SA 580 (AAS 11)

REPRESENTATIONS BY MANAGEMENT

(Effective for all audits relating to a
ccounting periods beginning on or after April 1, 1995)

Contents

Paragraph(s)

Standard on Auditing (SA) 580[*], "Representations by Management" should be read in the context of the "Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services"[1] , which sets out the authority of SAs.

[*] Issued in February, 1996.
[1] Published in the July 2007 issue of the Journal.

Introduction

1. The purpose of this Standard is to establish standards on the use of management representations as audit evidence, the procedures to be applied in evaluating and documenting management representations, and the action to be taken if management refuses to provide appropriate representations.

2. The auditor should obtain representations from management, where considered appropriate.

Acknowledgement by Management of its Responsibility for the Financial Information

3. The auditor should obtain evidence that management acknowledges its responsibility for the appropriate preparation and presentation of financial information and that management has approved the financial information.

Representations by Management as Audit Evidence

4. The auditor should exercise his professional judgement in determining the matters on which he wishes to obtain representations from management. Similarly, the matters on which the auditor wishes to obtain such representations in writing should also be determined by the auditor using his professional judgement. However, representations should be obtained from management invariably in writing on matters material to financial information, either individually or collectively, when other sufficient appropriate audit evidence cannot reasonably be expected to exist. Matters which might be included in a representation letter from management in an audit of financial statements are contained in the example of a management representation letter in the Appendix.

5. During the course of an audit, management makes many representations to the auditor, either unsolicited or in response to specific enquiries. When such representations relate to matters which are material to the financial information, the auditor should:

(a) seek corroborative audit evidence from sources inside or outside the entity;

(b) evaluate whether the representations made by management appear reasonable and consistent with other audit evidence obtained, including other representations; and

(c) consider whether the individuals making the representations can be expected to be well-informed on the matter.

6. Representations by management cannot be a substitute for other audit evidence that the auditor could reasonably expect to be available. For example, a representation by management as to the quantity, existence and cost of inventories is no substitute for adopting normal audit procedures regarding verification and valuation of inventories. If the auditor is unable to obtain sufficient appropriate audit evidence that he believes would be available regarding a matter which has or may have a material effect on the financial information, this will constitute a limitation on the scope of his examination even if he has obtained a representation from management on the matter.

7. In certain instances such as where knowledge of the facts is confined to management or where the matter is principally one of intention, a representation by management may be the only audit evidence which can reasonably be expected to be available; for example, intention of management to hold a specific investment for long-term appreciation.

8. If a representation by management is contradicted by other evidence, the auditor should examine the circumstances and, when necessary, reconsider the reliability of other representations made by management.

Documentation of Representations by Management

9. The auditor should document in his working papers evidence of management's representations.

10. A written representation is better audit evidence than an oral representation and can take the form of:

(a) a representation letter from management;

(b) a letter from the auditor outlining the auditor's understanding of management's representations, duly acknowledged and confirmed by management;

(c) a duly authenticated copy of relevant minutes of meetings of the board of directors or similar body.

Basic Elements of a Management Representation Letter

11. A management representation letter should be addressed to the auditor, containing the relevant information and be appropriately dated and signed.

12. A management representation letter would normally be dated the same date as the auditor's report on the financial information or a date prior thereto. However, in certain circumstances, in respect to specific transactions or events, separate representation letters may also be obtained during the course of audit.

13. A management representation letter should ordinarily be signed by the members of management who have primary responsibility for the entity and its financial aspects, e.g., managing director, finance director.

14. If management refuses to provide representations on any matter that the auditor considers necessary, this will constitute a limitation on the scope of his examination. In such circumstances, the auditor should evaluate any reliance he has placed on other representations made by management during the course of his examination and consider if the refusal may have any additional effect on his report.

15. In case management is not willing to give in writing the representations made by it during the course of audit, the auditor should himself prepare a letter in writing setting out his understanding of management's representations that have been made to him during the course of audit and send it to management with a request to acknowledge and confirm that his understanding of the representations is correct. If the management refuses to acknowledge or confirm the letter sent by the auditor, this will constitute a limitation on the scope of his examination. In such circumstances, the auditor should evaluate any reliance on those representations and consider if the refusal may have any additional effect on his report.

Effective Date

16. This Standard on Auditing becomes operative for all audits relating to accounting periods beginning on or after April 1, 1995.

Appendix

Example of a Management Representation Letter
in an Audit of Financial Statements

(Ref. Paragraph 4)

The following letter is for use as a general guide in conjunction with the considerations set forth in this Standard. Representations by management will vary from one entity to another and from one year to the next. Therefore, this letter is not intended to be a standard letter and should be adapted in the light of individual requirements and circumstances.

[Letterhead of Entity]

[Date]

[Name and Address of the Auditor]

Dear Sir,

This representation letter is provided in connection with your audit of the financial statements of .... for the year ended ...... for the purpose of expressing an opinion as to whether the financial statements give a true and fair view of the financial position of .... as of ...... and of the results of operations for the year then ended. We acknowledge our responsibility for preparation of financial statements in accordance with the requirements of the Companies Act, 1956[2] and recognised accounting policies and practices, including the Accounting Standards issued by the Institute of Chartered Accountants of India.

