Project Audit Manual

Foreign Aided Projects Audit Directorate






Office of the Comptroller & Auditor General of Bangladesh

Project Audit Manual

Foreign Aided Projects Audit Directorate (FAPAD)

Office of the Comptroller and Auditor General of Bangladesh

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Foreword

Audit is an indispensable part of sound financial management, especially, in the public sector as it provides assurance to intended users not only on integrity of the financial statements but also on proper use of resources placed at the hand of the responsible party namely executive agencies. The constitution of Bangladesh entrusts Comptroller and Auditor General (CAG) with the responsibility of auditing. The prime user of the audit report prepared by CAG under constitutional mandate is the parliament. CAG fulfils this solemn constitutional mandate through different audit directorates.

In addition to the mandate referred above, Office of the Comptroller and Auditor General (OCAG) also conducts audit of special purpose financial statements for government projects funded by development partners. For obvious reason, development partners desire an independent assurance on the financial statements and on appropriate use of funds of these projects. Due to the unique mandate provided by the constitution in the field of public sector auditing, development partners place their full confidence on CAG for audit of foreign aided projects.

Foreign Aided Projects Audit Directorate (FAPAD) was established in 1982 as a specialised directorate to conduct audit of foreign aided projects. Any audit of Project financial statements conducted by FAPAD with regard to the reporting requirements of development partners is an additional responsibility and completely separate from the audit required to fulfil the CAG's constitutional obligation.

Since the development partners expect the audit of Project financial statements to be conducted in line with international best practices such as International Standards of Supreme Audit Institutions (ISSAI) issued by the International Organization of Supreme Audit Institutions (INTOSAI) and other related standards. I am pleased to see that the previous Project Audit Manual published in 2007 has been updated reflecting all required changes.

I expect that FAPAD personnel shall extensively follow this manual in conducting audit of financial statements of foreign aided projects in Bangladesh with a view to enhance the robustness of public financial management.

Date: 15 June 2021

Mohammad Muslim Chowdhury
Comptroller and Auditor General of Bangladesh

Preface

The Foreign Aided Projects Audit Directorate (FAPAD) is a specialised dedicated arm of the OCAG Bangladesh to provide independent assurance to Development Partners on the Project Financial Statements and use of project resources.

The last version of the Project Audit Manual (PAM) used by the Foreign Aided Projects Audit Directorate (FAPAD) of the Office of the Comptroller and Auditor General of Bangladesh (OCAG) was published in 2007.

Since then substantial changes took place in various auditing standards as well as reporting requirements of various development partners. As a result, there was a need for updating the existing Project Audit Manual for FAPAD in conducting audit of Project Financial Statements. With this objective, Asian Development Bank (ADB) has taken a project to update the existing "Project Audit Manual" of FAPAD. I am delighted that the Project supported by ADB has successfully completed the task of updating the "Project Audit Manual".

The Project Audit Manual has been developed to provide guidelines to audit engagement teams of FAPAD while conducting audit of Foreign Aided Projects. In this regard, all personnel of FAPAD shall adhere to the requirements of this manual while carrying out audits of Foreign Aided Project financial statements.

The manual is intended to assist in meeting development partner requirements regarding audit of Project financial statements and reporting thereon. These audit requirements are laid out in the relevant financing agreement.

The Manual is developed in accordance with the 'Government Auditing Standards of Bangladesh' (GASB) issued by the Office of the Comptroller and Auditors General (OCAG) of Bangladesh which are based on the International Standards of Supreme Audit Institutions (ISSAIs) issued by International Organization of Supreme Audit Institutions (INTOSAI), existing Audit Manuals of the OCAG and specific audit requirements of various development partners.

The manual has been structured in a manner that allows systematic description of key audit processes along with various annexure to guide detail audit process to be taken by the FAPAD audit engagement teams.

This Manual will be updated periodically or as and when necessary by FAPAD.

I am thankful to the Asian Development Bank (ADB) for funding the Project to update this Manual.

Date: 15 June 2021

Md. Shariful Islam
Director General
Foreign Aided Projects Audit Directorate

List of Abbreviations

ADB	Asian Development Bank
ADP	Annual Development Program
AR	Audit Risk
ASOSAI	Asian Organization of Supreme Audit Institutions
CAG	The Comptroller and Auditor General
CAAT	Computer Assisted Audit Techniques
CR	Control Risk
DAG	Deputy Accountant General
DR	Detection Risk
DP	Development Partners
DG	Director General
EA/IA	Executing/Implementing Agencies
ERD	Economic Relations Division
EQCR	Engagement Quality Control Review
FAM	Financial Audit Manual
FAO	Field Audit Offices
FAP	Foreign Aided Projects
FAPAD	Foreign Aided Projects Audit Directorate
IDB	Islamic Development Bank
IFAC	International Federation of Accountants
IQCC	Internal Quality Control Check
ISSAI	International Standards of Supreme Audit Institutions
IR	Inherent Risk
INTOSAI	International Organization of Supreme Audit Institutions
ISA	International Standard on Auditing
IT	Information Technology
IPSAS	International Public Sector Accounting Standards
JICA	Japan International Co-operation Agency
MOF	Ministry of Finance (MoF)
MUS	Monetary Unit Sampling
PAC	Public Accounts Committee
PMU	Project Management Unit
PIU	Project Implementation Unit
OCAG	Office of the Comptroller and Auditor General
QCC	Quality Control Check
RMM	Risk of Material Misstatement
SAARC	South Asian Association for Regional Cooperation
SAI	Supreme Audit Institutions
USAID	United States Agency for International Development
WB	World Bank

Glossary

Accounting estimate— An approximation of a monetary amount in the absence of a precise means of measurement. This term is used for an amount measured at fair value where there is estimation uncertainty, as well as for other amounts that require estimation.

Accounting records—The records of initial accounting entries and supporting records, such as checks and records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers, journal entries and other adjustments to the financial statements that are not reflected in formal journal entries; and records such as work sheets and spreadsheets supporting cost allocations, computations, reconciliations and disclosures.

Analytical procedures— Evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

Appropriation of funds – An authorization granted by a legislative body to allocate funds for purposes specified by the legislature or similar authority

Applicable financial reporting framework— The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation. The term "fair presentation framework" is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

Application controls in information technology— Application controls can be preventative or detective in nature and are designed to ensure the integrity of the accounting records. Application controls relate to procedures used to initiate, record, process and report transactions or other financial data.

Appropriateness—The measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor's opinion is based.

Arm's length transaction — A transaction conducted on such terms and conditions as between a willing buyer and a willing seller who are unrelated and are acting independently of each other and pursuing their own best interests.

Assertions — Representations by management, explicit or otherwise, that are embodied in the financial statements, as used by the auditor to consider the different types of potential misstatements that may occur. In the context of international standards on auditing assertions are defined as representations by the entity, explicit or otherwise as used by the practitioner to consider the different types of potential misstatements that may occur.

Audit documentation—The record of audit procedures performed, relevant audit evidence obtained, and conclusions the audit or reached (terms such as "working papers" or "work papers" are also sometimes used).

Audit evidence—Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information.

Audit File- One or more folders or other storage media, in physical or electronic form, containing the records that comprise the audit documentation for a specific engagement.

Audit risk—The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.

Audit opinion - The opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Audit sampling (sampling)—The application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population.

Auditor— "Auditor" is used to refer to the person or persons conducting the audit, usually the engagement team leader or other members of the engagement team, or, as applicable, the OCAG/ FAPAD.

Audit mandate – The auditing authority, responsibilities, discretions and duties conferred on a Supreme Audit Institution under the constitution or other lawful authority of a state.

Audited entity– An organization, program, project, activity or function subject to audit.

Comparative financial statements—Comparative information where amounts and other disclosures for the prior period are included for comparison with the financial statements of the current period but, if audited, are referred to in the auditor's opinion. The level of information included in those comparative financial statements is comparable with that of the financial statements of the current period.

Comparative information—The amounts and disclosures included in the financial statements in respect of one or more prior periods in accordance with the applicable financial reporting framework.

Compliance audit – Compliance audit deals with the degree to which the audited entity follows rules, laws and regulation, policies, established codes, or agreed upon terms and conditions etc. Compliance auditing may cover a wide range of subject matters. In general, the purpose of a compliance audit is to provide assurance to intended users about the outcome of the evaluation or measurement of a subject matter against suitable criteria.

Computer-Assisted Audit Techniques—Applications of auditing procedures using the computer as an audit tool.

Control activities—Those policies and procedures that help ensure that management directives are carried out. Control activities are a component of internal control.

Control environment—Includes the governance and management functions and the attitudes, awareness and actions of those charged with governance and management concerning the entity's internal control and its importance in the entity. The control environment is a component of internal control.

Control risk: The risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's internal control.

Corresponding figures—Comparative information where amounts and other disclosures for the prior period are included as an integral part of the current period financial statements, and are intended to be read only in relation to the amounts and other disclosures relating to the current period (referred to as "current period figures").

Date of report (in relation to quality control)—The dates elected by the audit orto date the report.

Date of the financial statements—The date of the end of the latest period covered by the financial statements.

Detection risk—The risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

Engagement Quality Control review—A process designed to provide an objective evaluation, on or before the date of the report, of the significant judgments the engagement team made and the conclusions it reached in formulating the report. The engagement quality control review process is for audits of financial statements of listed entities and those other engagements, if any, for which the firm has determined an engagement quality control review, is required.

Evidence—Information used by the practitioner in arriving at the practitioner's conclusion. Evidence includes both information contained in relevant information systems, if any, and other information. For purposes of the ISAEs:

- Sufficiency of evidence is the measure of the quantity of evidence.
- Appropriateness of evidence is the measure of the quality of evidence.

Exception—A response that indicates a difference between information requested to be confirmed, or contained in the entity's records, and information provided by the confirming party.

External confirmation—Audit evidence obtained as a direct written response to the audit or from a third party (the confirming party), in paper form, or by electronic or other medium.

Financial audit – An independent assessment, resulting in a reasonable assurance opinion, of whether an entity's reported financial condition, results, and use of resources are presented fairly in accordance with the financial reporting framework.

Financial statements—A structured representation of historical financial information, including disclosures, intended to communicate an entity's economic resources or obligations at a point in time, or the changes there in for a period of time, in accordance with a financial reporting framework. The term "financial statements" ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework, but can also refer to a single financial statement. Disclosures comprise explanatory or descriptive information, set out as required, expressly permitted or otherwise all owed by the applicable financial reporting framework, on the face of a financial statement, or in the notes, or incorporated there in by cross-reference.

Fraud—An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.

Fraud risk factors—Events or conditions that indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud.

General IT controls—Policies and procedures that relate to many applications and support the effective functioning of application controls by helping to ensure the continued proper operation of information systems. General IT controls commonly include controls over data center and network operations; system software acquisition, change and maintenance; access security; and application system acquisition, development, and maintenance.

General purpose financial statements—Financial statements prepared in accordance with a general-purpose framework.

Historical financial information—Information expressed in financial terms in relation to a particular entity, derived primarily from that entity's accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

Information system relevant to financial reporting—A component of internal control that includes the financial reporting system, and consists of the procedures and records established to initiate, record, process and report entity transactions (as well as events and conditions) and to maintain accountability for the related assets, liabilities and equity.

Independence Comprises:
Independence of mind—The state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise competency and professional skepticism.

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

Inherent risk: The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.

Internal control—The process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. The term "controls" refers to any aspects of one or more of the components of internal control.

International Financial Reporting Standards—The International Financial Reporting Standards issued by the International Accounting Standards Board.

International Public Sector Accounting Standards- International Public Sector Accounting Standards (IPSASs) promulgated by the International Public Sector Accounting Standards Board.

Key audit matters—Those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance.

Legislature – An officially elected or otherwise selected body of people vested with the responsibility and power to make laws for a sovereign unit, such as a state or nation.

Management—The person(s) with executive responsibility for the conduct of the entity's operations. For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.

Management's expert—An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements.

Misstatement—A difference between the reported amount, classification, presentation, or disclosure of a financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Misstatements can arise from error or fraud.

Modified opinion—A qualified opinion, an adverse opinion or a disclaimer opinion on the financial statements.

Negative confirmation request—A request that the confirming party respond directly to the audit or only if the confirming party disagrees with the information provided in the request.

Opening balances—Those account balances that exist at the beginning of the period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period and also include matters requiring disclosure that existed at the beginning of the period, i.e. contingencies and commitments.

Other information— Financial or non-financial information (other than financial statements and the auditor's report thereon) included in an entity's annual report.

Performance audit – An audit of the economy, efficiency and effectiveness with which the audited entity uses its resources in carrying out its responsibilities, also known as Value for money audit.

Performance materiality—The amount or amounts set by the audit or at less than materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. If applicable, performance materiality also refers to the amount or amounts set by the auditor at less than the materiality level or levels for particular classes of transactions, account balances or disclosures.

Pervasive—A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient and appropriate audit evidence. Pervasive effects on the financial statements are those that, in the auditor's judgment:

- Are not confined to specific elements, accounts or items of the financial statements;
- If so confined, represent or could represent a substantial proportion of the financial statements; or
- In relation to disclosures, are fundamental to users' understanding of the financial statements.

Population—The entire set of data from which a sample is selected and about which the auditor wishes to draw conclusions.

Positive confirmation request—A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information.

Practice Note – Included in the INTOSAI Financial Audit Guidelines. The Practice Note explains how to apply the ISA in a financial audit in the public sector. They also contain guidance relevant to audits of public sector entities in addition to what is provided for in the ISA.

Professional judgment—The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.

Professional skepticism—An 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 evidence.

Reasonable assurance (in the context of audit engagements, and in quality control)—A high, but not absolute, level of assurance.

Prospective financial information—Financial information based on assumptions about events that may occur in the future and possible actions by an entity. Prospective financial information can be in the form of a forecast, a projection or a combination of both. (see *Forecast* and *Projection*)
Public sector—National governments, regional (for example, state, provincial, territorial) governments, local (for example, city, town) governments and related governmental entities (for example, agencies, boards, commissions and enterprises).

Related party—A party that is either: A related party as defined in the applicable financial reporting framework; or Where the applicable financial reporting framework establishes minimal or no related party requirements: A person or other entity that has control or significant influence, directly or indirectly through one or more intermediaries, over the reporting entity; Another entity over which the reporting entity has control or significant influence, directly or indirectly through one or more intermediaries; or Another entity that is under common control with the reporting entity.

Risk assessment procedures—The audit procedures performed to obtain an understanding of the entity and its environment, including the entity's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.

Risk of material misstatement—The risk that the financial statements are materially misstated prior to audit. This consists of two components, i.e. inherent risk and control risk.

Sampling risk—The risk that the auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. Sampling risk can lead to two types of erroneous conclusions: In the case of a test of controls, that controls are more effective than they actually are, or in the case of a test of details, that a material misstatement does not exist when in fact it does. The auditor is primarily concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion. In the case of a test of controls, that controls are less effective than they actually are, or in the case of a test of details, that a material misstatement exists when in fact it does not. This type of erroneous conclusion affects audit efficiency as it would usually lead to additional work to establish that initial conclusions were incorrect.

Sampling unit—The individual items constituting a population.

Significant deficiency in internal control—A deficiency or combination of deficiencies in internal control that, in the auditor's professional judgment, is of sufficient importance to merit the attention of those charged with governance.

Significant risk—An identified and assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration.

Statistical sampling—An approach to sampling that has the following characteristics: Random selection of the sample items; and the use of probability theory to evaluate sample results, including measurement of sampling risk. A sampling approach that does not have characteristics (a) and (b) is considered non- statistical sampling.

Statutory – Decided or controlled by law.

Stratification—The process of dividing a population into sub-populations, each of which is a group of sampling units which have similar characteristics (often monetary value).

Subsequent events—Events occurring between the date of the financial statements and the date of the auditor's report, and facts that become known to the auditor after the date of the auditor's report.

Substantive procedure—An audit procedure designed to detect material misstatements at the assertion level. Substantive procedures comprise: Tests of details (of classes of transactions, account balances, and disclosures); and Substantive analytical procedures.

Sufficiency (of audit evidence)—The measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement and also by the quality of such audit evidence.

Supreme Audit Institution – The public body of a State which, however designated, constituted or organized, exercises by virtue of law, the highest public auditing function of that State. In some Supreme Audit Institutions there are a single appointed Auditor General who acts in a role equivalent to that of "engagement partner" and who has overall responsibility for public sector audits. Other Supreme Audit Institutions may be organized as a Court of Accounts or having a collegiate or board system. In Bangladesh, OCAG is the Supreme Audit Institution and FAPAD as a directorate of the OCAG discharge delegated audit activities.

Those charged with governance – In the public sector, governance responsibilities may exist at several organizational levels as well as in several functions (i.e. vertically or horizontally). As a result, there may be instances where several distinct groups are identified as those charged with governance. Furthermore, an audit in the public sector might involve both financial statement objectives as well as compliance objectives and in some cases that may involve separate governance bodies.

Tests of controls—An audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level.

Tolerable misstatement—A monetary amount set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the monetary amount set by the auditor is not exceeded by the actual misstatement in the population.

Uncertainty—A matter whose outcome depends on future actions or events not under the direct control of the entity but that may affect the financial statements.

Uncorrected misstatements—Misstatements that the auditor has accumulated during the audit and that have not been corrected.

Unmodified opinion—The opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Walk-through test—Involves tracing a few transactions through the financial reporting system.

Written representation—A written statement by management provided to the auditor to confirm certain matters or to support other audit evidence. Written representations in this context do not include financial statements, the assertions therein, or supporting books and records.

Contents

The contents of this Audit Manual have been divided into the following chapters:

Chapter no	Chapter name	Brief Contents of the Chapter
One	Introduction	Objective of the manual and its applicability, reporting requirements of development partners, related pronouncements and standards.
Two	Planning	This chapter is divided into two sections: Planning at FAPAD level focused on maintenance of a comprehensive audit plan for the year, agreeing terms of audit engagement, human resource and communication with Project. Planning at engagement level covers understanding the Project, audit risk assessment, calculation of materiality, planning analytical, sampling and other planning related matters specified in ISSAI.
Three	Audit Execution/ fieldwork	This chapter deals with audit approach and audit procedures to gather various types of audit evidence, both control and substantive testing along with documentation requirement.
Four	Audit Completion	This chapter covers certain specific audit procedures required to be conducted as per ISSAI and drawing an overall conclusion.
Five	Reporting	This chapter explains various types of audit opinion and related templates to use for issuance of audit report. In addition, other aspects of reporting such as specific requirements of development partners as well as management letter are also addressed here.
Six	Quality assurance	This chapter explains quality control at FAPAD level as well as at audit engagement level.

Chapter One
Introduction






1.1 Objective of the manual and its applicability

This Project Audit Manual has been developed to provide Foreign Aided Project Audit Directorate (FAPAD) of the Office of the Comptroller and Auditor General of Bangladesh with a set of updated auditing standards, concepts, techniques and quality assurance arrangements that are consistent with the applicable international standards.

The purpose of this Audit Manual is to promote consistency and efficiency in the conduct of audits, and to enhance the quality of audit work. FAPAD auditors are expected to exercise professional judgment in the application of this Manual.

This Project Audit Manual has been prepared with an objective to provide guidelines to personnel of FAPAD of the Office of the Comptroller and Auditor General of Bangladesh involved in audit of Foreign Aided Projects funded by various development partners and implemented by respective Executing/Implementing Agencies.

The Manual shall be used by the FAPAD audit engagement teams both at head office as well as at all phases of audit of all Foreign Aided Projects funded by various development partners and implemented by respective Executing/Implementing Agencies.

It is also worthwhile to mention that the audit of the Project financial statements conducted by FAPAD audit engagement team on behalf of the CAG is to fulfil the specific requirements of the Development Partners as specified in the related Loan/Grant agreement executed with the Government. Therefore, this specific audit is different from the independent audit conducted by the Office of Comptroller and Auditor General (OCAG) of Bangladesh as constitutional requirement.

1.2 Reporting Requirements of Development Partners in Bangladesh

Projects funded by development partners are normally guided by the rules and regulations of both the Government of Bangladesh such as Project Accounting Manual issued under the authority of Finance Division, Ministry of Finance, Government of Bangladesh as well as the related development partner(s). Accordingly, two major types of procedures and reporting requirements are applicable for audit of development Projects in Bangladesh.

The primary requirements for development partners on financial reporting are the "Project Financial Statements" prepared on the basis of acceptable accounting framework such as IFRS, IPSAS (Cash Basis) and an opinion on those Project Financial Statements based on audit conducted in accordance with auditing standards such as ISSAI or ISA. The Government Auditing Standards of Bangladesh (GASB) issued by the OCAG are based on ISSAI and hence compliance with GASB shall also ensure compliance of ISSAI.

The additional reporting requirements from development partners include certain specific certification from the auditors of foreign aided projects on matters such as;

- The funds are utilized for the intended purposes and as per the activity plan;
- The Project executing/implementing agency has complied with all financial covenants;
- The Project has complied with various requirements specified in the related Loan/Grant agreement;
- The Reimbursements/SOE/Imprest account procedures are duly complied with the instructions of the related development partners; and
- The procurement of goods and services has been made in accordance with the Grant/Financing Agreements and Development Partner's procurement regulations.

From the compliance perspective, the development partner funded projects (the "Project") usually follow two types of rules and procedures:

- The Government funding portion of the Project required to comply with Bangladesh Government policies and procedures (i.e. public procurement policy); and
- The development partner funded portion is specific rules and procedures of the respective development partners and project specific guidance (project administrative manual, project finance manual, project procurement plan etc.)

The FAPAD audit team shall ensure that specific reporting requirements of respective development partners are also met during the audit. Accordingly, the audit team shall obtain thorough understanding of all these specific reporting requirements.

1.3 Code of Ethics and Independence

Supreme Audit Institution (SAI) is held to meet high expectations and strives to earn the trust of stakeholders (citizens, legislative and executive bodies, responsible parties and others). As ethical behaviour is a key component in establishing and sustaining the trust and reputation, a code of ethics is a prerequisite for the functioning of a SAI.

Accordingly, the Office of the Comptroller and Auditor General of Bangladesh (OCAG) has issued 'Code of Ethics' in February 2021 as guideline of conduct for its personnel reflecting moral standards and ethical values that would ensure a credible environment of professionalism. The Code is based the 'INTOSAI' Code of Ethics for Auditors in the Public Sector, in particular International Standards of Supreme Audit Institutions (ISSAI) 130 and covers the ethical requirements of government auditors, including their professional obligations.

FAPAD auditors being a part of the OCAG also need to comply with relevant ethical requirements including the 'Code of Ethics' issued by the OCAG and to be independent from the responsible entity. Ethical principles should be embodied in an auditor's behavior.

Ethics ensure that the audit is conducted with a professional attitude. The key principles of ethics are integrity, objectivity, professional competence and due care, confidentiality and professional behaviour. Auditors should be honest, reliable and truthful when conducting an audit. Auditors should remain independent so that their opinions/conclusions/findings will be impartial and be seen as such by third parties.

Independence is defined as freedom from situations and relationships which could impair the auditor's objectivity. Independence is an attitude of mind and appearance. It safeguards the ability to perform an audit without being affected by influences that might compromise professional judgement.

International Organization of Supreme Audit Institutions (INTOSAI) has issued INTOSAI P 1: The Lima Declaration of Guidelines on Auditing Precepts, ISSAI 10- Mexico Declaration on SAI Independence as well as ISSAI 11- INTOSAI Guidelines and Good Practices related to SAI Independence and ISSAI 30 - Code of Ethics to cover ethics and independence rules and codes.

1.3.1 INTOSAI P 1: The Lima Declaration of Guidelines on Auditing Precepts (the Lima Declaration) (Formerly ISSAI 1)

The main aim of the Lima Declaration is to call for independent government auditing and hence a Supreme Audit Institution needs to be Independent. In addition, it also discuss about SAI's Power, its relationship to parliament, government and the administration, audit methods, audit staff, international exchange of experiences, reporting etc. under the following seven chapters:

I. General

II. Independence

III. Relationship to Parliament, government and the administration

IV. Powers of Supreme Audit Institutions

V. Audit methods, audit staff, international exchange of experiences

VI. Reporting

VII. Audit powers of Supreme Audit Institutions

1.3.2 *INTOSAI P 10: Mexico Declaration on SAI Independence*

The Mexico declaration emphasizes on SAI Independence and hence introduced Eight Principles as essential requirements of proper public sector auditing. All FAPAD personnel should be fully conversant of these core principles. These eight core principles are:

1. The existence of an appropriate and effective constitutional/ statutory/ legal framework and of de facto application provisions of this framework.
2. The independence of SAI heads and members, including security of tenure and legal immunity in the normal discharge of their duties.
3. A sufficiently broad mandate and full discretion, in the discharge of SAI functions.
4. Unrestricted access to information.
5. The right and obligation to report on their work.

6. The freedom to decide the content and timing of audit reports and to publish and disseminate them.
7. The existence of effective follow-up mechanisms on SAI recommendations.
8. Financial and managerial/ administrative autonomy and the availability of appropriate human, material, and monetary resources.

1.3.3 ISSAI 130: Code of Ethics

The *ISSAI 130 - Code of Ethics* (the Code) intends to provide SAIs and the staff working for them with a set of values and principles on which to base their behaviour. Furthermore, recognising the specific environment of public sector auditing which is often different from private sector auditing, it gives additional guidance on how to embed those values in daily audit work and in the particular situations of a SAI like the OCAG/FAPAD.

The Code is intended for all those who work for, or on behalf of, FAPAD. This includes the DG of FAPAD, all directors, staff and all individuals directly employed by, or contracted to conduct business on behalf of FAPAD. The Code comprises an overall approach to ethical behaviour, a description of the FAPAD's overall responsibilities and the five fundamental values that guide ethical conduct.

The Code is written at a principle level and requires FAPAD and its staff to apply their professional judgement to the circumstances they encounter and follow the relevant requirements set out in this code.

Ethical values are defined as the concepts of what is an important and ethical principle guide how these values should be carried out in practice and, therefore, what should be appropriate behaviour. The Code has specified the following five fundamental values:

a) Integrity
FAPAD audit personnel shall act honestly, reliably, in good faith and in the public interest. They should conduct their work without any fear or favour to preserve public trust on FAPAD.

b) Independence and objectivity
Independence is defined as a situation free from circumstances or influences that compromise, or may be seen as compromising, professional judgement, and to act in an impartial and unbiased manner. Independence comprises:

Independence of mind—the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, 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 a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm's, or a member of the assurance team's integrity, objectivity or professional skepticism had been compromised.

c) Competence

Competency is to acquire and maintain knowledge and skills appropriate for the role, and to act in accordance with applicable standards, and with due care.

d) Professional behaviour

Auditors shall comply with applicable laws, regulations and conventions, and to avoid any conduct that may disgrace FAPAD as well as themselves. Accordingly, FAPAD audit teams shall be aware of the professional behaviours expected from them by all stakeholders including development partners.

e) Confidentiality and transparency

FAPAD audit team shall appropriately protect information and preserve confidentiality and at the same time balancing this with the need for transparency and accountability. Confidential information obtained during the course of audit shall not be used for personal gain or gain of third parties. Any inadvertent disclosure of confidential information to third parties shall be dealt by promptly and a defined process shall be in place to manage this situation. FAPAD personnel need to ensure this confidentiality even after transfer to other department/role.

Risks (often referred as "threats") of non-compliance with the above values can be can be either real or perceived, and influenced by a number of risk factors/sources, such as:

- Self-interest threats;
- Advocacy threats;
- Familiarity threats;
- Self-review threats; and
- Intimidation threats.

Where risks are identified that threaten any of the five fundamental values, the significance of such threats is evaluated and appropriate controls (often also referred to as "safeguards") need to be put in place to reduce the risk of unethical behaviour to an acceptable level. Safeguards may reduce such threats, and may be created either by external structures (for example, OCAG Code of Ethics), or by the auditor's work environment (for example, quality control policies and procedures at FAPAD).

As per the Code, FAPAD is responsible for implementing independence and objectivity related controls such as, declarations of interests and conflicts of interest to help identify and mitigate threats to independence. Accordingly, on an annual basis all FAPAD personnel shall submit a declaration to the Director General specifying that s/he shall comply with the Code at all times, and if there are any real or perceived conflict of interest situation during any audit assignment s/he shall immediately notify the matter to the DG, FAPAD.

1.4 ISSAI 100: Fundamental Principles of Public Sector Auditing

The International Organisation of Supreme Audit Institutions (INTOSAI) has published the INTOSAI Framework of Professional Pronouncements (IFPP) consisting of principles and standards governing public sector audit. INTOSAI has also developed the International Standards of Supreme Audit Institutions (ISSAIs) to promote independent and effective auditing by Supreme Audit Institutions (SAIs), like the Office of Comptroller and Auditor General (OCAG) of Bangladesh.

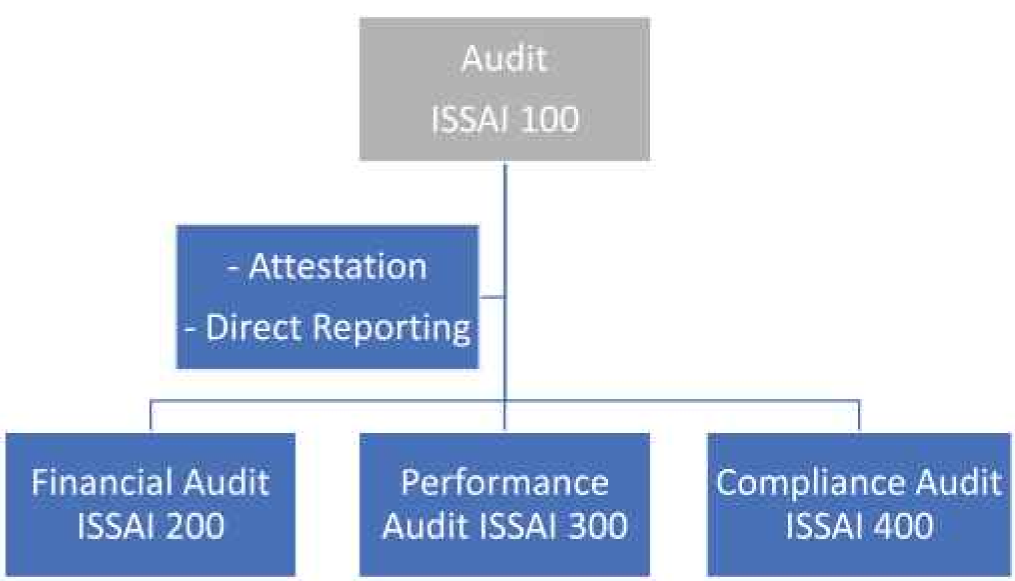
The ISSAIs encompass public-sector auditing requirements at the organisational (SAI) level, while on the level of individual audits they aim to support the members of INTOSAI in the development of their own professional approach in accordance with their mandates and with national laws and regulations. Accordingly, the OCAG Bangladesh in February 2021 has issued 'Government Auditing Standards of Bangladesh' which are based on ISSAIs and are consistent with the global standards. Therefore, compliance with this Project Audit Manual by the FAPAD Personnel will also ensure observance of the relevant requirements of the Government Auditing Standards of Bangladesh.

ISSAI 100 – Fundamental Principles of Public-sector Auditing establishes fundamental principles which are applicable to all public-sector audit engagements, irrespective of their form or context and provides detailed information on:

- The purpose and authority of the ISSAIs;
- The framework for public-sector auditing;
- The elements of public-sector auditing;
- The principles to be applied in public-sector auditing.

It also establishes fundamental principles which are applicable to all public-sector audits and introduce some key concepts like audit risk, materiality, quality control, documentation etc. Therefore, auditors of FAPAD should have understanding of these standard and related topics.

The three main types of public-sector audit are defined as follows:



A. **Financial audit:** Financial audit focuses on determining whether an entity's financial information is presented in accordance with the applicable financial reporting and regulatory framework. This is accomplished by obtaining sufficient and appropriate audit evidence to enable the auditor to express an opinion as to whether the financial information is free from material misstatement due to fraud or error.

B. **Performance audit:** Performance audit focuses on whether interventions, programmes and institutions are performing in accordance with the principles of economy, efficiency and effectiveness and whether there is room for improvement. Performance is examined against suitable criteria, and the causes of deviations from those criteria or other problems are analysed.

C. **Compliance audit:** Compliance audit focuses on whether a particular subject matter is in compliance with authorities identified as criteria. Compliance auditing is performed by assessing whether activities, financial transactions and information are, in all material respects, in compliance with the authorities which govern the audited entity. These authorities may include rules, laws and regulations, budgetary resolutions, policy, established codes, etc.

All public-sector audits have the same basic elements: the auditor, the responsible party, intended users, criteria for assessing the subject matter and the resulting subject matter information. They can be categorised as two different types of audit engagement:

- Attestation engagements; and
- Direct reporting engagements.

Financial audits are always attestation engagements, as they are based on financial information presented by the responsible party. Performance audits are normally direct reporting engagements. Compliance audits may be attestation or direct reporting engagements, or both at once.

The three parties

Public-sector audits involve at least the following three separate parties:

i. **The auditor:** In public-sector auditing, the role of auditor is fulfilled by the Head of the SAI and by persons to whom the task of conducting the audits is delegated. The overall responsibility for public-sector auditing remains as defined by the SAI's mandate.

ii. **The responsible party:** In public-sector auditing, the relevant responsibilities are determined by constitutional or legislative arrangement. The responsible parties may be responsible for the subject matter information, for managing the subject matter or for addressing recommendations, and may be individuals or organisations.

iii. **Intended users:** The individuals, organisations or classes thereof for whom the auditor prepares the audit report. The intended users may be legislative or oversight bodies, those charged with governance or the general public.

1.5 ISSAI 140: Quality Control for SAIs

Quality Control System (QCS) in a Supreme Audit Institution is an important step towards ensuring high quality audit work. Accordingly, INTOSAI has issued International Standards of Supreme Audit Institutions (ISSAI) 140- Quality control for SAIs, which is based on the key principles of the International Standard on Quality Control 1 (ISQC-1) published by International Federation of Accountants (IFAC). The purpose of ISSAI 140 - Quality control for SAIs is to assist SAI to establish and maintain an appropriate system of quality control which covers all of its activities and help to design a system of quality control which is appropriate.

Accordingly, the Office of the Comptroller and Auditor General (OCAG) in February 2021 has issued Quality Control System (QCS) in OCAG Bangladesh based on the principles and requirements of ISSAI 140. While designing the QCS by the OCAG appropriate guidance has been taken from International Standards on Auditing (ISA) 220 published by International Auditing and Assurance Standards Board (IAASB).

Therefore, to deliver high quality audit it is important that FAPAD should have a strong quality assurance process in line with the QCS issued by the OCAG. FAPAD shall establish and maintain an appropriate system of quality control which covers all of its activities and design a system of quality control which is appropriate in full range of FAPAD's work as per its mandate and circumstances. Accordingly, quality control required both at FAPAD level as well as individual audit engagement level as mentioned in the following diagram and covered in detail in Chapter Six.

Compliance with the requirement specified in Chapter Six would ensure compliance with the QCS issued by the OCAG Bangladesh as well as ISSAI 140.

1.6 ISSAI 200: Fundamental Principles of Financial Auditing

The purpose of an audit of financial statements is to enhance the degree of confidence of intended users in the financial statements. This is achieved through the expression of an opinion by the auditor as to whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. An audit conducted in accordance with standards based on the INTOSAI Fundamental Principles of Financial Auditing and relevant ethical requirements will enable the auditor to express such an opinion.

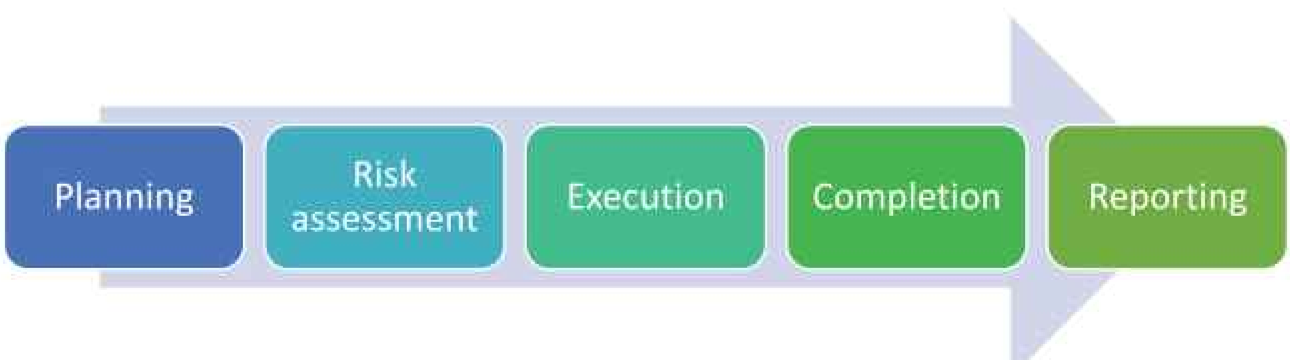
The auditor should have clear knowledge about the all INTOSAI and ISSAI standards. ISSAI 200 – Fundamental Principles of Financial Auditing has been developed to address the key principles related to an audit of financial statements in the public sector. It builds on and further develops the fundamental principles of ISSAI 100 to suit the specific context of audits of financial statements, and constitutes the basis for auditing standards related to audits of financial statements.

ISSAI 200 represents the core of the detailed auditing standards provided by ISSAIs 2000 to 2999 (previously ISSAIs 1000 to 1810) at level 4 of the ISSAI Framework.

ISSAI 2200:2999 Series Financial Auditing Standards

These standards are actually adopted from International Standards on Auditing (ISA)and renamed as ISSAI with prefixing 2 before the respective ISAs. For example, ISA 200 is codified as ISAI 2200. These standards cover the following:

- General Principles and Responsibilities (ISSAI 2200-2299),
- Risk assessment and response to assessed risks (ISSAI 2300-2499),
- Audit evidence (2500-2599),
- Using the work of others (ISSAI 2600-2699),
- Audit Conclusions and reporting (ISSAI 2700-2799),
- Specialised areas (2800-2899).



Financial audit process

<u>Refer to Appendix 3for the list of all ISSAI that have taken from ISAs and re-numbered with 2 prefix.</u>

1.7 ISSAI 300: Fundamental Principles of Performance Auditing

ISSAI 100 – Fundamental Principles of Public-Sector Auditing provides the fundamental principles for public-sector auditing in general and defines the authority of the ISSAIs. *ISSAI 300 - Fundamental Principles of Performance Auditing* builds on and further develops the fundamental principles of ISSAI 100 to suit the specific context of performance auditing.

Performance auditing is an independent, objective and reliable examination of whether government undertakings, systems, operations, programmes, activities or organisations are operating in accordance with the principles of economy, efficiency and effectiveness and whether there is room for improvement. Therefore, performance auditing is quite different to financial auditing.

The main objective of performance auditing is constructively to promote economical, effective and efficient governance. It also contributes to accountability and transparency

Performance auditing seeks to provide new information, analysis or insights and, where appropriate, recommendations for improvement. Performance audits deliver new information, knowledge or value by:

- Providing new analytical insights (broader or deeper analysis or new perspectives);
- Making existing information more accessible to various stakeholders;
- Providing an independent and authoritative view or conclusion based on audit evidence; and
- Providing recommendations based on an analysis of audit findings.

The principles of economy, efficiency and effectiveness can be defined as follows:

The principle of *economy* means minimising the costs of resources. The resources used should be available in due time, in and of appropriate quantity and quality and at the best price.

The principle of *efficiency* means getting the most from the available resources. It is concerned with the relationship between resources employed and outputs delivered in terms of quantity, quality and timing.

The principle of *effectiveness* concerns meeting the objectives set and achieving the intended results.

Performance audits often include an analysis of the conditions that are necessary to ensure that the principles of economy, efficiency and effectiveness can be upheld. These conditions may include good management practices and procedures to ensure the correct and timely delivery of services. Where appropriate, the impact of the regulatory or institutional framework on the performance of the audited entity should also be taken into account.

1.8 ISSAI 400: Fundamental Principles of Compliance Auditing

ISSAI 400 – Fundamental Principles of Compliance Auditing builds on and further develops the fundamental principles of ISSAI 100 to suit the specific context of compliance auditing. Compliance auditing is the independent assessment of whether a given subject matter is in compliance with applicable authorities identified as criteria.

Compliance auditing is the independent assessment of whether a given subject matter is in compliance with applicable authorities identified as criteria. Compliance audits are carried out by assessing whether activities, financial transactions and information comply, in all material respects, with the authorities who govern the audited entity.

The objective of public-sector compliance auditing, therefore, is to enable the SAI to assess whether the activities of public-sector entities are in accordance with the authorities governing those entities. This involves reporting on the degree to which the audited entity complies with established criteria. Reporting may vary between brief standardised opinions and various forms of conclusions, presented in short or long form. Compliance auditing may be concerned with *regularity* (adherence to formal criteria such as relevant laws, regulations and agreements) or with *propriety* (observance of the general principles governing sound financial management and the conduct of public officials). While regularity is the main focus of compliance auditing, propriety may also be pertinent given the public-sector context, in which there are certain expectations concerning financial management and the conduct of officials.

ISSAI 400 constitutes the basis for compliance auditing standards in accordance with the ISSAIs and defines compliance auditing framework, elements, principles and the different ways in which compliance audits are conducted.

