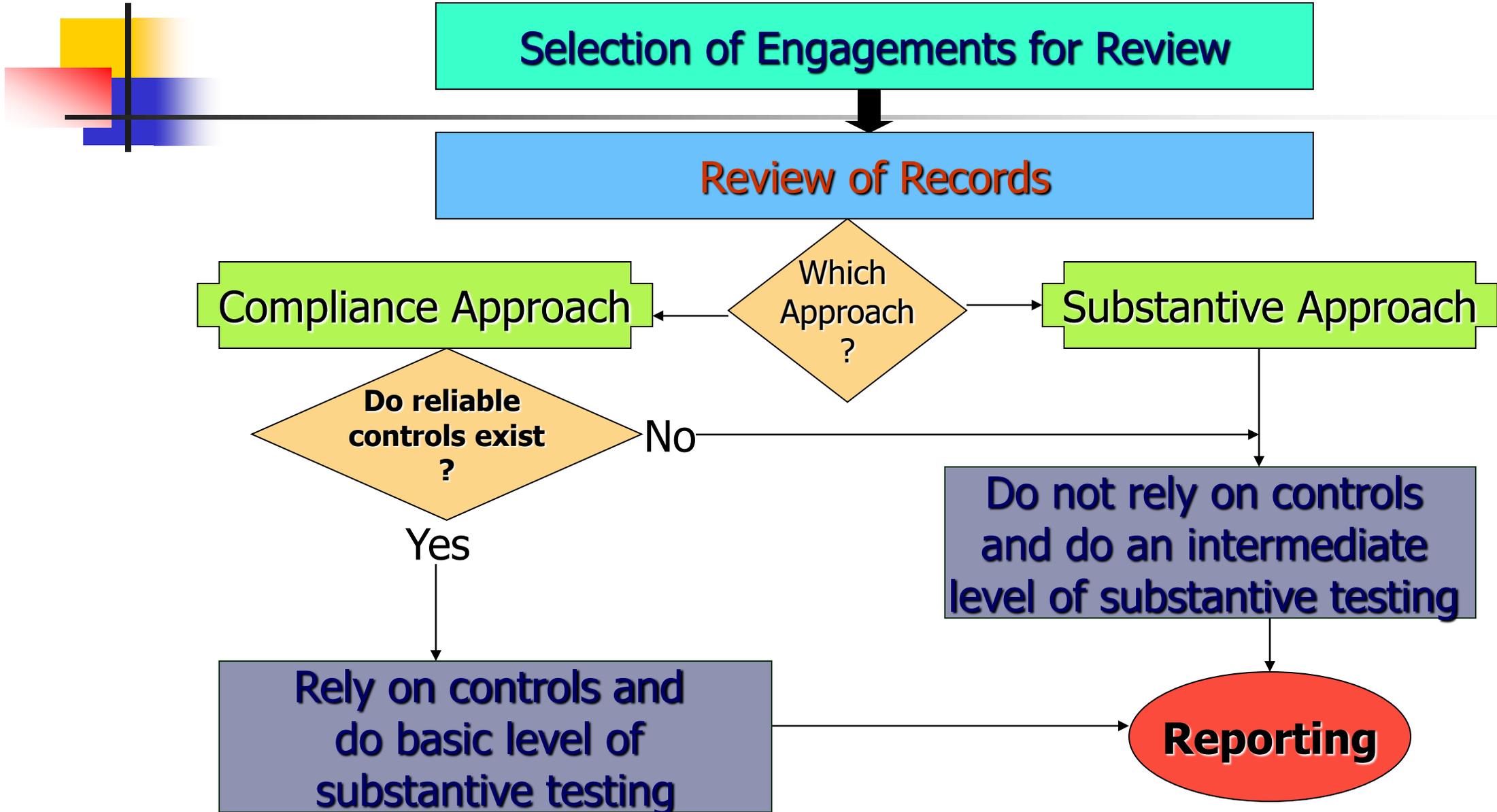
Ensuring that professional attitude and ethical behaviour is developed



