

# Chapter - 11 " Ethics and Terms of Audit Engagement "

- Topics Covered:
- (1) Ethics and Fundamental Principles
  - (2) Independence, Threats to Independence and Safeguards
  - (3) Professional Skepticism
  - (4) Agreeing the Terms of Audit Engagement (SA 210)

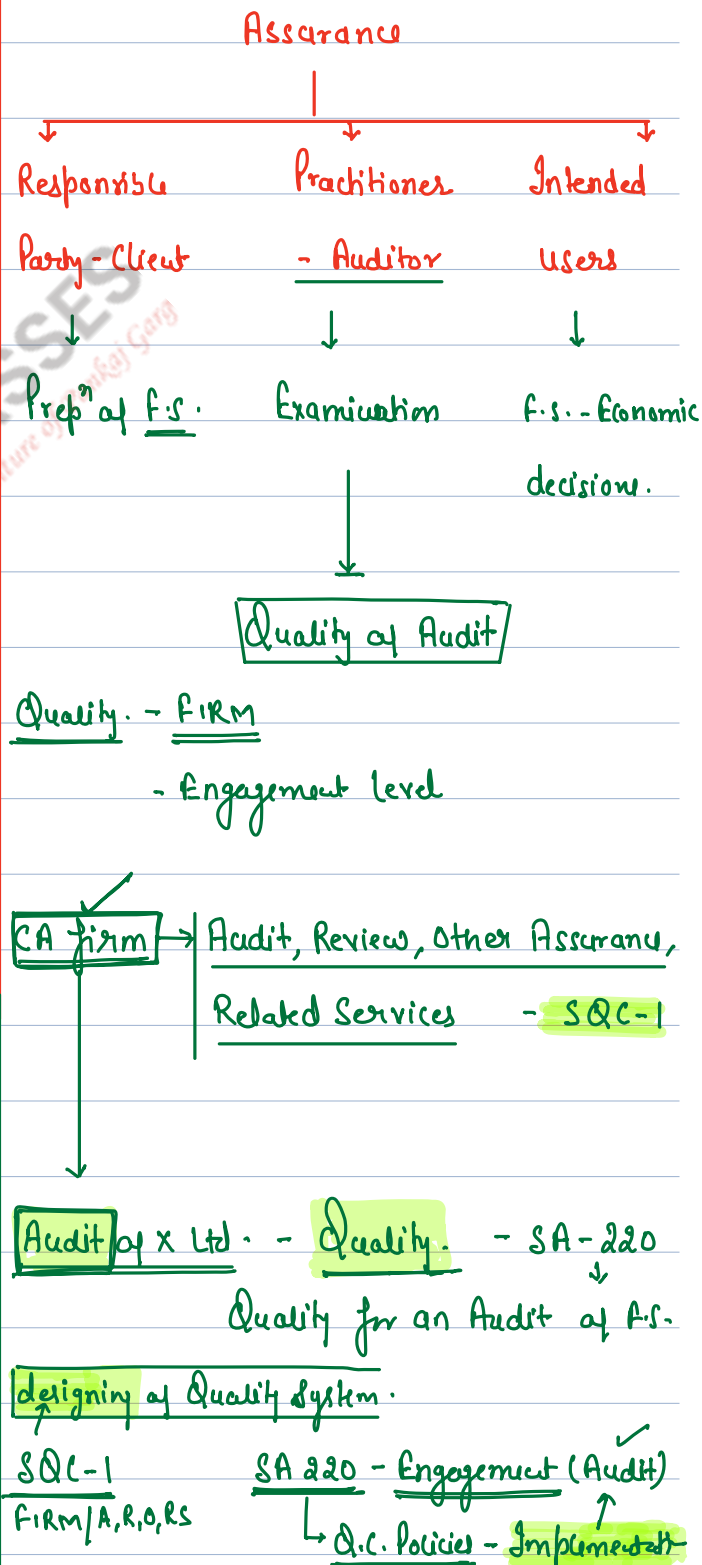
## (5) Audit Quality:

(A) SQC-1 "Quality Controls for Firms that performs audit and review of Historical Financial Information and Other Assurance and Related Services Engagements"

### (i) Purpose of SQC-1:

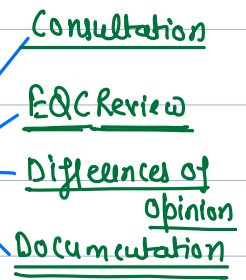
SQC-1 is a parent standard that requires firms to establish a system of Quality Control designed to provide a reasonable assurance that:

- (EP and others)
- (a) Firm and its personnel comply with the Professional Standards, legal and Regulatory Requirements; and
  - (b) Appropriate Reports are being issued in the circumstances.