Compliance auditing can be part of a combined audit that may also include other aspects. Though other possibilities exist, compliance auditing is generally conducted either:

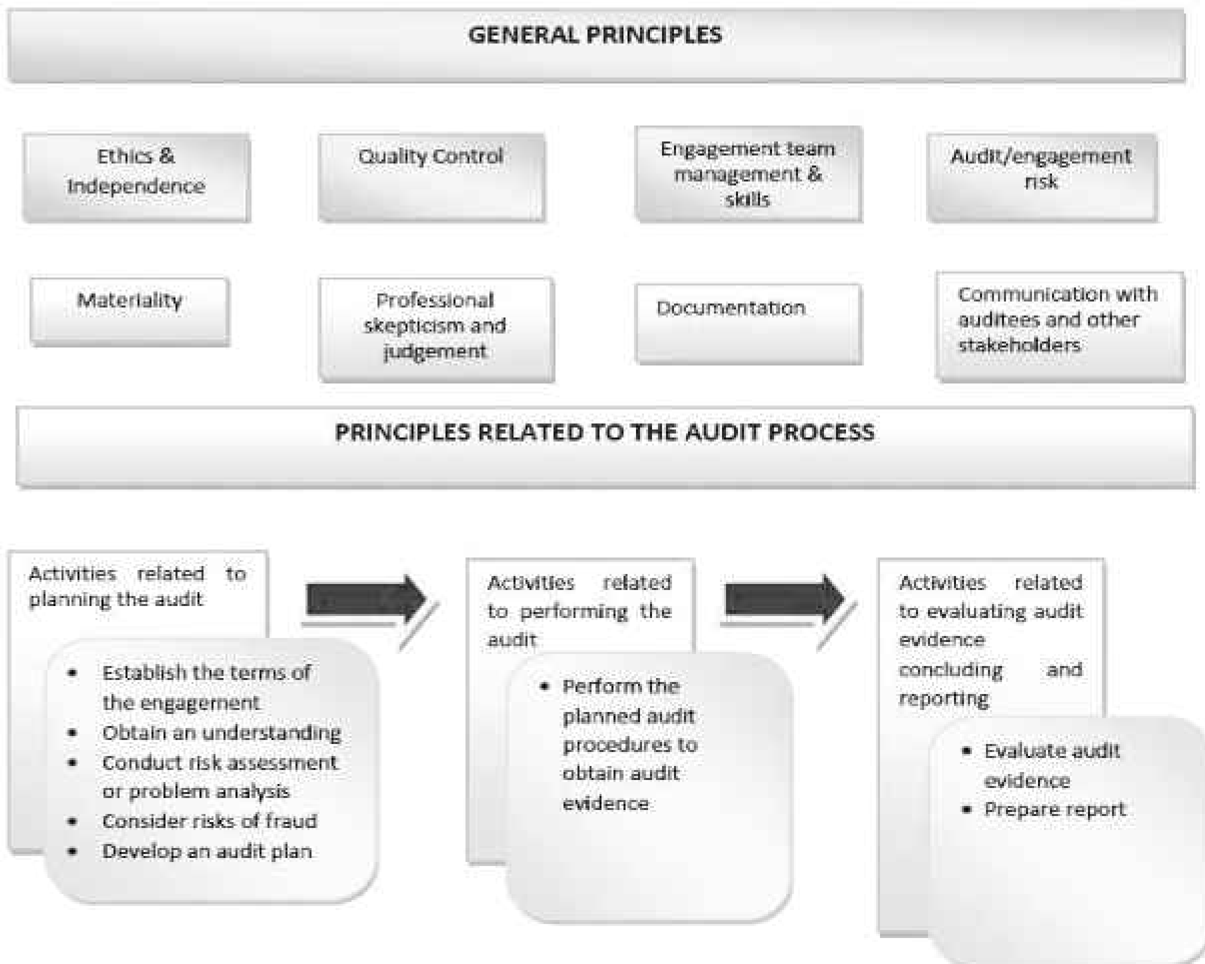
- In relation with the audit of financial statements, or
- Separately from the audit of financial statements, or
- In combination with performance auditing.

Laws and regulations are important both in compliance auditing and in the audit of financial statements. Which laws and regulations apply in each field will depend on the audit objective. Compliance auditing is the independent assessment of whether a given subject matter is in compliance with applicable authorities identified as criteria; it focuses on obtaining sufficient and appropriate evidence regarding compliance with those criteria. The audit of financial statements seeks to ascertain whether the financial statements of the entity concerned were prepared in accordance with an acceptable financial reporting framework and to obtain sufficient and appropriate audit evidence regarding the laws and regulations that have a direct and material effect on the financial statements. Whereas, in the audit of financial statements, only those laws and regulations with a direct and material effect on the financial statement are relevant, in compliance auditing any laws and regulations relevant to the subject matter may be relevant for the audit.

1.9 Audit Framework

An audit conducted in compliance with relevant standards like ISSAI/ISA required audit activities to be conducted in an orderly fashion. Normally first stage of an audit would be planning, second stage execution/fieldwork including control evaluation, third stage completion of specific procedures and finally in fourth stage reporting.

This is provided in the following diagram.



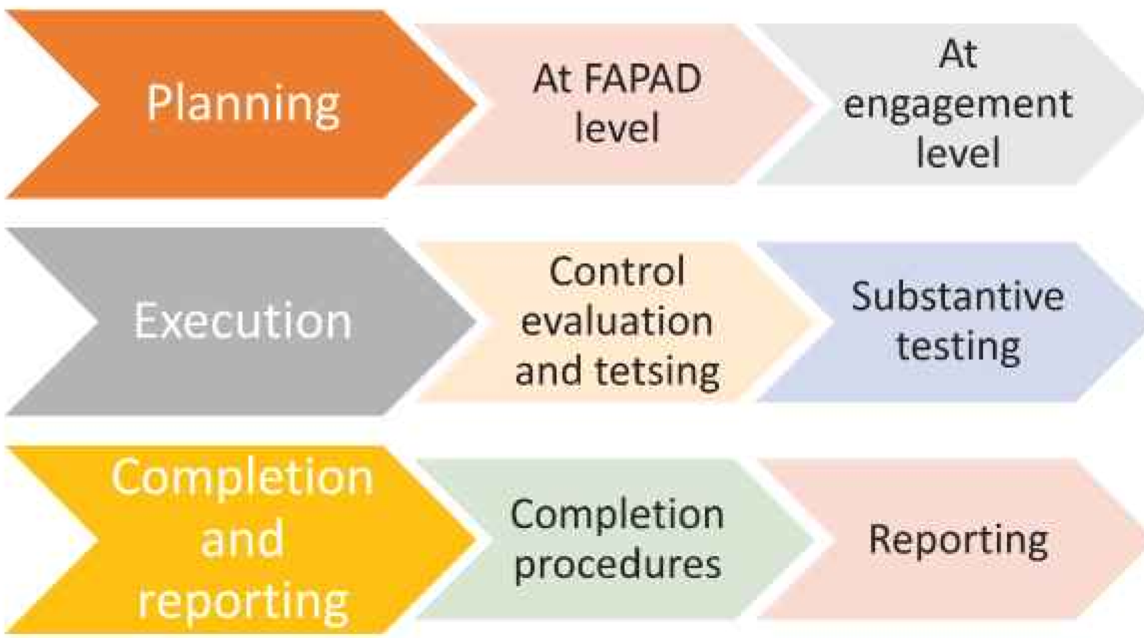
Chapter Two
Planning






Section One: Planning at FAPAD Level

As per the fundamental principles related to the audit process as described in ISSAI 100, Planning should take place once at SAI (FAPAD) level as well as at the audit engagement level. Critical aspects of audit planning at engagement level involves establish the terms of the audit, obtain understanding, conduct risk assessment or problem analysis, identify risks of fraud and develop an audit plan.



2.1.1 Maintenance of an annual audit plan for all projects to be audited

The starting point for planning at FAPAD level is the 'Annual Development Program (ADP)' prepared by the Ministry of Planning (MoP), Government of the People's Republic of Bangladesh. Economic Relations Division (ERD) of the Ministry of Finance (MoF) is involved in mobilization of external resources for socio-economic development of the country and act as the focal point of the Government for interfacing with the development partners as well as for co-ordination of all external assistance inflows into the country. It assesses the needs of external assistance, devises strategy for negotiations and mobilizing foreign assistance, formalizes and enables aid mobilization through signing of loans and grants agreements, determines and executes external economic policy.

In accordance with the conditions of the respective loan/grant agreement, all foreign funded projects included in the ADP are subject to audit by FAPAD on behalf of the OCAG. ERD maintains a comprehensive database of all funding received from development partners including nature of such funding (i.e. grant, loan etc.). On an annual basis ERD sends a list of all Projects funded by development partners requiring audit during the fiscal period to FAPAD.

FAPAD maintains a master database of all Projects requiring audit during the fiscal year along with related information such as project name, description, location, executing agency, major funding agencies, project size, start and completion date, audit deadline, prior year audit team, key findings in PY etc. Upon receiving the list of Projects requiring audit, FAPAD update the database and prepare an Annual Audit Plan for the year ensuring that all Projects notified by ERD have been considered for audit and an audit team is assigned.

The audit plan is a living document and regularly updated which contain the following information:

- The total number of audits for which the Directorate is responsible;
- The total number of audits assigned to each sector;
- The total number of audits completed;
- The total number audits in progress;
- The total number of audit for which the draft audit reports/management letter has been sent.

Unlike other Audit Directorates of the OCAG, FAPAD has a limitation to complete all Project audits allocated to it with the specific deadline. If there is any delay in submission of audit report, it would cause a breach in covenants by the development partners and hence timeliness of audit completion is very important for FAPAD.

To ensure this master database is updated, the office of the FAPAD DG shall send a formal request to ERD by 15 January of each year at prescribed format asking for required information to prepare/update the database. Upon receiving the information, this master database shall be updated along with the tentative timeframe to conduct each audit allocated to FAPAD.

2.1.2 Agreeing terms of reference/ audit engagement letter

As per ISSAI 2210, the auditor shall agree the terms of the audit engagement with management prior to the start of audit. If consider appropriate, FAPAD in conjunction with the OCAG will develop a standard template specifying the terms of the audit engagement and in such case instead of separate engagement letter for each project audit, FAPAD audit team can refer to this standard template as engagement letter.

Objective for the audit of foreign aided projects is to express an opinion on the financial statements of the Project as to whether the financial information presented in those financial statements provide a true and fair view in all material respects as to the utilization of funds obtained by the Government of Bangladesh under the relevant agreements with development partners. These audits intended to provide assurance to those development partners as to the accountability of funds entrusted to the Government of Bangladesh.

The auditor shall consider applicable financial reporting framework, including applicable regulatory requirements and Development-partner-specific requirements related to financial reporting in order to define the scope of audit of the Project financial statements. The Foreign Aided Projects in Bangladesh are required to follow the Project Accounting Manual issued by the Finance Division MoF, GoB and mainly adopted IPSAS Cash Basis for the purposes of preparing and presenting financial statements.

The auditor shall obtain an understanding of the relevant development partners' financial reporting requirements. These requirements are usually laid out in the legal agreements (Loan/grant covenants, project agreement, project implementation letters, etc.) related to the Project.

At a minimum, the letter of engagement should contain the following items under separate headings:

- Introduction
- The objective and scope of the audit of the financial statements;
- The responsibilities of the auditor;
- The responsibilities of management;
- Applicable financial reporting framework for preparation of the financial statements;
- 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.

<u>An example of pro forma letter of engagement is given in Appendix 4.</u>

2.1.3 Human resource, training, transfer etc.

Quality control aspects are fundamental in any audit. This quality control happens in two stages; one at FAPAD level and another at engagement level.

Policies and procedures at FAPAD level to monitor capacity, workload, availability, required training etc. of audit personnel would assist in quality assurance which is more elaborated in ISQC 1 and ISSAI 140. Personnel issues relevant to FAPAD's policies and procedures related to human resources include, for example:

- Performance evaluation;
- Capabilities, including time to perform assignments;
- Competence;
- Career development;
- Promotion.

Competence can be developed through a variety of methods, including the following:

- Professional education.
- Continuing professional development, including training.
- Work experience.
- Coaching by more experienced staff, for example, other members of the engagement team.
- Independence education for personnel who are required to be independent.

FAPAD shall provide all personnel with continuing professional development and training, necessary resources and assistance to develop and maintain the required competence and capabilities.

2.1.4 Communication with the responsible entity

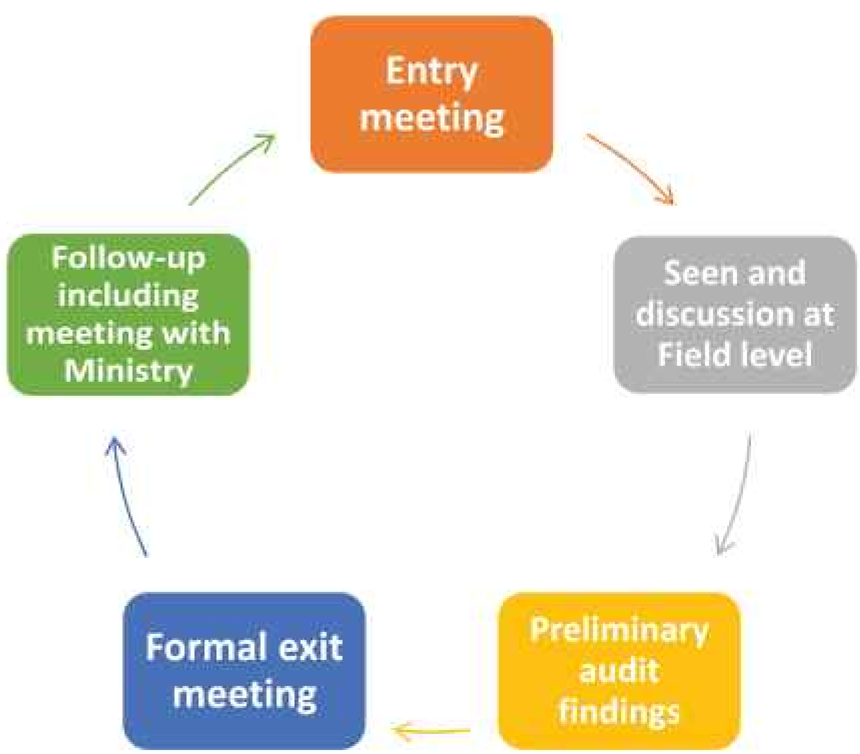
Communication with the responsible entity is an important part and requires proper policy and procedures. Lack of timely/proper communication amongst auditor and responsible party can be a big impediment on successful audit execution and ensuring audit quality. FAPAD audit teams should ensure effective communication with the responsible Project.

Communication with Project's management at the time of planning reduces the expectation gap between the auditor and Project's management and also streamlines the flow of provision of necessary documents and information for the purpose of conductance of well-organized effective and efficient audit.

As a first step, assigned FAPAD Audit team shall send an engagement letter or terms of reference letter accompanied with a detailed information requisition enlisting documents necessary for the auditor to undertake effective audit planning. The Project management shall be requested to provide the draft financial statements pertaining to the period under audit within specified timeframe from receipt of the engagement letter and/or requisition letter.

<u>Refer to the pro forma Engagement Letter in Appendix 4 incorporating requested information.</u>

Other communication steps during the audit shall include at least the following elements:



Entry Meeting: Meeting conducted with the Project management along with representatives from development partner at FAPAD level when beginning the audit.

Seen and discussion meeting at field level of the Project: Upon completion of the field work at the Project level, the audit team may consider to have a preliminary meeting at the Project office/site to confirm factual findings. If possible, the minute of this discussion can be prepared and signed by both parties. This will assist to minimize any dispute in later stages while finalizing the audit findings.

Preliminary Audit Report along with draft management letter: the audit report issued to the Project management to communicate all significant issues found during audit and to provide management with an opportunity to respond and discuss during the exit meeting.

Exit/Discussion Meeting: meeting conducted with the Project management along with representatives from DP at FAPAD level to discuss key audit findings and provide the opportunity to management to respond and/or produce evidences regarding the audit findings.

Meeting with the EA/IA/Line Ministry: FAPAD audit team may require arranging a meeting with the EA/IA or the concerned line ministry of the Project to satisfy its obligation to communicate with those charged with governance.

Final Audit Report: the audit report issued to the Project management stating audit opinion and final management letter containing all unsettled audit issues, after considering the responsible party's responses and the evidence for the audit issues stipulated in the preliminary audit report.

Follow-up of prior year Management letter: At times an interim follow-up of pending issues may require.

2.1.5 Maintenance of permanent file and prior year working paper

Most foreign aided projects in Bangladesh are running for more than one year and subject to recurring audit by FAPAD teams. Therefore, it is important to create and maintain permanent audit file for those projects where audit in subsequent period is needed. Certain critical documents can be kept on these permanent files so that on one hand the Project would save resources to produce same thing repeatedly and also the audit team would get time to familiarise themselves on key audit related matters prior to the start of audit.

The purpose of the permanent audit file is to maintain documentation and information of continuing relevance to the audit. The file must be reviewed at least annually, with material that is no longer of use being removed from the file and archived. The file should not be considered to be a permanent repository for all documentation that may once have been pertinent.

A permanent audit file should be retained with the documentation of the working papers and supporting evidence that are applicable for more than one financial year. Working papers, documents and information that may be useful in planning and performing audits for subsequent years should be retained in the permanent file. The permanent audit file may be maintained systematically at an appropriate level such as project-level, ministry-level or audit unit level so that the papers, documents and information can be easily used in subsequent audits. Relevant laws, rules, regulation, applicable policy, directives and official circulars need to be documented in the Permanent Audit file.

The permanent file contains information of continuing nature about the Project's operations, organizational structure, accounting systems and other features (for example loan/funding agreements) that are important to the conduct of the audit. The contents of the permanent file should be reviewed at every audit and schedules updated to show the latest position. Schedules considered to be outdated, should be removed. This file may include the following information:

- Information concerning the legal and organizational structure, physical and financial size of the Project and the related Executing/Implementing Agency and Line Ministry;
- Strategic plan, important policies, procedures and functional manuals of the Project;
- Appropriate statutory or legal regulations, extracts or copies of important legal documents, agreements and minutes;
- Loan or grant agreements, project appraisal report, review mission reports, projects' periodic and completion reports;
- A short description of the type of business activities carried on and the places of business;
- Names, title and responsibilities of key personnel of the Project;
- Notes regarding significant accounting policies and areas of significant estimated and judgments;
- A brief reference of each audit performed, including nature, date and period of audit;
- Important comments and results and the matters or issues to be reviewed or followed up bysubsequent audits.

An example of contents of permanent file is given in Appendix 5.

2.1.6 Basis for team formation including specialist involvement

The allocation of audit staff to specific audits should take account of their existing experience, training and expertise. Specialisation should also be a feature of the allocation of resources for audit.

For example, a Deputy Director could be given responsibility for a specific audit issue, topic or service in an audit year or more. A number of Project audits can be allocated to him/her and specialise on these issues, topics or services until the audit field work is completed. Specialisation will assist to improve the efficiency and quality of audit as well as its image to the responsible party.

Accordingly, following factors shall be considered at the time of selecting an audit team for the Project audit:

- Understanding of, and practical experience with, audits of a similar nature and complexity through appropriate training and participation;
- Understanding of donor guidelines/regulations, professional standards and applicable legal and regulatory requirements;
- Technical knowledge and expertise, including knowledge of relevant information technology;
- Knowledge of relevant industries in which the clients operate;
- Ability to apply professional judgment; and
- Understanding of the FAPAD quality control policies and procedures.

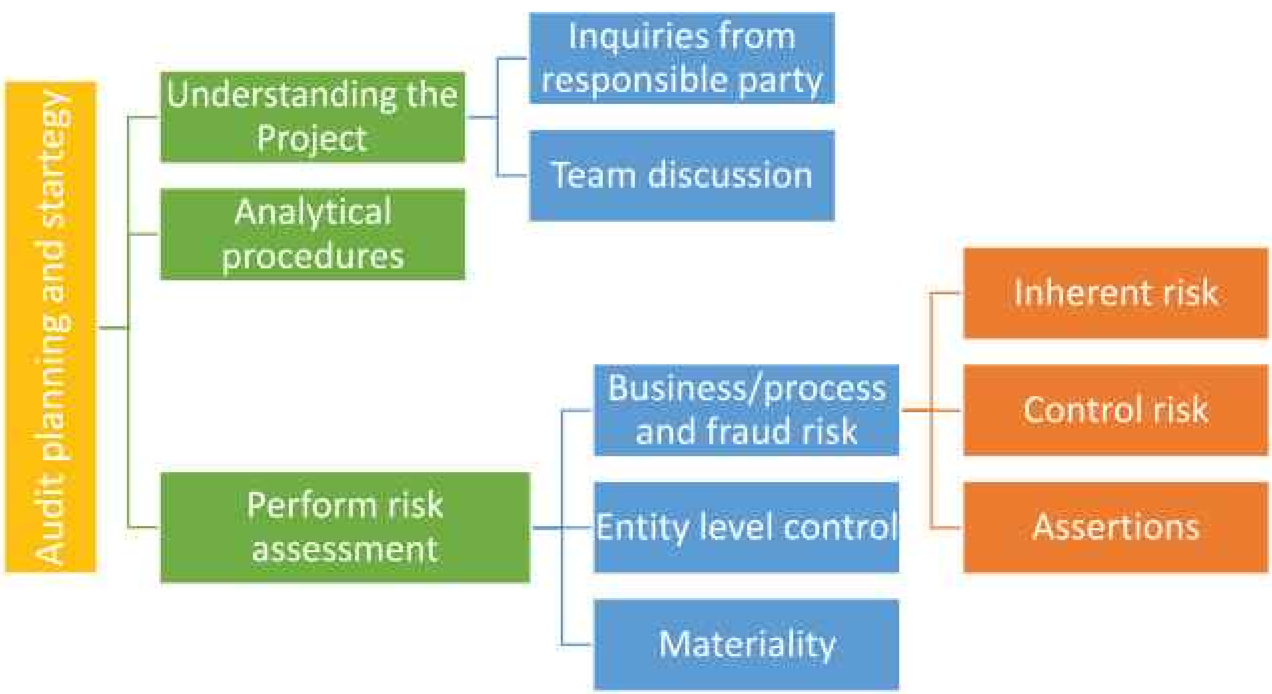
Subject to the prior approval of the OCAG, in exceptional cases, FAPAD may use a suitably qualified external person, when internal technical and training resources are unavailable.

As per ISSAI 2620 Para 7, if expertise in a field other than accounting or auditing is necessary to obtain sufficient appropriate audit evidence, the FAPAD audit team shall determine whether to use the work of an auditor's expert.

Many project audits conducted by FAPAD personnel may require involvement of such experts. For example, lawyer involvement may require for the interpretation of contracts, laws and regulations, specialists needed for the valuation of environmental liabilities and site clean-up costs, professional valuer for the valuation of land and buildings, plant and machinery and assets that may have been impaired. If no such in-house experts are available, they may consider either hiring external resources or seek from other Directorates of the OCAG.

Section Two: Planning at engagement/assignment level

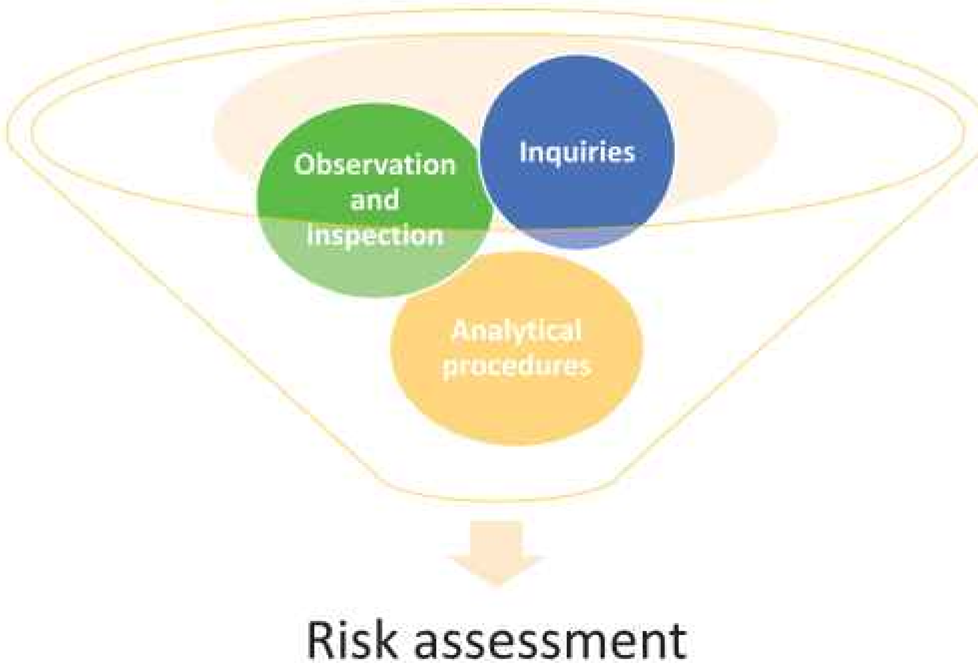
Auditing standards issued by INTOSAI (i.e. ISSAI) require FAPAD to conduct risk based audit. The risk assessment phase of the audit starts with accepting the audit and compliance with required ethical code which are described in Chapter One. Once the planning activities at FAPAD level are completed (as detailed in Section one of this Chapter), the audit team shall obtain an understanding of the Project and its environment including internal control and financial matters to identify inherent and control risks. Since risk assessment procedures require considerable professional judgment, this phase will require significant time from the team leader (i.e. Director) and senior audit team members in identifying and assessing various types of risk, determining materiality and then developing appropriate audit response. The audit team shall also agree the audit plan and audit strategy with the FAPAD DG.



2.2.1 Risk assessment procedures for financial audit

Risk assessment procedures are described as the audit procedures performed by FAPAD audit team to obtain an understanding of the Project and its environment, including the Project's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.

FAPAD audit team shall perform risk assessment procedures to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. The risk assessment procedures shall include the following:



(a) Inquiries of management and others within the Project who in the auditor's judgment may have information likely to assist in identifying risks of material misstatement in the FS.
(b) Analytical procedures.
(c) Observation and inspection.

If the FAPAD audit team has performed other engagements for the same Executing/Implementing Agency or other Projects run by the same management, the FAPAD audit team shall consider whether information obtained is relevant to identify risks of material misstatement.

Where FAPAD audit team intends to use information obtained from the previous audit experience with the Project and from audit procedures performed in previous audits, the audit team shall determine whether changes have occurred since the previous audit that may affect its relevance to the current audit.

2.2.2 Understanding the Project including its nature, objective, activities.

As per ISSAI 2315, Para 11, the auditor shall obtain an understanding of the following:

(a) Relevant industry, regulatory, and other external factors including the applicable financial reporting framework.

(b) The nature of the Project, including:

- its operations;
- its ownership and governance structures;
- the types of investments that the entity is making and plans to make, including investments in special-purpose entities; and
- the way that the Project is structured and how it is financed,

(c) The Project's selection and application of accounting policies, including the reasons for changes thereto. The auditor shall evaluate whether the Project's accounting policies are appropriate for its business and consistent with the applicable financial reporting framework and accounting policies used in the relevant industry.

(d) The Project's objectives and strategies, and those related business risks that may result in risks of material misstatement.

(e) The measurement and review of the Project's financial performance.

(f) The nature and extent of the Project's related party relationships.

2.2.3 Specific topics inquiry from the responsible Party (Project Personnel)

As per ISSAI 2300, FAPAD audit team may decide to discuss elements of planning with the Project's management during the conduct of the audit engagement. When discussing matters included in the overall audit strategy or audit plan, care is required in order not to compromise the effectiveness of the audit. For example, discussing the nature and timing of detailed audit procedures with management may compromise the effectiveness of the audit by making the audit procedures too predictable.

As per ISSAI 2315, the auditor shall make inquiries of management, of appropriate individuals within the internal audit function (if the function exists), and of others within the Project who in the auditor's judgment may have information that is likely to assist in identifying risks of material misstatement due to fraud or error.

Much of the information obtained by the auditor's inquiries is obtained from management and those responsible for financial reporting. Information may also be obtained by the auditor through inquiries with the internal audit function, if the Project or the EA/IA has such a function and others within the Project. As obtaining an understanding of the Project and its environment is a continual, dynamic process, the auditor's inquiries may occur throughout the audit engagement.

If the Project itself or the Implementing/Executing Agency has an internal audit function, inquiries of the appropriate individuals within the function may provide information that is useful to the auditor in obtaining an understanding of the Project and its environment, and in identifying and assessing risks of material misstatement at the financial statement and assertion levels.

Auditor shall design and perform audit procedures in order to identify litigation and claims involving the Project which may give rise to a risk of material misstatement.

Litigation and claims involving the project may have a material effect on the financial statements and thus may be required to be disclosed or accounted for in the financial statements. Accordingly, the audit team shall make specific inquiry to seek information about litigation and claims both pending and/or threatened.

Similarly, noncompliance with critical laws and regulation may have direct adverse impact on the financial statements and hence the audit team shall inquire form Project management about any non-compliance with laws and regulations.

2.2.4 Preliminary analytical procedures

ISSAI 2315.6(b) states that the auditor should apply analytical procedures as risk assessment procedures to obtain an understanding of the entity and its environment. The main purpose of this procedure is to determine the overall audit approach by, for example:

- Identifying abnormal trends, transactions, balances or ratios meriting further enquiry;
- Highlighting new transactions, balances or areas of increased importance; or
- Indicating whether extensive analytical review or control reliance might be appropriate.

Analytical procedures performed as risk assessment procedures may identify aspects of the Project of which the auditor was unaware and may assist in assessing the risks of material misstatement in order to provide a basis for designing and implementing responses to the assessed risks. Analytical procedures performed as risk assessment procedures may include both financial and non-financial information.

Analytical procedures may help to identify the existence of unusual transactions or events, and amounts, ratios, and trends that might indicate matters that have audit implications. Unusual or unexpected relationships that are identified may assist the auditor in identifying risks of material misstatement, especially risks of material misstatement due to fraud.

The knowledge which the auditor gains from analytical procedure at the planning stage can be used to support the rest of the planning process and the development of the audit approach for the examination of specific account balances. Where analytical procedures used for planning reveal significant deviations from expectations the auditor will need to develop specific procedures to discover the cause of these fluctuations.

Typically, the auditor may consider information such as:

- Prior year financial statements;
- Organization's budget and forecasts;
- Appropriate external reports (e.g. performance and statistical reports);
- Relevant non-financial information (e.g. staff numbers, claims processed);
- Statistics and other information about the organization's activities;
- Interim financial statements, reports and other analysis comparing the current period results with prior periods and with current period budgets and forecast;
- Data on significant ratios and achievements against performance targets; and
- Achievement against budgets and performance targets.

Preliminary analytical procedures may include amongst other the following activities:

- Comparison of current year expenditure with budget and previous year figures;
- Comparison of current year expenditure in relation to KPI's as compared to previous year expenditure in relation to KPI's;
- Comparison of elements in the current period's financial statements with corresponding relationship with previous year's financial statements (i.e. expense by type as a percentage of total expenditure);
- Comparing amounts spent as percentage of total budget with the level of physical execution of the work;
- Comparing actual monthly budgetary expenditure to budget which may show that a significant part of the expenditure is incurred during a holiday period, thereby indicating the possible existence of a problem;
- Comparison of reported expenditure with development partner sources (i.e. for ADB Credit LFIS information); and
- Use of existing experience of similar projects to develop an expectation of values of expenses.

Once the preliminary analytical review is carried out, it will have to be repeated at the final analytical review stage if the figures have changed significantly. In other cases, the final ratios of the current year should be compared to the preliminary ones, with an explanation being given of changes arising during the course of the audit.

Preliminary analytical review will not always provide audit assurance of it, but may be used as an introduction to extensive analytical review, which forms part of substantive audit testing.

The most important point to note is that a conclusion to the work is required. This will normally be expressed in terms of whether any particular problems have been identified or whether there are any particular areas of the client's operations that require more detailed investigation.

2.2.5 Team discussion for risk assessment and planning purposes

The team leader and other key members of the FAPAD engagement team shall be involved in planning the audit, including planning and participating in the discussion among engagement team members as required by ISSAI 2300.

The discussion among the engagement team about the susceptibility of the Project's financial statements to material misstatement provides an opportunity for more experienced engagement team members, including the DG of FAPAD, to share their insights based on their knowledge of the entity. It also assists the engagement team members to gain a better understanding of the potential for material misstatement of the financial statements in the specific areas assigned to them, and to understand how the results of the audit procedures that they perform may affect other aspects of the audit including the decisions about the nature, timing and extent of further audit procedures.

As part of the discussion among the engagement team, consideration of the disclosure requirements of the applicable financial reporting framework assists in identifying early in the audit where there may be risks of material misstatement in relation to disclosures.

ISSAI 2240 provides further requirements and guidance in relation to the discussion among the engagement team about the risks of fraud. The discussion shall place particular emphasis on:

- How and where the Project's financial statements (including disclosures) may be susceptible to material misstatement due to fraud, including how fraud might occur;
- How management could perpetrate and conceal fraudulent financial reporting;
- How the assets of the Project could be misappropriated; and
- How fraud might be perpetrated or concealed by omitting or presenting incomplete or inaccurate disclosures.
- How management may attempt to present disclosures in a manner that may obscure a proper understanding of the matters disclosed (for example, by including too much immaterial information or by using unclear or ambiguous language).
- How management's involvement in overseeing employees with access to cash or other assets susceptible to misappropriation.

Many small Project audits are carried out entirely by one responsible person of FAPAD without involvement of any other personnel. In such situations, it is the person who, having conducted the planning of the audit would be responsible for considering the susceptibility of the Project's financial statements to material misstatement due to fraud or error.

2.2.6 Audit Strategy and Audit Plan

ISSAI 2300 deals with the auditor's responsibility to plan an audit of financial statements. As per paragraph 2 of ISSAI 2300, planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. Adequate planning benefits the audit of financial statements in several ways, including the following:

- Helping the auditor to devote appropriate attention to important areas of the audit.
- Helping the auditor to identify and resolve potential problems on a timely basis.
- Helping the auditor to organize properly and manage the audit engagement so that it is performed in an effective and efficient manner.
- Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks, and the proper assignment of work to them.
- Facilitating the direction and supervision of engagement team members and review of their work.
- Assisting, where applicable, in coordination of work done by auditors of components and experts.

As per ISSAI 2300 paragraphs 7 to 10, the auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit and that guides the development of the audit plan. In establishing the overall audit strategy, the auditor shall:

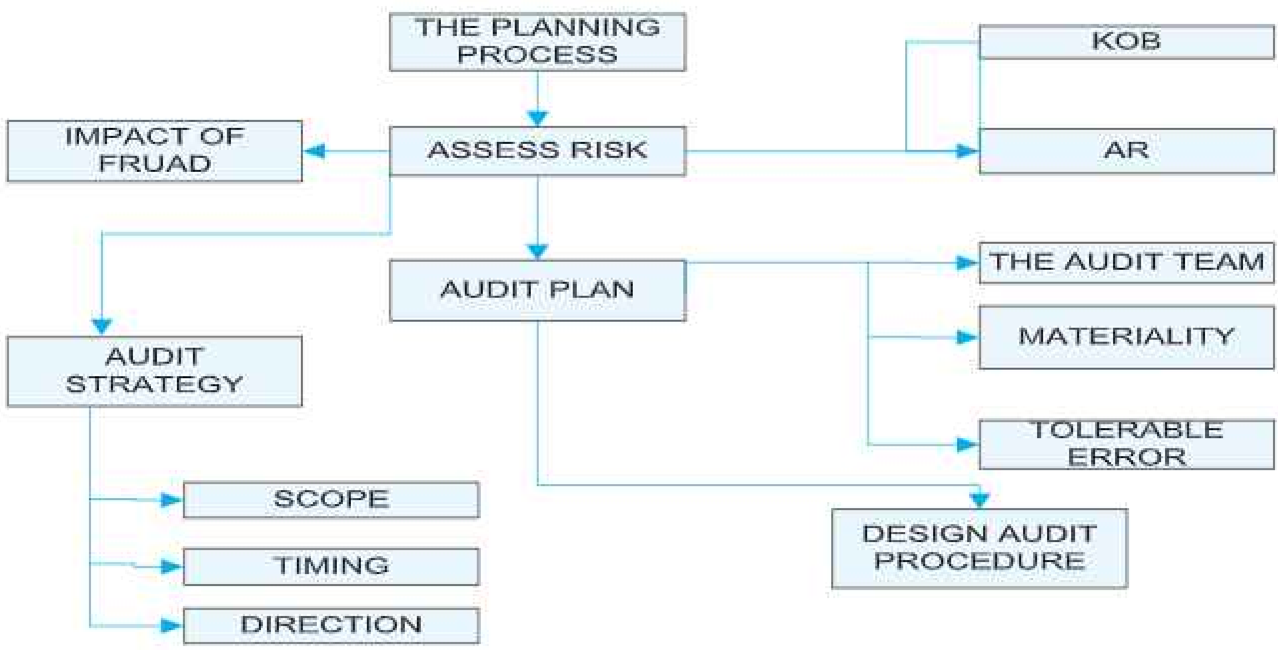
(a) Identify the characteristics of the engagement that define its scope;
(b) Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required;
(c) Consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts;
(d) Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant; and
(e) Ascertain the nature, timing and extent of resources necessary to perform the engagement.

The process of establishing the overall audit strategy assists the auditor to determine, subject to the completion of the auditor's risk assessment procedures, such matters as:

- The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas or the involvement of experts on complex matters;
- The amount of resources to allocate to specific audit areas or the audit budget in hours to allocate to high risk areas;
- When these resources are to be deployed, such as whether at an interim audit stage or at key cutoff dates; and
- How such resources are managed, directed and supervised and whether to complete engagement quality control reviews.

Once the overall audit strategy has been established, an audit plan can be developed to address the various matters identified in the overall audit strategy, taking into account the need to achieve the audit objectives through the efficient use of the auditor's resources. The establishment of the overall audit strategy and the detailed audit plan are not necessarily discrete or sequential processes, but are closely inter-related since changes in one may result in consequential changes to the other.

The audit plan is more detailed than the overall audit strategy and includes the nature, timing and extent of audit procedures to be performed by engagement team members. Planning for these audit procedures takes place over the course of the audit as the audit plan for the engagement develops. For example, planning of the auditor's risk assessment procedures occurs early in the audit process. However, planning the nature, timing and extent of specific further audit procedures depends on the outcome of those risk assessment procedures. In addition, the auditor may begin the execution of further audit procedures for some classes of transactions, account balances and disclosures before planning all remaining further audit procedures.



The auditor shall develop an audit plan that shall include a description of:

(a) The nature, timing and extent of planned risk assessment procedures;

(b) The nature, timing and extent of planned further audit procedures at the assertion level; and

(c) Standard audit programs and audit completion checkliststhat are required to be carried out.

The nature and extent of planning activities will vary according to the size and complexity of the entity, the key engagement team members' previous experience with the Project, and changes in circumstances that occur during the audit engagement.

As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and thereby the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks.

Considerations Specific to Smaller Projects

In audits of small projects, the entire audit may be conducted by a very small engagement team. Many audits of small projects may involve only one person without any other engagement team members. With a smaller team, co-ordination of, and communication between, team members are easier. Establishing the overall audit strategy for the audit of a small Project need not be a complex or time-consuming exercise; it varies according to the size of the Project, the complexity of the audit, and the size of the engagement team. For example, a brief memorandum prepared at the completion of the previous audit, based on a review of the working papers and highlighting issues identified in the audit just completed, updated in the current period based on discussions with the Project management, can serve as the documented audit strategy for the current audit engagement if it covers the related matters.

Refer to Appendix 6 for a pro forma Audit Strategy and Planning Document template

2.2.7 Consideration of fraud in audit and applying professional scepticism

Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional. ISSAI 2240 '*The Auditor's Responsibility Relating to Fraud in an Audit of Financial Statements*' provides detailed guidance on their responsibility to consider fraud at all stages during the course of the audit.

Although fraud is a broad legal concept, for the purposes of the financial audit, the auditor is concerned with fraud that causes a material misstatement in the financial statements. Two types of intentional misstatements are relevant to the auditor:

i. Misstatements resulting from fraudulent financial reporting; and
ii. Misstatements resulting from misappropriation of assets.

Although the auditor may suspect or identify the occurrence of fraud, but the auditor normally does not make legal determinations of whether fraud has actually occurred. Accordingly, if any FAPAD auditor has identified or suspected a fraud, he/she should promptly bring this to the attention of the Director or the DG.

The primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the Project and its management. It is important that management, with the oversight of those charged with governance, place a strong emphasis on fraud prevention, which may reduce opportunities for fraud to take place, and fraud deterrence, which could persuade individuals not to commit fraud because of the likelihood of detection and punishment. This involves a commitment to create a culture of honesty and ethical behavior which can be reinforced by an active oversight by those charged with governance. Oversight by those charged with governance includes considering the potential for override of controls or other inappropriate influence over the financial reporting process, especially when the Project Director is the only person with authority to incur expenses or make payments.

An auditor conducting an audit in accordance with INTOSAI standards 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. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the require auditing standards such as ISSAIs.

The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error. This is because fraud may involve sophisticated and carefully organized schemes designed to conceal it, such as forgery, deliberate failure to record transactions, or intentional misrepresentations being made to the auditor. Such attempts at concealment may be even more difficult to detect when accompanied by collusion. Collusion may cause the auditor to believe that audit evidence is persuasive when it is, in fact, false.

Furthermore, the risk of the auditor not detecting a material misstatement resulting from management fraud is greater than for employee fraud, because management is frequently in a position to directly or indirectly manipulate accounting records, present fraudulent financial information or override control procedures designed to prevent similar frauds by other employees.

When obtaining reasonable assurance, the auditor is responsible for maintaining professional skepticism throughout the audit, considering the potential for management override of controls and recognizing the fact that audit procedures that are effective for detecting error may not be effective in detecting fraud.

