

## ETHICS AND TERMS OF AUDIT ENGAGEMENT

### MEANING

moral principles which govern a person's behaviour or his conducting of an activity

### FUNDAMENTAL PRINCIPLES

INTEGRITY	<ul style="list-style-type: none"> <li>Accountant to be <u>straightforward and honest</u></li> <li>implies <u>fair dealing and truthfulness</u></li> <li><u>not knowingly</u> be associated where the accountant believes that the <u>information contains a materially false or misleading statement</u></li> </ul>
OBJECTIVITY	Not to compromise professional judgment because of <u>bias, conflict of interest or undue influence</u>
PROFESSIONAL COMPETENCE AND DUE CARE	<ul style="list-style-type: none"> <li>Ensure that a client receives <u>competent professional service, based on current technical and professional standards and relevant legislation</u>; and</li> <li><u>Act diligently</u> and in accordance with applicable standards</li> </ul>
CONFIDENTIALITY	<ul style="list-style-type: none"> <li>accountant to respect the <u>confidentiality of information acquired as a result of professional or business relationships</u>.</li> <li>However, such confidential information may be disclosed, for example, when it is <u>required by law</u></li> </ul>
PROFESSIONAL BEHAVIOUR	<ul style="list-style-type: none"> <li>It requires an accountant to comply with <u>relevant laws and regulations</u> and</li> <li>avoid any <u>conduct that the accountant knows or should know might discredit the profession</u>.</li> </ul>

### PROFESSIONAL SKEPTICISM

- Attitude that includes a
  - questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.
- Maintaining professional skepticism throughout the audit is necessary if the auditor is to reduce the risks of:
  - Overlooking unusual circumstances, over generalising when drawing conclusions from audit observations and using inappropriate assumptions in determining the nature, timing, and extent of the audit procedures and evaluating the results thereof
- **Example of Professional skepticism**
  - Audit evidence that contradicts other audit evidence obtained, information that brings into question the reliability of documents, fraud indicator conditions

**INDEPENDENCE**

**MEANING**

implies that the **judgement of a person is not subordinate** to the wishes or direction of another person

**INDEPENDENCE OF MIND**

the state of mind that **permits the provision of an opinion without being affected by influences**

**INDEPENDENCE OF APPEARANCE**

avoidance of facts and circumstances that are so significant that a reasonable and informed third party would reasonably conclude **firms or a member objectivity is compromised**

**THREATS TO INDEPENDENCE**

<b>Self-interest threats</b>	When an auditing firm, its partner or associate could benefit from a financial interest in an audit client EXAMPLE -Direct financial interest with client, loan or guarantee to/from client, <b>undue dependence</b> on a client's fees, close business relationship
<b>Self-review threats</b>	It occurs when during a review of any judgement or conclusion reached in a previous audit or non-audit engagement EXAMPLE - Auditor having recently been a director, auditors perform services which are subject matters of audit
<b>Advocacy threats</b>	It occurs when the auditor promotes, a client's opinion to a point where people may believe that <b>objectivity is getting compromised</b> , EXAMPLE - Auditor deals with shares or securities of company, becomes <b>client's advocate</b> in litigation
<b>Familiarity threats</b>	When auditors form relationships with the client where they end up being too <b>sympathetic</b> to the client's interests EXAMPLE - <b>Close relative</b> of the auditor, long association between partner and auditor, <b>acceptance of significant gifts</b> or hospitality
<b>Intimidation threats</b>	It occurs when <u>auditors are deterred from acting objectively</u> EXAMPLE - <b>threat of replacement over disagreements</b> , <b>pressure to reduce audit fees</b> , being threatened with litigation.

**SAFEGUARDS TO INDEPENDENCE**

Before taking on any work, an auditor must **conscientiously consider whether it involves threats to his independence**. -----> When such threats exist, the auditor should either desist from the task or eliminate the threat or at the very least, put in place safeguards which reduce the threats to an acceptable level. ----> If the auditor is unable to fully implement credible and adequate safeguards, then he must not accept the work.