(ii) Elements of System of Q.C.:

- ✓(A) Leadership Responsibilities
- ✓(B) Ethical Requirements including Independence
- ✓(C) Acceptance and Continuance of Client Relationship and Specific Engagements.
- ✓(D) Human Resources
- ✓(E) Engagement Performance
- (F) Monitoring



(A) Leadership Responsibilities:

- Firm should establish policies and procedures designed to - promote an Internal culture based on recognition that quality is essential.
- Firm CEO/Managing Partner shall assume overall responsibility of Q.C. System.
- Persons assigned with operational Responsibility should have sufficient experience, ability and authority to assume that responsibility.

(B) Ethical Requirements:

Firm should establish policies and procedures designed to - provide it with reasonable assurance that firm and its Personnel comply with relevant Ethical Requirement.



Fundamental Principles as per Code of Ethics:

- (a) Integrity
- (b) Objectivity
- (c) Professional Competence and Due Care.
- (d) Confidentiality
- (e) Professional Behaviour.

## Policies and Procedures w.r.t. Independence:

Firm should establish policies and procedures to ensure that the firm, its personnel and others maintain Independence.

Such policies and procedures enable the firm to:

- (a) Communicate independence requirements to personnel.
- (b) Identify and evaluate the circumstances that create threats to independence.
- (c) Take appropriate action to eliminate the threats or reduce threats to acceptable level.

Note: If considered appropriate in the circumstances, firm should withdraw from the engagement.

SQC-1 also requires the following:

- (i) All breaches of Independence should be promptly notified to firm for appropriate action.
- (ii) Firm should obtain Annual written Confirmation from all firm personnel as to compliance with independence requirements.

## (c) Acceptance and Continuance of Client Relationship and Specific Engagements:

- Firms should establish policies and procedures to assure that clients are accepted / continued only when:

- (a) Client integrity has been considered;
- (b) Competency and capability required to perform an engagement has been evaluated; and
- (c) Compliance to ethical requirements has been ensured.

← Accepting engagement with client.

→ Continue an Existing Engagement with client.

← Accepting new Engagement with Existing client.

- If there is any conflict of interest between the firm and the client, it should be properly resolved before accepting the Engagement.
- If after accepting the Engagement, firm obtain any information that would have caused it to decline the engagement, firm should consider:
  - (a) Professional and legal responsibilities to report to the person who made the appointment or to regulatory authorities; and
  - (b) Possibility of withdrawal from Engagement.

### Considerations as to Integrity of clients: (Noting - H.W.-)

(D) Human Resources: Firm should establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the capabilities, competency and commitment to Ethical Principles to perform its engagement;

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in compliance with professional standards, legal and regulatory requirements and appropriate reports are being issued in the circumstances.

Such policies and procedures shall address the following:

- (a) Staff Recruitment
- (b) Career development;
- (c) Capabilities, competencies
- (d) Promotion;
- (e) Compensation
- (f) Performance Evaluation
- (g) Estimation of Personnel needs. etc.

## (E) Engagement Performance:

- (i) Consultation: - Consultation should take place on difficult matters.
- " may be with the persons having appropriate knowledge and Experience. (within the firm or outside the firm).
  - Outside consultation may be required if firm is not having appropriate internal resources.

(ii) Engagement Quality Control Review: Significant judgements made in an engagement should be reviewed by EQC Reviewer for taking an Objective View before the report is issued.

Note: (a) EQCR is mandatory for audit of F.S. of listed Entities.

(b) Extent of EQCR depends upon complexity of engagement.

(iii) Difference of opinion: among Engagement team members, with consultants, with EQC Reviewer.

Ensure that reports are to be issued only after resolution of differences.

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(iv) Documentation: Firm should establish policies and procedures designed (Working Papers) for ensuring that final engagement file should be assembled on a timely basis.

(i.e. within 60 days after the date of audit report)

- Ensure Confidentiality, safe custody, integrity and retrievability of documents.
- Ownership: Audit documentation is property of auditor. Extracts of audit documentation may be made

available to client at discretion of auditor.

- Retention Period: 7 years from date of audit report.

(F) Monitoring: Ongoing consideration and evaluation of firm system of Quality Control



to ensure their relevancy,  
adequacy,  
operating effectiveness; and  
Compliance.