Unless the auditor has reason to believe the contrary, the auditor may accept records and documents as genuine. If conditions identified during the audit made the auditor to believe that a document may not be authentic or that terms in a document have been modified but not disclosed to the auditor, the auditor shall investigate further.

Refer to Appendix 7 for Fraud Risk Factor as specified in ISSAI 2240

2.2.8 Understanding the Project's Internal Control

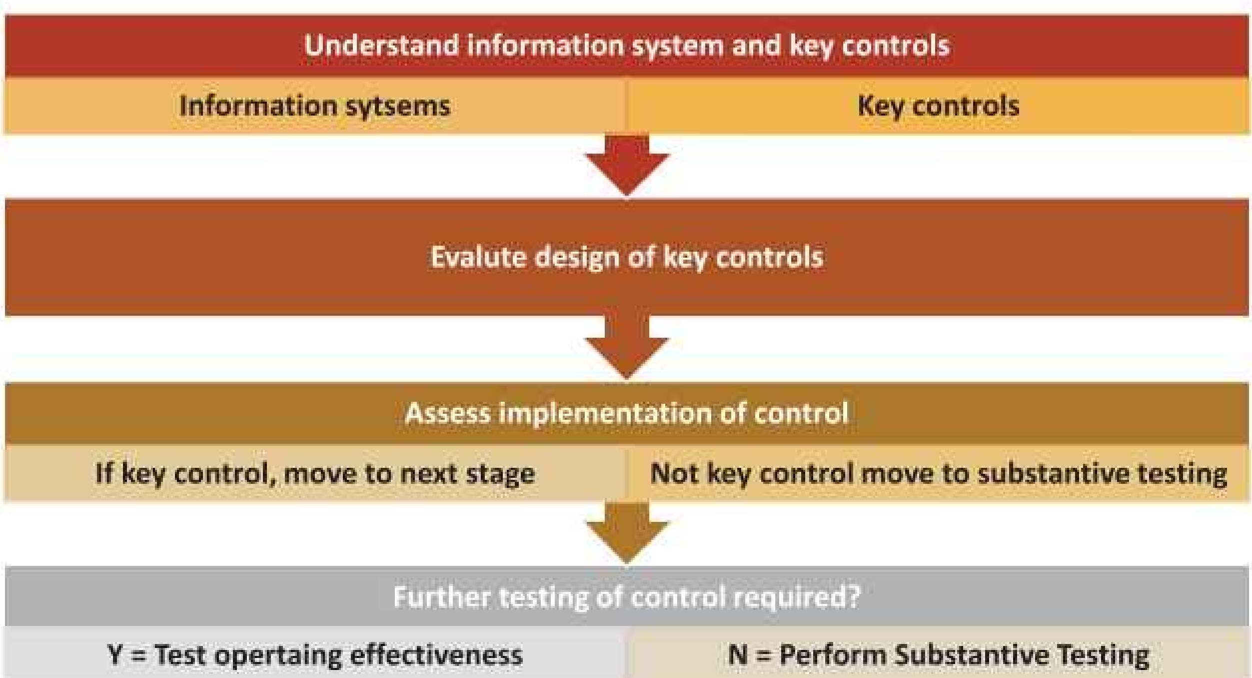
Internal control is designed, implemented and maintained to address identified business risks that threaten the achievement of any of the Project's objectives that concern:

- The reliability of the Project's financial reporting;
- The effectiveness and efficiency of its operations; and
- Its compliance with applicable laws and regulations.

As per ISSAI 2315 paragraphs 12-14, the auditor shall obtain an understanding of internal control and control environment relevant to the audit. Although most controls relevant to the audit are likely to relate to financial reporting, not all controls that relate to financial reporting are relevant to the audit. It is a matter of the auditor's professional judgment whether a control, individually or in combination with others, is relevant to the audit.

When obtaining an understanding of controls that are relevant to the audit, the auditor shall evaluate the design of those controls and determine whether they have been implemented, by performing procedures in addition to inquiry of the Project's personnel.

Evaluating the design of a control involves considering whether the control, individually or in combination with other controls, is capable of effectively preventing, or detecting and correcting, material misstatements. Implementation of a control means that the control exists and that the entity is using it. There is little point in assessing the implementation of a control that is not effective, and so the design of a control is considered first. An improperly designed control may represent a significant deficiency in internal control.



Risk assessment procedures to obtain audit evidence about the design and implementation of relevant controls may include:

- Inquiring of entity personnel.
- Observing the application of specific controls.
- Inspecting documents and reports.
- Tracing transactions through the information system relevant to financial reporting (i.e. walk through test).

As per ISSAI 2315, the division of internal control into the following five components provides a useful framework for auditors to consider how different aspects of an entity's internal control may affect the audit:

(a) Control environment;
(b) Risk assessment process;
(c) Information system, including the related business processes, relevant to financial reporting, and communication;
(d) Control activities; and
(e) Monitoring of controls.

Each of these five components is described below:

1) Control Environment

The purpose of understanding the control environment is to understand whether, Project management with the oversight of those charged with governance (i.e. EA/IA/Line Ministry), has created and maintained a culture of honesty and ethical behaviour and the strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control.

2) The Project's risk assessment process

The Project's risk assessment process forms the basis for how management determines the risks to be managed. If that process is appropriate to the circumstances, including the nature, size and complexity of the Project, it assists the auditor in identifying risks of material misstatement. For example, the Project's risk assessment process may address how the Project considers the possibility of unrecorded transactions or identifies and analyzes significant estimates.

3) Monitoring of controls

Monitoring of controls is a process to assess the effectiveness of internal control performance over time. It involves assessing the effectiveness of controls on a timely basis and taking necessary remedial actions. Management accomplishes monitoring of controls through ongoing activities, separate evaluations, or a combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of an entity and include regular management and supervisory activities.

4) Control activities

Control activities are the policies and procedures that help ensure that management directives are carried out. Control activities, whether within IT or manual systems, have various objectives and are applied at various organizational and functional levels. Examples of specific control activities include those relating to the following:

- Authorization.
- Performance reviews.
- Information processing.
- Physical controls.
- Segregation of duties.

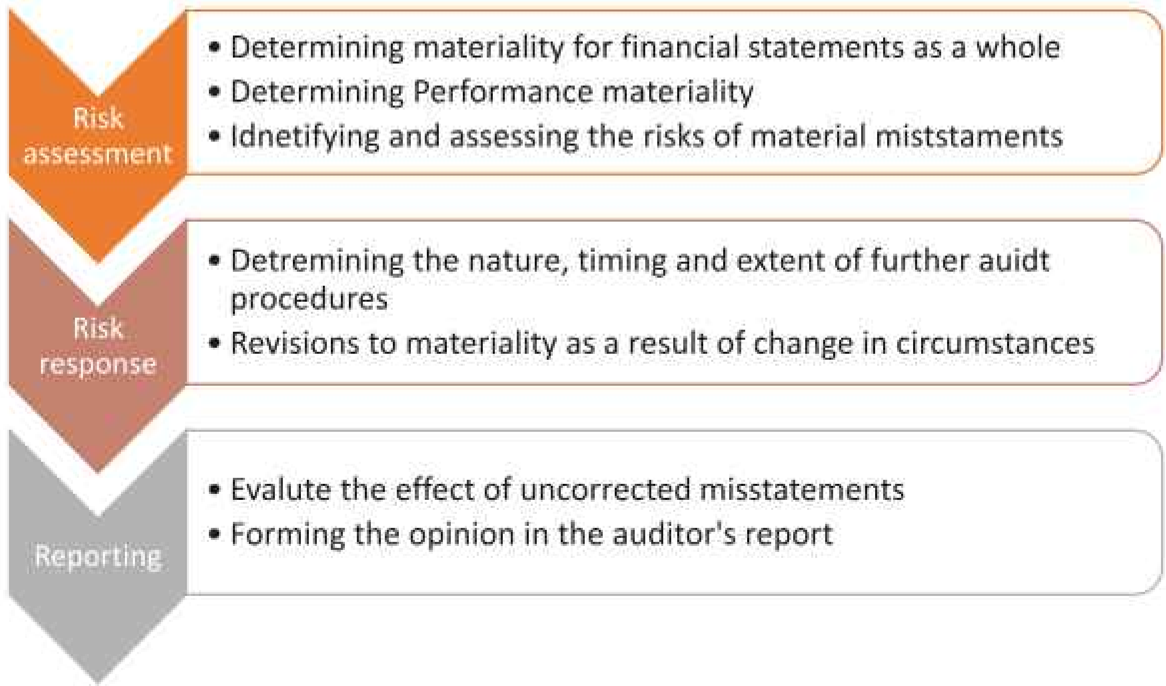
5) The information system

The information system relevant to financial reporting objectives, which includes the accounting system, consists of the procedures and records designed and established to:

- Initiate, record, process, and report Project transactions (as well as events and conditions) and to maintain accountability for the related assets, liabilities, and equity;
- Resolve incorrect processing of transactions, for example, automated suspense files and procedures followed to clear suspense items out on a timely basis;
- Process and account for system overrides or bypasses to controls;
- Transfer information from transaction processing systems to the general ledger;
- Capture information relevant to financial reporting for events and conditions other than transactions, such as the depreciation and amortization of assets and changes in the recoverability of accounts receivables; and
- Ensure information required to be disclosed by the applicable financial reporting framework is accumulated, recorded, processed, summarized and appropriately reported in the financial statements.

The understanding of the information system relevant to financial reporting is a matter of the auditor's professional judgment. An information system consists of infrastructure (physical and hardware components), software, people, procedures, and data. Many information systems make extensive use of information technology (IT).

2.2.9 Materiality for planning purpose and performance materiality



After gathering relevant information to gain knowledge of the Project, the auditor needs to consider materiality, which is one of the key parameters that affect the audit strategy. The auditor needs to ensure that the audit efforts are concentrated on those areas and account components which are material.

Materiality is one of the basic and major concepts of auditing, central to planning and performing the audit, evaluating the effect of identified misstatements on the financial statements, and in forming the audit opinion. It is not possible for the auditor to form an opinion on financial statements without considering materiality.

Financial statements can rarely be absolutely correct and even if this were the case the user is unlikely to require this level of precision. A degree of tolerance in their accuracy is, therefore, accepted and this is recognized in the "properly presents", "presents fairly" and "true and fair" opinions that the auditor gives on most of the financial statements that he or she audits.

As per the definition provided in ISSAI 2320, materiality is defined as "misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements".

In other words, a matter may be judged material if knowledge of it would be likely to influence the decisions of intended users. The concept of materiality recognises that some matters are important, either individually or in aggregate, and others are not. Materiality is often considered in terms of value but the inherent nature of characteristics of an item may also render a matter material.

Therefore, materiality is divided into two categories namely; quantitative and qualitative materiality.

Quantitative materiality is referred when judgments about materiality are made in light of surrounding circumstances and are affected by the size or value of financial statement values.

Qualitative materiality is used when the judgments are measured in terms of the nature of the item in question. For example, procurement by a particular project may not be material in terms of the total value of the financial statements but may be deemed material because of poor procedural practices in past years or a development partner requirement to review all procurements or lack of rationale.

The concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report. Therefore, the auditor shall set levels of materiality for the audit of Project's financial statements as follows:

1. Determine materiality for the financial statements as a whole; and
2. Determine performance materiality.

Determine materiality for the financial statements as a whole
Given the nature of Projects being audited by FAPAD which are mostly not for profit and IPSAS Cash basis of Accounting is used, the benchmark for setting the materiality threshold will be total fund receipts or expenditure incurred during the period under audit. The threshold will be normally within 1% ~ 3% of the total amount of funds received or expenditure incurred during the period.

Once established, the overall materiality amount becomes the standard by which the ultimate success or failure of the audit will be judged. For example, assuming that overall materiality was set at an amount of BDT 20,000. If as a result of performing audit procedures:

- No errors were found — an unqualified opinion would be provided.
- Uncorrected errors exceeding materiality (of BDT 20,000) were found and the Project management was unwilling to make the necessary adjustments — a qualified or adverse opinion would be required.
- Uncorrected errors exceeding materiality (of BDT 20,000) exist in the financial statements but were not detected by the auditor — an inappropriate unqualified audit opinion may be issued.

Determine performance materiality

The auditor shall determine performance materiality for the purposes of assessing the risks of material misstatement and determining the nature, timing and extent of further audit procedures. Auditor shall determine performance materiality at an amount (or amounts) that reduces to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in the financial statements exceeds materiality for the financial statements as a whole (the aggregation risk).

The choice of performance materiality levels will depend on the detection risk of material misstatement: the higher the detection risks the lower the level of performance materiality, leading to more tests of controls or substantive procedures (and vice versa). Hence, there is an "inverse" relationship between performance materiality and detection risks of material misstatement.

Setting an appropriate amount for performance materiality will ensure that more work is performed, which increases the likelihood that misstatements (if they exist) will be identified. For example, if overall materiality was BDT 20,000 and audit procedures were planned to detect all errors in excess of BDT 20,000, it is quite possible that an error of say BDT 8,000 would go undetected. If three such errors existed, amounting to BDT 24,000, the financial statements would be materially misstated. However, if performance materiality was set at BDT 12,000, it would be much more likely that at least one or all of the BDT 8,000 errors would be detected. Even if only one of the three errors was identified and corrected, the remaining misstatement of BDT 16,000 would be less than the overall materiality and the financial statements as a whole would not be materially misstated.

Setting an appropriate amount for performance materiality involves the exercise of professional judgment and is not a simple mechanical calculation such as a percentage (for example 50%) of the overall materiality level. However, based on the particular circumstances of the entity being audited, it could be set as a single amount for the financial statements as a whole, or at individual amounts for particular balances, transactions and disclosures. An example is given below:

Benchmark	Amount	Percentage used	Materiality Amount
At Financial Statements level			
Total receipts	10,000,000	2% (normally between 1% to 3%)	200,000
At Class of Transaction level			
Travel	500,000	1%	5,000
Employee costs	1,000,000	2%	20,000

From the above example, any travel expenditure misstatement above BDT5000 will be considered material. However, in comparison with materiality for the financial statements as whole, the misstatement may not be material but could still influence the decisions of users of the financial statements; travel expenses could be a critical area of expenditure.

The overall materiality is further allocated as 'Performance Materiality" which normally range between 50% to 75% of the overall materiality.

Refer to Appendix 8 for Illustrative Factors for Consideration of Materiality

2.2.10 Risk Assessment (audit risk = inherent x control x detection)

The auditor shall design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level. The auditor obtains reasonable assurance by obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level. Audit risk is the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated.

Audit risk is a function of the risks of material misstatement (The risk that the financial statements are materially misstated prior to audit) and detection risk.

*Detection risk is th*e risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

Therefore, Audit risk is the product of the following risk factors:
Audit Risk ("AR") = Risk of material misstatement ("RoMM") x Detection Risk ("DR")

The risks of material misstatement at the assertion level consist of two components: inherent risk and control risk. Inherent risk and control risk are the entity's risks; they exist independently of the audit of the financial statements.

Risk of material misstatement ("RoMM") = Inherent Risk ("IR") x Control Risk ("CR")
Auditing Standards do not ordinarily refer to inherent risk and control risk separately, but rather to a combined assessment of the "risks of material misstatement."

Inherent risk is the risk of misstatement through susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls to prevent or detect and correct such misstatements.

Control risk is the risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's internal control.

Auditor need to manage the Audit Risk and bring it down to the acceptable level to avoid the risk of issuing an inappropriate audit opinion. Detection risk arises partly from uncertainties that exist when the auditor does not examine 100% of transactions and balances, and partly from uncertainties that exist even if the auditor were to carry out a 100% examination some material misstatements remain undetected. The way to minimize Detection Risk or to manage Audit Risk auditor will change the nature, extent and timing of the audit procedures as illustrated below.

The auditor's assessment of the components of audit risk may change during the course of an audit. For example, information may come to the auditor's attention when he/she performing substantive procedures that differ significantly from information on which the auditor originally assessed inherent and control risks. In such cases the auditor would modify the planned substantive procedures based on a revision of the assessed levels of inherent and control risks.

Regardless of the assessed levels of inherent and control risks, the auditor should perform some substantive procedures on material account balances and classes of transactions. The higher the assessment of inherent and control risks the more audit evidence the auditor should obtain from the performance of substantive procedures. When both inherent and control risks are assessed as high the auditor needs to consider whether or not substantive procedures can provide sufficient and appropriate audit evidence to reduce detection risk and, therefore, audit risk to an acceptably low level.

2.2.11 Audit assertions

In the context of financial audit, Assertions are defined as representations by management that are embodied in the financial statements and used by the auditor to consider the different types of potential misstatements that may occur.

As described in the earlier section of the manual, FAPAD audit team shall perform risk assessment procedures to obtain an understanding of the Project and its environment, including the Project's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error, at both the financial statement and assertion levels. Assertions used by the auditor in considering the different types of potential misstatements may fall into the following categories:

(a) Assertions about classes of transactions and events, and related disclosures, for the period:

(i) Occurrence—transactions and events that have been recorded or disclosed, have occurred, and such transactions and events pertain to the entity. For example, for payroll an employee being paid by the Project is a genuine employee of the Project and not a ghost employee.
Relevant test – select a sample of entries from the salary register and trace the employee to the other records and also check physically where that employee is working.

(ii) Completeness—all transactions and events that should have been recorded and all related disclosures that should have been included in the financial statements have been included. For example, payroll transactions of 12 months are posted to the ledger during the year.
Relevant test – select a sample of monthly payroll transactions and check with bank statements as well as posting to the general ledger.

(iii) Accuracy— this means that there have been no errors while preparing documents or in posting transactions to ledgers, amounts and other data relating to recorded transactions and events have been recorded appropriately, and related disclosures have been appropriately measured and described. For example: the amount paid agrees to the invoice, the correct amount was paid in accordance with the contract and the invoice was checked against the purchase order; and once the matching was satisfactory only then it was paid.
Relevant test – re performance of calculations on payroll, contractor payment etc, and the review of control account reconciliations are designed to provide assurance about accuracy.

(iv) Cut-off—transactions and events have been recorded in the correct accounting period. For example, a payment made to Project Contractor on 30 June 2018 should be charged to the financial year ended 30 June 2018 and not the financial year ended 30 June 2019.
Relevant test –Tracing last purchase of goods from contractor to purchase invoices to ensure that goods received before the year–end are recorded in purchasing at the year end.

(v) Classification- Transactions and events have been recorded in the proper accounts. For example, an item of income or expenditure is charged to the correct account/budget/economic code.
Relevant test – check purchase invoices postings to nominal ledger accounts.

(vi) Presentation- This means that the descriptions and disclosures of transactions are relevant and easy to understand. There is a reference to transactions being appropriately aggregated or disaggregated. Aggregation is the adding together of individual items. Disaggregation is the separation of an item, or an aggregated group of items, into component parts. The notes to the financial statements are often used to disaggregate totals shown in the statement of profit or loss. Materiality needs to be considered when judgements are made about the level of aggregation and disaggregation. Related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.
Relevant test – confirm that the total employee benefits expense is analysed in the notes to the financial statements under separate headings– i.e. wages and salaries, pension costs, social security contributions and taxes, etc.

(b) Assertions about account balances, and related disclosures, at the period end (i.e. balance sheet):
(i) Existence— means that assets and liabilities really do exist and there has been no overstatement – for example, by the inclusion of fictitious receivables or inventory. This assertion is very closely related to the *occurrence* assertion for transactions.
Relevant tests – physical verification of non–current assets, circularization of receivables, payables and the bank letter.

(ii) Rights and obligations—the Project holds or controls the rights to assets, and liabilities are the obligations of the Project. For example, contingent liabilities note includes only material cases that pertain to the Project.
Relevant tests – in the case of property, deeds of title can be reviewed. Current assets are often agreed to purchase invoices although these are primarily used to confirm cost. Long term liabilities such as loans can be agreed to the relevant loan agreement.

(iii) Completeness—all assets, liabilities and equity interests that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included. In other words, there has been no understatement of assets or liabilities.
Relevant tests – A review of the repairs and expenditure account can sometimes identify items that should have been capitalised and have been omitted from non–current assets. Reconciliation of payables ledger balances to suppliers' statements is primarily designed to confirm completeness although it also gives assurance about existence.

(iv) Accuracy, valuation and allocation—assets, liabilities, and equity interests have been included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments have been appropriately recorded, and related disclosures have been appropriately measured and described. For example, a contingent liability is disclosed in an account note on the basis that there is a high likelihood that the court case involving a payment dispute with the Project Contractor may be lost within the next year that would result in a payment being made. The estimated value is based on expert legal advice.
Relevant tests – Vouching the cost of assets to purchase invoices and checking depreciation rates and calculations.

(v) Classification—assets, liabilities and equity interests have been recorded in the proper accounts. For example, a segmental note reflects the way the audited entity is structured and significant allocation and apportionment methodologies are explained in the note.
Relevant tests – the test for transactions of checking purchase invoice postings to the appropriate accounts in the general ledger will be relevant again.

(vi) Presentation— this means that the descriptions and disclosures of assets, liabilities and equity interests are appropriately aggregated or disaggregated and clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.
Relevant tests – auditors often use disclosure checklists to ensure that financial statement presentation complies with accounting standards and relevant legislation. These cover all items (transactions, assets, liabilities and equity interests) and would include for example confirming that disclosures relating to non–current assets include cost, additions, disposals, depreciation.

(c) Assertions about other disclosures
The assertions may also be used by the auditor in considering the different types of potential misstatements that may occur in disclosures not directly related to recorded classes of transactions, events, or account balances. As an example of such a disclosure, the Project may be required to describe its exposure to risks arising from financial instruments, including how the risks arise; the objectives, policies and processes for managing the risks; and the methods used to measure the risks. As per ISSAI, an auditor is required to consider risk of material misstatements at the assertion level for classes of transactions, account balances and disclosures to determine the nature, timing and extent of further audit procedures necessary to obtain sufficient and appropriate audit evidence. The auditor uses relevant assertions for considering different types of potential misstatements and thereafter design and perform appropriate audit procedures.

Relationship between assertion and risk

STEP 1: Identify the risk that will cause material misstatement at the assertion level

The identified risk that will cause material misstatements in the financial statement should relate to the assertion being affected because of risk, which will also provide clarity in terms of designing the audit procedures

STEP 2: Identify the assertion to be tested

Audit procedures are designed and performed to test financial statement assertions based on assessed risks of material misstatements. Therefore, the second step in designing the audit procedure is to identify the assertion that needs to be tested.

STEP 3: Design audit procedures

The next step is to design the appropriate audit procedure to test the assertion and detect material misstatement in the financial statements because of the risk identified in Step 1. The audit procedures can take the form of tests of controls or substantive tests.

Financial Statement Assertions and examples

Transactions and Events

For a transaction such as the purchase of office equipment, the management is asserting that:

Occurrence: The purchase really did take place.

Completeness: All purchase transactions are included in the financial statements.

Accuracy: The quantities and prices are correctly stated.

Cut-off: The transaction was dealt with in the correct accounting period.

Classification: It really is a purchase of equipment, not a payroll cost or a motor vehicle and it has been accounted for accordingly.

Compliance: The payment of travel allowance was made in accordance with travel regulations.

Account balances at the year end

For account balances at the year end, the assertions are slightly different, because the things about which the assertions are made are different:

Existence

- Are all these motor vehicles, office equipment, land and buildings, inventories real? Do they exist?
- Are these trade receivables real? Have we sold them something for which they owe us money?
- Was something actually bought from these trade payables and do we really owe them some money?

Rights and obligations

- Do we own the factory? The car? The computer?
- The trade receivables may exist, but have we pledged them or otherwise transferred our rights?

Accuracy, Valuation and allocation

- Has depreciation been calculated correctly on the non-current assets?
- Are the trade debtors going to pay us?
- Is the inventory damaged, slow moving or obsolete?

2.2.12 Assessment of IT General Control

Testing IT General Control on areas such as related policies and procedures, IT access rights, physical and logical security of IT equipment, criticality of IT, changes and upgrades, business continuity and disaster recovery plan etc. are quite important factor if IT is considered critical for the entity. Accordingly, FAPAD audit team should assess criticality of IT on the operation of the Project.

If the Project has large scale dependency on IT, the audit team shall assess IT General Control while conducting the audit of that Project. This should cover the following key elements of IT general control:

1. Access to programs and data
2. Program changes
3. Computer operations
4. Program development
5. End-user computing

Each of the above five elements are described below:

1. Access to programs and data

The audit team shall determine whether adequate controls for access to programs and data have been established to reduce the risk of unauthorized/inappropriate access to the relevant information systems related to financial reporting. The audit team shall consider controls associated with the programs and data access components for each relevant application such as information security policy / user awareness, physical access and configuration of access rules, Access administration, Identification and authentication, Monitoring, Super user/administrator ID, etc.

2. Program changes

The audit team should determine whether adequate controls for program changes have been established to ensure that changes to existing systems/applications are authorized, tested, approved, properly implemented and documented. Audit team shall also assess any changes to the configuration setting which may impact the design, implementation and/or operating effectiveness of application controls. Audit team to assess whether management has controls in place related to testing, validating and approving system and application configuration changes to reduce the risk that changes in the configurations have a negative impact on the design, implementation and/or operating effectiveness of application controls.

3. Computer operations

The auditor shall determine whether adequate controls for computer operations have been established to ensure that system/application processing is appropriately authorized and scheduled and deviations from scheduled processing are identified and resolved. The audit team should give particular attention to check whether management has controls in place over the design and execution of system jobs to ensure accuracy, completeness, and timely processing of system jobs, including batch jobs and interfaces, for relevant information systems related to financial reporting and appropriate backup and recovery procedures are implemented.

4. Program development

Check whether adequate controls for program development have been established to ensure that new systems/applications which are developed or acquired are authorized, tested, approved, properly implemented and documented. Program development often involves converting data from an old application or system before it can be used within the new application or system. Audit team should check whether management has controls in place to ensure that data conversion relevant to financial reporting is accurate and complete.

5. End-user computing

End-user computing (e.g., spreadsheets and other user-developed programs) provides a unique set of general control needs within an entity. By its nature, end-user computing brings the development and processing of information systems closer to the user. The auditor shall determine whether management has implemented appropriate policies and procedures to ensure IT general controls are properly applied to end-user computing environment.

Chapter Three

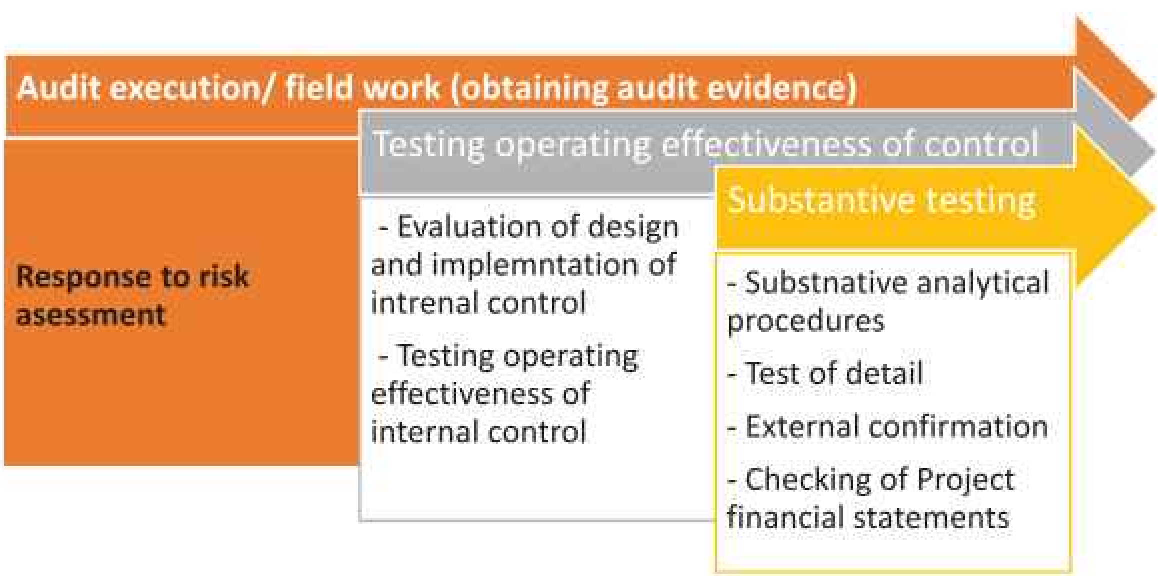
Audit execution/fieldwork






Audit execution/fieldwork

As per auditing standards, after planning phase the auditor shall perform the planned audit procedures to obtain audit evidence and evaluate audit evidence and draw conclusions. We have structured this chapter to include key audit steps required during the conduct of audit.



3.1 Audit procedures for various types of audit evidence

The audit evidence to draw reasonable conclusions on which to base the auditor's opinion collected from risk assessment procedures and further audit procedures comprising both tests of controls and substantive procedures, including tests of details and substantive analytical procedures. Various types of audit techniques that may be used by the auditor to obtain audit evidence include:

Inspection

Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production. An example of inspection used as a test of controls is inspection of records for evidence of authorization. Some documents represent direct audit evidence of the existence of an asset, for example, a document constituting a financial instrument such as a stock or bond. Inspection of such documents may not necessarily provide audit evidence about ownership or value. Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the Project's rights and obligations or the valuation of the assets.

Observation

Observation consists of looking at a process or procedure being performed by others, for example, the auditor's observation of inventory counting by the entity's personnel, or of the performance of control activities. Observation provides audit evidence about the performance of a process or procedure, but is limited to the point in time at which the observation takes place, and by the fact that the act of being observed may affect how the process or procedure is performed.

External Confirmation

An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium. External confirmation procedures frequently are relevant when addressing assertions associated with certain account balances and their elements. However, external confirmations need not be restricted to account balances only. For example, the auditor may request confirmation of the terms of agreements or transactions an entity has with third parties; the confirmation request may be designed to ask if any modifications have been made to the agreement and, if so, what the relevant details are. External confirmation procedures also are used to obtain audit evidence about the absence of certain conditions, for example, the absence of a "side agreement" that may influence revenue recognition.

Recalculation

Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.

Re-performance

Re-performance involves the auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal control.

Analytical Procedures

Analytical procedures consist of evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

Inquiry

Inquiry consists of seeking information of knowledgeable persons, both financial and non-financial, within the entity or outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures. Inquiries may range from formal written inquiries to informal oral inquiries. Evaluating responses to inquiries is an integral part of the inquiry process.

Responses to inquiries may provide the auditor with information not previously possessed or with corroborative audit evidence. Alternatively, responses might provide information that differs significantly from other information that the auditor has obtained, for example, information regarding the possibility of management override of controls. In some cases, responses to inquiries provide a basis for the auditor to modify or perform additional audit procedures. In respect of some matters, the auditor may consider it necessary to obtain written representations from management and, where appropriate, those charged with governance to confirm responses to oral inquiries.

3.2 Sampling

In selecting items for testing, the auditor is required to determine the relevance, reliability and effectiveness (sufficiency) of information to be used as audit evidence. The means available to the auditor for selecting items for testing are; selecting all items (100% examination), selecting specific items, and audit sampling.

The application of any one or combination of the above three means may be appropriate depending on the particular circumstances.

a. Selecting All Items

The auditor may decide that it will be most appropriate to examine the entire population of items that make up a class of transactions or account balance when, for example:

- The population constitutes a small number of large value items;
- There is a significant risk and other means do not provide sufficient appropriate audit evidence;
- The repetitive nature of a calculation or other process performed automatically by an information system makes a 100% examination cost effective.

b. Selecting Specific Items

The auditor may decide to select specific items from a population. In making this decision, factors that may be relevant include the auditor's understanding of the Project, the assessed risks of material misstatement, and the characteristics of the population being tested. The judgmental selection of specific items is subject to non-sampling risk. Specific items selected may include:

- *High value or key items:* The auditor may decide to select specific items within a population because they are of high value, or exhibit some other characteristic, for example, items that are suspicious, unusual, and particularly risk-prone or that have a history of error.

- *All items over a certain amount*: The auditor may decide to examine items whose recorded values exceed a certain amount so as to verify a large proportion of the total amount of a class of transactions or account balance.

c. *Audit Sampling*

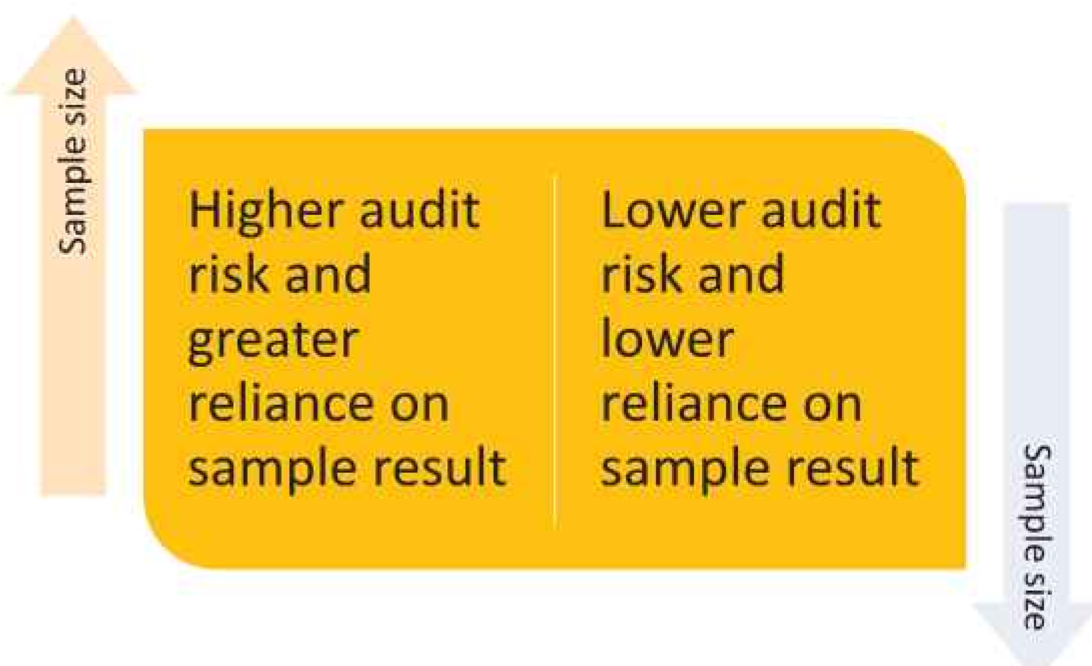
Audit sampling is designed to enable conclusions to be drawn about an entire population on the basis of testing a sample drawn from it.

ISSAI 2530 defines sampling as "The application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population."

Audit sampling enables the auditor to obtain and evaluate audit evidence about some characteristic of the items selected in order to form or assist in forming a conclusion concerning the population from which the sample is drawn. When performing audit sampling, the auditor performs audit procedures to obtain evidence that the population from which the audit sample is drawn is complete.

The results of audit procedures applied to a sample of items within a section can only be projected to the items that make up that section. To draw a conclusion on the entire population, the auditor will need to consider the risk of material misstatement in relation to whatever other section make up the entire population. For example, 20% of the items in a population may make up 90% of the value of an account balance. The auditor may decide to examine a sample of these items. The auditor evaluates the results of this sample and reaches a conclusion on the 90% of value separately from the remaining 10%, on which a further sample or other means of gathering audit evidence will be used, or which may be considered immaterial.

The level of sampling risk that the auditor is willing to accept and importance given to the item being tested affects the sample size required. The greater reliance of the results and lower the risk the auditor is willing to accept, the higher sample size need to be selected, and vice versa.



The sample size can be determined by the application of a statistically-based formula or through the exercise of professional judgment.

With statistical sampling, sample items are selected in a way that each sampling unit has a known probability of being selected. With non-statistical sampling, judgment is used to select sample items. Because the purpose of sampling is to provide a reasonable basis for the auditor to draw conclusions about the population from which the sample is selected, it is important that the auditor selects a representative sample, so that bias is avoided, by choosing sample items which have characteristics typical of the population.

The principal methods of selecting samples are the use of random selection, systematic selection, haphazard selection, block selection and monetary unit sampling. Each of these methods is discussed below:

(a) Random selection (applied through random number generators, for example, random number tables). The use of this selection method ensures that all items in the population have an equal chance of being selected.

(b) Systematic selection, in which the number of sampling units in the population is divided by the sample size to give a sampling interval. For example, there is a population of 1,000 from which required sample will be 20 and hence the interval of sample will be 50. Having determined a starting point within the first 50, each 50th sampling unit thereafter is selected. When using systematic selection, the auditor would need to determine that sampling units within the population are not structured in such a way that the sampling interval corresponds with a particular pattern in the population.

(c) Monetary Unit Sampling is a type of value-weighted selection in which sample size, selection and evaluation results in a conclusion in monetary amounts. This type of statistical sample uses a monetary unit as a basis of selection (such as BDT) rather than a physical sample. One key advantage of using an MUS sample is that large items are automatically selected.

(d) Haphazard selection, in which the auditor selects the sample without following a structured technique, in other word with no particular reason for including or excluding particular items. Although no structured technique is used, the auditor would nonetheless avoid any conscious bias or predictability (for example, selecting or avoiding difficult to locate items, unusual items, items having unique characteristics, the first or last entries on a page, etc.) and thus attempt to ensure that all items in the population have a chance of selection.

(e) Block selection involves selection of a block(s) of contiguous items from within the population. For example, the auditor may examine all transaction of specific month (i.e. January) based on substantial expenditure or irregularities or risks observed in previous years.

If the auditor decides to use audit sampling as an approach, in designing the sample approach, the auditor should consider the purpose of the audit procedure and the characteristics of the population.

Evaluating sample results

Having carried out the audit procedures to each sample item, which are appropriate to the particular audit objective, the auditor should evaluate the sample results, the nature and cause of any deviations or misstatements identified, and their possible effect on the particular audit objective and other areas of the audit. Additionally, the auditors should evaluate whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

For tests of controls, an unexpectedly high sample error rate may lead to an increase in the assessed risk of material misstatement, unless further audit evidence substantiating the initial assessment is obtained.

For tests of details, an unexpectedly high misstatement amount in a sample may cause the auditor to believe that a class of transactions or account balance is materially misstated, in the absence of further audit evidence that no material misstatement exists.

In analyzing the errors detected in the sample, the auditor should first determine whether an item in question is in fact an error. In designing the sample, the auditor should define those conditions, which constitute an error by reference to the audit objectives. For example, in a test of details relating to the existence of accounts receivable, such as confirmation, payments made by the customer before the confirmation date but received shortly after that date by the client, are not considered a misstatement. Also, a misposting between customer accounts does not affect the total accounts receivable balance. Therefore, it may not be appropriate to consider this a misstatement in evaluating the sample results of this particular audit procedure, even though it may have an important effect on other areas of the audit, such as the assessment of the risk of fraud or the adequacy of the allowance for doubtful accounts.

In the case of tests of details, the projected misstatement plus anomalous misstatement, if any, is the auditor's best estimate of misstatement in the population. When the projected misstatement plus anomalous misstatement, if any, exceeds tolerable misstatement, the sample does not provide a reasonable basis for conclusions about the population that has been tested. The closer the projected misstatement plus anomalous misstatement is to tolerable misstatement, the more likely that actual misstatement in the population may exceed tolerable misstatement. Also if the projected misstatement is greater than the auditor's expectations of misstatement used to determine the sample size, the auditor may conclude that there is an unacceptable sampling risk that the actual misstatement in the population exceeds the tolerable misstatement. Considering the results of other audit procedures helps the auditor to assess the risk that actual misstatement in the population exceeds tolerable misstatement, and the risk may be reduced if additional audit evidence is obtained.

When the expected audit evidence regarding a specific sample item cannot be obtained, auditors may be able to obtain sufficient and appropriate audit evidence through performing alternative procedures. In analyzing the errors discovered, the auditors may observe that many have a common feature. For example, type of transaction, location, product line or period of time.

3.3 Computer Assisted Audit Techniques (CAAT)

Computer Assisted Audit Techniques ('CAATs') describes a variety of methods of using information technology in audits, ranging from simple automation of checks such as casting of totals through to sophisticated analyses which would not be practical without using software.

The use of CAATs may enable 100% tests of electronic transactions and account files to be performed efficiently. This may be particularly useful in responding to Significant Risks. CAATs can be used to automate a number of audit procedures, such as:

- Selection of statistically valid samples;
- Reperforming calculations;
- Reconciling the general ledger to sub-ledgers;
- Recalculating totals or subtotals in files;
- Analysing and summarising data;
- Developing expectations for substantive analytical procedures;
- Selection of items with particular characteristics in a balance.

CAATs can be used to select sample transactions from key electronic files, to sort transactions with specific characteristics, to test an entire population or to select a sample of transactions.

It is best practice to use a number of simple CAATs during audit testing to increase the effectiveness and efficiency of the work by the auditors e.g. replacing manual consistency checks.

The auditor may also design CAATs as risk assessment procedures or audit tests to obtain assurance over assertions or address Significant Risks. CAATs can be used in risk assessment procedures or audit tests.

Any use of CAATs is dependent upon handling electronic data produced by the entity. All auditors should be aware of the need to respect and protect this data to hold it securely, only hold it for as long as is necessary, and dispose of it securely once it is no longer needed.

When using CAATs, the auditor should evaluate whether the information is sufficiently reliable for the purposes, including as necessary in the circumstances:
(a) Obtaining audit evidence about the accuracy and completeness of the information; and
(b) Evaluating whether the information is sufficiently precise and detailed for the auditor's purposes.

