

1. MOON Limited replaced its statutory auditor for the financial year 2023-24. During the course of audit, the new auditor found a credit item of Rs 5 Million. On enquiry the company explained him that it is, a very old credits balance. The creditor had either approached for the payment nor he is traceable. Under the circumstances, no confirmation of the credit balance is available.

Auditor's duty in case of non-availability of External Confirmation

- ISA 505 "External Confirmations" provides that if the auditor has determined that a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence, and alternative audit procedures will not provide that audit evidence the auditor requires, he should determine the implications for the audit and the auditor's opinion in accordance with ISA 705

- In the present case, the identities of trade payables are not traceable to confirm the credit balance as appearing in the financial statements of the company. It is also not a case of pending litigation. It might be a case that an income of Rs. 5 Million had been hidden in the previous year/

- The statutory should examine the validity of the credit balance as appeared in the company's financial statements. He should obtain sufficient evidence in support of the balance. He should apply alternative audit procedures to get documentary proof for the transactions and should not rely entirely on the management representation. Finally he should include matter by the way of the qualification in his audit report to the members.

2. As an auditor how would you deal with the following: When the audit team visited the client to perform substantive audit of debtor, the client produced ledger account of customers and confirmations for the top 10 customers. One of the debtors was more than 5 years old, but it had confirmed his balance.

Auditor's duties in case of doubt over reliability of external confirmations:

- ISA 505 "External Confirmations" deal with the auditor's use of external confirmation procedures to obtain audit evidence. External confirmation is the process of obtaining and evaluating audit evidence through a direct communication from a third party in response to a request for information about a particular item affecting assertions made by the management in the financial statements.

As per ISA 505, the auditor is required to maintain a control over the process of selecting those to whom a request will be sent out, the preparation and sending of confirmation requests and responses to those requests. This is because there have been several cases of clients presenting forged confirmation to auditors when such control was absent.

- In the present case, one of the debtors of more than 5 years old had confirmed his balance. The auditor should enquire into the debtor whose dues are outstanding for 5 years or more about his financial abilities and why he has not paid, reasons behind the same, and if found adverse, the client should be advised to provide for "provisions for bad debts" and also to confirm that it is not a forged confirmation.

3. During the course of audit of Star Limited the auditor received some of the confirmation of the balances of trade payables outstanding in the balance sheet through external confirmation by negative confirmation request. In the list of trade payables, there are number of trade payables of small balances except one, old outstanding of 15 Million, of whom, no confirmation on the credit balance received. Comment with respect to International Standard of Auditing

Response to negative confirmation request:

- As per ISA 505, "External Confirmation", Negative Confirmation is a request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.
- Negative confirmations provide less persuasive audit evidence than positive confirmations. In case of negative confirmation request, confirming parties may be more likely to respond indicating their disagreement with a confirmation request when the information in the request is not in their favour, and less likely to respond otherwise.
- In the instant case, the auditor sent the negative confirmation requesting the trade payables having outstanding balances in the balance sheet while doing of audit Star Limited. One of the old outstanding of 15 Million has not sent the confirmation on the credit balance.
- Non-response for negative. Confirmation request does not mean that there is some misstatement as negative confirmation request itself is to respond to the auditor only if the confirming party disagrees with the information provided in the request

In the present case, considering the materiality of the account balance, the auditor may examine subsequent cash disbursements or correspondence from third parties, and other records, such as good received notes

4. A Company's net worth is eroded and trade payables are unpaid due to liquidity constraints. The management represents to the unsecured loan to meet the liquidity constraints and that negotiations are underway to secure large export orders.

It is not a mitigating factor, and hence modify opinion.

5. As a statutory auditor of the company, comment on the following: While verifying the employee records of a company, it was found that a major portion of the labor employed was child labor . On questioning the management, the auditor was told that it was outside his scope of the financial audit and to look into compliance with other laws.

Auditor's responsibility for consideration of other laws:

- ISA 250 "Consideration of laws and regulation in an Audit of Financial statements" requires the auditor to obtain sufficient appropriate audit evidence regarding the compliance with the provisions of those laws and regulations generally recognized to have a direct impact on the determination of material amounts and disclosures in the financial statements including tax and labour laws.
- For other laws, the auditor's responsibility is limited to undertake specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial statements.
- Non-compliance with other laws and regulations may result in fines, litigation or other consequences for the entity, the costs of which may need to be provided for.
- In the instant case, major portion of the labour employed was child labour.

CONCLUSION: Auditor should enclose the disclosure of the above fact and provision of the cost of fines, litigation or other consequences. In case auditor concludes that non-compliance may have a material effect on financial statements, he should modify his opinion accordingly.