Evaluation of General Controls



Procedure





To Decide the Effectiveness

**Review of
Controls**

**Compliance
Approach**

**Substantive
Approach**

Specific Controls – Six Key Controls



Audit Record Administration

Review and Evaluation of System of Internal Controls

Substantive Tests

Financial Statement Presentation

Audit Conclusion and

Audit Report



- **Substantive Testing**

Substantive Testing - 1



- Appointment of auditor

Terms of engagement

Accounting records available

Composition of management

Book-keepers & authorized signatories

Memorandum/Articles, Prospectus, Partnership Deed

Substantive Testing - 2



■ Understand the client's business

■ Understand the controls environment

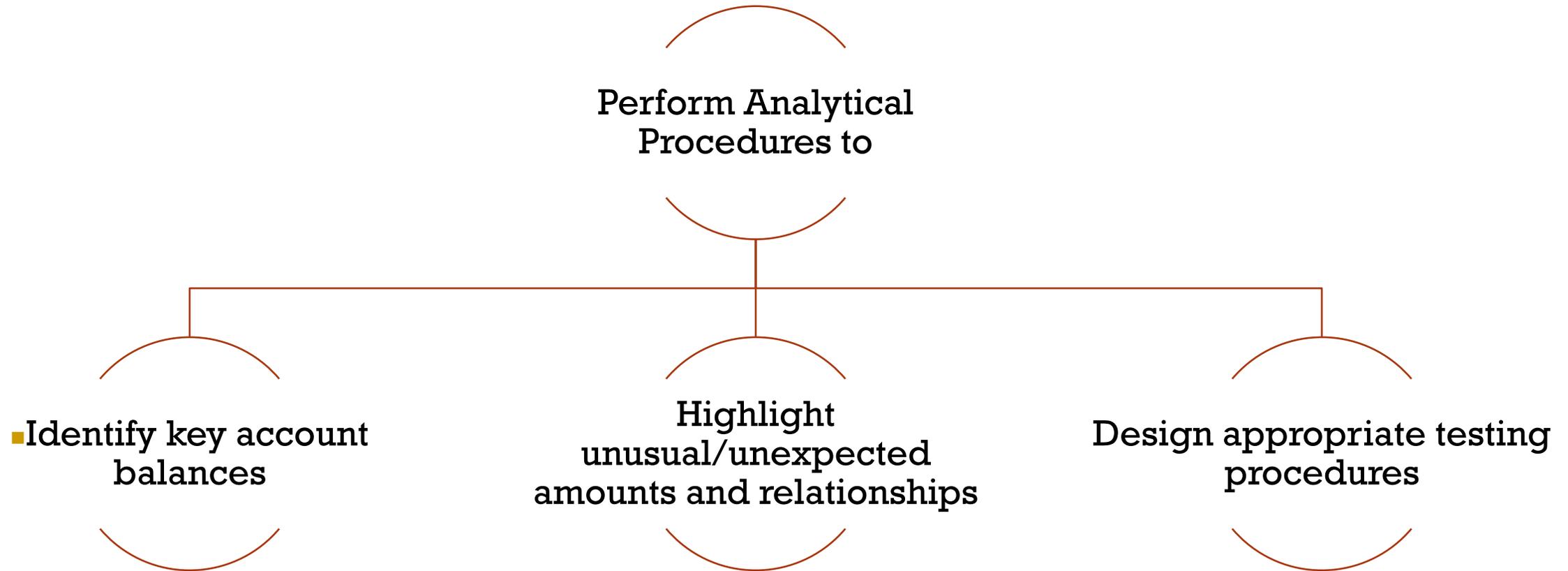
■ Understand the accounting systems

■ Past financial statements & Reports of internal/statutory auditors

■ Evaluate audit risk using professional judgment

■ Design procedures to mitigate risk

Substantive Testing - 3



Substantive Testing - 4



Determine materiality estimate for the audit engagement



Plan for account balances to be tested and sampling methodology



Selection of samples



Perform controls testing and conclude on controls reliability



Communicate control weaknesses to management

Substantive Testing - 5



Perform substantive analytical testing



Perform substantive tests of detail



Ensure prevalence of fundamental accounting assumptions – consistency, going concern, accrual accounting



Examine and report changes in accounting policies and their impact



Branch audit reports – qualifications, scope limit reservations

Substantive Testing - 6



Working papers (WPs) to have adequate audit evidence for assertions made in financial statements