An auditor can use CAAT in different stages of the audit like

- Reliability and accuracy of system data
- Selecting samples for testing operating effectiveness
- Selecting samples for substantive testing
- Performing substantive analytical procedures

3.4 Use of Information Produced by the Project

When using information produced by the Project, FAPAD audit team should evaluate whether the information is sufficiently reliable, precise and detailed for their purposes, including accuracy and completeness of the information.

Evidence about accuracy and completeness of information used in performing an audit procedure can be obtained concurrently as an integral part of the audit procedure itself, by testing controls over the preparation and maintenance of the information, or by additional audit procedures.

The preparation of the financial statements may require expertise in fields other than accounting or auditing, such as actuarial calculations, valuations or engineering data and the Project management may employ or engage experts to provide the necessary expertise.

Where information used in the audit has been prepared using the work of an expert employed or engaged by the Project, then the auditor should evaluate the competence, capabilities and objectivity of the expert and obtain an understanding of the work conducted by the expert. The nature, timing and extent of the audit procedures required may be affected by such matters as:

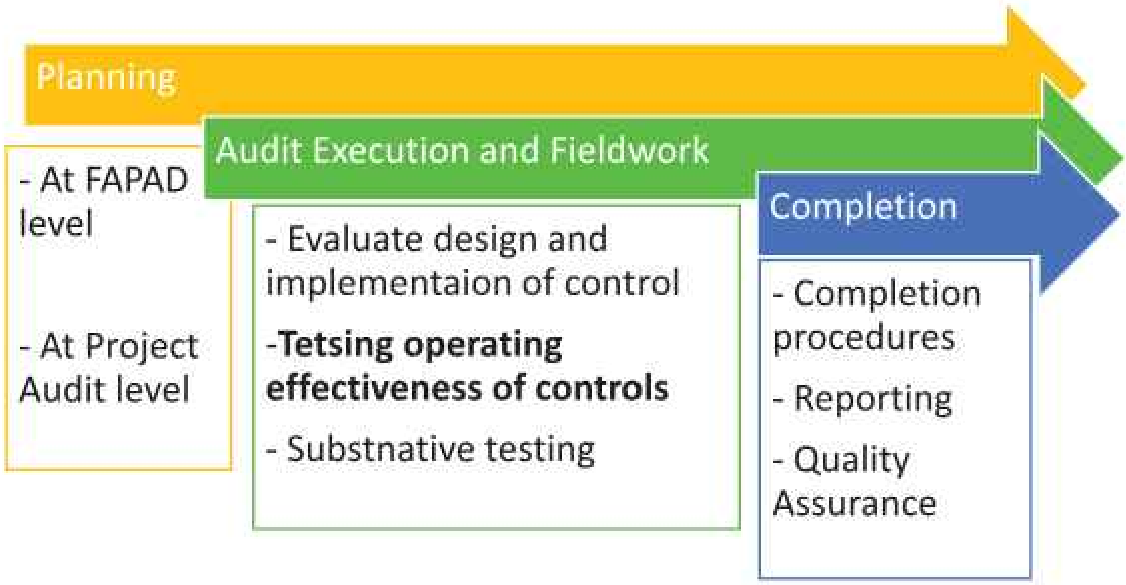
- The nature and complexity of the matter to which management's expert's work relates;
- The risks of material misstatement;
- The availability of alternative sources of audit evidence;
- The nature, scope and objectives of management's expert's work;
- Whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services;
- The extent to which management can exercise control or influence over the work of management's expert;
- Whether management's expert is subject to technical performance standards or other professional or industry requirements;
- The nature and extent of any controls within the entity over management's expert's work;
- The auditor's knowledge and experience of management's expert's field of expertise; and
- Their previous experience of the work of that expert.

The auditor should evaluate the appropriateness of management's expert's work, including consideration of:

- The relevance and reasonableness of that expert's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial statements;
- If that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods; and
- If that expert's work involves significant use of source data the relevance, completeness, and accuracy of that source data.

3.5 Testing operating effectiveness of controls

Test of controls is an audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level. Tests of controls are performed as part of auditor's response to the risks of material misstatement identified during risk assessment process.



As per Para 8-10 of ISSAI 2330, the auditor shall design and perform tests of controls to obtain sufficient and appropriate audit evidence as to the operating effectiveness of relevant controls if:

(a) The auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively; or

(b) Substantive procedures alone cannot provide sufficient and appropriate audit evidence at the assertion level.

The auditor shall design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level.

In designing and performing tests of controls, the auditor shall perform other audit procedures in combination with inquiry to obtain audit evidence about the operating effectiveness of the controls, including:

(i) How the controls were applied at relevant times during the period under audit;

(ii) Whether they operated consistently throughout the period; and

(iii) Who operated the controls or if automated controls by what means they were applied?

The auditor shall also determine whether the controls to be tested depend upon other controls (indirect controls), and, if so, whether it is necessary to obtain audit evidence supporting the effective operation of those indirect controls. In some circumstances, it may be necessary to obtain audit evidence supporting the effective operation of indirect controls.

Tests of controls are performed only on those controls that the auditor has determined are suitably designed to prevent, or detect and correct, a material misstatement in an assertion. In other word, if the auditor is determined that the controls are not designed properly, there is no point to test operating effectiveness since it is bound to fail.

Testing the operating effectiveness of controls is different from obtaining an understanding of and evaluating the design and implementation of controls as mentioned in the previous section. However, the same types of audit procedures are used for both types of testing. The auditor may, therefore, decide it is efficient to test the operating effectiveness of controls at the same time as evaluating their design and determining that they have been implemented.

Although some risk assessment procedures may not have been specifically designed as tests of controls, they may nevertheless provide audit evidence about the operating effectiveness of the controls and, consequently, serve as tests of controls. For example, the auditor's risk assessment procedures may have included:

- Inquiring about management's use of budgets.
- Observing management's comparison of monthly budgeted and actual expenses.
- Inspecting reports pertaining to the investigation of variances between actual and budget.

These audit procedures provide knowledge about the design of the Project's budgeting policies and whether they have been implemented, but may also provide audit evidence about the effectiveness of the operation of budgeting policies in preventing or detecting material misstatements in the classification of expenses.

In addition, the auditor may design a test of controls to be performed concurrently with a test of details on the same transaction. Although the purpose of a test of controls is different from the purpose of a test of details, both may be accomplished concurrently by performing a test of controls and a test of details on the same transaction, also known as a dual-purpose test. For example, the auditor may design, and evaluate the results of, a test to examine a contractor invoice to determine whether it has been approved by the PMU and to provide substantive audit evidence of a transaction. A dual-purpose test is designed and evaluated by considering each purpose of the test separately.

A higher level of assurance may be sought about the operating effectiveness of controls when the approach adopted consists primarily of tests of controls, in particular where it is not possible or practicable to obtain sufficient appropriate audit evidence only from substantive procedures. For example, if the account balance comprises of numerous small value invoices of homogenous nature only substantive testing may not be an effective and efficient method to gather audit evidence. In such case test of control can be an effective tool.

Inquiry alone is not sufficient to test the operating effectiveness of controls. Accordingly, other audit procedures are performed in combination with inquiry. In this regard, inquiry combined with inspection or re-performance may provide more assurance than inquiry and observation, since an observation is pertinent only at the point in time at which it is made.

Using audit evidence obtained in previous audits

Since most of the Project audits conducted by FAPAD are recurring audit engagement, in certain circumstances, audit evidence obtained from previous audits may provide audit evidence where the auditor performs audit procedures to establish its continuing relevance. For example, in performing a previous audit, the auditor may have determined that an automated control was functioning as intended. The auditor may obtain audit evidence to determine whether changes to the automated control have been made that affect its continued effective functioning through, for example, inquiries of management and the inspection of logs to indicate what controls have been changed. Consideration of audit evidence about these changes may support either increasing or decreasing the expected audit evidence to be obtained in the current period about the operating effectiveness of the controls.

Evaluating the Operating Effectiveness of Controls

The concept of effectiveness of the operation of controls recognizes that some deviations in the way controls are applied by the Project may occur. Deviations from prescribed controls may be caused by such factors as changes in key personnel, significant seasonal fluctuations in volume of transactions and human error. The detected rate of deviation, in particular in comparison with the expected rate, may indicate that the control cannot be relied on to reduce risk at the assertion level to that assessed by the auditor.

When evaluating the operating effectiveness of relevant controls, the auditor shall evaluate whether misstatements that have been detected by substantive procedures indicate that controls are not operating effectively. The absence of misstatements detected by substantive procedures, however, does not provide audit evidence that controls related to the assertion being tested are effective.

When evaluating a deviation discovered in testing controls to determine whether it is a control deficiency, the auditor may consider several factors, including:

- How was the deviation detected?
- Is the deviation confined to a single location, process or application, or is it pervasive in the organization?
- How significant is the control deviation from stated policy?
- How often were deviations detected in relation to how frequently the control is performed?

If the auditor has evaluated the design and implementation of a control to be effective, and tests of operating effectiveness do not identify any deficiencies, then the auditor may conclude that the control is operating effectively.

Where a control is found to be ineffective and the auditor still chooses to rely on controls for the relevant assertions, the auditor shall both identify compensating controls and test those, or if the control is remediated by management, the auditor shall test the remediated control.

<u>Refer Appendix 9on Pro forma Internal Control Questionnaire (ICQ) template</u>

3.6 Substantive testing (nature, extent and timing)

ISSAI 2330 requires the auditor to design and perform substantive procedures for each material class of transactions, account balance, and disclosure, irrespective of the assessed risks of material misstatement. This requirement reflects the facts that:

(a) The auditor's assessment of risk is judgmental and so may not identify all risks of material misstatement; and

(b) There are inherent limitations to internal control, including management override.

Depending on the circumstances, substantive procedures at the assertion level may include:

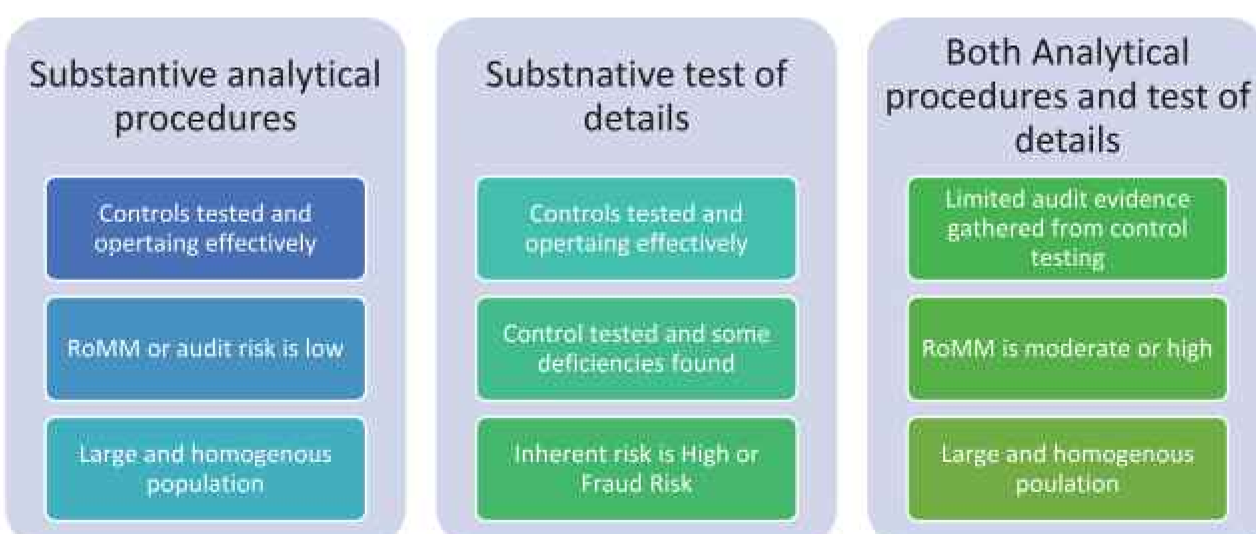
- Only substantive analytical procedures;
- Only tests of details are appropriate; and
- A combination of both tests of details and substantive analytical procedures.

The decision about which audit procedures to perform is based on the auditor's judgment about the expected effectiveness and efficiency of the available audit procedures to reduce audit risk at the assertion level to an acceptably low level.

The nature, timing and extent of the planned audit procedures should be based on, and responsive to, the assessed risks of material misstatement for the Audit Area, i.e. the appropriate procedures to test a particular assertion will vary depending upon the nature of the balance.

Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. ISSAI 2520 establishes requirements and provides guidance on the application of analytical procedures during an audit.

Because the assessment of the risk of material misstatement takes account of internal control, the extent of substantive procedures may need to be increased when the results from tests of controls are unsatisfactory.



3.7 Substantive analytical procedures

In accordance with auditing standards, "Analytical procedures" means evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

Analytical procedures are normally used during the following three phases of the audit:

- At the planning stage as part of risk assessment under ISSAI 2315;
- As substantive audit procedures in accordance with ISSAI2330; and
- Near the end of the audit to assist the auditor forming an overall conclusion whether the financial statements are consistent with the auditor's understanding of the Project under ISSAI 2520.

When designing and performing substantive analytical procedures, either alone or in combination with tests of details, as substantive procedures in accordance with ISSAI2330, the auditor shall follow the following steps:

(a) Suitability of test: Determine the suitability of particular substantive analytical procedures for given assertions, taking account of the assessed risks of material misstatement and tests of details, if any, for these assertions;

(b) Reliability of data: Evaluate the reliability of data from which the auditor's expectation of recorded amounts or ratios is developed, taking account of source, comparability, and nature and relevance of information available, and controls over preparation;

(c) Expectation and comparison: Develop an expectation of recorded amounts or ratios and compare the expected amount with the actual amount recorded;

(d) Evaluate: Evaluate whether there has been any difference between the expected values and recorded amounts and determine whether such difference is acceptable without further investigation;

(e) Explanation: If there is significant variation between the predicted value and recorded amount the auditor should seek explanations from Project management to corroborate the difference and may perform re-computation for the revised expected value to see whether the difference is still unacceptable; and

(f) Conclusion: Upon completing the above steps, the auditor shall decide whether sufficient and appropriate audit evidence has been collected to satisfy audit objective or any further testing is required along with any reportable matters.

Analytical procedures include comparisons of the Project's financial information with:

- Comparable information for prior periods, month on month comparison.
- Anticipated results of the Project, such as budgets or forecasts, or expectations of the auditor, such as an estimation of depreciation.
- Similar industry information, such as a comparison of the Project's ratio of average salary per person with industry averages or with other Projects being audited by FAPAD.

Analytical procedures also include consideration of relationships, for example, among elements of financial information that would be expected to conform to a predictable pattern based on the Project's experience, such as depreciation percentages and between financial information and relevant non-financial information, such as payroll costs to number of employees.

Reliability of Data

The reliability of data is influenced by its source and nature and is dependent on the circumstances under which it is obtained. Accordingly, the auditor should evaluate whether data is reliable for the purposes of designing substantive analytical procedures.

The auditor may consider testing the operating effectiveness of controls, if any, over the Project's preparation of information used by the auditor in performing substantive analytical procedures in response to assessed risks. When such controls are effective, the auditor generally has greater confidence in the reliability of the information and, therefore, in the results of analytical procedures. ISSAI2500 establishes requirements and provides guidance in determining the audit procedures to be performed on the information to be used for substantive analytical procedures.

Setting predictive value

When undertaking detailed analytical review, it is necessary to set expectations. In setting these expectations, auditors need to establish plausible and predictable relationships relevant to the figures being audited. Often, analytical review is confined to a mere comparison of trends and ratios. This is of limited value as all the information is generated by the client.

Having set expectations, it is then necessary to predict the expected outcome. This prediction must then be compared with the actual figures and any material differences enquired into. Explanations given as to any variances must be corroborated, fully documented and the analytical review concluded upon.

Evaluate differences from predicted value

The auditor's determination of the amount of difference from the expectation that can be accepted without further investigation is influenced by materiality and the consistency with the desired level of assurance, taking account of the possibility that a misstatement, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated. ISSAI2330 requires the auditor to obtain more persuasive audit evidence the higher the auditor's assessment of risk. Accordingly, as the assessed risk increases, the amount of difference considered acceptable without investigation decreases in order to achieve the desired level of persuasive evidence.

The need to perform other audit procedures may arise when, for example, management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate.

Applicability of substantive analytical procedures

Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. The application of planned analytical procedures is based on the expectation that relationships among data exist and continue in the absence of known conditions to the contrary. However, the suitability of a particular analytical procedure will depend upon the auditor's assessment of how effective it will be in detecting a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated.

In some cases, even an unsophisticated predictive model may be effective as an analytical procedure. For example, where a Project has a known number of employees at fixed rates of pay throughout the period, it may be possible for the auditor to use this data to estimate the total payroll costs for the period with a high degree of accuracy, thereby providing audit evidence for a significant item in the financial statements and reducing the need to perform tests of details on the payroll.

The determination of the suitability of particular substantive analytical procedures is influenced by the nature of the assertion and the auditor's assessment of the risk of material misstatement. For example, if controls over approval of contractor payments are deficient, the auditor may place more reliance on tests of details rather than on substantive analytical procedures for assertions related to contractor payments.

The relationships between individual financial statements items traditionally considered in the audit of business entities may not always be relevant in the audit of a Project funded by development partners; for example, in a Project there may be little direct relationship between revenue and expenditure. In addition, because expenditure on the acquisition of assets may not be capitalized, there may be no relationship between expenditures on, for example, inventories and fixed assets and the amount of those assets reported in the financial statements. Also, industry data or statistics for comparative purposes may not be available for such project. However, other relationships may be relevant, for example, variations in the cost per square feet of school building construction.

Many smaller Projects, although not being able to produce full financial accounts for the auditor to audit, may well prepare certain schedules from which the auditor can prepare the accounts. A potential example of this would be a daily payment record. The auditor could then assess whether or not the daily payment record indicated any pattern and whether consistent with expectations and previous years.

3.8 Substantive test of details

Tests of detail' are substantive audit procedures which do not include analytical review. Tests of detail can include 100% tests, covering every item in a population or audit sampling. The procedures performed may include:

- Physical examination;
- Vouching;
- Recalculation;
- Confirmation of individual items or transactions;
- Observation; and
- Inspection.

The appropriateness of a test to obtain the planned level of assurance depends upon the nature, timing and extent of the planned audit procedures and should be based on, and responsive to, the assessed risks of material misstatement for the audit area.

In planning Tests of Detail, the auditor should consider the appropriate direction(s) of testing to obtain assurance over an assertion. For example, tests of detail related to the completeness assertion may involve selecting from items that are expected to be included in the relevant financial statement amount and investigating whether they are included. On the other hand, tests of detail related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence.

Similarly, for the completeness assertion, the auditors require assurance that the expenditure or receipts are not understated (as the list is not complete). Therefore, in this case, the auditor would seek to select their sample from the source population, e.g. for expenditure the source population might be all payments as detailed on the bank statement or cash book, and the auditor might add a test in their audit programme to check for a sample of payment transactions that the auditor selects from the bank statement that they are properly recorded in the listing of payments made that the auditor is testing as part of the audit. Different tests are likely to be needed for completeness of income, as there is a higher risk with cash receipts that all or part of the receipt is misappropriated and never enters the bank account or the listing of receipts.

The auditor may obtain more persuasive evidence by increasing the quantity of the evidence through more extensive testing, or by obtaining evidence that is more relevant or reliable, for example, by placing more emphasis on obtaining third party evidence.

The members of the audit team designing and performing the procedures should have a clear understanding of what would constitute a misstatement so that the results of the procedures can be appropriately evaluated.

If the auditor has identified a Specific Risk, he or she should plan and perform procedures that are specifically responsive to that risk.

A test only provides assurance over an assertion if the nature of the test is appropriate. For example:

- Inspection of documents evidencing existence of an asset (such as a share certificate) may not provide assurance over ownership or valuation.
- Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity's rights and obligations or the valuation of the assets.
- Evidence of post year-end receipt of payment on a debtor may evidence valuation, but not that it was a debtor of the entity at the balance sheet date (i.e. cut-off).

Types of test of details

External Confirmation - This is a specific type of enquiry, where representation of information is obtained directly from a third party. A bank certificate giving details of a bank balance at a specific date is an example of confirmation evidence.

Recalculation - This involves checking the mathematical accuracy of documents or records. Recalculation can be performed through the use of information technology, for example, by obtaining an electronic file from the entity and using CAATs to check the accuracy of the summarisation of the file.

Inspection - Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production.

Re-performance - Independently executing procedures that were originally performed as, e.g., part of the client's internal control. This may be done manually or through the use of CAATs.

Observation - Looking at a process or procedure being performed by others. Examples include the observation of the performance of control activities and observation of the counting of inventory by the client staff. Observation provides audit evidence about the performance of a process or procedure, but it is limited to the point in time at which the observation takes place.

Enquiry - Seeking information from knowledgeable persons, both financial and non-financial, within and outside the client's organisation. Enquiry alone ordinarily does not provide sufficient audit evidence and it should, therefore, be supported with corroboration.

Timing

Tests of detail may be performed at an interim date or at the period end.

The higher the risk of material misstatement, the more likely it is that the auditor may decide it is more effective to perform substantive procedures nearer to, or at the period end rather than at an earlier date, or to perform audit procedures unannounced or at unpredictable times (for example, performing audit procedures at selected locations on an unannounced basis). This is particularly relevant when considering the response to the risks of fraud.

Example: Risk of fraud affecting timing of work

The auditor has identified a number of factors which indicate a Specific Risk of management understating expenditure to avoid overspend against budget. The majority of testing had historically been performed at an interim stage, with procedures at year-end to roll-forward testing to year-end. However, due to the nature of the risk identified, the auditor concluded that it would not be effective to rely on a roll-forward of completeness testing. All work on completeness of liabilities was performed at year-end.

However, performing tests at an interim date may enable us to identify significant matters at an early stage. This enables us to resolve them with the assistance of management, or to develop an effective audit approach to address the issue.

Certain audit procedures can be performed only at or after the period end, for example:

- Agreeing the financial statements to the accounting records;
- Examining adjustments made during the course of preparing the financial statements; and
- Procedures to respond to a risk that, at the period end, the entity may have entered into improper payments in advance of need, or transactions may not have been finalised.

Other factors that influence the auditor's consideration of when to perform audit procedures include:

- The control environment (as a strong control environment supports performing work at an interim date);
- When relevant information is available (for example, electronic files may subsequently be overwritten, or procedures to be observed may occur only at certain times);
- The nature of the risk (for example, if there is a risk of manipulation of the inventory balance, the auditor may wish to attend a year-end inventory count); and
- The period or date to which the audit evidence being tested relates.

The use of Computer Assisted Audit Techniques (CAATs) may enable more extensive testing of electronic transactions and account files, which may be useful to enable more extensive testing in response to a risk of fraud or material error. Such techniques can be used to select sample transactions from key electronic files to sort transactions with specific characteristics, or to test an entire population instead of a sample.

3.9 External confirmation including development partner's records and from banks

ISSAI 2500 indicates that the reliability of audit evidence is influenced by its source and nature, and is dependent on the individual circumstances under which it is obtained. That standard also includes the following generalizations applicable to audit evidence:

- Audit evidence is more reliable when it is obtained from independent sources outside the entity.
- Audit evidence obtained directly by the auditor is more reliable than audit evidence obtained indirectly or by inference.
- Audit evidence is more reliable when it exists in documentary form, whether paper, electronic or other medium.

Accordingly, depending on the circumstances of the audit, audit evidence in the form of external confirmations received directly by the auditor from confirming parties may be more reliable than evidence generated internally by the entity.

ISSAI 2330 requires that the auditor obtain more persuasive audit evidence the higher the auditor's assessment of risk. To do this, the auditor may increase the quantity of the evidence or obtain evidence that is more relevant or reliable, or both. For example, the auditor may place more emphasis on obtaining evidence directly from third parties or obtaining corroborating evidence from a number of independent sources. ISSAI 2330 also indicates that external confirmation procedures may assist the auditor in obtaining audit evidence with the high level of reliability that the auditor requires to respond to significant risks of material misstatement, whether due to fraud or error.

The auditor shall consider whether external confirmation procedures are to be performed as substantive audit procedures. External confirmation procedures are frequently relevant when addressing assertions associated with account balances and their elements, but need not be restricted to these items. For example, the auditor may request external confirmation of the terms of agreements, contracts, or transactions between an entity and other parties. External confirmation procedures may also be performed to obtain audit evidence about the absence of certain conditions. For example, a request may specifically seek confirmation that no "side agreement" exists that may be relevant to an entity's revenue cutoff assertion.

To confirm the balance of grant/loan appearing in the Project Financial Statements with the balance recorded by the development partner as well as verification of bank balance the auditor may require seeking direct confirmation from third party source like the relevant development partner and/or the respective bank.

Some of the frequently used confirmation procedures that can be used by FAPAD team are as follows:

- Bank balances and other information relevant to banking relationships.
- Accounts receivable balances and terms.

- Inventories held by third parties at bonded warehouses for processing or on consignment.
- Property title deeds held by lawyers or financiers for safe custody or as security.
- Investments held for safekeeping by third parties, or purchased from stockbrokers but not delivered at the balance sheet date.
- Amounts due to lenders, including relevant terms of repayment and restrictive covenants.
- Accounts payable balances and terms.

Although external confirmations may provide relevant audit evidence relating to certain assertions, there are some assertions for which external confirmations provide less relevant audit evidence. For example, external confirmations provide less relevant audit evidence relating to the recoverability of accounts receivable balances, than they do of their existence.

The auditor may determine that external confirmation procedures performed for one purpose provide an opportunity to obtain audit evidence about other matters. For example, confirmation requests for bank balances often include requests for information relevant to other financial statement assertions. Such considerations may influence the auditor's decision about whether to perform external confirmation procedures.

Factors that may assist the auditor in determining whether external confirmation procedures are to be performed as substantive audit procedures include:

- The confirming party's knowledge of the subject matter – responses may be more reliable if provided by a person at the confirming party who has the requisite knowledge about the information being confirmed.
- The ability or willingness of the intended confirming party to respond – for example, the confirming party:
  - May not accept responsibility for responding to a confirmation request;
  - May consider responding too costly or time consuming;
  - May have concerns about the potential legal liability resulting from responding;
  - May account for transactions in different currencies; or
  - May operate in an environment where responding to confirmation requests is not a significant aspect of day-to-day operations.

In such situations, confirming parties may not respond, may respond in a casual manner or may attempt to restrict the reliance placed on the response.

The objectivity of the intended confirming party – If the confirming party is a related party of the entity, responses to confirmation requests may be less reliable.

<u>Refer Appendix 10 for pro forma bank confirmation request</u>

3.10 Physical verification of Project asset/work

If during the year for which audit is being conducted there has been substantial amount spent for construction or procurement of assets, the auditor shall obtain sufficient and appropriate audit evidence regarding the existence and condition of such assets by physical attendance at site where such asset has been constructed/installed, unless impracticable, and to inspect the asset.

Based on physical verification by the audit team if it is found that the payment has been made for certain work which is not yet completed or delivered, the audit team shall try to quantify the amount of such excess payment.

Based on the amount involved, the auditor either need to modify the audit report (i.e. if the amount is material but not pervasive it will be qualified audit opinion and if the amount is pervasive adverse audit opinion). If the amount of excess payment is not material the audit team may decide not to modify the audit report (i.e. give unqualified audit opinion) but it can be still referred in the management letter and/or any other form of reporting addressed to the Executing Agency/Line Ministry/Development Partners.

3.11 Substantive testing for non-significant items

If performing Substantive Analytical Procedures over non-significant balances, the auditor should set tolerable error at the lower of Performance Materiality

The INTOSAI standards only require substantive audit procedures be performed for classes of transactions, account balances, and disclosures that are material (i.e. significant Audit Areas). However, the auditor should plan to do a minimum level of substantive procedures on non-significant Audit Areas. This is below the level of testing that would be required for a significant Audit Area.

The auditor should consider whether the nature of balance means that additional audit procedures should be performed to gain assurance over any particular assertion. If more complex tests are required to address an Audit Area, this may indicate that this is in fact a significant Audit Area.

Substantive analytical procedures can, if considered appropriate by the auditor, be based upon a comparison to prior year.

Tolerable error should be set at the lower of Performance Materiality or 25% of recorded amount (unless a lower tolerable difference is considered appropriate).

Example: auditing a non-significant revenue audit area
Interest receipts are a non-significant element of income at a total of Tk. 2.6 million (prior year Tk. 3.1 million) made up of receipts of interest during the year being audited from a number of fixed term bank deposits. The auditor has tested by agreeing the amount received to the trial balance and assessing its reasonableness through predictive analytical procedures against the average amount of money on deposit during the year and prevailing interest rates for fixed term deposits.

While performing substantive procedures the auditor shall exercise professional judgment to identify misstatements that are greater than performance materiality and audit evidence for a non-significant account may be less persuasive than audit evidence for a significant account.

3.12 Conclusion on substantive testing

The auditor may be able to evaluate management's responses in the context of his/her understanding of the entity and other audit evidence obtained, or he/she may need to obtain additional audit evidence to support their explanations

Concluding by Audit Area

When each individual audit programme has been completed, a conclusion should be made for each audit area as to whether all planned work has been completed and whether more work is needed. Any further work to that planned should be agreed with the team leader. If no further audit work is considered necessary, then a conclusion should be made for each audit area as to whether the planned assurance has been obtained towards all relevant audit assertions. In cases where errors have been identified, they should be extrapolated where appropriate to evaluate whether they are material.

Also, for each audit area, audit findings of a similar nature should be grouped and summarised and included in a list of all proposed findings, with observations, causes, effects and recommendations for inclusion in the audit report.

Overall Conclusion

Conclusions for all audit areas should be brought together and summarised in order to evaluate the total extent of error in the audit and decide the appropriate overall opinion to give – see the next chapter for details.

3.13 Checking of project financial statements and agreeing to records

If the audit work on classes of transactions and account balances takes place after management has prepared a draft financial statements, typically agreeing or reconciling the financial statements with the underlying accounting records will involve:

Before beginning testing as part of the year-end audit:

- Obtaining management's mapping from the receipt and payment account or trial balance (where applicable) to the financial statements;
- Checking that the mapping of individual lines of the receipt and payment account or financial statements to audit areas is appropriate;
- Identifying adjustments between the receipt and payment account or trial balance (where applicable) and the draft financial statements; and
- Preparing lead schedules based upon the draft financial statements.

In performing testing as part of the year-end audit:

- Testing material journal entries in the preparation of the draft financial statements where accrual system of accounting is maintained (typically as part of responding to the pervasive risk of management override of controls);
- Testing material adjustments between the receipt and payment account or trial balance (where applicable) and the draft financial statements (for example change of the heading of expenses from consultancy payments to construction costs); and
- If any reclassification is done between the items disclosed in the receipt and payment account or trial balance and the draft financial statements.

Depending on the basis of accounting used for the preparation of Project financial statements (i.e. cash basis or accrual basis), the audit team may need to conduct some or all of the following procedures:

- Update lead schedules for adjustments between draft and final financial statements;
- Testing material journal entries between the draft and final financial statements;
- Testing material adjustments between the draft and final financial statements; and
- Testing other journal entries and adjustments in the preparation of the final financial statements where appropriate (typically most adjustments in preparing the final account will be tested)

Where it is not possible/ practical to audit from a draft financial statements, it may be necessary to perform the audit work on classes of transactions and account balances from the receipt and payment account or trial balance and later perform procedures on the financial statements.

Evaluate Presentation and Disclosures

The auditor should perform audit procedures to evaluate whether the overall presentation of the financial statements, including the related disclosures, is in accordance with the applicable financial reporting framework. This includes evaluating whether:

- The individual financial statements are presented in a manner that reflects the appropriate classification and description of financial information in accordance with the applicable financial reporting framework;
- The form, arrangement, and content of the financial statements and their appended notes are in accordance with the applicable financial reporting framework; and
- The terminologies used, the amount of detail given, the classification of items in the statements, and the accounting bases used are in accordance with the applicable financial reporting framework.

Information Accompanying the Financial Statements

The auditor should read information accompanying the financial statements that is not included in the financial statements and ensure it is consistent with the financial statements.

If, on reading the information, the auditor identifies a material inconsistency, the auditor should determine whether the audited financial statements or the other information needs to be revised.

If revision of the audited financial statements is necessary and management refuses to make the revision, the auditor should modify the opinion in the audit report.

If revision of the information is necessary and management refuses to make the revision, the auditor should:

a) Include in the audit report an Other Matter(s) paragraph describing the material inconsistency;
b) Withhold the audit report; or
c) Withdraw from the audit engagement where possible.

The working paper file should demonstrate that the financial statements agree or reconcile with the underlying accounting records.

The documentation on the working paper file should include a referenced and tied in version of the final financial statements.

A clear audit trail between initial audit work and the final account, including clear documentation of how adjustments have been audited, is important in evidencing that the audit opinion is appropriately supported.

3.14 Examining Journals and Other Adjustments

Projects audited by FAPAD teams mostly prepare financial statements following IPSAS cash basis of accounting and hence there will not be any journal entries to test as part of audit process.

However, if any Project follow accrual basis of accounting there might be some journal entries for areas like accrual and receivable process, asset recognition and depreciation, prepayments etc. In such cases audit team need to cover testing of journal entries as part of the audit process.

Although standard journal entries are quite common and a recurring process, special focus needed for non-standard journal entries which are made to record nonrecurring, unusual transactions or adjustments. In addition, the auditor is required to test journal entries as part of their response to the Pervasive Risk of fraud through management override of controls.

Since, fraudulent journal entries and other adjustments are often made at the end of a reporting period, in designing and performing audit procedures for such tests, an auditor shall focus on journal entries and other adjustments made at the end of a reporting period or post-closing journal entries and adjustments.

The procedures around year-end journal entries will normally be combined with the procedures performed in responding to the pervasive risk of management override of controls. If there is a specific year-end journal process, the auditor should ensure that the testing includes all material year-end journals.

In some accounting systems, year-end journals are reflected in an additional "Period 13" accounting period, or otherwise segregated within the accounting system. In other entities, adjustments may be posted directly in the preparation of the financial statements, without adjustments necessarily being reflected in the underlying records.

The nature and extent of procedures on journal entries and other adjustments in preparing the financial statements depend on the nature and complexity of the financial reporting close down process and any risks identified.

Chapter Four
Completion






Completion

As per auditing standards, prior to the issuance of audit report, the auditor needs to conclude on certain specific topics (such as going concern, related parties, litigation and claims, compliance with laws and regulation, subsequent events, disclosures in financial statements, evaluation of errors etc.) and also the auditor needs to evaluate sufficiency and appropriateness of the audit evidence collected during the audit. All these procedures along with overall review of financial statements and other reporting obligations are included in this Chapter.

4.1 Evaluating the Sufficiency and Appropriateness of Audit Evidence

The sufficiency and appropriateness of audit evidence are interrelated. Sufficiency is the measure of the quantity of audit evidence. The quantity of audit evidence needed is affected by the auditor's assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence, however, may not compensate for its poor quality.

The auditor should design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient and appropriate audit evidence. These audit procedures should be collated by audit area and included in audit programmes to ensure that all planned audit procedures are carried out. Based on the audit procedures performed and the audit evidence obtained, the Auditor should evaluate before the conclusion of the audit whether the assessments of the risks of material misstatement at the assertion level remain appropriate. In forming an opinion, the auditor should consider all relevant audit evidence, regardless of whether it appears to corroborate or to contradict the assertions in the financial statements.

If the auditor has not obtained sufficient and appropriate audit evidence as to a material financial statement assertion, they should attempt to obtain further audit evidence. If the auditor is unable to obtain sufficient and appropriate audit evidence, they shall express a qualified opinion or disclaim an opinion on the financial statements, which are described in more detail in Chapter Five.

The auditor's judgement as to what constitutes sufficient and appropriate audit evidence is influenced by such factors as:

- The significance of the potential misstatement in the assertion and the likelihood of its having a material effect, either individually or aggregated with other, on the financial statements;
- The effectiveness of management's responses and controls to address the risks;
- Experience gained during previous audits with respect to similar potential misstatements;
- The results of audit procedures performed, including whether such audit procedures identified specific instances of fraud or error;
- The source and reliability of the available information;
- Persuasiveness of the audit evidence; and
- Understanding of the Project and its environment, including the Project's internal control.

The Team Leader or Director General should review and assess the audit evidence obtained during the course of the audit and conclude whether this provides a suitable basis for the audit opinion. This can be facilitated by on-going dialogue within the auditors working on the audit during the course of the audit and the use of on-site or 'hot' review.

4.2 Concluding in Final Analytical Procedures

The conclusions drawn from the results of analytical procedures designed and performed are intended to corroborate conclusions formed during the audit of individual components or elements of the financial statements. This assists the auditor to draw reasonable conclusions on which to base the auditor's opinion.

The auditor should design and perform analytical procedures near the end of the audit to assist in forming an overall conclusion as to whether the financial statements are consistent with the understanding of the Project.

Concluding Analytical Procedures are intended to corroborate conclusions formed during the audit of individual components or elements of the financial statements. This enables the team to draw reasonable conclusions on which to base the audit opinion.

The analytical procedures performed may be similar to those used for Preliminary Analytical Procedures as a part of Risk Assessment Procedures, but will reflect the final financial statement position. Considerations when carrying out such procedures may include:

(a) Whether the financial statements adequately reflect the information and explanations previously obtained and conclusions previously reached during the course of the audit;
(b) Whether the procedures reveal any new factors which may affect the presentation of or disclosures in the financial statements;
(c) Whether analytical procedures applied when completing the audit, such as comparing the information in the financial statements with other pertinent data, produce results which assist in arriving at the overall conclusion as to whether the financial statements as a whole are consistent with their knowledge of the entity's business;
(d) Whether the presentation adopted in the financial statements may have been unduly influenced by the desire of those charged with governance to present matters in a favourable or unfavorable light; and
(e) The potential impact on the financial statements of the aggregate of uncorrected misstatements (including those arising from bias in making accounting estimates) identified during the course of the audit and the preceding period's audit, if any.

The results of such analytical procedures may identify a previously unrecognized risk of material misstatement. In such circumstances, ISSAI 1315 requires the auditor to revise their assessment of the risks of material misstatement and may require the performance of further controls and/or substantive procedures.

4.3 Consideration of Fraud Risk

The auditor should evaluate whether analytical procedures that are performed near the end of the audit, when forming an overall conclusion as to whether the financial statements are consistent with their understanding of the entity, indicate a previously unrecognized risk of material misstatement due to fraud

ISSAI2240 'The Auditor's Responsibility Relating to Fraud in an Audit of Financial Statements' provides detailed guidance on their responsibility to consider fraud at all stages during the course of the audit.

If the auditor identifies a misstatement, he/she should evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the auditor should 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.

If the auditor confirms that, or is unable to conclude whether, the financial statements are materially misstated as a result of fraud, the auditor should evaluate the implications for the audit.

If the auditor identifies the possible existence of fraud and considers that this fraud could have a material impact on the financial statements, the auditor must undertake additional testing in order to confirm or dispel the suspicion of fraud. If the additional testing undertaken does not confirm or dispel their suspicions, the auditor should discuss the issue with the Project's management and considers whether the potential fraud has been properly considered or corrected in the financial statements. If senior management is involved in the fraudulent activity then to avoid the risk of tipping off, the auditor should consider whether a report should be made to the related Ministry and in applicable cases to the concerned Development Partner.

Where the auditor confirms that the financial statements are materially misstated as a result of fraud, or is unable to confirm otherwise, the Director General should consider the implications for the audit opinion, in particular the audit opinion on true and fairness of the financial statements. More detailed guidance on modifications to the audit opinion is provided later in this manual.

4.4 Evaluation of Independence and Ethical Issues

While closing the audit the auditor once again need to reassess that there has been no breach of any independence and ethical matters and all conflicts are mitigated.

The Director General of FAPAD should consider the independence and objectivity of the audit team at the planning stage of the audit and document this consideration on working paper as stated in earlier section of this manual.

In addition, the Director General must also consider any independence or ethical issues which arise during the audit and evaluate the impact of any identified breaches of the OCAG's policies and procedures to determine whether any such breaches represent a threat to the independence and objectivity of the FAPAD, and if any such cases are identified should detail consideration and relevant action on working paper.

4.5 Conducting specific audit procedures on litigation and claims ISSAI 2501

Litigation and claims involving the Project may have a material effect on the financial statements and thus may be required to be disclosed or accounted for in the financial statements.

The auditor shall design and perform audit procedures in order to identify litigation and claims involving the Project which may give rise to a risk of material misstatement. Auditor may get information about litigation and claims by performing the following procedures;

(a) Inquiry of management and, where applicable, others within the Project, including in-house legal counsel;
(b) Reading minutes of progress meetings of Project's management, EA/IA, related governing bodies or ministries held during, and subsequent to, the period being audited;
(c) Read contracts, loan agreements, leases and correspondence from external legal counsel, taxing or other governmental agencies and major vendors and similar documents;
(d) Reviewing legal expense accounts.

If the auditor assesses a risk of material misstatement regarding litigation or claims that have been identified, or when audit procedures performed indicate that other material litigation or claims may exist, the auditor shall, in addition to the procedures required by other ISSAIs, seek direct communication with the Project's/EA/IA's external legal counsel. The auditor shall do so through a letter of inquiry, prepared by management and sent by the auditor, requesting the Project's/EA/IA's external legal counsel to communicate directly with the auditor. If law, regulation or the respective legal professional body prohibits the Project's/EA/IA's external legal counsel from communicating directly with the auditor, the auditor shall perform alternative audit procedures.

If, management refuses to give the auditor permission to communicate or meet with the entity's external legal counsel, or the Project's/EA/IA's external legal counsel refuses to respond appropriately to the letter of inquiry, or is prohibited from responding; and the auditor is unable to obtain sufficient and appropriate audit evidence by performing alternative audit procedures, the auditor shall modify the opinion in the auditor's report in accordance with ISSAI2705 (Revised).