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

**OBJECTIVE -**

establish a system of quality control designed to provide it with reasonable assurance that the firm and its **personnel comply with professional standards and regulatory and legal requirements and the report issued is appropriate in circumstances**

**ELEMENTS OF QUALITY CONTROL**

<b>LEADERSHIP RESPONSIBILITIES FOR QUALITY WITHIN THE FIRM</b>	Such policies and procedures should require the <b>firm's CEO or the MD to assume ultimate responsibility</b> for the firm's system of quality control. Further, persons assigned operational responsibilities for the firm's quality control system should have <b>sufficient and appropriate experience, ability and the necessary authority to assume that responsibility</b>
<b>ETHICAL REQUIREMENTS</b>	The firm should establish policies and procedures designed to ensure that the firm and its personnel comply with relevant ethical requirements contained in the Code of ethics issued by ICAI. Also, <b>Observance of "Independence"</b> in all engagements is the basic requirement.
<b>ACCEPTANCE AND CONTINUANCE OF CLIENT RELATIONSHIPS AND SPECIFIC ENGAGEMENTS</b>	A firm before accepting an engagement should acquire vital information about the client. Such an information should help firm to decide about: - <ul style="list-style-type: none"> <li>• <b>Integrity of Client</b></li> <li>• <b>Competence</b> (including capabilities, time and resources) to perform engagement</li> <li>• <b>Compliance with ethical requirements</b></li> </ul>
<b>HUMAN RESOURCES</b>	Firm should establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the <b>capabilities, competence, and commitment to ethical principles</b> to perform the engagement
<b>ENGAGEMENT PERFORMANCE</b>	Consultation should take place in <b>difficult or contentious matters pertaining to an engagement</b> <b>Significant judgments made in an engagement</b> should be reviewed by an engagement quality control reviewer The report should only be issued after <b>resolution of such differences of opinion</b> Establish policies and procedures to complete the assembly of final engagement files on a <b>timely basis after the engagement reports have been finalized</b>
<b>MONITORING</b>	The firm should ensure that policies and procedures relating to the <b>system of quality control are relevant, adequate, operating effectively and complied with in practice</b>

**SA 220 - QUALITY CONTROL FOR AN AUDIT OF FINANCIAL STATEMENTS**

**OBJECTIVE -**

Ensure that audit complies with **professional standards and regulatory and legal requirements** and the auditor's report issued is **appropriate** in the circumstances

**ELEMENTS OF QUALITY CONTROL**

<p><b>LEADERSHIP RESPONSIBILITIES FOR QUALITY ON AUDITS</b></p>	<p>The actions of the engagement partner and engagement team, <b>emphasise</b> the importance to <b>audit quality</b> of: -</p> <ul style="list-style-type: none"> <li>- Performing work that complies with <b>professional standards and regulatory and legal requirements</b>;</li> <li>- Complying with the <b>firm's quality control policies and procedures</b></li> <li>- Issuing <b>auditor's reports</b> that are appropriate in the circumstances;</li> <li>- The engagement team's <b>ability to raise concerns without fear of reprisals</b>.</li> <li>- The fact that <b>quality is essential</b> in performing audit engagements.</li> </ul>
<p><b>RELEVANT ETHICAL REQUIREMENTS</b></p>	<ul style="list-style-type: none"> <li>- <b>Identifying a threat to independence</b> that <b>safeguards may not be able to eliminate</b> or reduce to an acceptable level and reporting by engagement partner to the relevant persons within the firm to determine appropriate action, [<b>eliminating the threat, or withdrawing from the audit engagement</b>]</li> </ul>
<p><b>ACCEPTANCE AND CONTINUANCE OF CLIENT RELATIONSHIPS AND AUDIT ENGAGEMENTS</b></p>	<p>Following information assist engagement partner like</p> <ul style="list-style-type: none"> <li>- <b>integrity</b> of principal owners,</li> <li>- <b>competence</b> of engagement team and</li> <li>- <b>consideration of necessary capabilities</b> including time and resources,</li> <li>- compliance with <b>relevant ethical requirements</b> and</li> <li>- <b>significant matters</b> arisen during current or previous audit engagement and their implications</li> </ul>
<p><b>ASSIGNMENT OF ENGAGEMENT TEAMS</b></p>	<p>Engagement team must have appropriate <b>competence and capabilities to perform the engagement in accordance with professional standards and regulatory and legal requirement</b></p>
<p><b>ENGAGEMENT PERFORMANCE</b></p>	<p>For audits of FS of listed entities, and those other audit engagements, if any, for which the firm has determined that an <b>engagement quality control review [EQCR]</b> is required, the engagement partner shall determine that an EQCRer <b>has been appointed</b>, <b>discuss significant matters arising during the audit engagement</b> with the EQCRer and <b>not date the auditor's report</b> until the completion of the EQCR.</p>
<p><b>MONITORING</b></p>	<p>The engagement partner should ensure that policies and procedures relating to the <b>system of quality control are relevant, adequate, operating effectively and complied with in practice</b></p>