WPs to agree with books of account, financials and are cross-referenced



Perform financial statements review



Prepare audit summary memorandum



Review assistants' work

Substantive Testing - 7



Ensure updation of Audit documentation file



Review individual and aggregate effect of unadjusted errors



Check compliance with legal and regulatory requirements



Subsequent Events Review

Substantive Testing - 8



- Final discussion points with the Client

- Draft audit opinion

- Management Representations

- Compare budgeted hours to actuals and analyze variances

- Debriefing meetings with client/staff

- Complete staff evaluation

- Start next year's planning

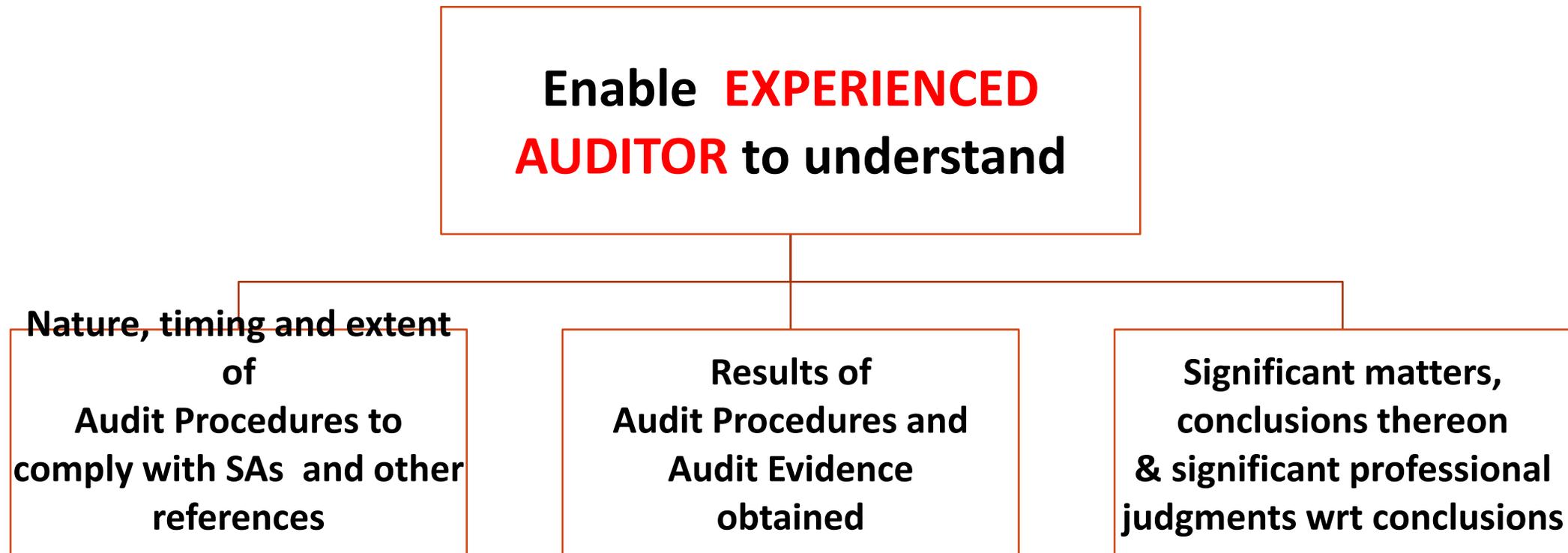


- Documentation of procedures performed by PU is of critical importance

Documentation of the Audit Procedures Performed & Audit Evidence Obtained



Auditor shall prepare audit documentation that is sufficient to **enable an Experienced Auditor**, having no previous connection with the audit to understand





Meaning of the term “Experienced Auditor”

An individual (whether internal or external to firm) having practical audit experience, and a reasonable understanding of:

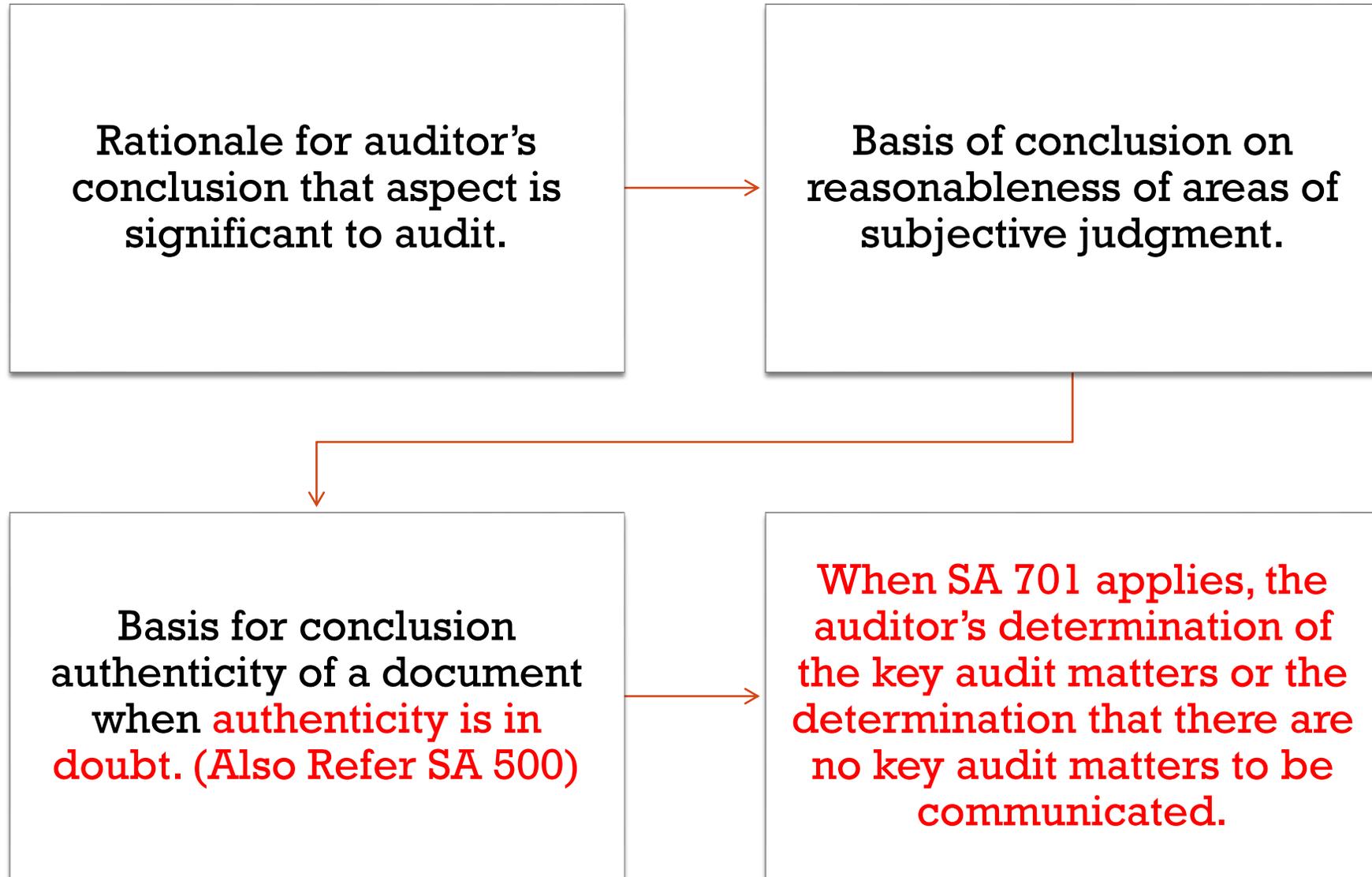
- Audit processes
- SAs and applicable requirements
- Business environment
- Auditing and financial reporting issues