The auditor shall request the Project management to provide written representations that all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

Direct communication with the Project's/EA/IA's external legal counsel assists in obtaining sufficient and appropriate audit evidence as to whether potentially material litigation and claims are known and management's appropriately considered and disclosed the implications in the financial statements.

Refer to Appendix 11 for pro forma letter of audit enquiry to the Project's legal counsel.

4.6 Compliance with laws and regulations

The effect on financial statements of laws and regulations vary considerably. Those laws and regulations to which a Project is subject constitute the legal and regulatory framework. The provisions of some laws or regulations have a direct effect on the financial statements in that they determine the reported amounts and disclosures in the Project's financial statements. Other laws or regulations are to be complied with by management or set the provisions under which the Project is allowed to conduct its business but do not have a direct effect on a Project's financial statements.

It is the responsibility of Project management, with the oversight of those charged with governance, to ensure that the Project's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in a Project's financial statements.

The following are examples of the types of policies and procedures an entity may implement to assist in the prevention and detection of non-compliance with laws and regulations:

- Monitoring legal requirements and ensuring that operating procedures are designed to meet these requirements.
- Instituting and operating appropriate systems of internal control.
- Developing, publicizing and following a code of conduct.
- Ensuring employees are properly trained and understand the code of conduct.
- Monitoring compliance with the code of conduct and acting appropriately to discipline employees who fail to comply with it.
- Engaging legal advisors to assist in monitoring legal requirements.
- Maintaining a register of significant laws and regulations with which the entity has to comply within its particular industry and a record of complaints.

Although the auditor is not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations, but the auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, due to non-compliance with laws and regulations. Accordingly, in conducting an audit of financial statements, the auditor takes into account the applicable legal and regulatory framework.

For conducting the audit of Projects co-financed by development partners and Government of Bangladesh there, there may be additional audit responsibilities for audit team of FAPAD with respect to the consideration of laws and regulations which may relate to the audit of financial statements or may extend to other aspects of the Project's operations (i.e. PPR compliance).

For those laws and regulations having a direct effect on the determination of material amounts and disclosures in the financial statements, the auditor's responsibility is to obtain sufficient and appropriate audit evidence regarding compliance with the provisions of those laws and regulations. For other types of laws and regulations, the auditor's responsibility is limited to undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial statements.

4.7 Going concern assessment (if relevant)

While conducting audit an auditor must assess the appropriateness of going concern assumption adopted by management in preparation of financial statements. If there is any going concern condition this shall be disclosed in the financial statements along with the mitigating factors. Based on outcome of the going concern assumption the auditor may require to modify its audit report.

Under the going concern basis of accounting, the financial statements are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future. General purpose financial statements are prepared using the going concern basis of accounting, unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so. Special purpose financial statements may or may not be prepared in accordance with a financial reporting framework for which the going concern basis of accounting is relevant (e.g., the going concern basis of accounting is not relevant for some financial statements prepared on a tax basis in particular jurisdictions). When the use of the going concern basis of accounting is appropriate, assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business.

Management's use of the going concern basis of accounting is also relevant to public sector entities. For example, International Public Sector Accounting Standard (IPSAS) 1 addresses the issue of the ability of public sector entities to continue as going concerns. Going concern risks may arise, but are not limited to, situations where public sector entities operate on a for-profit basis, where government support may be reduced or withdrawn, or in the case of privatization. Events or conditions that may cast significant doubt on an entity's ability to continue as a going concern in the public sector may include situations where the public sector entity lacks funding for its continued existence or when policy decisions are made that affect the services provided by the public sector entity

In relation to the audit of Projects which prepared financial statements in accordance with IPSAS cash basis of accounting, the implication of inappropriate use of going concern is much lesser as compared to the accrual basis framework such as IFRS, IPSAS accrual basis. Nevertheless, FAPAD audit team shall always take into cognizance the Project's budget, approved duration, remaining funding, unpaid liabilities and commitments, legal or constructive obligations, assets disposal/transfer while conducting the audit, if any going concern issue is identified.

4.8 Obtaining management representation letter

Written management representations are an important source of audit evidence. 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.

Normally an auditor shall obtain written representations from management and, where appropriate, those charged with governance to seek confirmation that they have fulfilled their responsibility for the preparation of the financial statements and for the completeness of the information provided to the auditor and to support other audit evidence relevant to the financial statements or specific assertions in the financial statements.

If taking individual management representation letter from each Project is considered difficult and time consuming, one master representation letter can be obtained from the relevant ministry/entity covering all Projects being implemented by that ministry/entity.

Refer to Appendix 12 for a pro forma management representation letter for use by FAPAD auditor.

4.9 Conducting specific audit procedures on Subsequent events

Financial statements may be affected by certain events that occur after the date of the financial statements. Many financial reporting frameworks specifically refer these as subsequent events. Such financial reporting frameworks ordinarily identify two types of events:

(a) Those that provide evidence of conditions that existed at the date of the financial statements; and
(b) Those that provide evidence of conditions that arose after the date of the financial statements.

ISSAI 2700 explains that the date of the auditor's report informs the reader that the auditor has considered the effect of events and transactions of which the auditor becomes aware and that occurred up to that date.

The auditor shall perform audit procedures designed to obtain sufficient and appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements have been identified. The auditor is not, however, expected to perform additional audit procedures on matters to which previously applied audit procedures have provided satisfactory conclusions.

The auditor shall perform the procedures so that they cover the period from the date of the financial statements to the date of the auditor's report, or as near as practicable thereto. The auditor shall take into account the auditor's risk assessment in determining the nature and extent of such audit procedures, which shall include the following:

(a) Obtaining an understanding of any procedures Project management has established to ensure that subsequent events are identified.
(b) Inquiring of Project management and, where appropriate, those charged with governance as to whether any subsequent events have occurred which might affect the financial statements.
(c) Reading minutes, if any, of the meetings of the Project management and executing agency that have been held after the date of the financial statements and inquiring about matters discussed at any such meetings for which minutes are not still available.
(d) Reading the Project's latest subsequent interim financial statements, if any.

If, as a result of the procedures performed as required above, the auditor identifies events that require adjustment of, or disclosure in, the financial statements, the auditor shall determine whether each such event is appropriately reflected in those financial statements in accordance with the applicable financial reporting framework.

4.10 Conducting specific audit procedures on Related Parties

As per ISSAI 2550, a Related Party is defined as a party that is either:

a. A person or other entity that has control or significant influence, directly or indirectly through one or more intermediaries, over the reporting entity;
b. Another entity over which the reporting entity has control or significant influence, directly or indirectly through one or more intermediaries; or
c. Another entity that is under common control with the reporting entity through having common controlling ownership, owners who are close family members or common key management.

However, entities that are under common control by a state (that is, a national, regional or local government) are not considered related unless they engage in significant transactions or share resources to a significant extent with one another. Therefore, while conducting audit of Projects, FAPAD audit team need to evaluate such related party relationship in the context of having a common PMU/EA/IA and sharing resources or conducting activities between themselves.

Because related parties are not independent of each other, financial reporting frameworks establish specific accounting and disclosure requirements for related party relationships, transactions and balances to enable users of the financial statements to understand their nature and actual or potential effects on the financial statements.

The auditor has a responsibility to perform audit procedures to identify, assess and respond to the risks of material misstatement arising from the Project's failure to appropriately account for or disclose related party relationships, transactions or balances in accordance with the requirements of the framework.

The auditor needs to obtain an understanding of the Project's related party relationships and transactions sufficient to be able to conclude whether the financial statements, insofar as they are affected by those relationships and transactions:

(a) Achieve fair presentation (for fair presentation frameworks); or
(b) Are not misleading (for compliance frameworks).

ISSAI 2550 has specified certain audit procedures designed to assist the auditor in identifying and assessing the risks of material misstatement associated with related party relationships and transactions, and in designing audit procedures to respond to the assessed risks.

4.11 Evaluation of errors (adjusted/unadjusted)

The auditor shall accumulate misstatements identified during the audit, other than those that are clearly trivial. Misstatements may result from:

(a) An inaccuracy in gathering or processing data from which the financial statements are prepared;

(b) An omission of an amount or disclosure, including inadequate or incomplete disclosures, and those disclosures required to meet disclosure objectives of certain financial reporting frameworks as applicable;

(c) An incorrect accounting estimate arising from overlooking, or clear misinterpretation of, facts;

(d) Judgments of management concerning accounting estimates that the auditor considers unreasonable or the selection and application of accounting policies that the auditor considers inappropriate.

(e) An inappropriate classification, aggregation or disaggregation, of information; and

(f) For financial statements prepared in accordance with a fair presentation framework, the omission of a disclosure necessary for the financial statements to achieve fair presentation beyond disclosures specifically required by the framework

The auditor may designate an amount below which misstatements of amounts in the individual statements would be clearly trivial, and would not need to be accumulated because the auditor expects that the accumulation of such amounts clearly would not have a material effect on the financial statements. However, misstatements of amounts that are above the designated amount are accumulated.

"Clearly trivial" is not another expression for "not material." Misstatements that are clearly trivial will be of a wholly different (smaller) order of magnitude, or of a wholly different nature than those that would be determined to be material, and will be misstatements that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any criteria of size, nature or circumstances. When there is any uncertainty about whether one or more items are clearly trivial, the misstatement is considered not to be clearly trivial.

The auditor shall determine whether the overall audit strategy and audit plan need to be revised if:

(a) The nature of identified misstatements and the circumstances of their occurrence indicate that other misstatements may exist that, when aggregated with misstatements accumulated during the audit, could be material; or

(b) The aggregate of misstatements accumulated during the audit approaches materiality determined in accordance with ISSAI2320.

If, at the auditor's request, management has examined a class of transactions, account balance or disclosure and corrected misstatements that were detected, the auditor shall perform additional audit procedures to determine whether misstatements remain.

Communication and Correction of Misstatements

The auditor shall communicate, unless prohibited by law or regulation, on a timely basis all misstatements accumulated during the audit with the appropriate level of management. The auditor shall request management to correct those misstatements.

If management refuses to correct some or all of the misstatements communicated by the auditor, the auditor shall obtain an understanding of management's reasons for not making the corrections and shall take that understanding into account when evaluating whether the financial statements as a whole are free from material misstatement.

Prior to evaluating the effect of uncorrected misstatements, the auditor shall reassess materiality determined in accordance with ISSAI2320 to confirm whether it remains appropriate in the context of the entity's actual financial results.

The auditor shall determine whether uncorrected misstatements are material, individually or in aggregate. In making this determination, the auditor shall consider:

(a) The size and nature of the misstatements, both in relation to particular classes of transactions, account balances or disclosures and the financial statements as a whole, and the particular circumstances of their occurrence; and

(b) The effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole.

Communication with Those Charged with Governance

The auditor shall communicate with those charged with governance uncorrected misstatements and the effect that they, individually or in aggregate, may have on the opinion in the auditor's report, unless prohibited by law or regulation. The auditor's communication shall identify material uncorrected misstatements individually. The auditor shall request that uncorrected misstatements be corrected.

The auditor shall also communicate with those charged with governance the effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole.

The auditor shall request a written representation from management and, where appropriate, those charged with governance whether they believe the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the financial statements as a whole. A summary of such items shall be included in or attached to the written representation.

4.12 Financial Reporting Framework (FRF) used for project financial statements

Financial statements ordinarily refer to a complete set of financial statements as determined by the requirements of the applicable Financial Reporting Framework(FRF) but can also refer to a single financial statement. Disclosures comprise explanatory or descriptive information, set out as required, expressly permitted or other allowed by the applicable financial reporting framework on the face of the financial statements, or in the notes, or incorporated therein by cross reference. There are two types of FRF, which are further explained in ISSAI 2200:

Fair presentation framework is used to refer to a FRF that requires compliance with the requirements of the framework and:

i. That acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or
ii. That acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

Compliance framework is used to refer to a FRF that requires compliance with the requirements of the framework but does not contain the acknowledgements in (i) and (ii) above.

In addition to using Fair Presentation or Compliance Framework, the Project can prepare financial statements tailored to meet the specific information needs of related ministry, development partners or other stakeholders. This is called special-purpose financial statements and may be prepared using a special-purpose reporting framework.

It is therefore important to determine whether the Project FRF is designed to meet the financial information needs of a wide range of users ("general-purpose framework") or the financial information needs of specific users.

When the auditor concludes that the accounting framework that is applied to prepare the Project financial statements to be audited is a special purpose framework, in addition to following other ISSAIs, the audit teams also apply ISSAI 2800 requirements as well.

The type of framework used to prepare the financial statements affects the wording of the auditor's opinion. In case of a **fair presentation framework,** audit team need to evaluate whether the financial statements achieve fair presentation, including a consideration of:

- The overall presentation, structure and content of the financial statements; and
- Whether the financial statements, including the related notes, represent the underlying transactions and events in a manner that achieves fair presentation.

When expressing an opinion on the financial statements prepared in accordance with the fair presentation framework, the auditor's report includes expressions such as *"the financial statements present fairly..."* or *"the financial statements give a true and fair view of..."*.

When the financial statements are prepared in accordance with a **compliance** framework, the auditor does not express an opinion on the fairness of presentation. Instead, the auditor is required to evaluate whether the financial statements are prepared, in all material respects, in accordance with the prescribed presentation of the financial statements that may be included in a specific FRF or in applicable laws and regulations. The use of a compliance framework should not be confused with a compliance audit. The wording of the opinion will be as follows: *"Financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework."*

As stated earlier, Foreign Funded Development Projects in Bangladesh normally prepare financial statements based on IPSAS Cash Basis of Accounting which is a "**fair presentation**" framework. However, the Project is not a legal entity and the requirements to prepare these financial statements are mandated by the relevant financing agreements executed between the Government and Development Partners. Accordingly, these are special purpose financial statements catering to the need of specified users.

The cash basis of accounting recognizes transactions and events only when cash (including cash equivalents) is received or paid by the Project. Financial statements prepared under the cash basis provide readers with information about the sources of cash raised during the period, the purposes for which cash was used and the cash balances at the reporting date. The measurement focus in the financial statements is balances of cash and changes therein. Notes to the financial statements may provide additional information about liabilities, such as payables and borrowings, and some non-cash assets, such as receivables, investments and property, plant and equipment.

Cash is controlled by a Project when the Project can use the cash for the achievement of its own objectives or otherwise benefit from the cash and exclude or regulate the access of others to that benefit. Cash collected by, or appropriated or granted to, a Project which the Project can use to fund its operating objectives, acquire capital assets or repay its debt is controlled by the Project. Amounts deposited in the bank account of a Project are controlled by that Project.

A Project shall prepare and present financial statements which include the following components:

- A statement of cash receipts and payments which recognizes all cash receipts, cash payments and cash balances controlled by the Project;
- Accounting policies and explanatory notes; and
- When the Project makes publicly available it's approved budget, a comparison of budget and actual amounts either as a separate additional financial statement or as a budget column in the statement of cash receipts and payments.

The financial statements comprise the statement of cash receipts and payments and other statements that disclose additional information about the cash receipts, payments and balances controlled by the Project and accounting policies and notes. Only cash receipts, cash payments and cash balances controlled by the Project will be recognized as such in the statement of cash receipts and payments or other statements that might be prepared. The financial statements may include a comparison of budget and actual amounts as an additional financial statement.

A Project can present a comparison of budget and actual amounts as additional budget columns in the statement of cash receipts and payments only where the financial statements and the budget are prepared on a comparable basis. When the budget and financial statements are not prepared on a comparable basis, a separate statement of comparison of budget and actual amounts is presented

The statement of cash receipts and payments shall present the following amounts for the reporting period:

- Total cash receipts of the Project showing separately a sub-classification of total cash receiptsusingaclassificationbasisappropriatetotheProject'soperations;
- Total cash payments of the Project showing separately a sub-classification of total cash payments using a classification basis appropriate to the Project's operations; and
- Beginning and closing cash balances of the Project.

Total cash receipts and total cash payments, and cash receipts and cash payments for each sub-classification of cash receipt and payment, shall be reported on a gross basis, except that cash receipts and payments may be reported on a net basis when:

- They arise from transactions which the Project administers on behalf of other parties and which are recognized in the statement of cash receipts and payments; or
- They are for items in which the turnover is quick, the amounts are large, and the maturities are short.

Line items, headings and sub-totals shall be presented in the statement of cash receipts and payments when such presentation is necessary to present fairly the Project's cash receipts, cash payments and cash balances.

The notes to the financial statements of a Project shall:

- Present information about the basis of preparation of the financial statements and the specific accounting policies selected and applied for significant transactions and other events; and
- Provide additional information which is not presented on the face of the financial statements but is necessary for a fair presentation of the Project's cash receipts, cash payments and cash balances.

Notes to the financial statements shall be presented in a systematic manner. Each item on the face of the statement of cash receipts and payments and other financial statements shall be cross referenced to any related information in the notes.

The accounting policies section of the notes to the financial statements shall describe each specific accounting policy that is necessary for a proper understanding of the financial statements, including the extent to which the Project has applied any transitional provisions in this standard.

Inappropriate accounting treatments are not rectified either by disclosure of the accounting policies used, or by notes or explanatory material.

A Project shall disclose the date when the financial statements were authorized for issue and who gave that authorization. If another body (i.e. the EA/IA or Ministry) has the power to amend the financial statements after issuance, the Project shall disclose that fact.

A Project shall disclose the following in the notes to the financial statements if not disclosed elsewhere in information published with the financial statements:

- The domicile and legal form of the Project, and the jurisdiction(s) within which it operates;
- A description of the nature of the Project's operations and principal activities;
- A reference to the relevant legislation governing the Project's operations, if any; and
- The significant entities or sectors of government that are presented in the financial statements, and changes in the significant entities or sectors that comprise the reporting entity and were presented in the previous periods financial statements.

Comparative information shall be disclosed in respect of the previous period for all numerical information to be disclosed in the financial statements. Comparative information shall be included in narrative and descriptive information when it is relevant to an understanding of the current period's financial statements.

When the presentation or classification of items required to be disclosed in the financial statements is amended, comparative amounts shall be reclassified, unless it is impractical to do so, to ensure comparability with the current period, and the nature, amount of, and reason for any reclassification shall be disclosed. When it is impractical to reclassify comparative amounts, the Project shall disclose the reason for not reclassifying and the nature of the changes that would have been made if amounts were reclassified.

Each component of the financial statements shall be clearly identified. In addition, the following information shall be prominently displayed and repeated when it is necessary for a proper understanding of the information presented:

- The name of the reporting entity (Project) or other means of identification;
- Whether the financial statements cover an individual entity or a group of entities;
- The reporting date or the period covered by the financial statements, whichever is appropriate to the related component of the financial statements;
- The presentation currency; and
- The level of precision used in the presentation of figures in the financial statements

Cash receipts and payments arising from transactions in a foreign currency shall be incorporated in the Statement of Receipts and Payments in the Project's presentation currency by applying to the foreign currency amount the spot exchange rate between the reporting currency and the foreign currency at the date of the receipts and payments. Cash balances held in a foreign currency shall be translated using the closing rate. The Project shall disclose the amount of exchange differences included as reconciling items between opening and closing cash balances for the period.

4.13 Overall Review of the Financial Statements including other information

The purpose of this review is to determine whether the financial statements have been prepared using the most appropriate accounting policies and that such policies have been consistently applied; the results shown in the financial statements are consistent with their knowledge of the business; all necessary disclosures are contained in the financial statements and are appropriately presented and clearly expressed and the uncorrected misstatements and disclosure deficiencies are immaterial to the financial statements.

Accounting treatment of other income

The Project at times receive various income/receipts such as interest from banks on deposit, sale of tender schedule, sale of scrap items, foreign exchange gain etc. which are not within the budgeted code/allocation.

Similarly, the Project may also incur various expenses/payments which are not budgeted like advertisement of tender notice, bank charges, foreign exchange losses, etc.

Accordingly, such income/receipts and expenses/payments are normally shown as a separate line item in the Project financial statements for ready reference. Either at the end of the Project or on a periodic basis any balance of other income after netting of other expenses shall be either transferred back to the Government/Development Partners or utilized for Project work upon receiving approval from all stakeholders.

Supporting ledgers for Financial Statements

Since the Project financial statements are prepared under the cash basis of Accounting, it is expected that the Project should at least maintain cash book, bank book, bank reconciliation statements, loan/grant ledger by the Donor/Lender, loan/grant reconciliation agreed with the counterparty confirmation, etc. In addition, as a best practice and effective internal control, a memorandum record should be maintained for all items of value which are charged as expenses under the cash basis of accounting but still in use by the Project such as fixed assets, inventories, spare etc.

As documentary evidence of completing all required audit procedures the audit team normally prepare audit completion checklist where the team leader and team manager confirm completion of certain audit procedures.

<u>Refer Appendix 13 for a pro forma audit completion checklist.</u>

Chapter Five
Reporting
The Auditor's Report



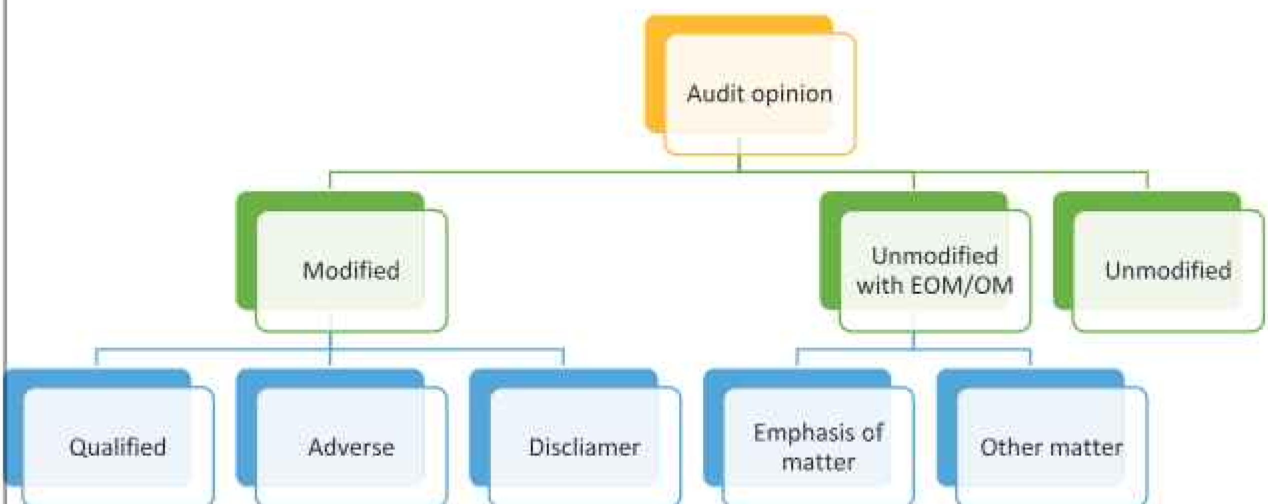



Reporting

As per ISSAI, at the conclusion of the audit, the auditor shall issue a clearly written opinion on the financial statements, as a whole. The purpose of this chapter is to consider the procedures necessary to form an opinion on the financial statements, including where the Director General, FAPAD decides to modify his audit opinion. Depending on the work performed and evidence gathered by the auditor, such opinion can be either unmodified or modified, which are discussed in more detail.

The Chapter provides guidance on the format of the auditor's report. It also sets out other types of reporting expected form FAPAD audit team such as management letter, specific reporting to the development partners and the concerned EA/IA.

As per INTOSAI standards, audit opinion has multiple classifications as mentioned below:



Refer to the Appendix 14 for a decision tree on various types of audit opinion.

5.1 The auditor's report and audit opinion

The auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. In order to form that opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. That conclusion shall take into account:

(a) The auditor's conclusion, in accordance with ISSAI2330, whether sufficient and appropriate audit evidence have been obtained;

(b) The auditor's conclusion, in accordance with ISSAI2450, whether uncorrected misstatements are material, individually or in aggregate; and

(c) The evaluations as mentioned in the succeeding paragraphs below.

The auditor shall evaluate whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework. This evaluation shall include consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgments. In particular, the auditor shall evaluate whether, in view of the requirements of the applicable financial reporting framework:

(a) The financial statements appropriately disclose the significant accounting policies selected and applied. In making this evaluation, the auditor shall consider the relevance of the accounting policies to the entity, and whether they have been presented in an understandable manner;

(b) The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;

(c) The accounting estimates made by management are reasonable;

(d) The information presented in the financial statements is relevant, reliable, comparable, and understandable. In making this evaluation, the auditor shall consider whether:

- The information that should have been has been included, and whether such information is appropriately classified, aggregated or disaggregated, and characterized.
- The overall presentation of the financial statements has been undermined by including information that is not relevant or that obscures a proper understanding of the matters disclosed.

(e) The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and

(f) The terminology used in the financial statements, including the title of each financial statement, is appropriate.

An auditor's opinion may be:

- Unmodified; or
- Modified

An unmodified auditor's opinion may contain an emphasis of matter or other matters paragraphs.

5.2 Contents of audit report

The content of the audit report shall include the following:

(a) A title.

(b) An addressee, as required by the circumstances of the engagement.

(c) An Opinion section containing an expression of opinion on the financial statements and a reference to the applicable financial reporting framework used to prepare the financial statements (i.e. International Financial Reporting Standards or International Public Sector Accounting Standards).

(d) An identification of the entity's financial statements that have been audited.

(e) A statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall refer to compliance of the Code of Ethics issued by the OCAG and the fact that these are based on the INTOSAI Code of Ethics for Auditors in the Public Sector.

(f) Where applicable, a section that addresses, and is not inconsistent with, the reporting requirements on going concern as per ISSAI 2570 (Revised).

(g) Where applicable, a Basis for Qualified (or Adverse) Opinion section that addresses, and is not inconsistent with, the reporting requirements in ISSAI2570 (Revised).

(h) Where applicable, a section that includes the information required by ISSAI2701, or additional information about the audit that is prescribed by law or regulation and that addresses, and is not inconsistent with, the reporting requirements in that ISA.

(i) Where applicable, a section that addresses the reporting requirements in ISSAI2720 (Revised).

(j) A description of management's responsibilities for the preparation of the financial statements and an identification of those responsible for the oversight of the financial reporting process that addresses, and is not inconsistent with, the requirements specified in ISSAI 2700.

(k) A reference to the Government Auditing Standards of Bangladesh which are based on the International Standards of Supreme Audit Institutions (ISSAI), and a description of the auditor's responsibilities for an audit of the financial statements that addresses, and is not inconsistent with, the requirements in paragraphs 37–40 of ISSAI 2700.

(l) The auditor's signature.

(m) The auditor's address.

(n) The date of the auditor's report.

<u>Refer to Appendix 2 for a template of Unmodified audit opinion</u>

5.3 Types of Modified Opinions

ISSAI2700 (Revised) requires the auditor, in order to form an opinion on the financial statements, to conclude as to whether reasonable assurance has been obtained about whether the financial statements as a whole are free from material misstatement. This conclusion takes into account the auditor's evaluation of uncorrected misstatements, if any, on the financial statements in accordance with ISSAI2450.

ISSAI 2450 defines a misstatement as a difference between the reported amounts, classification, presentation, or disclosure of a financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Accordingly, a material misstatement of the financial statements may arise in relation to:

(a) The appropriateness of the selected accounting policies;
(b) The application of the selected accounting policies; or
(c) The appropriateness or adequacy of disclosures in the financial statements.

Appropriateness of the Selected Accounting Policies

In relation to the appropriateness of the accounting policies management has selected, material misstatements of the financial statements may arise for example when:

(a) The selected accounting policies are not consistent with the applicable financial reporting framework;
(b) The financial statements do not correctly describe an accounting policy relating to a significant item in the statement of financial position, the statement of comprehensive income, the statement of changes in equity or the statement of cash flows; or
(c) The financial statements do not represent or disclose the underlying transactions and events in a manner that achieves fair presentation.

Financial reporting frameworks often contain requirements for the accounting for, and disclosure of, changes in accounting policies. Where the Project has changed its selection of significant accounting policies, a material misstatement of the financial statements may arise when the Project has not complied with these requirements.

Application of the Selected Accounting Policies

In relation to the application of the selected accounting policies, material misstatements of the financial statements may arise:

(a) When management has not applied the selected accounting policies consistently with the financial reporting framework, including when management has not applied the selected accounting policies consistently between periods or to similar transactions and events (consistency in application); or
(b) Due to the method of application of the selected accounting policies (such as an unintentional error in application).

Appropriateness or Adequacy of Disclosures in the Financial Statements

In relation to the appropriateness or adequacy of disclosures in the financial statements, material misstatements of the financial statements may arise when:

(a) The financial statements do not include all of the disclosures required by the applicable financial reporting framework;

(b) The disclosures in the financial statements are not presented in accordance with the applicable financial reporting framework; or

(c) The financial statements do not provide the additional disclosures necessary to achieve fair presentation beyond disclosures specifically required by the applicable financial reporting framework.

The auditor should modify the opinion in the auditor's report when:

a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or

b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

ISSAI2705 establishes three types of modified opinions:

- Qualified opinion;
- Disclaimer opinion;
- Adverse opinion.

The auditor's judgement of the nature of the matter giving rise to the opinion and the pervasiveness of its effects on the financial statements affects the type of the opinion to be expressed:

Nature of Matter Giving Rise to the Modification	**Auditor's Judgement about the pervasiveness of the Effects or Possible Effects on the Financial Statement**	
	Material but not pervasive	***Material and Pervasive***
Financial statements are materially misstated	Qualified opinion-except for disagreement	Adverse opinion
Inability to obtain sufficient and appropriates audit evidence	Qualified opinion- except for limitation of scope	Disclaimer of opinion

To ensure that audit opinions are clear and easy to understand, it is important to maintain as much uniformity as possible in the content and style of the audit reports. Accordingly suggested wording has been given in ISSAI2705.

<u>A flowchart outlining the steps to consider when forming an opinion on the financial statements is set out in Appendix 14.</u>

5.4 Qualified Opinion

The auditor should issue a qualified opinion when:

(a) Having obtained sufficient appropriate audit evidence, they conclude that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or

(b) They are unable to obtain sufficient and appropriate audit evidence on which to base the opinion, but they conclude that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive (limitation of scope).

As stated in earlier section, a material misstatement of the financial statements may arise due to:

- The appropriateness of the selected accounting policies;
- The application of the selected accounting policies; or
- The appropriateness or adequacy of disclosures in the financial statements.

Nature of an Inability to Obtain Sufficient and Appropriate Audit Evidence

The auditor's inability to obtain sufficient and appropriate audit evidence (also referred to as a limitation on the scope of the audit) may arise from:

(a) Circumstances beyond the control of the entity;

(b) Circumstances relating to the nature or timing of the auditor's work; or

(c) Limitations imposed by management.

An inability to perform a specific procedure does not constitute a limitation on the scope of the audit if the auditor is able to obtain sufficient appropriate audit evidence by performing alternative procedures. Limitations imposed by management may have other implications for the audit, such as for the auditor's assessment of fraud risks and consideration of engagement continuance.

Examples of circumstances beyond the control of the entity include when:

- The entity's accounting records have been destroyed.
- The accounting records of a significant component have been seized indefinitely by governmental authorities.

Examples of circumstances relating to the nature or timing of the auditor's work include when:

- The entity is required to use the equity method of accounting for an associated entity, and the auditor is unable to obtain sufficient and appropriate audit evidence about the latter's financial information to evaluate whether the equity method has been appropriately applied.
- The timing of the auditor's appointment is such that the auditor is unable to observe the counting of the physical inventories.
- The auditor determines that performing substantive procedures alone is not sufficient, but the entity's controls are not effective.

Examples of an inability to obtain sufficient and appropriate audit evidence arising from a limitation on the scope of the audit imposed by management include when:

- Management prevents the auditor from observing the counting of the physical inventory.
- Management prevents the auditor from requesting external confirmation of specific account balances.

If, after starting the audit, FAPAD audit team become aware that Project management has imposed a limitation on the scope of the audit that they consider likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, they should request that management remove the limitation. If management refuses to remove the limitation, the audit team should communicate the matter to the respective EA/IA/Ministry, and determine whether it is possible to perform alternative procedures to obtain sufficient and appropriate audit evidence. If the auditor is unable to obtain sufficient and appropriate audit evidence, they should suitably modify the audit opinion (i.e. qualified or disclaimer).

In case of qualified audit opinion, the audit team shall add a 'Basis for Qualification' paragraph in the audit report to explain the reason for qualifying his opinion. When the auditor expresses a qualified opinion due to a material misstatement in the financial statements, the auditor shall add "except for" in opinion paragraph and refer to the basis for qualification paragraph.

Example qualified opinion

In our opinion, except for the effects of the matter described in the *Basis for Qualified Opinion* section of our report, the accompanying financial statements present fairly, in all material respects, (or *give a true and fair view of*) the statement of Project sources and uses of funds as at and for the year ended on 30 June 20X1 in accordance with IPSAS *Financial Reporting Under the Cash Basis of Accounting*.

Basis for Qualified Opinion

The Project's total expenditure for the year includes BDT 22.5 million of payments made to a Contractor M/S ABC Enterprise on account of construction and civil work. As per documentation supplied by the Contractor and approved for payment by Project Management the construction and civil work of two storied school building is completed at the time of invoice submission. However, as per physical verification of the Project site the audit team found that construction of only the ground floor of the building is completed. Payment of the entire contracted amount to the Contractor before completion of the project work constitutes violation of the Project SOP and departure from IPSAS cash basis of accounting. As a result of this payment expense for the year is overstated and cash at bank is understated by an amount of BDT 22.5 million, respectively.

5.5 Adverse Opinion

The auditor should express an adverse opinion when, having obtained sufficient and appropriate audit evidence, they conclude that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

The term *pervasive* is defined in the ISA as the effects on the financial statements of misstatements or the possible effects on the financial statements of undetected misstatements, if any. Pervasive effects on the financial statements are those that, in the auditor's judgement:

i. Are not confined to specific elements, accounts or items of the financial statements;
ii. If so confined, represent or could represent a substantial proportion of the financial statements; or
iii. In relation to disclosures, are fundamental to users' understanding of the financial statements.

In case of an adverse opinion, the audit team shall add a paragraph under the heading 'basis for adverse opinion' to explain the reason(s) why the auditor is issuing an adverse opinion. The examples of wording that can be used are provided below:

When the auditor expresses an adverse opinion, the auditor shall state that, in the auditor's opinion,

Example of adverse opinion
In our opinion, because of the significance of the matter discussed in the *Basis for Adverse Opinion* section of our report, the accompanying financial statements do not present fairly (or *do not give a true and fair view of*) the statement of Project sources and uses of funds as at and for the year ended on 30 June 20X1 in accordance with IPSAS *Financial Reporting Under the Cash Basis of Accounting*.

Basis for adverse opinion
As explained in Note X, as per the Project Accounting Manual (PAM) the Project should account for all Project related receipts and payments through its own Bank account (DOSA, CONTASA, Imprest) as well any direct payments made by Development Partners directly to supplier/contractor. However, the Project sources and uses of funds as at and for the year ended 30 June 20X1 has not included any direct payments of project expenditure made by Development Partners. The amount of Project related direct payment is considered to be material and pervasive.

5.6 Disclaimer Opinion

The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient and appropriate audit evidence on which to base the opinion, and they conclude that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

When the auditor disclaims an opinion due to an inability to obtain sufficient and appropriate audit evidence, the auditor shall:

(a) State that the auditor does not express an opinion on the accompanying financial statements;

(b) State that, because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor has not been able to obtain sufficient and appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and

(c) Amend the statement, which indicates that the financial statements have been audited, to state that the auditor was engaged to audit the financial statements.

Example of disclaimer of opinion

We were engaged to audit the financial statements of ABC Project (the Project), which comprise the statement of the Project sources and uses of funds as of and for the year ended 30 June 20X1 and notes to the financial statements, including a summary of significant accounting policies.

We do not express an opinion on the accompanying financial statements of the Project. Because of the significance of the matter described in the *Basis for Disclaimer of Opinion* section of our report, we have not been able to obtain sufficient and appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for Disclaimer of Opinion

The Project management informed us that on the evening of 18 July 20X1, there was heavy rainfall and sudden flood in the locality where the Project Office was situated. The rain and flood water entered the ground floor office of the Project and destroyed most of the documents including accounting records and statements. As a result, we were not able to check any payment related documents at the Project site. We were unable to satisfy ourselves by alternative means concerning the payments made during the year ended 30 June 20X1 which are shown in the statement of Project sources and uses of funds as amount spent during the year.

5.7 Emphasis of Matter and Other Matter Paragraphs

In some circumstances, it may be necessary, without modifying the audit opinion, to draw the users' attention to a matter, disclosed or not disclosed in the financial statements, that is relevant to the users' understanding of the financial statements.

This may take the form of an Emphasis of Matter paragraph, or an Other Matter paragraph. These are defined in ISSAI 2706 as follows:

- Emphasis of Matter paragraph – A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements.
- Other Matter paragraph – A paragraph included in the auditor's report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements, the auditor should include an Emphasis of Matter paragraph in the auditor's report provided the auditor has obtained sufficient and appropriate audit evidence that the matter is not materially misstated in the financial statements. Such a paragraph shall refer only to information presented or disclosed in the financial statements. An auditor should consider emphasis of matter paragraphs under the following circumstances:

- There is a material uncertainty relating to the going concern assumption;
- The accounts are prepared on a basis other than going concern;
- There is a significant uncertainty relating to a future action or event which is outside the Project's control and which, may have a material impact on the financial statements;
- Where the prior year accounts were qualified and the matter giving rise to the qualification has been resolved with appropriate disclosures or adjustments made to the corresponding figures, but the prior period financial statements have not been adjusted.
- An uncertainty relating to the future outcome of exceptional litigation or regulatory action.
- A significant subsequent event that occurs between the date of the financial statements and the date of the auditor's report.
- Early application (where permitted) of a new accounting standard that has a material effect on the financial statements.
- A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position.

The emphasis of matter paragraph should give details of the matter giving rise to the significant uncertainty, and its possible effects on the financial statements, including quantification if possible. Where it is not possible to quantify the effects on the financial statements, a statement to this effect should be included. Clarity for the reader is enhanced by using an appropriate sub-heading in the report to differentiate the emphasis of matter paragraph from other paragraphs in the audit certificate.

An emphasis of matter paragraph may also be used to report on other matters that affect the financial statements. An example of this is where an amendment is required to the other information published with the audited financial statements and the entity refuse to make the amendment – the auditor would consider referring to this in an emphasis of matter paragraph.

Example of EOM Paragraph in audit report

We draw attention to Note X of the financial statements, which describes the on-going dispute due to National Board of Revenue (NBR)'s additional tax demand on account of withholding income tax from payments made to the contractor and Management's own assessment. Our opinion is not modified in respect of this matter.

If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in their judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report and this is not prohibited by law or regulation, they should do so in a paragraph in the auditor's report, with the heading "Other Matter," or other appropriate heading. The following are examples of where it may be appropriate to include an Other Matter paragraph:

- Where the auditor is unable to withdraw from an engagement even though the possible effect of an inability to obtain sufficient appropriate audit evidence due to a limitation on the scope of the audit imposed by management is pervasive, the auditor may consider it necessary to include an Other Matter paragraph in the auditor's report to explain why it is not possible for us to withdraw from the engagement.

- Where there is a material inconsistency between the financial statements and the surrounding information arising from a misstatement in the surrounding information; or

- Where financial statements are prepared for a specific purpose in accordance with a general purpose framework, because the intended users have determined that such general purpose financial statements meet their financial information needs, since the auditor's report is intended for specific users, they may consider it necessary in the circumstances to include an Other Matter paragraph, stating that the auditor's report is intended solely for the intended users, and should not be distributed to or used by other parties.

Example of Other Matter Paragraph in audit report

We have been informed about the requirement to start audit of the Project after the year-end and hence FAPAD audit team could not attend at physical inventory counting conducted by Management on 30 June 2019. However, we have conducted alternate audit procedures including subsequent attendance in inventory count and reconciliation documents to obtain sufficient and appropriate audit evidence regarding the existence and condition of inventory as at year-end date.

5.8 Comparative information disclosed in the financial statements

(a) Comparative information – The amounts and disclosures included in the financial statements in respect of one or more prior periods in accordance with the applicable financial reporting framework.

(b) Corresponding figures – Comparative information where amounts and other disclosures for the prior period are included as an integral part of the current period financial statements, and are intended to be read only in relation to the amounts and other disclosures relating to the current period (referred to as "current period figures"). The level of detail presented in the corresponding amounts and disclosures is dictated primarily by its relevance to the current period figures.

(c) Comparative financial statements – Comparative information where amounts and other disclosures for the prior period are included for comparison with the financial statements of the current period but, if audited, are referred to in the auditor's opinion. The level of information included in those comparative financial statements is comparable with that of the financial statements of the current period.

The auditor shall determine whether the financial statements include the comparative information required by the applicable financial reporting framework and whether such information is appropriately classified. For this purpose, the auditor shall evaluate whether:

(a) To obtain sufficient and appropriate audit evidence about whether the comparative information included in the financial statements has been presented, in all material respects, in accordance with the requirements for comparative information in the applicable financial reporting framework;
(b) The comparative information agrees with the amounts and other disclosures presented in the prior period or, when appropriate, have been restated; and
(c) The accounting policies reflected in the comparative information are consistent with those applied in the current period or, if there have been changes in accounting policies, whether those changes have been properly accounted for and adequately presented and disclosed.