SA 210 - AGREEING THE TERMS OF AUDIT ENGAGEMENTS

**OBJECTIVE -**

- (A) Establishing whether the preconditions for an audit are present
- (B) Confirming that there is a common understanding between the auditor and management and, where appropriate, those charged with governance of the terms of the audit engagement

**Preconditions for an audit --->**

- (a) Determine whether the financial reporting framework is acceptable and
- (b) Obtain the agreement of management that it acknowledges and understands its responsibility:
  - For the preparation of the FS in accordance with the applicable FRF
  - For such internal control as management considers necessary to enable the preparation of FS and
  - To provide the auditor with:
    - Access to all information of which management is aware that is relevant to the preparation of the FS
    - Additional information that the auditor may request from management for the purpose of the audit; and
    - Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

**Content of engagement letter --->**

- The objective and scope of the audit of the FS
- The responsibilities of the auditor
- The responsibilities of management
- Identification of the applicable FRF for the preparation of the FS and
- Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

If law or regulation prescribes in sufficient detail the terms of the audit engagement, the auditor need not record them in a written agreement

**RECURRING AUDIT**

The auditor does not send a new audit engagement letter each period. However, the following factors may make it appropriate to revise the terms of the audit engagement:

- Any indication that the entity misunderstands the objective and scope of the audit.
- Any revised or special terms of the audit engagement.
- A recent change of senior management.
- A significant change in ownership.
- A significant change in nature or size of the entity's business.
- A change in legal or regulatory requirements.
- A change in the FRF adopted in the preparation of the FS.
- A change in other reporting requirements

**IF THE MANAGEMENT REQUEST FOR CHANGE IN TERMS OF ENGAGEMENT**

**Change results from -**

- a **change in circumstances** affecting the need for the service,
- a **misunderstanding** as to the nature of an audit as originally requested or
- a **restriction on the scope of the audit engagement**, whether imposed by management or caused by other circumstances.

If the auditor is unable to agree to a change of the terms of the audit engagement -

- (a) **Withdraw from the audit engagement** where possible under applicable law or regulation
- (b) **Determine whether there is any obligation to report** the circumstances to other parties or TCWG

**Change in the audit engagement -**

to an engagement that conveys a **lower level of assurance**

The auditor shall determine whether there is **reasonable justification** for doing so. ---→  
If yes, the auditor shall ensure **work required to be performed and the report to be issued** would be those appropriate to the revised engagement ---→

In order to avoid confusing the reader, the report on the related service would not include reference to:

- (a) The **original audit engagement** or
- (b) Any **procedures that may have been performed in the original audit engagement**, except in case of agreed-upon procedures

**THE AUDITOR SHALL NOT ACCEPT THE ENGAGEMENT**

If the management or TCWG impose a limitation on the scope of the auditor's work and limitation will result in the auditor **disclaiming an opinion on the financial statements**

If **FRF is not acceptable** or if the **engagement agreement** has not been obtained.

If **preconditions to audit** are not present

**You won't always be motivated  
So, you must learn to be disciplined**