Form, Content and Extent of Documentation shall depend on

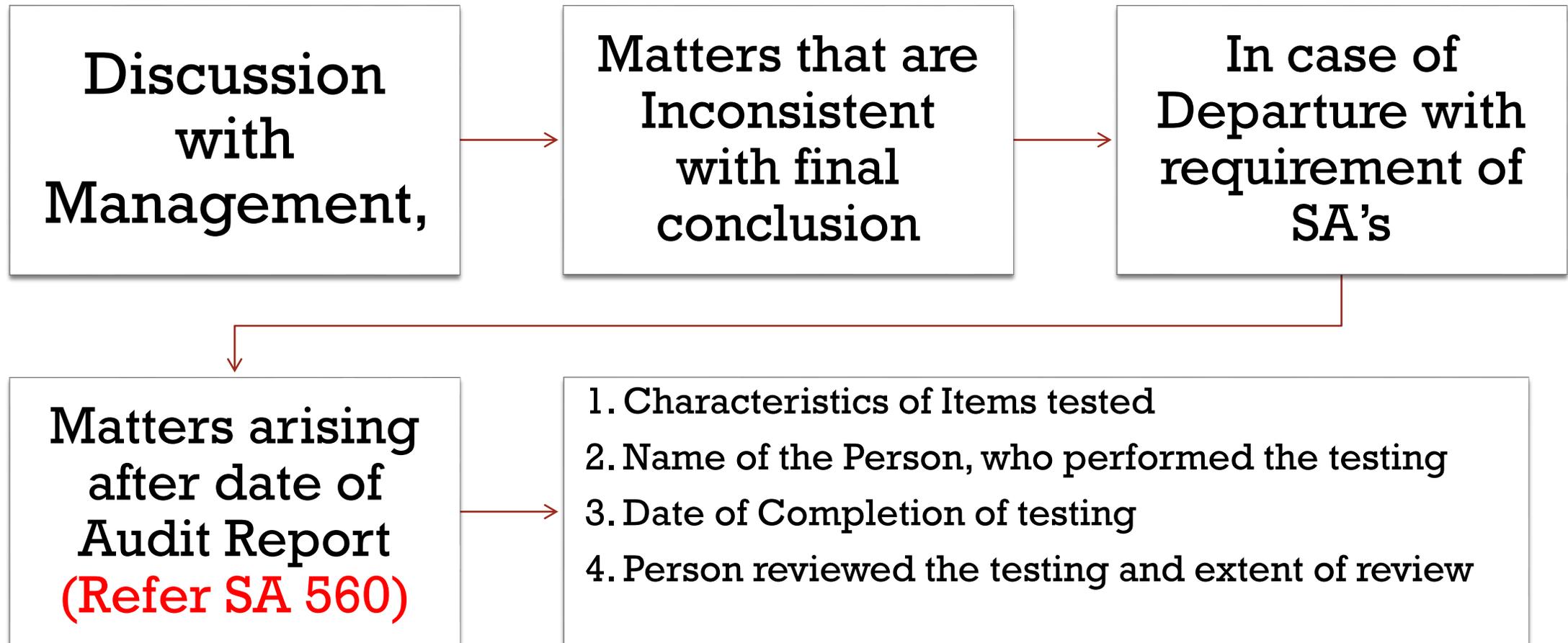


- Size, complexity of the entity
- Identified risk of Material Misstatement
- Nature of audit procedures Performed
- Significance of audit evidence
- Audit methodology, tools used
- Nature, extent of identified exceptions during audit

Significant Matters that requires Documentation



Specific Aspects for Documentation





Specific Aspects in case of Smaller Entities

Audit Documentation for Audit of Smaller Entity

Generally less extensive than that for the audit of a larger entity.

No Documentation requirement for Team Discussions or Supervision

But “Experienced Auditor” condition still applicable

Meaning of Smaller Entity - As per SA 200



Possessing Qualitative Characteristics such as

Concentration of ownership & Management

in a small number of individuals (either natural person or another enterprise that owns the entity)

&

Having One or more of the following characteristics:

- (i) Straightforward or uncomplicated transactions;
- (ii) Simple record-keeping;
- (iii) Few lines of business and few products within business lines;
- (iv) Few internal controls;
- (v) Few levels of management with responsibility for a broad range of controls; or
- (vi) Few personnel, many having a wide range of duties

Some Observations



While the PU has documented policies for independence, there was no evidence on record to show that the said policies or the related quality controls were implemented.

The engagement files examined also contained no evidence that any engagement specific procedures were followed to ensure that the engagement teams were independent of the client.

Amendment to SQC 1 - Retention Period for Engagement Documentation (Working Papers)

The Council of the Institute of Chartered Accountants of India, at its 289th meeting held on August 19, 2009 at New Delhi, pursuant to the provisions of Rule 12 of the Chartered Accountants (Procedures of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007, has decided to amend paragraph 83 of the SQC 1 as follows:

: “83. The needs of the firm for retention

..... In the specific case of audit engagements, the retention period ordinarily is no shorter than seven years from the date of the auditor’s report, or, if later, the date of the group auditor’s report.” (emphasis added)

Some Observations



The PU does not have a practice of obtaining engagement letters as required under SA 210, Agreeing the Terms of Audit Engagement.

Some Observations



It was observed during examination of engagement files that the staff deployed lacked industry expertise and was, in general, inexperienced.

The PU does not have a system of supporting and encouraging its resources to undergo relevant professional education necessary to execute audits of entities in specialised industries. Moreover, there was no evidence in the working papers prepared by articled assistants of any review performed by a senior resource.

Some Observations



During review of one of the audit files it was found that the entity's current liabilities were in excess of its current assets by several multiples, the entity had made cash losses during the last three years and its accumulated losses were five times its share capital.

In spite of this, there was no evidence in the audit file of the engagement team's evaluation of the management's assessment of going concern in accordance with SA 570, Going Concern, while the financial statements were prepared on a going concern basis.



Thank You
Learned audience for
patient hearing

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