If the auditor becomes aware of a possible material misstatement in the comparative information while performing the current period audit, the auditor shall perform such additional audit procedures as are necessary in the circumstances to obtain sufficient and appropriate audit evidence to determine whether a material misstatement exists. If the prior period financial statements are amended, the auditor shall determine that the comparative information agrees with the amended financial statements

When the prior period financial statements are not audited, the auditor should state in the auditor's report that the corresponding figures or comparative financial statements are unaudited as applicable.

When corresponding figures are presented, the auditor's opinion should not specifically refer to the corresponding figures, since the audit opinion is on the current period financial statements as a whole, including those figures.

5.9 Impact of a Prior Year Qualification

If the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matters which give rise to the modification is unresolved, they should modify the auditor's opinion on the current period's financial statements.

In the basis for modification paragraph in the auditor's report, they should either:

c) Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or

d) In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.

If the matter that gave rise to the modified opinion has been resolved and properly corrected in the prior year comparatives in the financial statements, the current certificate does not need to refer to the previous modification. However, if the matter is material to the current period, the auditor may want to include an emphasis of matter paragraph to give further information about the situation.

5.10 Opinion on Other Information Presented with the Financial Statements

The auditor's responsibilities extend to the other information disclosed in any documents accompanying the Project financial statements, which are not required to be audited, but require to be considered for consistency with the financial statements and auditor's knowledge of the Project.

ISSAI 2720 requires the auditor to read and consider the other information because other information that is materially inconsistent with the financial statements or the auditor's knowledge obtained in the audit may indicate that there is a material misstatement of the financial statements or that a material misstatement of the other information exists, either of which may undermine the credibility of the financial statements and the auditor's report thereon. Such material misstatements may also inappropriately influence the economic decisions of the users for whom the auditor's report is prepared

Other information may include amounts or other items that are intended to be the same as, to summarize, or to provide greater detail, about amounts or other items in the financial statements, and other amounts or other items about which the auditor has obtained knowledge in the audit. Other information may also include other matters.

If the auditor concludes that a material misstatement exists in other information obtained prior to the date of the auditor's report, and the other information is not corrected even after communicating with management and those charged with governance, the auditor shall address the material misstatement in the auditor's report.

5.11 Management letter

The auditor shall determine whether, on the basis of the audit work performed, the auditor has identified one or more deficiencies in internal control.

Deficiency in internal control exists when:

(i) A control is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements on a timely basis; or

(ii) A control necessary to prevent, or detect and correct, misstatements in the financial statements on a timely basis is missing.

Significant deficiency in internal control is defined as a deficiency or combination of deficiencies in internal control that, in the auditor's professional judgment, is of sufficient importance to merit the attention of those charged with governance.

If the auditor has identified one or more deficiencies in internal control, the auditor shall determine, on the basis of the audit work performed, whether, individually or in combination, they constitute significant deficiencies.

The auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis.

The auditor shall also communicate to management at an appropriate level of responsibility on a timely basis:

(a) In writing, significant deficiencies in internal control that the auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances; and

(b) Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties and that, in the auditor's professional judgment, are of sufficient importance to merit management's attention.

In determining whether the auditor has identified one or more deficiencies in internal control, the auditor may discuss the relevant facts and circumstances of the auditor's findings with the appropriate level of management. This discussion provides an opportunity for the auditor to alert management on a timely basis to the existence of deficiencies of which management may not have been previously aware of. The level of management with whom it is appropriate to discuss the findings is one that is familiar with the internal control area concerned and that has the authority to take remedial action on any identified deficiencies in internal control. In some circumstances, it may not be appropriate for the auditor to discuss the auditor's findings directly with management, for example, if the findings appear to call management's integrity or competence into question

In discussing the facts and circumstances of the auditor's findings with management, the auditor may obtain other relevant information for further consideration, such as:

- Management understands of the actual or suspected causes of the deficiencies.
- Exceptions arising from the deficiencies that management may have noted, for example, misstatements that were not prevented by the relevant Information Technology (IT) controls.
- A preliminary indication from management of its response to the findings.

During the audit, the auditor may identify other deficiencies in internal control that are not significant deficiencies but that may be of sufficient importance to merit management's attention. The determination as to which other deficiencies in internal control merit management's attention is a matter of professional judgment in the circumstances, taking into account the likelihood and potential magnitude of misstatements that may arise in the financial statements as a result of those deficiencies.

Normally the auditor communicates deficiencies in internal control or other matters in the form of "Management Letter". The management letter should be shared with Project management initially in the draft form. This would allow management an opportunity to clarify and/or remediate the findings so that the same can be resolved prior to finalization of the management letter and any implications such findings may have on the auditor's report.

For each audit finding, the draft management letter shall exhibit:

- Title of observation;
- Account heading;
- Observation;
- Implications;
- Recommendations;
- Management response; and
- Auditor's comments/follow-up;

If the auditor has communicated deficiencies in internal control other than significant deficiencies to management in a prior period and management has chosen not to remedy them for cost or other reasons, the auditor need not repeat the communication in the current period. The auditor is also not required to repeat information about such deficiencies if it has been previously communicated to management by other parties, such as the internal audit function or regulators. It may, however, be appropriate for the auditor to re-communicate these other deficiencies if there has been a change of management, or if new information has come to the auditor's attention that alters the prior understanding of the auditor and management regarding the deficiencies. Nevertheless, the failure of management to remedy other deficiencies in internal control that were previously communicated may become a significant deficiency requiring communication with those charged with governance. Whether this is the case depends on the auditor's judgment in the circumstances.

5.12 Communication with those charged with governance (EA/IA)

As stated in earlier section, the auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis. The auditor shall determine the appropriate person(s) within the entity's governance structure with whom to communicate.

Those charged with governance is defined in ISSAI 2265 as the person(s) or organization(s) (e.g., a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager. In the context of the Project Audit conducted by FAPAD, those charged with governance is considered as the Head of the concerned Executing/Implementing Agency and/or the Secretary of the related line Ministry.

As per ISSAI 2265, in addition to the significant deficiencies in internal control identified during the audit, the auditor shall also communicate the following matters with those charged with governance:

- The responsibilities of the auditor in relation to the financial statement audit, and an overview of the planned scope and timing of the audit;
- The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures;
- Significant difficulties, if any, encountered during the audit;
- Significant matters arising during the audit that were discussed, or subject to correspondence, with management;
- Any unadjusted audit differences;
- Written representations the auditor is requesting;
- Circumstances that affect the form and content of the auditor's report, if any; and
- Any other significant matters arising during the audit that, in the auditor's professional judgment, are relevant to the oversight of the financial reporting process.

The communication of findings from the audit may include requesting further information from those charged with governance in order to complete the audit evidence obtained. For example, the auditor may confirm that those charged with governance have the same understanding of the facts and circumstances relevant to specific transactions or events.

5.13 Additional Reporting to Development Partners

All development partners require the recipient of the fund and the Project's executing agency to have the project financial statements for each year prepared in accordance with acceptable financial reporting standards, audited by an independent auditor, and that the audit is conducted in accordance with auditing standards that are internationally acceptable.
To ensure all development partners are provided with reliable, comprehensive, and timely information, the following are required on an annual basis:

(i) Audited Project Financial Statements (APFS) including an auditor's opinion on whether the project financial statements are presented fairly, in all material respects, or give a true and fair view of the project's financial position, its financial performance and cash flows.

(ii) Specific additional auditor's opinions on:

a. Use of funds provided to Project – to confirm whether the fund recipient or executing agency has utilized the proceeds of the fund only for the purpose(s) of the Project; and

b. Compliance with financial covenants (where applicable) – to confirm the level of compliance for each financial covenant contained in the legal agreement(s) for the project (Auditors are expected to opine solely on financial covenants like debt-service-coverage ratio, self-financing ratio, debt-equity ratio etc.). The auditor will also indicate, where applicable, the extent of any non-compliance by reference to the specified (required) and actual performance measurements for each financial covenant for the fiscal year concerned.

(iii) Management letter.

Project Financial Statements

The auditor will verify that the Project financial statements have been prepared in accordance with the Project Accounting Manual issued by the Finance Division, MoF, GoB along with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) or International Public Sector Accounting Standard (IPSAS) promulgated by the International Public Sector Accounting Standards Board (IPSASB). The executing agency and/or implementing agency are responsible for preparing financial statements, not the auditor.

Project financial statements will include all project-related expenditures, irrespective of funding source. Since the Project Financial Statements are normally prepared following IPSAS Cash Basis of Accounting, the following items are required for a complete set of Project Financial Statements:

- A statement of cash receipts and payments
- A statement of budgeted versus actual expenditures
- A statement of imprest account (where applicable)
- A summary statement of expenditures (where applicable)
- Significant accounting policies and explanatory notes
- Any additional schedules agreed (e.g., a summary of assets)

The notes to the financial statements will provide sufficient information and explanations in narrative form or through provision of appropriate schedules. Supplementary schedules may include a detailed list of inventories, a summary of long-term debts, and a summary of accounts receivable and accounts payable. These schedules and other additional disclosures may be provided separately or incorporated in the notes to the financial statements.

The annual project financial statements will include comparative and cumulative figures and be presented in the local currency with the basis for conversion of any foreign exchange transactions or commitments explicitly stated.

Additional Auditor's Opinion

The auditor will, during the course of the audit, pay particular attention to the following:

i. The use of external funds in accordance with the relevant legal and financing agreements.

ii. The provision of counterpart funds in accordance with the relevant agreements and their use only for the purposes intended.

iii. The maintenance of proper books and records.

iv. The existence of project fixed assets and internal controls related thereto.

v. Any weaknesses in internal controls over the procurement process.

vi. On the imprest fund procedure (where applicable), audit procedures are planned and performed to ensure:
   - The imprest account (and any sub-accounts) has been managed in accordance with the Development Partner's Fund Disbursement Guideline
   - The cash balance of the imprest account (and any sub-accounts) is supported by evidence,
   - The expenditures paid from the imprest account (and any sub-accounts) comply with the approved project purpose and cost categories stipulated in the loan agreement, and
   - The amount of expenditures paid from the imprest account (and any sub-accounts) comply with the disbursement percentages stipulated in the loan agreement.

vii. Adequate supporting documentation has been maintained to authenticate claims stated in the SOE for reimbursement of eligible expenditures incurred and liquidation of advances provided to the imprest account (where applicable). On the SOE procedure, audit procedures are planned and performed to ensure
   - o The SOEs have been prepared in accordance with Fund Disbursement Guideline
   - o The individual payments for expenditures stated in the SOE are supported by evidence,
   - o The expenditures stated in the SOEs comply with the approved project purpose and cost categories stipulated in the loan agreement, and

- The amount of expenditures stated in the SOEs comply with disbursement percentages stipulated in the loan agreement.

Management Letter

Development Partners require the executing agency and/or implementing agency to provide a copy of the auditor's management letter. At the minimum, this will include:

(i) Any weaknesses in the accounting and internal control systems that were identified during the audit, including any irregularity in the use of the imprest fund and SOE procedures (where applicable);

(ii) Any identified internal control weaknesses related to the procurement process such as, over the bidding, evaluation and contract management domains;

(iii) Recommendations to rectify identified weaknesses;

(iv) Management's comments on the audit recommendations along with the timeframe for implementation;

(v) The status of significant matters raised in previous management letters;

(vi) Any other matters that the auditor considers should be brought to the attention of the project's management; and

(vii) Details of any ineligible expenditure identified during the audit. Expenditure is considered ineligible if it refers to expenditures incurred for purposes other than the ones intended under the legal agreement(s); expenditures not allowed under the terms of the legal/financing agreements; and expenditures incurred in violation of applicable government regulations. It is to be noted that only when the amount of any such ineligible expenditure is not material it should be included as part of management letter. However, if the amount of ineligible expenditure is material it shall be disclosed in relevant section of the audit report along with detail disclosure in the related attachment.

Chapter Six

Quality Assurance






Quality assurance

6.1 Quality control at FAPAD level

The quality of work performed by FAPAD affects their reputation and credibility, and ultimately their ability to fulfil their mandate. Accordingly, quality shall be built into the performance of the audit work conducted by FAPAD, rather than being an additional process once a report is produced.

As a component of the OCAG (SAI of Bangladesh), FAPAD is required to comply with the Quality Control System (QCS) issued by the OCAG which are based on the ISSAI 140 'Quality Control for SAIs' issued by INTOSAI, and which in turn is based on the key principles in the 'International Standard on Quality Control 1- Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and other Assurance and Related Services Engagements (ISQC 1)' issued by International Federation of Accountants (IFAC).

ISSAI 140 provides principles and application guidance to assist FAPAD in applying the key principles of ISQC-1 to the full range of their work, as appropriate to their mandate and circumstances.

FAPAD shall establish a system of quality control that adequately addresses to risks which may arise in many different aspects of FAPAD's work. For example, risks to quality may arise in the application of professional judgement, the design and implementation of policies and procedures, or in the methods used by FAPAD to communicate the results of their work. Maintaining a system of quality control requires ongoing monitoring and a commitment to continuous improvement.

Accordingly, FAPAD shall establish and maintain a system of quality control that covers each of the following elements:

(a) Leadership responsibilities for quality within FAPAD - the Director General of FAPAD retains overall responsibility for the system of quality control and the DG would assign a Person (preferably at a Director level) with sufficient and appropriate experience and ability for the operational responsibility of ensuring FAPAD's system of quality control.

(b) Relevant ethical requirements- FAPAD shall ensure all its audit personnel has complied with related ethical requirements stated in Section xx of Chapter of this Manual, including annual sign off by all individuals.

(c) Acceptance and continuance of client relationships and specific engagements- FAPAD should ensure that it will only carry out audits where its personnel are competent to perform the work and has the capabilities, including time and resources, to do so.

(d) Human resources- FAPAD shall ensure that it has sufficient personnel with the competence, capabilities, and commitment to ethical principles necessary to perform audit engagements in accordance with professional standards and applicable legal and regulatory requirements. Competence can be developed through a variety of methods, including the following:
- Professional education.
- Continuing professional development, including training.
- Work experience.
- Coaching by more experienced staff, like other members of the engagement team.
- Independent education for personnel who are required to be independent.

(e) Engagement performance: FAPAD shall promote consistency in the quality of engagement performance, supervision and review responsibilities to ensure that all audits are performed in accordance with professional standards and applicable legal and regulatory requirements, and that the Director General of FAPAD or any of its delegated personnel issue reports that are appropriate in the circumstances. The firm's review responsibility policies and procedures shall be determined on the basis that work of less experienced team members is reviewed by more experienced engagement team members and also include matters such as quality control review; appropriate consultation takes place on difficult or contentious matters etc. Appropriate teamwork and training assist less experienced members of the engagement team to clearly understand the objectives of the assigned work

(f) Monitoring - FAPAD should establish a monitoring process that should include an ongoing evaluation of its own system of quality control, including a review of completed audit work on sample basis by some independent senior personnel (preferably at a Director level) with sufficient and appropriate experience and authority and who was not involved in that audit assignment.

All the above policies and procedures shall be documented and communicated them to FAPAD personnel.

6.2 Quality control at Engagement Level

As stated in earlier section, under ISQC 1/ISSAI 140, FAPAD shall ensure that its personnel comply with professional standards and applicable legal and regulatory requirements and audit reports issued are appropriate in the circumstances.

Engagement teams have a responsibility to implement quality control procedures that are applicable to the respective audit engagement. The audit team leader (i.e. the Director or the Deputy Director) shall take responsibility for the overall quality on each audit engagement to which that person is assigned. The audit team leader shall be satisfied that the engagement team and any experts involved to assist the engagement team collectively have the appropriate competence and capabilities to perform the audit engagement in accordance with professional standards and applicable legal and regulatory requirements, and enable an appropriate auditor's report to be issued.

On or before the date of the auditor's report, the audit team leader shall, through a review of the audit documentation and discussion with the engagement team, be satisfied that sufficient and appropriate audit evidence has been obtained to support the conclusions reached and for the auditor's report to be issued. The audit team leader shall also be satisfied that members of the engagement team have undertaken appropriate consultation during the course of the engagement, both within the engagement team and others at the appropriate level within FAPAD or OCAG and determine that conclusions resulting from such consultations have been implemented during the audit.

Timely reviews of the following by the team leader at appropriate stages during the engagement allow significant matters to be resolved on a timely basis to the team leader's satisfaction on or before the date of the auditor's report:

- All evaluations and conclusions are soundly based and are supported by competent, reliable, relevant and reasonable audit evidence
- Critical areas of judgment, especially those relating to difficult or contentious matters identified during the course of the engagement have been resolved;
- Significant risks are identified and satisfactorily concluded;
- All errors, deficiencies and unusual matters have been properly identified, documented and evaluated; and
- Changes and improvements necessary to the conduct of future audits are identified, recorded and taken into account in later audit plans and in staff development activities
- Other areas the engagement partner considers important.

The audit team leader shall review certain minimum audit documentation before issuance of the audit report.

6.3 Audit documentation

Audit documentation refers to the record of audit procedures performed, relevant working papers and audit evidence that has been prepared and obtained throughout the audit to support conclusions and judgments reached by the auditor. Audit documentation may be recorded manually, electronically or in any other media. As per ISSAI 2230, the auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:

(a) The nature, timing and extent of the audit procedures performed to comply with the ISAs and applicable legal and regulatory requirements;
(b) The results of the audit procedures performed, and the audit evidence obtained; and
(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

In documenting the nature, timing and extent of audit procedures performed, the auditor shall record:

i. The identifying characteristics of the specific items or matters tested;
ii. Who performed the audit work and the date of such work was completed; and
iii. Who reviewed the audit work performed and the date and extent of such review?

The auditor shall document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place.

If the auditor identified information that is inconsistent with the auditor's final conclusion regarding a significant matter, the auditor shall document how the auditor addressed the inconsistency.

The auditor shall include in the audit documentation:

- Issues identified with respect to compliance with relevant ethical requirements and how they were resolved.
- Conclusions on compliance with independence requirements that apply to the audit, and any relevant discussions with the DG FAPAD that support these conclusions.
- The nature and scope of, and conclusions resulting from, consultations undertaken during the course of the audit.

In addition to working papers, audit documentation may also include documents, reports, and third party confirmations (i.e. bank balance certificates, external confirmations), reports on the work done by other auditors and other evidence supporting the audit findings etc.

The auditor shall prepare audit documentation on a timely basis. Preparing sufficient and appropriate audit documentation on a timely basis helps to enhance the quality of the audit and facilitates the effective review and evaluation of the audit evidence obtained and conclusions reached before the auditor's report is finalized. Documentation prepared after the audit work has been performed is likely to be less accurate than documentation prepared at the time such work is performed.

Audit working papers should be duly signed by the auditor conducting the examination i.e. the team member (e.g. deputy director), team leader (e.g. director) and the Director General of FAPAD. While completing documentation requirements, FAPAD audit teams shall ensure the following:

1. Whether the audit documentation is prepared on a timely basis?
2. Whether the audit documentation is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the following?
   - The nature, timing, and extent of the audit procedures performed to comply with auditing standards and applicable legal and regulatory requirements;
   - The results of the audit procedures performed, and the audit evidence obtained; and
   - Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.
3. While documenting the nature, timing and extent of audit procedures performed, whether the following was recorded
   - The identifying characteristics of the specific items or matters tested;
   - Who performed the audit work and the date of such work was completed; and
   - Who reviewed the audit work performed and the date and extent of such review?
4. Whether the documentation includes discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place.
5. Where it is identified that information is inconsistent with the auditor's final conclusion regarding a significant matter, whether it is documented as to how the inconsistency was addressed?
6. Where it is considered necessary in exceptional circumstances to depart from a relevant requirement in a SA, whether the audit documentation reflects how the alternative audit procedures performed achieved the aim of that requirement and the reasons for the departure.
7. Where in exceptional circumstances, new or additional audit procedures are performed or new conclusions are reached after the date of the audit report, whether the following were documented?
   - The circumstances encountered;
   - The new or additional audit procedures performed, audit evidence obtained, and conclusions reached, and their effect on the auditor's report; and
   - When and by whom the resulting changes to audit documentation were made and reviewed.
8. Is it ensured that after the assembly of the final audit file has been completed, no deletion or discard of audit documentation of any nature has taken place before the end of its retention period?
9. Where it is necessary to modify existing audit documentation or add new audit documentation after the assembly of the final audit file has been completed, whether the following were documented?
   - The specific reasons for making them; and
   - When and by whom they were made and reviewed.

The auditor shall document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place.

The form, content and extent of audit documentation by FAPAD team will depend on factors like:

- The size and complexity of the Project.
- The nature of the audit procedures to be performed.
- The identified risks of material misstatement.
- The significance of the audit evidence obtained.
- The nature and extent of exceptions identified.
- The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained.
- The audit methodology and tools used.

Audit documentation may be recorded on paper or on electronic or other media. Examples of audit documentation include:

- Audit programs.
- Analyses.
- Observations memo
- Summaries of significant matters.
- Letters of confirmation and representation.
- Checklists.
- Correspondence (including e-mail) concerning significant matters.

The auditor may include abstracts or copies of the Project's records (for example, significant and specific contracts and agreements) as part of audit documentation. Audit documentation, however, is not a substitute for the Project's accounting records.

In addition to the above specified documentation the auditor may include in the file:

- Documentation of Compliance with ISSAIs
- Consultation Documentation
- Documentation of Discussions of Significant Matters with Project Management, EA/IA and
- Others such as persons providing professional advice to the Project.

The auditor need not include in audit documentation superseded drafts of working papers and financial statements, notes that reflect incomplete or preliminary thinking, previous copies of documents corrected for typographical or other errors, and duplicates of documents.

6.4 Review of work done by one auditor by another senior auditor

Under ISQC 1, the quality control aspects of FAPAD shall ensure that the work of less experienced team members is reviewed by more experienced team members. A review consists of consideration whether, for example:

- The work has been performed in accordance with professional standards and applicable legal and regulatory 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

Supervision involves ensuring that:

- The members of the audit team fully understand all of the planning decisions before commencing the fieldwork;
- The fieldwork is performed in accordance with applicable auditing standards (e.g. ISSAI);
- The audit programs are completed as planned, unless changes are required;
- If changes are required to the audit plan/program, those changes are made by experienced audit team members and the work is properly performed based on those changes;
- Sufficient evidence has been obtained at the completion of audit work;
- Audit findings and conclusions are adequately supported by evidence in working papers;
- The audit is performed within the time budget and within deadline; and

The audit team leader shall ensure that all team members are properly supervised during the audit assignment. The extent of the required supervision will vary from situation to situation. In general:

- Junior audit team member should be supervised more closely than senior audit team member;
- Audit team members not familiar with the Project or the audit procedures being performed should be supervised more closely than those who are familiar with the Project or audit procedures; and
- Audit team members performing audit procedures requiring higher professional judgment should be supervised more closely than auditors performing simple, routine audit procedures.

Normally supervising team members remotely or from offsite can be difficult and less effective. Therefore, as far as practicable, audit team leader shall ensure on the ground supervision during the conduct of audit work at Project site.

To improve quality of the junior member, the reviewer should provide with feedback on his/her performance shortly after the file review, as opposed to waiting until the end of the audit assignment.

6.5 Involvement of Engagement Quality Control Reviewer (EQCR) in audit

Engagement quality control review is a process designed to provide an objective evaluation, on or before the date of the auditor's report, of the significant judgments the engagement team made and the conclusions it reached in formulating the auditor's report.

Based on pre-defined policies and considering the matter of public interest, the DG, FAPAD shall select Project that may require the involvement of engagement quality control reviewer during the audit process.

Engagement quality control reviewer is a senior personnel within FAPAD (i.e. a Director) or from other directorate of the OCAG, or a suitably qualified external person who is not part of the engagement team. Such EQCR shall have sufficient and appropriate experience and authority to objectively evaluate the significant judgments the engagement team made and the conclusions it reached in formulating the auditor's report.

For audits of Project for which FAPAD has determined that an engagement quality control review is required, the engagement team leader shall ensure that an engagement quality control reviewer has been appointed and discussed all significant matters arising during the audit engagement with the engagement quality control reviewer.

The engagement quality control reviewer shall perform an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor's report. This evaluation shall involve:

(a) Discussion of significant matters with the engagement partner;
(b) Review of the financial statements and the proposed auditor's report;
(c) Review of selected audit documentation relating to the significant judgments the engagement team made and the conclusions it reached;
(d) 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; and
(e) Evaluation of the conclusions reached in formulating the auditor's report and consideration of whether the proposed auditor's report is appropriate.

The engagement quality control reviewer shall document that the procedures required by FAPAD's policies on engagement quality control review have been performed and 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 it reached were not appropriate.

6.6 Audit files completion and retention

The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report.

After the assembly of the final audit file has been completed, the auditor shall not delete or discard audit documentation of any nature before the end of its retention period.

ISQC 1 requires FAPAD to establish policies and procedures for the timely completion of the assembly of audit files. An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor's report.

As per ISSAI 2230, the completion of the assembly of the final audit file after the date of the auditor's report is an administrative process that does not involve the performance of new audit procedures or the drawing of new conclusions. Changes may, however, be made to the audit documentation during the final assembly process if they are administrative in nature. Examples of such changes include:

- Deleting or discarding superseded documentation.
- Sorting, collating and cross-referencing working papers.
- Signing off on completion checklists relating to the file assembly process.
- Documenting audit evidence that the auditor has obtained, discussed and agreed with the relevant members of the engagement team before the date of the auditor's report.

6.7 Procedures to resolve disputed between the Audit Team and the Project or EA/IA

At times differences of opinion can arise within the engagement team, with those consulted or, where applicable, between the engagement team leader and the engagement quality control reviewer. Auditing standards require FAPAD to establish policies and procedures for dealing with and resolving differences of opinion.

FAPAD shall establish policies and procedures for dealing with and resolving differences of opinion within the audit engagement team, with those consulted and, where applicable, between the engagement team leader and the engagement quality control reviewer. Such policies and procedures shall require that:

(a) Conclusions reached be documented and implemented; and
(b) The report not is dated until the matter is resolved.

Effective procedures encourage identification of differences of opinion at an early stage, provide clear guidelines as to the successive steps to be taken thereafter, and require documentation regarding the resolution of the differences and the implementation of the conclusions reached.

Procedures to resolve such differences may include consulting with another senior personnel with FAPAD not involved in audit of that Project, or the OCAG or any of its other Directorate.

If differences of opinion arise within the engagement team, with those consulted or, where applicable, between the engagement team leader and the engagement quality control reviewer, the engagement team shall follow FAPAD policies and procedures for dealing with and resolving differences of opinion.

6.8 Complaints and Allegations

FAPAD shall establish policies and procedures requiring documentation of complaints and allegations and the responses to them and to provide it with reasonable assurance that it deals appropriately with:

(c) Complaints and allegations that the work performed by FAPAD audit team fails to comply with professional standards and applicable legal and regulatory requirements; and
(d) Allegations of non-compliance with FAPAD/OCAG's system of quality control.

As part of this process, FAPAD shall establish clearly defined channels for FAPAD personnel to raise any concerns in a manner that enables them to come forward without fear of reprisals.

If during the investigations into complaints and allegations, deficiencies in the design or operation of FAPAD's quality control policies and procedures or non-compliance with FAPAD and/or OCAG's system of quality control by an individual or individuals are identified, FAPAD shall take appropriate actions.

Source of Complaints and Allegations

Complaints and allegations (which do not include those that are clearly frivolous) may originate from within or outside FAPAD. They may be made by FAPAD personnel, Projects being audited, related EA/IA or other third parties. They may be received by engagement team members or other FAPAD personnel.

Investigation Policies and Procedures
Policies and procedures established for the investigation of complaints and allegations may include for example, that the Director or other personnel appointed by the Director General supervising the investigation:

- Has sufficient and appropriate experience;
- Has authority within FAPAD; and
- Is otherwise not involved in the audit engagement.

The person appointed by the DG, FAPAD for supervising the investigation may involve legal counsel, as necessary.

Appendix 1: Pro forma project financial statements

Project financial statements (GOB Approved Model)

As of and for the years ended 30 June 2020

…………… (Development partner's) Grant/Loan Resources	Notes	Opening balance as at 1 July 2019 (Cumulative prior period)	For the year ended 30 June 2020 (current period)	Closing balance as at 30 June 2020 (Cumulative current period)
Government of Bangladesh	6			
Loan from lender/donor	7			
Other resources	8			
Cash opening balance	5			
Total resources				

Expenditure and Cash				
1. Consultancy				
2.				
3.				
4.				
Total Expenditure				

Cash closing balance				
Imprest account				
Operating Account (RPA)				
Operating Account (GOB)				
Total Expenditure and Cash	5			

The annexed notes 1 to 12 form an integral part of these special purpose financial statements.

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Project Director Chief Accountant

Statement of the Project sources and uses of funds of Project —— funded by Grant/Loan no ….

As of and for the year ended 30 June 2020

In (currency)		Actual		Budget		Difference	
	Notes	For the year ended 30 June 2020	Cumulative as of 30 June 2020	For the year ended 30 June 2020	Cumulative as of 30 June 2020	For the year ended 30 June 2020	Cumulative as of 30 June 2020
Cash and bank balances as at 01 July 2019	**5**	**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**
Add: Funding from Government of Bangladesh	**6**	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Funding from Development Partner (loan from lender/donor)	**7**	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Funding from other sources	**8**	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Total financing		**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**
Exchange difference		xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Other income		xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Total Resources (financing and other receipts)		**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**
Less: Expenses from Government of Bangladesh	**9**	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Expenses from Development Partner	**10**	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Expenses from other sources	**11**	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Total Project expenses		**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**
Exchange rate differences		xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Other expenses		xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Total Project expenses and other expenses		**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**
Cash and bank balances as at 30 June 2020	**5**	**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**	**xxxx**

The annexed notes 1 to 12 form an integral part of these special purpose financial statements.

Project Director

Chief Accountant

Statement of uses of funds by Project activity and comparison to budget

As of and for the years ended 30 June 2020

................(Development partner's) Grant/Loan				
	For the year ended 30 June 2020	**Cumulative as of 30 June 2020**	**For the year ended 30 June 2020**	**Cumulative as of 30 June 2020**
Category 1: Civil Works or as per DCA				
Category 2: Equipment or as per DCA				
Category 3: Instructors or as per DCA				
Category 4: Fellowships or as per DCA				
Category 5: Local Training or as per DCA				
Category 6: International Consultant or as per DCA				
Category 7: Unallocated or as per DCA				
Category 8: or as per DCA				
Total Project expenses				
Total	xx	xx		

The annexed notes 1 to 12 form an integral part of these special purpose financial statements.

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Project Director Chief Accountant

Statement on cash flow on Cash /Imprest accounts

As of and for the year ended 30 June 2020

Balance as of 01 July 2019		**xx**
Add:		
	Receipt from Government	xx
	Receipt from Development Partner	
	Exchange rate difference	xx
Total		**xxx**
Less:		
	Amount of eligible expenses	xx
	Exchange rate difference	xx
Total		**xx**
Balance as of 30 June 2020		**xx**

The annexed notes 1 to 12 form an integral part of these special purpose financial statements.

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Project Director Chief Accountant

Note: Statement of cash flow may be prepared separately based on bank account.

Notes to the financial statements

1. General Information

The following information may be added:

A summary of the Project is to be given including Loan/Grant date agreement of between Government and development partners.

- A brief of the objective of the project and its components.
- Expected closing date for the project.
- The total number of staff involved.
- The approval date and authority of these financial statements.

2. Significant Accounting policies

Basis of preparation
The financial statements of the Project have been prepared in accordance with IPSAS *Financial Reporting Under the Cash Basis of Accounting,* and comply with the Project Accounting Manual issued by the Finance Division, Ministry of Finance, Government of Bangladesh as well as …… (development partners requirements) and the covenants of the …. (Loan/Grant). These special purpose financial statements reflect the data for the year ended 30 June 2020.

Under this basis of accounting, financing is recognized when received rather than when earned and expenses are recognized when paid rather than when incurred. Expenses are resources directed for the payment of works, goods and services, recognized in the financial statements in the period when they are paid.

Financing
The disbursement procedures need to be described briefly.

The amounts of Government financing are recognized as such and included in the special purpose financial statements when the funds are transmitted to the Project Current account (the "Government financing account").

Expenses
Consistent with the cash basis of accounting, the Project expenses are recognized and included in the special purpose financial statements when the payment is actually made to suppliers of goods, works and/or services as opposed to when goods are received/ services are rendered.

Functional and presentation currency
BDT is the national currency of the Government of Bangladesh. The special purpose financial statements of the Project are presented in BDT/USD (presentation currency) and rounded to the nearest integer of BDT/USD. Income and expenses denominated in BDT are converted into USD applying the exchange rate set out by the Bangladesh Bank on the date of the transaction.

Account balances denominated in BDT are converted into USD applying the exchange rate set out by the Bangladesh Bank at the reporting date. As of 30 June 2020 the exchange rate is xxxx.

3. Taxation

According to the Loan/Grant Agreement, the loan and grant amounts should not be used to pay any taxes and duties.

4. Fixed Assets

Fixed assets of the Project include office equipment, vehicles and furniture procured for project implementation. Cost of fixed assets includes the cost of procurement and other related expenditures.

Due to the cash basis of accounting, the fixed assets procured under the Project are measured on the basis of cost of procurement and reflected in the special purpose financial statement as expenditures instead of capitalization in balance sheet. The record of fixed assets is maintained in inventory sheets.

Considering non-commercial status of the Project and cash basis of accounting, depreciation for the fixed assets is not accrued.

5. Cash and bank balances / Cash and cash equivalents

The Project maintains xx number of bank accounts, an imprest bank account or revolving fund, which is kept at xxx Bank to hold funds advanced/received from Donor and an operating account at xxx Bank to hold funds advanced/received from GOB as well as funds transferred from the imprest bank account. Year-end cash balances were as follows:

	Opening balance as at 30 June 2019 (inception to 30 June 2019)	For the year ended 30 June 2020	Closing balance as at 30 June 2020 (inception to 30 June 2020)
Imprest account	xx		xx
Operating account (RPA)	xx		xx
Operating account (GOB)	xx		xx
Total	xx		xx

6. Funding received from Government of Bangladesh

Funds are allocated by the Government of Bangladesh to cover GOB's share of eligible project expenditures, as specified in the project manual and in annual development programme for each of the Project. Any allocated funds that have not been expended by the end of a fiscal year lapse and must be returned to GOB. GOB contribution to the Project since inception and for the year are as follows:

	Opening balance as at 30 June 2019 (inception to 30 June 2019)	For the year ended 30 June 2020	Closing balance as at 30 June 2020 (inception to 30 June 2020)
Disbursement by GOB	xx	xx	xx
Less: Refund to GOB	xx	xx	xx
Total	xx	xx	Xx

7. Funding received from Development Partners (loans from lender/donor)

The (name of the lender/donor) has provided funds to the Project to cover its share of eligible project expenditure. These funds, which must be repaid to the (name of the lender/donor) after the conclusion of the Project, have been drawn by the Project in accordance with the following withdrawal procedures:

	Opening balance as at 30 June 2019 (inception to 30 June 2019)	For the year ended 30 June 2020	Closing balance as at 30 June 2020 (inception to 30 June 2020)
SOE Procedures	xx	xx	xx
Direct payments	xx	xx	xx
Imprest account replenishments	xx	xx	xx
Others	xx	xx	xx
Total	xx	xx	xx

8. Funding from other resources

Other resources consist of the following:

	Opening balance as at 30 June 2019 (inception to 30 June 2019)	For the year ended 30 June 2020	Closing balance as at 30 June 2020 (inception to 30 June 2020)
Project revenues	xx	xx	xx
Exchange gain and loss	xx	xx	xx
Less: TDS on interest and other fees	xx	xx	xx
Total	xx	xx	xx

9. Expenses from Government fund

In (currency)	Actual		Budget		Difference	
	For the period ended 30 June 2019	Cumulative as of 30 June 2019	For the period ended 30 June 2019	Cumulative as of 30 June 2019	For the period ended 30 June 2019	Cumulative as of 30 June 2019
Category 1: Civil Works or as per DCA						
Category 2: Equipment or as per DCA						
Category 3: Instructors or as per DCA						
Category 4: Fellowships or as per DCA						
Category 5: Local Training or as per DCA						
Category 6: International Consultant or as per DCA						
Category 7: Unallocated or as per DCA						
Category 8: or as per DCA						
Total Project expenses						

10. Expenses from Development partners

In (currency)	Actual		Budget		Difference	
	For the period ended 30 June 2019	Cumulative as of 30 June 2019	For the period ended 30 June 2019	Cumulative as of 30 June 2019	For the period ended 30 June 2019	Cumulative as of 30 June 2019
Category 1: Civil Works or as per DCA						
Category 2: Equipment or as per DCA						
Category 3: Instructors or as per DCA						
Category 4: Fellowships or as per DCA						
Category 5: Local Training or as per DCA						
Category 6: International Consultant or as per DCA						
Category 7: Unallocated or as per DCA						
Category 8: or as per DCA						
Total Project expenses						

10.1 Reconciliation of expenses by funding methods

Nature of expense claim	**Category 1**	**Category 2**	**Category 3**	**Category 4**	**Category 5**	**Category 6**	**Category 7**	**Category 8**	**Amount Received**	**Amount Claimed**	**Difference**
SOE											
Direct payments											
Imprest account											
Others											
Total expenses claimed											
Memorandum record											
Add: Expenses not claimed at year-end											
Less: Unclaimed expenses at previous year-end											
Total expenditure											

10.2 Summary of Withdrawal Applications (SOE)

SOE No	Date	Category 1	Category 2	Category 3	Category 4	Category 5	Category 6	Category 7	Category 8	Amount Received	Amount Claimed	Difference
Total										**xxxx**	**xxxxx**	**xxxx**

10.3 Summary of Withdrawal Applications (Imprest Account Replenishment)

No	Date	Category 1	Category 2	Category 3	Category 4	Category 5	Category 6	Category 7	Category 8	Amount Received	Amount Claimed	Difference
Total										**xxxx**	**xxxxx**	**xxxx**

10.4 Summary of Withdrawal Applications (Direct Payment)

No	Date	Category 1	Category 2	Category 3	Category 4	Category 5	Category 6	Category 7	Category 8	Amount Received	Amount Claimed	Difference
Total										**xxxx**	**xxxxx**	**xxxx**

11. Expenses from other resources

In (currency)	Actual		Budget		Difference	
	For the period ended 30 June 2019	Cumulative as of 30 June 2019	For the period ended 30 June 2019	Cumulative as of 30 June 2019	For the period ended 30 June 2019	Cumulative as of 30 June 2019
Consultant fee	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Operating cost	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Others	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
Total Project expenses	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx

Note: According to IPSAs 1.7.8 (c) an explanation is required about the material difference between the budget and actual amount.

12. Project implementation

As of 30 June 2020, overall xx% of Grant/Loan has been implemented in the framework of the Grant/Loan Agreement xxxxx. The project expenses by categories are presented in the tables below:

Loan/ Grant	Expenses as of 30 June 2020 in currency unit	Budget as of 30 June 2020 in currency unit	Budgeted expenses as of 30 June 2020 (in percentage)	Total Project Budget in Currency unit	Project implementation as of 30 June 2020 (in percentage)
Category 1: Civil Works or as per DCA					
Category 2: Equipment or as per DCA					
Category 3: Instructors or as per DCA					
Category 4: Fellowships or as per DCA					
Category 5: Local Training or as per DCA					
Category 6: International Consultant or as per DCA					
Category 7: Unallocated or as per DCA					
Category 8: or as per DCA					
Total Project expenses					

Appendix 2: Pro forma audit report

Independent Auditor's Report
To the Secretary, Ministry of xxxx, Bangladesh Secretariat, Dhaka
Report on the Audit of the Project Financial Statements

Opinion

We have audited the accompanying financial statements of xxxxxx (the "Project"), which comprise of the statement of cash receipts and expenditure, statement of comparison of budget and actual expenditure as at and for the year ended 30 June 2020, and a summary of significant accounting policies and other explanatory notes *(modify as applicable based on project financial statements prepared by EA/IA)*.

In our opinion, the project financial statements present fairly, in all material respects the cash and cash equivalents of the Project as at 30 June 2020 and the funds received and expenses incurred for the year then ended in accordance with the IPSAS *Financial Reporting Under the Cash Basis of Accounting* and the requirements of Project Accounting Manual issued by the Finance Division, Ministry of Finance, Government of Bangladesh as well as those of xxxxxx (development partner's guidelines and agreement).

Basis for opinion

We conducted our audit in accordance with the 'Government Auditing Standards of Bangladesh' (GASB) issued by the Office of the Comptroller and Auditors General (OCAG) of Bangladesh which are based on the International Standards of Supreme Audit Institutions (ISSAIs) issued by International Organization of Supreme Audit Institutions (INTOSAI)Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Project in accordance with the 'Code of Ethics' issued by the OCAG Bangladesh which is based onISSAI 130 - Code of Ethics (INTOSAI Code), and we have fulfilled our other ethical responsibilities in accordance with these ethical requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Matter

This audit of the Project financial statements has been conducted to comply with the specific requirements of the Development Partner as specified in the related Loan/Grant agreement. OCAG reserves all the rights to incorporate any audit observation from this report in the CAG's audit report for being laid before Parliament to fulfil the constitutional responsibilities.

Responsibilities of Management for the Financial Statements and Internal Controls

Management of the Project Management Unit (the "PMU") of Ministry of xxxx is responsible for the preparation and fair presentation of these special purpose financial statements in accordance with the International Public Sector Accounting Standard ("IPSAS") Financial Reporting Under the Cash Basis of Accounting issued by the International Public Sector Accounting Standards Board (the IPSASB) of the International Federation of Accountants (IFAC), the requirements of Project Accounting Manual issued by the Finance Division, MoF, GoB as well as those of the xxxxxx (development partner's guidelines and agreement), and for such internal control as management determines is necessary to enable the preparation of special purpose financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibilities for the Audit of the Special Purpose Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statement are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with GASB which are based on ISSAI will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these special purpose financial statements.

As part of an audit in accordance with the Government Auditing Standards of Bangladesh which are based on ISSAIs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entities internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Report on Requirements of the Development Partner

In accordance with the Grant/Loan agreement number xxx executed on xx 20xx, between the Government of Bangladesh and World Bank/Asian Development Bank, We also report that:

a) in our opinion the funds were utilized for the purposes described in the Financing Agreements and agreed Project's annual work plans; (if no material exception is identified)

or

except for the amount of Tk xxxx as described in detail in the Attachment I to this report, in our opinion the funds were utilized for the purposes described in the Financing Agreements and agreed Project's annual work plans; (if material exception has been identified)

b) in our opinion, the imprest account statements give a true and fair view of the imprest accounts as at 30 June 2020 and the cash movements of these accounts for the period then ended, in accordance with the …. (developments partners) Guidelines; (if no material exception is identified)

or

except for the amount of Tk xxxx as described in detail in the Attachment II to this report, in our opinion the imprest account statements give a true and fair view of the imprest accounts as at 30 June 2020 and the cash movements of these accounts for the period then ended, in accordance with the …. (developments partners) Guidelines; (use this only if material exception has been identified)

c) in our opinion, project expenditures disbursed and expenses claimed are in compliance with established proper procedures and according to the provisions of the Financing Agreements, Loan/Grant Disbursement Handbook, and guidelines on Financial Management and Analysis of Projects issued by the …. (developments partners); (if no material exception is identified)

or

except for the amount of Tk xxxx as described in detail in the Attachment III to this report, in our opinion project expenditures disbursed and expenses claimed are in compliance with established proper procedures and according to the provisions of the Financing Agreements, Loan/Grant Disbursement Handbook, and guidelines on Financial Management and Analysis of Projects issued by the …. (developments partners); (use this only if material exception has been identified)

d) the procurement of goods, services and civil works have been made in accordance with the Financing Agreements and …….(developments partners) procurement regulations; and(if no material exception is identified)

or

except for the amount of Tk xxxx as described in detail in the Attachment IV to this report, in our opinion procurement of goods, services and civil works have been made in accordance with the Financing Agreements and …….(developments partners) procurement regulations, and; (use this only if material exception has been identified)

e) the EA/PMU has complied with covenants specified in the Grant/Loan Agreement xxxxxxx. (if no material exception is identified)

or

except for the non-compliance of covenants as described in detail in the Attachment V to this report, the EA/PMU has complied with covenants specified in the Grant/Loan Agreement xxxxxxx. (use this only if material exception has been identified)

Name of Auditor

Designation: Director/Deputy Director
For Director General
Foreign Aided Projects Audit Directorate

Place: Dhaka Date:

Attachments I to V referred above are attached herewith and forms an integral part of this audit report.

Appendix 3

LIST OF ISSAI FOR AUDITS OF HISTORICAL FINANCIAL INFORMATION

200–299 GENERAL PRINCIPLES AND RESPONSIBILITIES

ISA 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing
ISA 210, Agreeing the Terms of Audit Engagements
ISA 220, Quality Control for an Audit of Financial Statements
ISA 230, Audit Documentation
ISA 240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements
ISA 250 (Revised), Consideration of Laws and Regulations in an Audit of Financial Statements
ISA 260 (Revised), Communication with Those Charged with Governance
ISA 265, Communicating Deficiencies in Internal Control to Those Charged with Governance and Management

300–499 RISK ASSESSMENT AND RESPONSE TO ASSESSED RISKS

ISA 300, Planning an Audit of Financial Statements
ISA 315 (Revised), Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment
ISA 320, Materiality in Planning and Performing an Audit
ISA 330, The Auditor's Responses to Assessed Risks
ISA 402, Audit Considerations Relating to an Entity Using a Service Organization
ISA 450, Evaluation of Misstatements Identified during the Audit

500–599 AUDIT EVIDENCE

ISA 500, Audit Evidence
ISA 501, Audit Evidence—Specific Considerations for Selected Items
ISA 505, External Confirmations
ISA 510, Initial Audit Engagements—Opening Balances
ISA 520, Analytical Procedures
ISA 530, Audit Sampling
ISA 540, Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures
ISA 550, Related Parties
ISA 560, Subsequent Events
ISA 570 (Revised), Going Concern
ISA 580, Written Representations

600–699 USING THE WORK OF OTHERS

ISA 600 Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)

ISA 610 (Revised 2013), Using the Work of Internal Auditors

ISA 620 Using the Work of an Auditor's Expert

700–799 AUDIT CONCLUSIONS AND REPORTING

ISA 700 (Revised), Forming an Opinion and Reporting on Financial Statements

ISA 701, Communicating Key Audit Matters in the Independent Auditor's Report

ISA 705 (Revised), Modifications to the Opinion in the Independent Auditor's Report

ISA 706 (Revised), Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report

ISA 710, Comparative Information—Corresponding Figures and Comparative Financial Statements

ISA 720 (Revised), The Auditor's Responsibilities Relating to Other Information

Appendix 4

Pro forma Audit Engagement Letter

Date

[Insert Address of Auditee]

Subject: Letter of engagement regarding the financial audit of [Insert Name of Project]

Reference:

Dear Sir

Introduction

The purpose of this letter is to set out the basis on which the Foreign Aided Project Audit Directorate (FAPAD) under the Office of the Comptroller and Auditor General (OCAG) of Bangladesh audits the financial statements of the [Insert Name of the Responsible Party/ Organisation/ Project/ Entity] and the respective responsibilities of the management of [Insert Name of Responsible Party/ Organisation/ Project/ Entity]. This engagement will be conducted with the sole objective of our expressing an opinion on the [Insert details of statements being audited] to fulfil the reporting responsibilities as set out in the related Loan/Grant agreement, and not for any other purposes.

The terms of the audit engagement are set out below. This letter will remain effective until a new audit engagement letter is issued.

Scope of the Audit

The financial audit will be conducted in accordance with the Government Auditing Standards of Bangladesh which are based on the International Standards for Supreme Audit Institutions (ISSAIs) and will cover the financial statements of the [Insert Name of Project] for the financial year [Insert Financial Year].

Responsibilities of auditors

FAPAD under the OCAG of Bangladesh conduct the audit of Project financial statements to comply with requirement specified in the Agreement for Financing Loan/Grant number xxxx with [Insert name of the Development Partner]. OCAG reserves all the rights to use any work done and any audit observation raised during this audit to fulfil the constitutional responsibilities.

Consequently, the FAPAD on behalf of the OCAG is responsible for reporting whether the financial statements of the [Insert name of the Project] give a true and fair view and whether the activities, financial transactions and information reflected in the financial statements are, in all material respects, in compliance with the authorities which govern them. This responsibility includes performing procedures to obtain audit evidence about whether the Project's expenditure and income have been applied to the purposes intended by the Development Partner. Such procedures include the assessment of the risks of material non-compliance.

The financial audit process
The audit will be conducted in accordance with the Government Auditing Standards of Bangladesh which are based on the International Standards of Supreme Audit Institutions (ISSAIs). These Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance over whether the Project financial statements are free from material misstatement.

We shall obtain an understanding of the accounting and internal control systems to assess their adequacy as a basis for the preparation of the Project financial statements and to establish whether proper accounting records have been maintained by the [name of Project]. We shall expect to obtain such appropriate evidence as we consider sufficient to enable us to draw reasonable conclusions there from.

The nature and extent of our procedures will vary according to our assessment of the [Insert name of Project] and, where we wish to place reliance on it, the internal control system, and may cover any aspect of the operations that we consider appropriate.

Project management responsibilities
Our audit will be conducted on the basis that the Project management and those charged with governance acknowledge and understand that they have responsibility for:

- The preparation of financial statements that show a true and fair view in accordance with the Project Accounting Manual issued by the Finance Division, Ministry of Finance, Government of Bangladesh and IPSAS Cash Basis of Accounting;

- For such internal control as the Project management and those charged with governance determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and

- To provide us with:
  - Access to all information of which the Project Management and those charged with governance are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
  - Additional information that we may request for the purpose of the audit; and
  - Unrestricted access to persons within the Project from whom we determine it necessary to obtain audit evidence.

In addition to the responsibility for the preparation and presentation of the financial statements described above, management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.

Management representations

As part of our audit process we will request from management written representations on matters material to the Project financial statements where other sufficient appropriate evidence cannot reasonably be expected to exist, and where management may have made certain oral representations (Letter of Representation).

Yours Sincerely,

Director General
Foreign Aided Project Audit Directorate (FAPAD)

For and on behalf of
The Office of the Comptroller and Auditor General

Appendix 5

Information to be maintained in Permanent File

Permanent File: Beginning of Planning

Every project will have an extensive databank to support a cost-effective audit of the project. The permanent file contains all project related information necessary to enhance auditor's understanding of the project, and should be the basis for project Audit Work plan.

Permanent File Summary Sheet

Project Name: ………………………………………………Loan/Grant No:…………………

Development Partner (s):……………………………………………………………………

Administrative Ministry:………………………… ………………………………………

Executing Agency:…………………………………………………………………………

Project Value: Donor: ……………………………………………..
GoB:…………………..

Project Period: Start: ……………………………………… End:……………………… .

Revised Date: Start: ……………………………………… End:……………………….

Project Manager: Name and Address:………………………………………………………...
……………………………………………………………………………………..
Telephone No: …………………………………

Project Sites:

1 Name and Address of Contract person……………………………………
Telephone No: ....

2 Name and Address of Contract person ………….…………
Tel………...

3 Name and Address of Contract person …………………….
Tel………...

Key Inputs (Original): Consultants' Services: …………………………
Equipment:…………..
Civil Works: …………………………………
Other:…………………

Key outputs (Original): Physical:………………………………………………………………….

Incremental Changes after revision: Time: …………………………………… Cost:…………...

Quantity: ………………………………………………………

Specification:……………...

Documents	Date placed in the File	Ref:, Page No., etc.	Revised Version if any
• Project Performa/DPP			
• Loan/Grant Agreement/DCA			
• Staff Appraisal Report			
• Disbursement Letter			
• Mission Report			
• Consultant's Studies			
• List of category of Expenditure			
	Year 200x	Year 200x	Year 200x
• Financial Statement			
• Budget			
• Project Work Plan			
• Audit Report			
• Monitoring Report			
• Management Letter			
• Unresolved audit observations			
• Any other/specify			

Permanent File inspected by Deputy Director/Director/Director General and updated.

Date: ……………………………………… Initial: ……………………………

Date: ………………………………………. Initial: …………………………….

Date: ………………………………………. Initial: ……………………………..

Identifying Project Expense Category:

The starting point in the project audit planning is the account areas/expense category that we come across in a given project. Plan the audit around transaction streams and balances. Below listed are expense categories/ operations common to project. Very often different titles are used in the financial document but by the nature they belong to some broad category of expenditure identified here. Auditor will go through the project the agreement carefully to ensure that no significant expense category has left out.

Expense Category/Operation:

1. Civil Works
2. Equipment and Materials
3. Consultant Service-Foreign/Local
4. Training and Studies/Seminar/Workshop
5. Incremental Staff
6. Interest and Commitment Charge
7. Front-end Fee
8. Research Support
9. Teaching Support
10. Project Costs
11. Project Personnel
12. Monitoring and Evaluation Costs
13. Mission Costs
14. Miscellaneous
15. Reporting Cost
16. Direct Payment/Charge by DPs
17. Sundries
18. NGO Fee
19. Travel cost
20. Technical Assistance
21. Land Acquisition/Land Development

Appendix 6

Documentation checklist

Adequacy of records both accounting and other is a pre-requisite for reliable accounting system and is an important internal control activity. Below is an exhaustive list of records that should be maintained in a project and availability of any record. Documents not relevant to a project may be ignored and mentioned as Not Required (NR).

Sl #	Name of Records/Document	Available	
		Yes	No
1.	Financial Statement		
2.	Imprest/CONTASA/DOSA/SAFE Account Statement from Bangladesh Bank		
3.	STD/Operating Account Statement		
4.	Authorization of Development Partners Fund from Ministry of Finance		
5.	Budget Allocation of GOB Fund/GO		
6.	Budget Register		
7.	Bill Register		
8.	Cheque Register		
9.	Bank Reconciliation Statement		
10.	Withdrawal Application and Register with Statement of Expenditure (SOE)		
11.	Cash Book		
12.	Journal/Ledger		
13.	Monthly Accounts		
14.	Miscellaneous Revenue Register		
15.	Payroll Register		
16.	Organogram		
17.	Contractor Ledger/IT and VAT Register		
18.	Work Authorization/Work Plan		
19.	Public/Tender Notice or Bidding Documents		
20.	Letter of Acceptance/ Letter of Indent		
21.	Comparative Statement/Bid Evaluation Report		
22.	Work Order/Bid Documents		
23.	Measurement Book/work Certificate		
24.	Security Deposit Register/ Performance Guarantee Register		
25.	Stock and Assets Register		

Sl #	Names of Records/Document	Available	
		Yes	No
26.	Stock and Assets Verification Report		
27.	Contract Agreement/ Purchase Contract		
28.	Letter of Credit(LC)		
29.	Suppliers Invoice and Certificate of Origin		
30.	Shipping or Import Documents and Inspection Certificate		
31.	Contractor Invoice and Work Certificate		
32.	Recurrent Cost Records		
33.	Evidence of Payment (Bill/Voucher)/ Bank Interim Payment Certificate (IPC)		
34.	File Regarding Land Acquisition (LA) Case		
35.	Survey Report		
36.	Sale/Lease Deed/ Possession Certificate		
37.	Administrative and Technical Sanction		
38.	Drawing and Design of the work		
39.	Copy of Advertisement		
40.	Schedule of Rate/Estimate		
41.	Work Completion Certificate		
42.	Work Progress Report		
43.	Development Partners Agreement/ Contract		
44.	Delegation of Financial Power		
45.	Terms of Reference (TOR)		
46.	Approval of Consultant Final Report		
47.	Employment Records/Service Book		
48.	Attendance Register		
49.	Retention Order		
50.	Government Orders(GO) of Foreign Training/ Study Tour/ Seminar/ Workshop		
51.	List of Participants For Training/ Workshop/ Seminar		
52.	Log Book/ Register of Vehicle		
53.	Records on Claims and Disputes Resolution		
54.	Formal Apparels by Bidders and Outcomes Register of Contracts		

Appendix 7

Fraud Risk Factors as per ISSAI 2240

Risk factors that relate to misstatements arising from misappropriation of assets are also classified according to the three conditions generally present when fraud exists: incentives/pressures, opportunities, and attitudes/rationalization. Some of the risk factors related to misstatements arising from fraudulent financial reporting also may be present when misstatements arising from misappropriation of assets occur. For example, ineffective monitoring of management and other deficiencies in internal control may be present when misstatements due to either fraudulent financial reporting or misappropriation of assets exist. The following are examples of risk factors related to misstatements arising from misappropriation of assets.

Incentives/Pressures

Personal financial obligations may create pressure on management or employees with access to cash or other assets susceptible to theft to misappropriate those assets.

Adverse relationships between the entity and employees with access to cash or other assets susceptible to theft may motivate those employees to misappropriate those assets. For example, adverse relationships may be created by the following:

- Known or anticipated future employee layoffs.
- Recent or anticipated changes to employee compensation or benefit plans.
- Promotions, compensation, or other rewards inconsistent with expectations.

Opportunities

Certain characteristics or circumstances may increase the susceptibility of assets to misappropriation. For example, opportunities to misappropriate assets increase when there are the following:

- Large amounts of cash on hand or processed.
- Inventory items that are small in size, of high value, or in high demand.
- Easily convertible assets, such as bearer bonds, diamonds, or computer chips.
- Fixed assets which are small in size, marketable, or lacking observable identification of ownership.

Inadequate internal control over assets may increase the susceptibility of misappropriation of those assets. For example, misappropriation of assets may occur because there is the following:

- Inadequate segregation of duties or independent checks.
- Inadequate oversight of senior management expenditures, such as travel and other re-imbursements.
- Inadequate management oversight of employees responsible for assets, for example, inadequate supervision or monitoring of remote locations.

- Inadequate job applicant screening of employees with access to assets.
- Inadequate record keeping with respect to assets.
- Inadequate system of authorization and approval of transactions (for example, in purchasing).
- Inadequate physical safeguards over cash, investments, inventory, or fixed assets.
- Lack of complete and timely reconciliations of assets.
- Lack of timely and appropriate documentation of transactions, for example, credits for merchandise returns.
- Lack of mandatory vacations for employees performing key control functions.
- Inadequate management understanding of information technology, which enables information technology employees to perpetrate a misappropriation.
- Inadequate access controls over automated records, including controls over and review of computer systems event logs.

Attitudes/Rationalizations

- Disregard for the need for monitoring or reducing risks related to misappropriations of assets.
- Disregard for internal control over misappropriation of assets by overriding existing controls or by failing to take appropriate remedial action on known deficiencies in internal control.
- Behavior indicating displeasure or dissatisfaction with the entity or its treatment of the employee.
- Changes in behavior or lifestyle that may indicate assets have been misappropriated.
- Tolerance of petty theft.

Consideration at the Assertion Level

Specific responses to the auditor's assessment of the risks of material misstatement due to fraud will vary depending upon the types or combinations of fraud risk factors or conditions identified, and the classes of transactions, account balances, disclosures and assertions they may affect.

Examples of responses to the auditor's assessment of the risk of material misstatements due to misappropriation of assets are as follows:

- Counting cash or securities at or near year-end.
- Confirming directly with customers the account activity (including credit memo and sales return activity as well as dates payments were made) for the period under audit.
- Analyzing recoveries of written-off accounts.
- Analyzing inventory shortages by location or product type.
- Comparing key inventory ratios to industry norm.
- Reviewing supporting documentation for reductions to the perpetual inventory records.
- Performing a computerized match of the vendor list with a list of employees to identify matches of addresses or phone numbers.
- Performing a computerized search of payroll records to identify duplicate addresses, employee identification or taxing authority numbers or bank accounts.

- Reviewing personnel files for those that contain little or no evidence of activity, for example, lack of performance evaluations.
- Analyzing sales discounts and returns for unusual patterns or trends.
- Confirming specific terms of contracts with third parties.
- Obtaining evidence that contracts are being carried out in accordance with their terms.
- Reviewing the propriety of large and unusual expenses.
- Reviewing the level and propriety of expense reports submitted by senior management.

Examples of Circumstances that Indicate the Possibility of Fraud

The following are examples of circumstances that may indicate the possibility that the financial statements may contain a material misstatement resulting from fraud.

Discrepancies in the accounting records, including:

- Transactions that are not recorded in a complete or timely manner or are improperly recorded as to amount, accounting period, classification, or entity policy.
- Unsupported or unauthorized balances or transactions.
- Last-minute adjustments that significantly affect financial results.
- Evidence of employees' access to systems and records inconsistent with that necessary to perform their authorized duties.
- Tips or complaints to the auditor about alleged fraud.

Conflicting or missing evidence, including:

- Missing documents.
- Documents that appear to have been altered.
- Unavailability of other than photocopied or electronically transmitted documents when documents in original form are expected to exist.
- Significant unexplained items on reconciliations.
- Unusual balance sheet changes, or changes in trends or important financial statement ratios or relationships – for example, receivables growing faster than revenues.
- Inconsistent, vague, or implausible responses from management or employees arising from inquiries or analytical procedures.
- Unusual discrepancies between the entity's records and confirmation replies.
- Large numbers of credit entries and other adjustments made to accounts receivable records.
- Unexplained or inadequately explained differences between the accounts receivable sub-ledger and the control account, or between the customer statements and the accounts receivable sub-ledger.
- Missing or non-existent cancelled checks in circumstances where cancelled checks are ordinarily returned to the entity with the bank statement.
- Missing inventory or physical assets of significant magnitude.

Appendix 8

Illustrative Factors for Consideration of Materiality

Whether or not the knowledge of an item would influence the decisions of users of financial statements would depend on a particular facts and circumstances of each case. It is not possible to lay down precisely, either in terms of specific items or in terms of amounts, what could be considered as material in all circumstances.

Factors for consideration	Illustration
Apart from the size (or magnitude) of an item, its nature is also an important factor in determining whether or not it is material in the facts and circumstances of a case.	Since the discovery of an illegal payment (i.e. bribe, corruption), even of a small amount could result in the funding cancellation by the Development Partner as well as Government, any amount of such illegal payment is material, regardless of size. Similarly, inadequate or improper description of an accounting policy would be material if it is likely to mislead the users of the financial statements
Materiality can be judged only in a relative context.	In a small project with total funding of Tk 1 crore, Tk 10 lacs would be material amount, whereas in a large multi-year project Tk 10 lacs may not be considered material.
An item of information is material, if its omission or misstatement can influence the economic decisions of the users of the information.	If a Project is undertaking certain activities as part of the 'Pilot Program' (say feeding of children in primary school in 10 selected school) and upon successful completion of this 'Pilot Program' the Development Partner would approve larger fund for the similar Project to be rolled out in bigger scale (in whole division comprising 1,000 school), the actual result of this Pilot program will be crucial for the subsequent receipt of larger fund. Based on the success of this Pilot Program substantial Grant can be received and Project duration can exceed. Therefore, while conducting the audit of this Pilot Program materiality consideration should also include the expectation of Project Management to secure larger future funding.

What is material depends upon the particular facts and circumstances of each case.	For example, omission to record contractor payment of an invoice of Tk 10 lacs for civil work completed for a project with a total contractor payment of Tk 100 crore for civil work during that year, may not normally be material. However the omission could become material if the total contractor payment of the year of that project were say BDT 1 crore.

Determining Performance Materiality

Example 1

Materiality for a Project AA implemented by the Ministry of has been set at BDT 5,000,000 for the current period audit and the engagement team is about to determine performance materiality next. Project AA is a development Project working in Irrigation and Water Resource sector managed by the Ministry of Water Resources. This is a multi-year Project and there have been no significant changes in the Project's management, activities, internal control or risks of material misstatement. FAPAD team has conducted of the audit of this Project for the last two years and this will be the third year of audit. The uncorrected misstatements have been in the region of 15% - 20% of materiality during the last two years. Last audit's uncorrected misstatement amounted to BDT 1,034,280 (none of which carry over to this period). The FAPAD audit team has determined performance materiality to be BDT 3,500,000.

Example 2

For the audit of Project AA as per Example 1, materiality has been set to Tk 5,000,000 again. The uncorrected misstatements in the previous audit were Tk 1,243,257. There have been no significant changes in the Project's activities, internal control or risks of material misstatement, but the Project has partly new management team including Project Director and Project Accountant starting a few months into the current period. In planning meetings with management they declared that they intend to correct all identified misstatements, unless clearly trivial. Considering the above circumstances, the engagement team determined performance materiality to be Tk 2,500,000.

Appendix 9

Internal Control Questionnaire

			Yes	No	WP Ref
Management of Human Capital	:	Is there appropriate personnel arrangement to ensure right person to meet the needs of the work?			
Organizational Structure	:	Is there a clear definition of key areas of authority and responsibility and appropriate line of authority?			
Delegation of Authority	:	Are authority and responsibility for operating activities defined?			
Supervision	:	Is the work of staff supervised effectively?			
Budgetary System	:	Is the work budgetary System compatible with objective and plan?			
Information System	:	Is there an appropriate information system to ensure early warning of deviation from targets, plans and budgets that require management attention?			
Authorization	:	Are expenses authorized by a competent person, lawfully so authorized?			
		Are bank accounts reconciled on regular basis and result documented?			
		Are there written procedures and do they match actual procedures?			
Documentation	:	Are the accounting documents filed in logical sequence to support clear audit trail?			
Responsibility	:	Is there a budget and performance variance report comparing actual to projected expenses and performance?			
Segregation of Duties	:	Are duties segregated so that no one person has control over the entire processing of any given system?			
Physical Control	:	Is there effective physical control over vulnerable assets?			
Monitoring	:	Is performance reviewed, measured against plan?			
Execution	:	Is there an execution plan for key transactions, events?			
Recording		Are transactions and events are recorded immediately after they take place?			
Internal Control	:	Are the controls documented and periodically reviewed for reliability?			

			Yes	No	WP Ref
Accounting Control	:	• Do the financials correspond to approve expenditure category of project?			
		• Is the transaction processing procedures segregated?			
		• Are the staffs skilled, experienced and have requisite knowledge?			
		• Are there written procedures and do they match actual procedure?			
		• Is independent physical stock take conducted of equipment and other assets?			
		• Are actions taken on the reported results?			
		• Is there internal audit?			
		• Are actions taken on such internal audit results?			
		• Is there audit by another external auditors?			
		• Are actions taken on such external audit results?			
		• Was the project inspected/ appraisal monitored by any external body? Are actions taken on the findings?			
		• Is there a physical/work progress budget in addition to a financial budget?			
		• Is there periodical financial and physical variance report?			
		• Is management response to such variance report quick and convincing?			
		• Is the system and procedures written and available to staffs as desk instruction?			
		• Is the organization structure adequate with clear line of control and authority?			

Appendix 10

Pro forma Bank confirmation request

Date

Name of the Bank
Name of the Branch
Address Line 1
Address Line 2

Dear Sir(s)

Name of the Project(s)

Please send direct to us at the above-noted address, and the Email address of the signatories, certificates as at the close of business on **Insert Year-end** confirming:

1. The balances (credit or debit) on all accounts carried by you in the name and/or on behalf of our above named Project(s);

2. Facilities granted in respect of advance, loans, overdrafts or cash credits, stating the limits authorized and the nature of the charges, e.g., Pledge, Hypothecation, Mortgage, Personal Guarantee etc.;

3. All investments, bills of exchange or other documents of title held by you for their account, specifying whether held for safe custody or as security; and

4. Outstanding balances in respect of all the letter of credit (L/C) opened and forward exchange contract made.

Please note that this request relates to **ALL** such balances, documents of title and contingent claims at the relevant date.

For your convenience & faster response, you may also send scan copy of the confirmation letter directly to the following email address: xxxx@fapad.org

In this connection we have included below signature of the authorized representative of the above Project.

Yours faithfully

	Authorized by
Signature of the FAPAD Audit Team Member or Authorised FAPAD Personnel	Signature(s) of the Authorised representative with Seal

Appendix 11

Pro forma confirmation letter to Lawyer

Date

Name of the Lawyer
Name of Legal Firm (If applicable)
Address Line 1
Address Line 2

Dear Sir(s)

Name of the Project(s)

In connection with our Audit for the year ended **Insert year-end** and at the request of our auditor, we should be obliged if you would forward to us the necessary information in respect of those matters which we have referred to you.

In particular, please advise us, in writing, of the following:

1. Details of any litigation or disputes in progress or pending, within all legal or arbitration jurisdictions, if known, these details should include the nature of the litigation, the current status of proceedings and the liability, which might arise.

2. Judicial and arbitration findings which may have arisen and which have not yet taken effect, detailing the nature of the transactions and the expected liability.

3. Details of any contractual commitments, guarantees, indemnities, etc., given by us which you are aware of and which could have material financial consequences for our Project.

4. Any claims against our company which you are aware of.

5. Any other issues which, in your opinion, merit specific mention in the context of the preparation of financial statements of the Project.

Your prompt attention to this request will be highly appreciated.

We should be obliged if you include any issue up to the date of your response.

Yours faithfully,

Signature, Name and Designation
Of the Authorised Personnel from the Project

Appendix 12

Management Representation Letter

The Director General
Foreign Aided Project Audit Directorate
Audit Complex, 6th Floor
SegunBagicha, Dhaka 1000
Bangladesh

Dear Sir

This representation letter is provided in connection with your audit of the special purpose financial statements of xxxxx Project (the "Project"), for the year ended 31 December 20xx.

We have fulfilled our responsibilities, as set out in the terms of the audit engagement dated [insert date], for the preparation and fair presentation of the special purpose financial statements in accordance with the International Public Sector Accounting Standard ("IPSAS") Financial Reporting Under the Cash Basis of Accounting issued by the International Public Sector Accounting Standards Board (the IPSASB) of the International Federation of Accountants (IFAC), the Project Accounting Manual issued by the Finance Division, MoF, Gob, the guidelines issued by the [insert Development Partner] and the relevant covenants specified in the Agreement of financing Grant/Loan dated dd/mm/yyyy executed between [insert Line Ministry, GOB] and [insert name of the Development Partner].

Certain representations in this letter are described as being limited to matters that are material. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.

We acknowledge that our responsibility includes:

- designing, implementing and maintaining internal control relevant to the preparation and fair presentation of special purpose financial statements that are free from material misstatement, whether due to fraud or error;

- selecting and applying appropriate accounting policies;

- making accounting estimates that are reasonable in the circumstances (if applicable);

- compliance with the Development Partner's Policy Manual as well as any other specific requirements of other funding agency;
- proper observance of all regulatory requirements applicable for the Project as endorsed by the Government of the People's Republic of Bangladesh, in particular regulation regarding procurement (PPP/PRA) and income tax, VAT and duties;
- disclose all variation from the IPSAS Standard *Financial Reporting Under the Cash Basis of Accounting*;
- disclose the results of our assessment of the risk of fraud;
- disclose any non-compliance including covenants specified in the financing/grant agreement;
- maintaining an accounting system that permits to provide information of financial status of the Project with enough degree of accuracy at any time and assure financial statements compliance with the Development Partner's requirements;
- there are no litigation pending against the Project;
- the loan/grant amounts provided by Development Partner has not been used for the payment of taxes and duties (if applicable); and
- taking measures within its competence to ensure the safeguarding of the Project assets.

We confirm that, to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

- All transactions have been recorded in the accounting records and are reflected in the financial statements.
- Related party relationships and transactions have been appropriately accounted for and disclosed.
- All events subsequent to the date of the financial statements and require adjustment or disclosure have been adjusted or disclosed.
- The effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the financial statements as a whole.

- We have provided you with access to all information of which we are aware that is relevant to the preparation of the financial statements, such as records, documentation and other matters. Additional information that you have requested from us for the purpose of the audit and unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.

- We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.

- We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity and involves Management, employees who have significant roles in internal control or others where the fraud could have a material effect on the financial statements.

- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the Project's financial statements communicated by employees, former employees, analysts, regulatory body or others.

- We have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements.

This special purpose financial statements for the period of 01 January 20xx to 31 December 20xx was approved by the Project Management on dd/mm/yyyy.

On behalf of the Project Management

Project Director Chief Accountant

Appendix 13

Audit Completion Checklist

I. Team leader and audit supervisor sign-off

	Team Leader sign-off and date	Audit supervisor sign-off and date	Note
Engagement acceptance/continuance I have, in accordance with applicable FAPAD policies obtained an appropriate engagement letter.			
Engagement team I am satisfied that: • the engagement team collectively has the appropriate capabilities, competence and time to perform the audit engagement in accordance with INTOSAI Standards requirements, and to enable an auditor's report that is appropriate in the circumstances to be issued. • the engagement team has implemented quality control procedures that are applicable to the audit engagement, including maintaining an objective state of mind and an appropriate level of professional skepticism, performing the work delegated in accordance with the ethical principle of due care, understanding the objectives of the work to be performed. • the engagement team has performed and documented its work in compliance with FAPAD policies, professional standards and regulatory and legal requirements, and the working papers demonstrate this compliance • the engagement team members have complied with ethical requirements, including independence requirements or, if any issue has arisen, I am satisfied that it has been resolved and appropriately documented. • the engagement team members have undertaken appropriate consultation during the course of the engagement, both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm, as necessary, and the nature and scope of, and conclusions resulting from, such consultations, if any, are documented and agreed with the party consulted. I have determined that conclusions resulting from consultations have been implemented.			

	Team Leader sign-off and date	Audit supervisor sign-off and date	Note
Risk assessment I am satisfied that appropriate audit risk assessment procedures have been performed and appropriately documented. This risk assessment and planning discussion includes, at a minimum, the following: • the importance of professional skepticism and the need to maintain a questioning mind, setting aside any of our prior beliefs that management is honest and has integrity, at all times during the audit • the responsibilities of engagement team members • our audit strategy decisions, including the determination of materiality for planning purposes and significant misstatement threshold and how these will be used to determine the extent of testing • our understanding of the Project resulting from our risk assessment procedures • how the Project's accounting policies, including unusual accounting procedures, address the application of the applicable financial reporting framework to the entity's facts and circumstances • a consideration of the known external and internal factors affecting the entity that may create an incentive or pressure for management or others to commit fraud, provide the opportunity for fraud to be perpetrated, and indicate a culture or environment that enables management or others to rationalize committing fraud (the "fraud triangle") • a consideration of the risk of management override of controls, including override through journal entries and other audit adjustments, significant accounting estimates, or significant unusual transactions, and the risk of fraudulent revenue recognition • the susceptibility of the Project's financial statements to material misstatements, whether caused by or error, with special emphasis on fraud, and • identified and the planned audit approach *The discussion was held on:* Date ____________________ *The participants were:*			

We made inquiries of management regarding the following:

Fraud

- knowledge of any actual, suspected or alleged fraud affecting the Project and its environment, including its internal control:
- management's assessment of the risk that the financial statements may be materially misstated due to fraud
- management's communication, if any, to employees regarding its processes for identifying and responding to the risks of fraud in the Project

Going concern (if relevant)

- knowledge of events or conditions (including related business risks) that may cast significant doubt on the Project's ability to continue as a going concern for the foreseeable future.

Laws and regulations

- the Project's policies and procedures regarding compliance with laws and regulations
- laws or regulations that may be expected to have a fundamental effect on the operations of the Project or an effect on the determination of material amounts and disclosures in the financial statements
- actual or potential instances of non-compliance with laws and regulations, including illegal acts

Litigation and claims

- policies and procedures adopted by the Project for identifying, evaluating and accounting for litigation and claims
- current litigation and claims (including those claims defended by insurance companies) and management's evaluation of each matter

  We send letters of audit inquiry to lawyers when we assess a risk of material misstatement regarding litigation or claims that have been identified or when we believe they may exist. Otherwise confirm the fact through corroborative inquiry.
- commitments and contingencies.

Related parties

- policies and procedures to identify, authorize, monitor and record related party transactions

The discussion was held on:

Date ____

FAPAD participants were:

Name: ____

The management participants were:

Name
and title: ____

____

Specific Topics, including fraud

I am satisfied that:

- If the following matters were identified during the audit, the appropriate audit procedures were performed and the effect on the financial statements and our report was determined, resolved and documented:
  - assertion level fraud risks
  - events or conditions that cast significant doubt on the entity's ability to continue as a going concern for the foreseeable future
  - possible instances of noncompliance with laws and regulations, including illegal acts
  - significant litigation and claims
  - significant transactions with related parties
  - subsequent events.
- If a misstatement was identified, we considered whether such a misstatement may be indicative of fraud and if there is such an indication, we considered the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management representations.
- Relevant correspondence with the relevant licensing or regulatory authorities was inspected.
- All significant accounting estimates were reviewed for bias by:
  - considering whether differences between accounting estimates best supported by audit evidence and those included in the financial statements may indicate bias, and
  - performing a retrospective review of the estimate made in the prior year to determine whether management judgments and assumptions indicate possible bias.
- The business rationale for all significant unusual transactions was evaluated.

Communication and reporting

I am satisfied that communications and reporting to management and those charged with governance has been in accordance with applicable policies including:

- making all required communications in the required manner
- making communications on a timely basis, and
- including required and other appropriate caveats, disclaimers and restrictions on deliverables and other communications.

Matters to be communicated include:

- audit matters of governance interest
- fraud matters
- noncompliance with laws and regulations
- material weaknesses
- misstatements.

Audit documentation

I have reviewed and signed the following working papers, where applicable:

- Engagement letter
- Planning and Completion Document
- Audit section with High Risk of Misstatement (RoSM) and/or Fraud Risk
- Management representation letter
- Summary of Audit Differences
- Financial statements
- Auditor's report

I am satisfied with the basis on which we have formed our decisions and such basis has been appropriately documented.

I am satisfied that:

- all working papers (including those maintained solely on computer media) are reviewed by another engagement team member more experienced than the preparer
- all working papers have been protected from loss, unauthorized destruction or unauthorized access
- we have obtained written management representations in accordance with applicable policies
- we have obtained and documented sufficient appropriate audit evidence that:
  - comparative financial information is appropriately reported and correct opening balances are processed and appropriately reported.
  - the overall financial statement presentation, including preparation of financial statements and related footnote disclosures and other additional information, and that the financial statements agree with or are reconciled to the underlying accounting records.
  - journal entries, including standard and non-standard journal entries and other adjustments, have been recorded appropriately.
  - recurring and nonrecurring adjustments to the consolidated financial statements, such as consolidating and eliminating entries, report combinations, classifications, and "top-side" journal entries, have been authorized and recorded appropriately.
  - the cash flows have been accumulated, recorded, processed, summarized and reported appropriately in the statement of cash flows.
  - the movements in equity have been accumulated, recorded, processed, summarized and reported appropriately in the statement of changes in equity.
  - all material subsequent events have been accumulated, recorded, processed, summarized and reported appropriately and our subsequent events procedures have been updated to the date of our auditor's report.

- we have obtained and reviewed the minutes of meetings of management and of those charged with governance (e.g., the board of directors and relevant board committees). The review of the minutes of meetings included a review of matters relevant to related parties and other specific topics.
- all relevant accounting and disclosure checklists required by FAPAD policy have been completed
- all review points have been cleared and all review notes discarded, except pursuant to relevant document retention policies
- the working papers will enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing, and extent of the audit procedures performed to comply with INTOSAI Standards and applicable legal and regulatory requirements; the results of the audit procedures and the audit evidence obtained; and significant matters arising during the audit and the conclusions reached thereon.
- the working papers include the identifying characteristics of the specific items or matters being tested for audit procedures performed.
- the preparer(s) and reviewer(s) of each working paper have dated (dd/mm/yy) and signed or initialed each working paper.

Forming an opinion

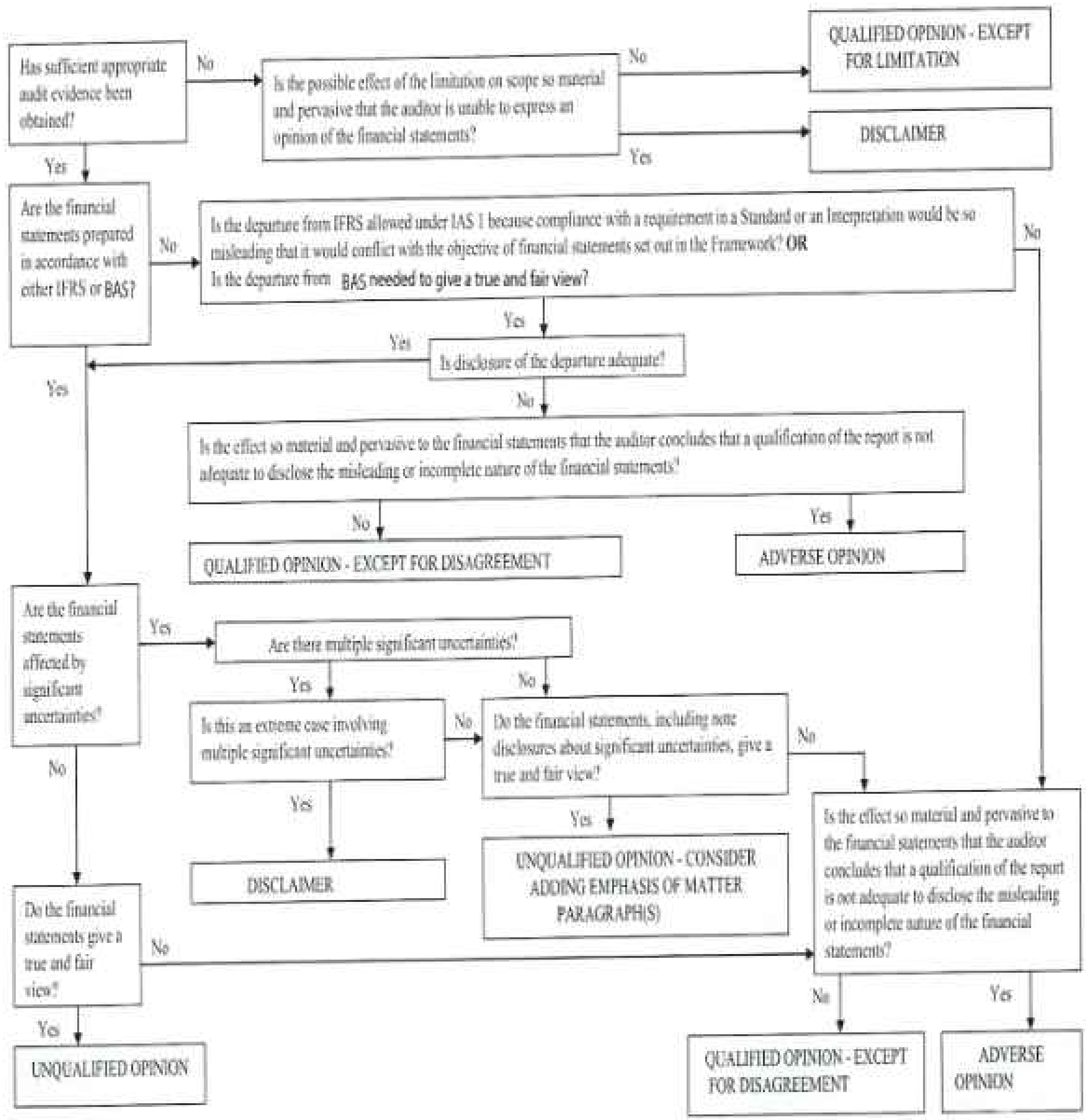
Based on the audit procedures performed and related results, I am satisfied that:

- sufficient appropriate audit evidence has been obtained to form an audit opinion
- the accounting principles used in the financial statements, including any changes thereto, are appropriate for the entity's business and industry and are consistent with the applicable financial reporting framework
- the financial statement presentations and disclosures are adequate and conform with the engagement team's understanding of the entity and its environment as well as with the applicable financial reporting framework
- the financial statements are free of material misstatement when an unqualified opinion is expressed
- the auditor's report to be issued are appropriate
- other information that contains the audited financial statements has no material inconsistencies or material misstatement of fact when compared to the audited financial statements, or if we are aware of such inconsistency or misstatement, we have taken further appropriate action.

Appendix 14

Steps for forming an audit opinion

Forming an Opinion on Financial Statements[1]



Appendix 15

Audit Program/ Checklist

Sl. No	Name of Records/ Document
1.	Lender / Donor Funding
2.	Reconciliation of Loan/Grant Balance
3.	Withdrawal Application
4.	Summary of Withdrawal Applications (SoE)
5.	Summary of Withdrawal Applications (Imprest account replenishment)
6.	Summary of Withdrawal Applications (Direct Payment)
7.	Summary of Withdrawal Applications (Reimbursement of expenses already made)
8.	Reconciliation of Expenditures to the Financial Statements
9.	Reconciliation of Expenditure Records to the Financial Statements
10.	GOB Contribution
11.	Summary of GOB Contribution
12.	Operating Bank Accounts and Cash
13.	Imprest/Special Account
14.	Statement of Expenditure (SOE)
15.	Checklist for recording transactions in Cash Book
16.	Checklist for procurement of goods & equipment
17.	Checklist for procurement of civil works
18.	Checklist of land acquisition/procurement
19.	Checklist of pay & allowances for manpower of Project
20.	Checklist of local & foreign travel for manpower of project
21.	. Checklist of local & foreign training for manpower of project
22.	Checklist for procurement of Consultancy service
23.	Checklist of Vehicles & Transportation (rental)

1. Lender / Donor Finding

Objective: To form an opinion as to whether the proceeds of the lender/donor agreement have been properly recorded in the project accounts and properly reflected in the financial statements.

Documents to be obtained:

- Extract of loan / grant/ donor agreement setting out the amounts to be paid and the dates on which they will be paid;
- Payment advices from the lender/donor;
- Bank statements for the periods when the proceeds of the loan/grant were paid out;
- All procedures specified under the loan/grant agreement for the withdrawal of funds from the loan/grant;
- Loan balance confirmation from the lander/donor.

Audit Steps:

1. Prepare the loan reconciliation work;
2. Compare the proceeds recorded to the proceeds which should have been received according to the loan/grant agreement;
3. Trace each deposit of the proceeds to the relevant bank account;
4. Compare the balance per the confirmation received from the lender/donor to the balance per the accounting records;
5. Compare the balance according to the accounting records to the balance shown on the financial statements.
6. Reconciliation of Loan/Grant balances as per the statement shown in next page.
7. Check whether the Project has maintained all books and records required by the Donor/Lender (i.e. for ADB documents to be maintained a specified in the Project Accounting Manual)

2. Reconciliation of Loan/Grant Balance

Opening loan/grant balance (note1) ……………………………………………………………

Add:

Loan/grant proceeds received during the year

Loan/grant balance at the end of the year……………………….

Loan/grant balance according to the confirmation received from the lander

Difference: (must be fully explained below)

Note: This should correspond to the closing balance of the previous year

Prepared by: ______________________________ Date: ______________

Reviewed by: ______________________________ Date: ______________

3. Withdrawal Application

Objectives: To form an opinion as to whether

1. All applications for withdrawal are accounted for;
2. All funds received through the withdrawal procedures are accounted for;
3. The applications are properly authorized;
4. The requirement of the loan agreement has been complied with in relation to the request for reimbursement of expenditures;
5. Applications are made in due time for the amount of expenditure incurred.

Documents to be obtained:

- Withdrawal register;
- All the applications for withdrawal which were prepared for the year under audit;
- The payment advice prepared by the lender/donor for each withdrawal application;
- The bank statement prepared by Bangladesh Bank for the year under audit. This should represent all the transections in the imprest account required by the loan agreement;
- All bank statement from the Bangladesh Bank or Commercial Banks in which the project has accounts;
- The minimum value for an application for this project from the permanent file Extract of Disbursement Letter;
- If there is an imprest/ Special account, determine the intervals at which replenishment must be requested and the minimum and maximum amounts from the Extract of Disbursement Letter;
- In the case of SOE's, obtain all the supporting vouchers for each SOE prepared during the year.

  Note: The amounts required to be entered on these worksheets are those actually received during the year. Those applications still outstanding at the end of the year are not to be shown here.

Audit Steps:

1. Prepare the summary of Withdrawal Applications.
2. For each withdrawal application paid by the lender/donor, obtain a photocopy of the advice sent by the lender/donor and verify that the amount recorded is correct;
3. In all cases where there is a difference between the amount claimed and the amount received, obtain an explanation of the refusal by the lender/donor to reimburse the expenditure;
4. Trace all payment on withdrawal applications to the imprest account maintained at Bangladesh Bank;

5. Trace all amounts transferred from the imprest account to the project operating account by comparing the amounts going from one account to the other. Any discrepancy must be explained in a separate working paper;
6. Add the transfers from the impest account and ensure that the total transfer for the year does not exceed the total amount authorized by the Ministry of Finance in its directive to the Bangladesh Bank;
7. For each withdrawal application, determine if the terms of the loan agreement have been complied with;
8. Determine if there are any major delays in the deposit of the replenishments once they have been approved by the lender/donor;
9. Determine that all the replenishment received have been entered in the cash book;
10. Agree the loan balances to the financial statements;
11. Agree the loan balances to the confirmation received from the lender/donor.

Withdrawal Application Questionnaire:

- Were all the reimbursements traced to the project bank accounts?
- Were all applications for withdrawal accepted by the lending agency?
- Were all supporting documents required for the withdrawal application available?
- Was the minimum application amount respected?
- If a special account is involved, were the withdrawal application submitted at the intervals specified in the disbursement letter?
- Were all the applications numbered sequentially?
- Were all the summary sheets available in instances where they were required?
- Is there a Withdrawal Register?
- Verify whether all funds received through the withdrawal procedures are accounted for.
- Verify whether the applications are properly authorized.
- Verify whether the requirements of the loan agreement have been complied with in relation to the request for reimbursement of expenditures.
- Verify whether all the Applications for Withdrawal which were prepared for the year under audit.
- Verify whether the payment advice prepared by the lender/donor for each withdrawal application.

4. Summary of Withdrawal Applications (SoE)

No	Date	Category 1	Category 2	Category 3	Category 4	Category 5	Category 6	Category 7	Category 8	Amount Received	Amount Claimed	Difference

Prepared by: ______________________ Date: ___________ Reviewed by: ____________________ Date: __________

5. Summary of Withdrawal Applications (Imprest account replenishment)

No	Date	Category 1	Category 2	Category 3	Category 4	Category 5	Category 6	Category 7	Category 8	Amount Received	Amount Claimed	Difference

Prepared by: ______________________ Date: __________ Reviewed by: ____________________ Date: __________

6. Summary of Withdrawal Applications (Direct Payment)

No	Date	Category 1	Category 2	Category 3	Category 4	Category 5	Category 6	Category 7	Category 8	Amount Received	Amount Claimed	Difference

Prepared by: ______________________ Date: ____________ Reviewed by: ______________________ Date: ___________

7. Summary of Withdrawal Applications (Reimbursement of expenses already made)

No	Date	Category 1	Category 2	Category 3	Category 4	Category 5	Category 6	Category 7	Category 8	Amount Received	Amount Claimed	Difference

Prepared by: ______________________ Date: __________ Reviewed by: ____________________ Date: __________

8. Reconciliation of Expenditures to the Financial Statements

Objective: Form an opinion as to whether the accounting records are accurately reflected in the Financial Statements as prepared by the project officers.

Documents to be obtained:

- Financial Statements for the period under review;
- Withdrawal Application prepared at the beginning of the audit and as provided in Worksheet 4, 5, 6 and 7;
- The accounting records from which the financial statements were prepared.

Audit Steps:

1. Complete the relevant Form attached;
2. Compare the totals from Worksheet 9 to the accounts shown on the Financial Statements for each category of expenditure;
3. In **ALL** cases where the amounts do not agree, obtain an explanation and reconcile the amounts.

9. Reconciliation of Expenditure Records to the Financial Statements

	Total Received	Category 1	Category 2	Category 3	Category 4	Category 5	Category 6	Category 7	Category 8
SOE									
Direct Payment									
Imprest Account Replenish									
Expenses already paid									
TOTAL RECEIVED									
Add:									
GOB Expenditures									
Expenditures not claimed at Y/E									
Total additions									
Sub-total									
Deduct:									
Unclaimed expenditure at previous Y/E									
Total Expenditures									

Prepared by: ______________________ Date: ___________ Reviewed by: ____________________ Date: __________

10. GOB Contribution

Objectives: To form an opinion as to whether the Government of Bangladesh contributions/ matching funds are properly recorded in the accounting records and the financial statements.

Documents to be obtained:

- Copy of the Budget allotment issued to the project by the Ministry of Finance setting out the annual budget allotment for the project;
- Copy of fund release order(GOs) of concern Ministry from GOB contribution.
- Copy of the Bank account to which the GOB contribution is paid (if applicable);
- Copy of the document setting out the authorized expenditures using the GOB contributions.
- All bill voucher of GOB Contribution for project at concern office.

Audit Steps:

1. Have the payments been recorded in the bank statement?
2. Have the payments been recorded in the Cash Book?
3. Verify that the payments have been recorded in the bank statement. (if applicable).
4. Verify that the payments have been recorded in the Cash Book.
5. Prepare Working Paper;
6. Is the balance shown on the financial statements reconciled to the balance shown in the accounting records?
7. Reconciliation statement between CAO and PD accounts.
8. Were all balances due to GOB at the end of the previous year paid back at the beginning of the current year as required by GOB regulations?
9. Check whether the Project is complying with the requirements to maintain books and records as per the 'Government Project Accounting Manual'.

11. Summary of GOB Contribution

Instalment number	Date authorized	Date deposited in bank	Amount deposited	Amount authorized	Difference if any
Total					

Prepared by: ____________________________ **Date:** ___________

Reviewed By: ____________________________ **Date:** ___________

12. Operating Bank Accounts and Cash

Objectives: To form an opinion as to whether the bank balances and cash have been properly reflected in the financial statements.

Documents to be obtained:

- All Bank Statements for the period;
- Cash Book;
- Cheque Register;
- Bank reconciliations for the year;
- Bank confirmation which should have been obtained at the time of gathering information for the permanent file.

Audit Steps:

1. Obtain a bank confirmation if it has not already been done;
2. Obtain a copy of the bank reconciliation at the financial statement date and carry out the following steps;
3. Compare the balance per the accounting records to the balance per the reconciliation. If they do not agree, explain the difference;
4. Compare the balance per the bank statement and the balance shown as the bank balance in the reconciliation;
5. Compare the balance per the bank reconciliation to the financial statements and if they differ, explain the difference;
6. Trace and deposits in transit at the end of the period to ensure that they have been recorded in the proper period;
7. Trace and deposits in transit at the beginning of the year to ensure that they are reflected in the proper accounting period;
8. Trace the outstanding cheques at year end to the subsequent bank statement to ensure that they are truly outstanding and the not simply recorded in the wrong period;
9. Verify the mathematical accuracy of the bank reconciliation;
10. Count the cash in hand;
11. Reconcile the cash balance to the cash balance in the general ledger.

13.Imprest/ Special Account

Objectives: To form an opinion as to whether the funds have been correctly accounted for.

Documents to be obtained:

- The bank statement at the June 30th from Bangladesh Bank;
- The bank reconciliation for the date of the financial statements;
- The bank confirmation which should have been obtained at the time of gathering of initial information for the permanent file;
- Withdrawal authorized from the Ministry of finance;
- Summary of withdrawal application(WA);
- Cash Book;
- Cheque Register.

Audit Steps:

1. Obtain a bank confirmation if it has not already been done;
2. Obtain a copy of the bank reconciliation at the financial statement date and carry out the following steps;
3. Compare the balance per the accounting records to the balance per the reconciliation. If they do not agree, explain the reason;
4. Compare the balance per the bank statement and the balance shown as the bank balance in the reconciliation;
5. Compare the balance per the bank reconciliation to the financial statements and if they differ, explain the difference;
6. Trace the deposits in transit at the end of the period to ensure that they have been recorded in the proper period;
7. Trace the deposits in transit at the beginning of the year to ensure that they are reflected in the proper accounting period;
8. Using the mathematical accuracy of the bank reconciliation;
9. Using the authorization issued by the Ministry of Finance, ensure that the authorized amounts have not been exceeded;
10. Compare the total per the accounting records and bank reconciliation to the amount shown on the financial statements.

14. Statement of Expenditure (SOE)

Definition:

SOE expenditure are used only for projects funded by the World Bank (IDA) and by the ADB. The borrower periodically requests withdrawal of loan proceeds through submission of a statement indicating expenditures for certain items referred to it the loan agreement. The SOE procedure simplifies and accelerates the lender's loan disbursement process by eliminating the requirement for the lender/donor to review supporting documentation for much small expenditure prior to authorizing disbursements. The SOE statements are not accompanied by supporting documentation. Therefore, both the World Bank and ADB require a separate audit opinion as to the accuracy and propriety of expenditures claimed under an SOE.

Objectives: To form an opinion as to whether:

1. The individual expenditures which make up the SOE are fully supported by documentation retained in the files of the implementing organization;
2. The expenditures are properly authorized;
3. The expenditures conform to provisions of guidelines issued by the lender/donor;
4. The expenditures are eligible under the loan/ grant agreement.

Documents to be obtained:

- The disbursements categories from the loan/grant agreement;
- Copies of all the Monthly Disbursements Summary for the year produced by the lender/donor and sent to the borrower;
- All the vouchers which were reimbursed by SOE's used during the period under review.

Audit Steps:

1. Reconcile the total reimbursement by SOE as shown on the Summary of Withdrawal Applications 4 to the Monthly Disbursements Summary produced by the lender/donor;
2. For each SOE shown on 4, add up all the vouchers to ensure that the amount shown on the SOE is fully supported by documentary evidence. This step will ensure that the total population of vouchers is known. Note all discrepancies on a separate sheet of paper;
3. Verify that these is signed by the required authorized signatories;
4. Verify that the SOE's respect the maximum and minimum values established by the lender/donor;
5. If this is a new project, check that the vouchers for the first two SOEs are not dated prior to the date specified in the Disbursement Letter as being the date at which the loan takes effect. If some payments are dated prior to the date, make photocopies and attach them to a working paper explaining why it occurred. If the explanation is not satisfactory, prepare an observation sheet;
6. If some payments are dated prior to the date, make photocopies and attach them to a working paper explaining why it occurred. If the explanation is not satisfactory, prepare an observation sheet;
7. Select sample of SOEs;

8. Carryout the audit programmes required for the type of expenditures;
9. Verify that only expenditures which belong to the current year are included in the last SOE prepared at year end;
10. By reference to previous year's working paper file, verify that no expenditures relating to the previous year have been included in the current year.

15. Check list for recording transactions in Cash Book

Books of accounts is reflection of project transactions. All transactions of a project are recorded in cash book in cash basis accounting system in Bangladesh.

The following records should be checked during conducting audit of transaction in cash basis accounting:

Sl. No	Name of Records/ Document
1	The fundamental accounting principle which must be adopted by all projects operating in Bangladesh is cash basis of accounting
	a. Records receipts when cash is received
	b. Record disbursements when payment is made
2	Following general rules are to be followed when processing & recording cash transaction:
	a. Receipt recorded when cash is received
	b. Disbursement is recorded when payment is made, not when liability arises
	c. Every transaction must be recorded subject to disbursement
	d. Transaction of field offices must be consolidated within the main project books of accounts
	e. Regular bank reconciliations for all project bank accounts must be carried out
	f. Regular reconciliations of books of accounts must be carried out
	g. Month end procedures must be carried out.
	h. Books of account duly signed by competent officer.

16. Check list for procurement of goods & equipment

Procurement of goods & equipment is an essential and important activity of any Project. Huge amount of project money involves for this activity. The area involves lot of risks. The following records should be checked during conducting audit of Procurement of goods & equipment:

Sl. No	Name of Records/ Document
1	Annual procurement plan
2	Public Procurement Act 2006 and P.P. Rules 2008, including amendments
3	Delegation of financial power
4	Official estimate approved by the competent authority
5	Financial and Treasury rules of Bangladesh
6	Terms and conditions of the tender document
7	Terms and conditions of the contract agreement
8	Terms and conditions of loan agreement with donors
9	Budget allocation register
10	Budget sanction letter
11	Tender notice
12	Specification of the goods
13	Advertisement of tender notice
14	Related tender file
15	Bidding documents
16	Comparative statement (CS)
17	Tender evaluation report
18	Contract agreement signed by two parties
19	Purchase order/supply order
20	Certification of receiving goods
21	Bill register
22	Contract register
23	Bill Vouchers
24	Inspection report
25	SRO of NBR related IT, CD-VAT
26	IT & VAT deduction register
27	Treasury chalan of IT, VAT & others receipts
28	LC documents
29	Shipping documents
30	Quality control report
31	Stock register
32	Stock account
33	Physical verification report
	Risks:
34	Deviation of terms and conditions written in the tender document & contract agreement
35	Sometime items procured with public fund are not used for right purpose

36	Procurement of the items below the required quality & quantity causes misuse of public money
37	The price of the items procured was not proper in consideration to market price
38	The government revenue like IT & VAT is not realized

	To be Verified:
39	Verify if there is any procurement plan with mentioning the purchase procedure
40	Verify if the plan was prepared as per approved policy/regulations and manual
41	Need analysis & evaluation report before procurement
42	Verify whether there is any approved list of registered vendors
43	Verify the process of vendor registration to ensure these done in a transparent and appropriate way
44	Pre-qualification of contractors was done on the basis of experience, capabilities of supply, financial solvency
45	Verify if there was appropriate tender opening committee & tender evaluation committee
46	Verify whether the purchase procedure were in place for competitive approach
47	Compare the tender documents with those of the recent years for same type of purchase
48	Verify whether adequate publicity and time allowed for prospective bidders to respond
49	Examined the comparative statement to ensure if the lowest tender was not accepted and if not the genuine reasons were recorded
50	Verify to ensure the realization of Earnest money/Security deposit from the contractors as per conditions of the tender notice
51	Verify that there was a recommendation of the TEC and proper approval
52	Verify whether notification of award was issued as per approved procedures
53	Ensure the purchase of goods was necessary and requisition was made by a responsible officer
54	Ensure no specific brand is allowed as standard in tender notice/tender documents

	Check list of payment procedure:
55	Check whether the payment of the bill for the supplies was approved by competent authority
56	Check if the bill was prepared as per contract document, check the arithmetical accuracy
57	Check the voucher and chalan was complete, correct with online verification and on all other respect
58	Check that paying officer followed all required financial rules while passing the bill
59	Check that the demand/bill was made in proper and approved form
60	Check that the payment was made to the right person/firm and under acknowledgement receipt
61	Check that the IT & VAT were duly realized from the bill, recorded in the concerned register and deposited to Govt. account

62	Check the bill amount, check amount entered in the cash book are in conformity.
63	Check whether there was bank guarantee for advance payment
64	Running bill was paid according to the progress of the work done as per contract
65	Ensure the justification of variance was entertained within the provision of contract
66	Check withdrawal of performance security was allowed as per approved criteria of the contract agreement
67	Ensure the time extension was entertained as per agreement
68	Check that the amount in voucher was properly entered in the books of account
69	Check that the payment amount was accounted in the correct classification of account
70	Ensure the purchase of the goods were essential for the operation of business of the project
71	Compare the specimen or sample in offer letter, catalogue etc. and goods received through physical verification
72	Ensure the same items were not purchased time and again and for spilt up to avoid sanction of concerned higher authority

17. Check list for procurement of civil works

Procurement of civil works is an essential and important activity of any project. Large amount of project money involves for this activity. The area involves lot of risks. The following records should be checked during conducting audit of Procurement of civil works:

Sl. No	Name of Records/ Document
1	Development/ Technical Project Proforma (DPP/TPP)
2	Annual procurement plan
3	Public procurement rule, 2008 and P. P. Act 2006, including amendments
4	Delegation of financial power
5	Financial and Treasury rules of Bangladesh
6	Terms and conditions of the tender document
7	Terms and conditions of the contract agreement
8	Terms and conditions of loan agreement with donors
9	Official estimate approved by the competent authority
10	Budget allocation
11	Budget sanction letter/GOs of fund release from concern Ministry
12	Tender notice
13	Copy of advertisement of tender notice
14	Administrative approval
15	Technical sanction
16	Tender documents
17	Tender file
18	Drawing & design of the work
19	Technical specification
20	Copy of the tender notice
21	Verify approval process of non- tender items
22	Comparative statement of the bidders
23	Tender evaluation report
24	Work order/Letter to proceeds
25	Contract agreement signed by the both parties
26	Schedule of rates
27	Bill of quantity (BoQ)
28	Measurement Book(MB)
29	Inventory of infrastructure i.e. road/bridge/culvert/ embankment/sluice gate/foot over bridge/building/market/passenger shed etc. with detail information like identification number, description of infrastructure, location, measurement, construction/ reconstruction period with source of fund etc.
30	All bill vouchers/IPC of the contractor
31	Sanction of expenditure
32	Register of security deposit/Performance security
34	Contractor ledger
35	Stock issue register
36	Equipment issue register

37	Progress report of the work
38	Completion certificate of work
39	Deduction of IT, CD VAT according to SROs of NBR
40	IT & VAT Register
41	Sales proceeds of tender schedule
	Risks in Civil works:
42	Non-compliance of the directives of the PPR
43	Awarding contract to a firm incapable of doing the job
44	Exceeding the budget for doing additional works
45	Use of construction materials & machineries under specified
46	Uncompetitive tendering process causes failures to accept competitive prices
47	Payment made for works not done/less done
48	Payment made for works not approved by the competent authority
49	Advance payments to the contractor beyond approved rules & regulations/specification
50	Faults in contract agreement causes loss of public money
51	Loss due to payment made for works not covered by the plan &design
52	Govt. taxes not realized and deposited
53	The bill amount and amount entered in the cash book are in conformity.
54	Whether any item exceeded the quoted rate
55	If penalty was imposed for delaying the completion as per contract
56	The bill amount is demanded as per description of the measurement book supported by completion certificate
57	The final bill amount is correct in conjunction with the passed running bills

18. Check list of land acquisition/procurement

Acquisition/procurement of land is an essential and important activity of any project. Huge amount of project money involves for this activity. The area involves significant risk. The following records should be checked during conducting audit of Procurement/acquisition of land:

Sl. No	Name of Records/ Document
1	Environment management Plan/Initial environment examination document
2	Feasibility study/Appraisal report
3	Development Project Pro forma (DPP)
4	Register of land
5	Survey report
6	Sales/Lease Deeds
7	Possession certificate
8	Official estimate for purchase/acquisition of land
9	Budget allocation
10	Budget sanction letter
11	Land purchases were carried out according to project and GOB rules
12	Land purchases were properly recorded in the accounting records
13	The proceeds of the sale of structures on the land were properly recorded
14	Permanent file of land acquisition/purchase
15	Deeds and correspondence
16	Cash book
	Verify that
17	land was purchased through the normal land acquisition process, that is using the GOB Land Acquisition Department facilities provided for that purpose.
18	the amount of land purchased in accordance with the land requirements
19	the payment recorded in the cash book is the same amount as that which was given in the estimate prepared by the Land Acquisition Department
20	the schedule of land required as given in the estimate was shown in the Gazette, the land lease document and the possession certificate
21	the land purchased fully utilized for the purposes specified in the Project Pro forma
22	the cost of land includes the cost of structures existing on the land
23	proper procedure followed for disposal of structures not relevant to the project
24	If there was a sale of structures, the revenue from the sale of properly reflected in the accounts
25	Environmental impact assessment has been carried out and mitigation plan is in place to address potential adverse impacts
26	Land is used most economically and land in excess of known requirement is released
27	Land procurement procedure is transparent, conducive to community interest, and documented

28	Public protest, if any, is addressed openly and promptly
29	Payment for land is timely and reliable
30	Cost of development and rehabilitation of the displaced have been included to evaluate land cost
31	Land pricing methodology is transparent and reliable.
32	Resettlement plan for peoples displaced by project activities
33	Budget provision for resettlement of displaced people
34	Payment made properly to displaced people
35	Deduction of taxes while payment made to land owner

19. Check list of pay & allowances for manpower of Project

Manpower is an essential and important element of any project. The Project need to pay salary & allowances as per DPP provision. The following records should be checked during conducting audit of Project manpower & their pay & allowances:

Sl. No	Name of Records/ Document
1	Development/ Technical Project Proforma (DPP/TPP)
2	Loan agreement
3	DPP Provision of manpower
4	Organization chart and list of approved positions for the project
5	List of manpower deputed from Govt. establishment
6	Deputation order from competent authority
7	List of manpower appointed for the project
8	Recruitment procedure file of project appointed staff
9	List of manpower from outsourcing
10	Qualifications of current job holders with what required
11	Documents of the duties, responsibility, obligations, functions and accountability of each position
12	Delegation and level of segregation of duties
13	Review of the need assessment process for staff
14	Retention order of manpower (if required)
15	Scale of sanction posts
16	Personal file of officers
17	Service book of employee
18	Last pay certificate of Govt. officer/employee
19	All pay bills
20	Code of conduct for staff to sign before an assignment is taken up

20. Check list of local & foreign travel for manpower of project

Project personnel have to travel across the country and abroad for project related work. The following records should be checked during audit of TA/DA bills of projects personnel:

Sl. No	Name of Records/ Document
1	DPP provision for local & foreign tour
2	Local & Foreign TA/DA rules
3	All TA/DA bill in respect of Domestic & Foreign
4	Basic pay of all officers
5	Budget allocation
6	Approved list of fare per kilometre
7	Approved tour programme
8	Govt. order for foreign tour approved by competent authority
9	Excess expenditure incurred for refreshment and lunch for training/workshop/seminar exceeding budget provision.

21. Check list of local & foreign training for manpower of project

Project Personnel have to participate in various training activities within the country and abroad for the benefit of the Project. The following records should be checked during conducting audit of training related documents and vouchers:

Sl. No	Name of Records/ Document
1	DPP Provision for local & foreign training
2	List of participants approved by competent authority
3	Documents setting out the applicable per diem rates
4	Whether the training courses provided are consistent with the project
5	Whether the participants are those that are the subject of the project
6	Whether the training costs are reasonable and allowed under the loan/grant agreement
7	Whether the rules applicable to the selection of participants, allowances and travel have been followed
8	Whether the training related expenses are in approved rates and conform to the regulations
9	Documentary evidence that training are carried out in accordance with set plan
10	Documentary evidence that participations on completion of training are actually using the new skill/expertise as intended
11	Foreign training are in accordance with Loan Agreement and for topics that add value
12	Candidate selected for training according to set standard and from those who are expected to continue in arras relevant to the project purpose
13	The training budget includes both financial and physical input/output data clearly quantified with which actual can be compared
14	Training have been managed cost effectively and within a previously approved training budget
15	Whether the duration of foreign training consistent with the terms of the loan/grant agreement
16	Whether the selection of participants done according to the criteria specified in the loan/grant agreement
17	Payment vouchers

22. Check list for procurement of Consultancy service

Procurement of consultancy services is an essential and important activity of any project. At times substantial amount of project money involves for this activity. The following records should be checked during conducting audit of Procurement of consultancy service:

Sl. No	Name of Records/ Document
1	DPP Provision for consultancy service
2	Consultant procurement plan, which should be approved by the lender
3	Particular contracts for consultancy services required for the project
4	Procurement plan comparable with the provision of Loan agreement and Project Pro forma/DPP
5	Procurement notice conformity with procurement plan
6	Advertisement arrangements is in relation to requirement
7	Merit of short list in light of information asked in the procurement notice
8	The short list prepared on the basis of EOI (Request for expression of interest)
9	Request for Proposal (RFP) is clarified to the instructions to consultant(ITC), Focuses will be on (a) evaluation criteria, (b) factors and their respective weights minimum passing quantity score, (c) key staff inputs
10	Evaluation committee comprises of three members with appropriate expertise or specialist and no conflict of interest
11	Technical evaluation report of the quality of proposal
12	Contract which should be basically the same as the original TOR
13	Contract should be prepared in standard form and clearly define the scope, content, duration, payment method, respective obligations, deliverable
14	Schedule of payments to consultants, actually payment made against contract and outputs
15	Verify appropriateness of substitution of key staff and its impact on quality
17	Substitution of key staff approved by the competent authority
18	Verify all payment vouchers of consultancy service
19	Verify all procurement process under provision of contract by the consultant
20	Duly deduction/realization of IT & VAT from the bill as per rule & duly deposited into Govt. treasury or accounted for Govt. account

23. Check list of Vehicles & Transportation (rental)

Quite often Vehicles/transportation is an essential item of a project and used for logistic support of project activities. The following records should be checked during conducting audit of payments relating to vehicle rental:

Sl. No	Name of Records/ Document
1	Register/list of vehicles
2	Register of spare parts
3	Log book of vehicle
4	File & register for repair and maintenance of vehicles
5	Contract agreement for hiring of vehicle
6	Provision of vehicles/hiring of vehicle in DPP/TPP/TO&E
7	Provision and govt. order & authority for uses of vehicles, fuel & purchase of fuel
8	Inward and outward register of vehicles
9	Official estimate for repair & maintenance of vehicle, purchase of fuel
10	Budget allocation & sanction letter for purchase of fuel, repair & maintenance of vehicles
11	Govt. authority i.e. PPR, GFR, Delegation of financial power, govt order for above expenditure
12	Procurement procedure for above items
13	Annual stock verification report
14	List of driver for each vehicle
15	Cash book, bill vouchers of all transactions
16	Expenditure incurring against vehicles not belonging to the project.
17	Expenditure incurring against vehicles beyond delegation of financial power
18	File regarding purchase of vehicles
19	Procurement procedure of vehicles cited in the check list of goods/equipment procurement may also be consulted

Appendix 16

Summary of Accounting Guideline and related matters for the Project

A. Understanding about Bangladesh Government Accounting

On 23rd December 1938, for the first time Government Accounts Code was published in Four Volume. Since then these Codes as well as Government accounting went through numerous changes, in Particular after the Independence of Bangladesh.

With growing need for changes, 1991 a committee named "CORBEC" was created to suggest required changes in Government budgeting and accounting. As per the suggestion of this committee a project named "Reform in Budgeting and Expenditure Control (RIBEC)" was taken to provide recommendation for necessary reform. As per the initiative of RIBEC Project, in 1996 new Accounts code with 13-digit classification chart was published to cater for the need of budget and accounts.

Subsequently, in continuation of RIBEC Project, another project named "Financial Management Reform Program (FMRP)" was taken. Some of the limitations of 13-digit classification code were that source of the fund could not be traced, how much fund is used in which area identified, allocation and actual spending of fund as per activities of Government (COFOG) was not available.

Finally, as per the recommendation of Taskforce and "Strengthening of Government Expenditure Project" by the Finance Division 9 Segment and 56-digit new budget and account code has been introduced under iBAS++ replacing the 4 level 13-digit code.

For detail guidance further reference can be made to "Budget and Accounting Classification System (BACS)" book published by the Ministry of Finance.

B. Source of Funding for Development Projects

There are currently 4 main funding mechanisms for disbursements out of the development budget. A general description of each is provided below.

1. Government of Bangladesh (GoB)

In respect of all project expenditure is funded by the GoB either partly or in its entirety, the Project Director (PD) submits bills for every claim to the Chief Accounts Officer (CAO) / District Accounts Officer (DAO)for approval. When the bill is submitted, a token number is issued to the Project by the CAO / DAO. The token number provides the audit trail or transaction link between the spending authority and the subsequent payment. Once the bill has been passed by the CAO / DAO the cheque(s) will be issued or the automated payment will be made to the payee.

Debt Servicing Liability
This is a situation which arises when funds in the nature of a loan, equity or investment is advanced to an autonomous body. The ultimate funding such loan is provided by the development partner (or more appropriately 'lender'). The following Two types of agreement exist in such funding situation:

- Main Loan Agreement between lender agency and GoB
- Subsidiary Loan Agreement between GoB and the autonomous body.

The underlying feature of this arrangement is that the loan is repayable in full by the autonomous or semi-autonomous body of the loan plus interest which has accrued on the principle amount. The autonomous body distributes the loan to spending authorities, i.e. projects. The terms and conditions of the loan are outlined in the amortization schedule per the subsidiary loan agreement. The Development wing of the Finance Division issues a yearly statement of Debt Servicing Liability repayable by the various institutions.

In respect of project accounting, this debt servicing arrangement does not affect the way projects should keep their books of accounts. Receipts and disbursements will be categorically treated as per transactions funded out of GoB. It is the autonomous body which has to account for the loan received and its subsequent repayment thereof.

2. Reimbursable Project Assistance (RPA) through GoB (RPA through GoB)

In respect of RPA through GoB the expenditure is initially incurred by GoB and is subsequently reimbursed by the donor and credited to the government bank account (Account 4B – Bangladesh Bank). The claim for reimbursement is prepared by the PD. When the withdrawal application has been approved by the donor the replenishment amount will be credited to the Government account in the Bangladesh Bank directly.

3. Reimbursable Project Assistance (RPA)

The expenditure is incurred by the Project and is fully funded by the donor. Special project bank accounts are credited with an imprest amount of fund by the donor. When the imprest balance has been expended by the Project, the PD will submit a claim / withdrawal application to the donor. The imprest amount will then be replenished by the donor. In this instance the amount will be usually credited to the Project's commercial bank account. There are four types of bank accounts which could be utilized by projects to administer RPA funds and expenditure.These are: -

- CONTASA (Convertible Taka Special Account)
- DOSA (Dollar Special Account)
- SAFE (Special Account Foreign Exchange)
- IMPREST Account

4. Direct Project Assistance (DPA)

DPA relates to expenditure incurred directly by the donor. While the direct costs and peripheral expenditure of employing expatriate consultants may often be known to the PD, other project related expenditures may not be informed to the PD by the donor. As a consequence, the complete amount of direct funding at times is only known to the donor.

Treasury model project/ Program concept-DLI/DLR (output based/result based)

In addition to the above traditional model of funding development projects, DLI/DLR based funding especially by World Bank is also used. Detail definition and concepts of these source of fund, maintenance of special accounts, fund release procedures, budgetary and administrative control including recording processes are described in the book named Fund Release Procedure- "Unnoyon Prokolper Ortho Obomukti O Bebohar Nirdeshika" issued by Finance Division, Ministry of Finance dated 21 June 2018.

C. Recordkeeping by Development Projects

A Project Accounting Manual (PAM) prescribing accounting procedures for development projects has been issued under the authority of Finance Division, Ministry of Finance to formalise and streamline project accounting practices.

The fundamental accounting principle which must be adopted by all foreign aided projects operating within Bangladesh is the 'cash basis of accounting'. The important concepts governing the recognition of transactions according to this principle in projects books of accounts can be simplified into two fundamental rules:

1. Record receipts when cash is received
2. Record disbursements when payment is made, not when liability arises

The cash basis of accounting nullifies the concepts of asset and liability and therefore funds receivable must not be recognized as a receivable asset (debtor) in the books of accounts. Consequently, bills payable must not be recognized as a payable liability (creditor) in the books of accounts.

Ledgers to be maintained

The types of ledgers and records to be maintained by projects can be generally divided into two categories:

Essential

- Receipts and disbursements ledger
- Bank control including periodic bank reconciliation
- Payroll register
- CD VAT control
- Advance control or advance memorandum

The essential ledgers must be maintained by each project in order to carry out the project accounting function satisfactorily.

Desirable

- Memorandum supplier ledger
- Bill logbook
- Withdrawal Application / Claim logbook
- Fixed Asset register
- Measurement book
- Inventory control

The desirable ledgers and records should be kept by each project to support the financial controls and aid the project management and accounting functions.

The essential and desirable categories have been drawn up in the context of project accounting only. In accordance with individual loan or grant agreement with respective donors it may be the case where it is compulsory for the project to maintain a fixed asset register and/or other records.

General Procedures

The cash accounting basis must be adopted by all projects in keeping their books of accounts. In respect of cash accounting the following fundamental principles must be adhered to by projects for recording every project transaction.

At time payments for the Project are made directly to the supplier/vendor by the donor and in such case the cash is not physically received. However, although the donor had directly made the disbursement on the Project's behalf, relevant entry will have to be made to record the notional receipt from donor. The disbursement will also have to be recorded.

Normally, the following general rules are to be adhered to when processing and recording transactions.

1. Receipt is recorded when cash is received.
2. Disbursement is recorded when payment is made, not when liability arises although a memorandum supplier ledger could be maintained to monitor amount payable.
3. Every transaction must be recorded subject to 1 and 2 above. Transactions of field offices must be consolidated within the main project books of accounts.
4. Regular bank reconciliations for all project bank accounts must be carried out.
5. Regular reconciliations of books of accounts must be carried out.
6. Month end procedures must be carried out.

D. <u>Financial statements of the Project</u>

Projects funded by development partners or foreign aided may have multiple reporting obligations to various stakeholders. The related Loan/Grant agreements would specify the reporting obligation of Project which shall be adhered to. However, most of the Projects would normally have the following reporting requirements:

1. Project Management Unit (PMU)
2. Donor Reporting
3. Management Accounting Unit (MAU) at Ministry
4. Chief Accounts Officer (CAO)
5. Foreign Aided Projects Audit Directorate (FAPAD)

Project Management Unit (PMU)
The types of reports required by PMU could range from monthly expenditure to percentage utilisation of year to date ADP allocation in respect of various activities categories of expenditure. This will vary between nature of projects and individual need of the PMU.

Donor Reporting
In this context the term 'donor' is taken to collectively mean donor and lender. The types of reports required by donors are largely donor specific and usually in donor prescribed format. However, as long as the financial statements are prepared in accordance with the IPSAS Cash Basis of Accounting it is expected to meet donor reporting requirements. **For illustration purposes the format for IPSAS Cash Basis of Accounts is provided in Appendix I.**

Management Accounting Unit (MAU)
In ministries where MAU has been set-up there are standardised reporting by projects to these MAU. A point to note is that the information collated by the MAU will largely serve the purposes of official GoB reporting requirements in respect of development and non-development budgets. The information on development budget will be provided by projects via the MAU input form. The information received from the projects will have to be reconciled to the proportion of development budget expenditure which is captured by the CGA system.

Chief Accounts Officer (CAO)
In respect of ministries where the MAU has yet to be established, alternative reporting documents have been prescribed by the C&AG. In this instance, projects are required to make monthly returns to the CAO in accordance with the prescribed format. The information for completion of the form can be obtained from the Receipts and Disbursements Ledger per the project accounting system.

Foreign Aided Projects Audit Directorate (FAPAD)
FAPAD has also developed a format for financial statements to be used by the Project and to provide to FAPAD team for timely completion of audit. The pro forma financial statement referred in Appendix I is prepared in line with FAPAD format with additional disclosure required by the IPSAS Cash Basis of Accounts.

Appendix 17

Pro forma management letter

Date

The Secretary
Ministry of xxxx
Bangladesh Secretariat
Dhaka, Bangladesh

Dear Sir

Subject: Submission of the management letter based on the audit of financial statements of the xxxx Project (the "Project") for the year ended 30 June 2020

We confirm that we have completed our audit of the books and accounts of 'xxxxxx Project' funded by Loan/Grant agreement no xxx for the year ended 30 June 2020 and pleased to submit the management letter dealing with certain matters concerning the Project's accounting procedure, systems of internal controls and other matters relating to the preparation and presentation of financial statements.

During the course of our audit, we have evaluated the Project's system of internal control to the extent we considered necessary as per the Government Auditing Standards of Bangladesh which are based on International Standards of Supreme Audit Institutions (ISSAI) as well as requirements of the relevant Loan/Grant agreements executed between the Government of Bangladesh and xxxx (i.e. ADB, JAICA, World Bank etc.). Our review of such areas include amongst other procurement process, utilisation of funds, management of imprest fundand SOE procedures (where applicable), regulatory compliance, maintenance of covenants, human resources etc.

The purposes of this review of internal control were to determine the nature, timing and extent of the auditing procedures necessary for expressing an independent opinion on the Project's financial statements. Our examination was carried out primarily to enable us to form an opinion on the financial statements as a whole on the basis of materiality and, therefore, did not necessarily bring to light all the weaknesses in the system of internal control, which a special review might have done.

We identified certain matters related to weaknesses of internal control and other deficiencies which may be of interest to you and the Project management. Accordingly, we have included these findings in this management report. Each of these findings has been divided into the following paragraphs:

- Title of observation;
- Account heading;
- Observation;
- Implications;
- Recommendations;
- Management response; and
- Auditor's comments/follow-up;

In addition, we have also added a section in this management letter on the follow-up and latest status of the prior year management letter points.

Please feel free to let us know if you require any clarification and/or further information about the matters referred above or about the attached draft special purpose financial statements.

We would like to place on record our sincerest appreciation of the courtesy and co-operation extended to our audit team by management and all grades of staff of the Project during the course of our audit.

Encl.
Management letter
Audited project financial statements

Copy to:

The Project Director
Xxx Project

The Project Officer
ADB Bangladesh Resident Mission
Dhaka, Bangladesh
(or as required)

The Project Officer
World Bank Bangladesh Resident Mission
Dhaka, Bangladesh