We confirm, to the best of our knowledge and belief, the following representations:

Accounting Policies

1. The accounting policies which are material or critical in determining the results of operations for the year or financial position are set out in the financial statements and are consistent with those adopted in the financial statements for the previous year. The financial statements are prepared on accrual basis.

Assets

2. The company has a satisfactory title to all assets and there are no liens or encumbrances on the company's assets, except for those that are

[2] or other relevant statute.

disclosed in Note X to the financial statements.

Fixed Assets

3. The net book values at which fixed assets are stated in the Balance Sheet are arrived at:

(a) after taking into account all capital expenditure on additions thereto, but no expenditure properly chargeable to revenue;

(b) after eliminating the cost and accumulated depreciation relating to items sold, discarded, demolished or destroyed;

(c) after providing adequate depreciation on fixed assets during the period.

Capital Commitments

4. At the balance sheet date, there were no outstanding commitments for capital expenditure excepting those disclosed in Note X to the financial statements.

Investments

5. The current investments as appearing in the Balance Sheet consist of only such investments as are by their nature readily realisable and intended to be held for not more than one year from the respective dates on which they were made. All other investments have been shown in the Balance Sheet as 'long-term investments'.

6. Current investments have been valued at the lower of cost and fair value. Long-term investments have been valued at cost, except that any permanent diminution in their value has been provided for in ascertaining their carrying amount.

7. In respect of offers of right issues received during the year, the rights have been either been subscribed to, or renunciated, or allowed to lapse. In no case have they been renunciated in favour of third parties without consideration which has been properly accounted for in the books of account.

8. All the investments produced to you for physical verification belong to the entity and they do not include any investments held on behalf of any other person.

9. The entity has clear title to all its investments including such investments which are in the process of being registered in the name of the entity or which are not held in the name of the entity and there are no

charges against the investments of the entity except those appearing in the records of the entity.

Inventories

10. Inventories at the year-end consisted of the following:

Raw Materials (including components)	Rs ....
Work-in-Process	Rs ....
Finished Goods (including by-products)	Rs ....
Maintenance supplies and Stores and Spare Parts	Rs ....
Loose Tools	Rs ....
Others (specify each major head separately)	Rs ....
Total	Rs ....

11. All quantities were determined by actual physical count or weight or measurement that was taken under our supervision and in accordance with written instructions, on .... (date/dates of physical verification), except as follows:[3]

....

....

12. All goods included in the inventory are the property of the entity, none of the goods are held as consignee for others or as bailee, and, except as set out below, none of the goods are subject to any charge.

....

....

13. All inventories owned by the entity, wherever located, have been recorded, including goods sent on consignment.

14. Inventories do not include goods sold to customers for which delivery is yet to be made.

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[3] Where physical verification of inventories is carried out at a date other than the closing date, this paragraph may be modified as below:

Inventories recorded in the books as at ....(date of balance sheet) aggregating to Rs. .... are based upon the physical inventories taken as at .... (date of physical verification) by actual count, weight or measurement. The material discrepancies noticed on physical verification of stocks as compared to book records have been properly dealt with in the books of account and subsequent transactions recorded in the accounts fairly reflect the changes in the inventories up to .... (balance sheet date).

15. Inventories have been valued on the following basis/bases:

Raw Materials (including components)

Work-in-Process

Finished Goods (including by-products)

Maintenance supplies and Stores and Spare Parts

Loose Tools

Others (specify each major head separately)

(In describing the basis/bases of valuation, the method of ascertaining the cost (e.g. FIFO, Average Cost or LIFO) should also be stated. Similarly, the extent to which overheads have been included in the cost should also be stated.)

16. The following provisions have been made in respect of excess, slow-moving, damaged, or obsolete inventories and these, in our view, are adequate.

....	....
....	....

17. No item of inventories has a net realisable value in the ordinary course of business which is less than the amount at which it is included in inventories.

18. The basis/bases of valuation is/are the same as that/those used in the previous year, except as set out below:

Class of inventory	Basis of Valuation		Effect of change in Basis of Valuation
	This Year	Last Year	
.....	....	....	....
.....	....	....	....

Debtors, Loans and Advances

19. The following items appearing in the books as at ....(date of the Balance Sheet) are considered good and fully recoverable with the exception of those specifically shown as “doubtful” in the Balance Sheet.

Sundry Debtors	Rs.
Loans and Advances	Rs.

Other Current Assets

20. In the opinion of the Board of Directors, other current assets have a value on realisation in the ordinary course of the company's business which is atleast equal to the amount at which they are stated in the Balance Sheet, except as stated in Note X to the financial statements.

Liabilities

21. We have recorded all known liabilities in the financial statements.

22. We have disclosed in notes to the financial statements all guarantees that we have given to third parties and all other contingent liabilities.

23. Contingent liabilities disclosed in the notes to the financial statements do not include any contingencies which are likely to result in a loss and which, therefore, require adjustment of assets or liabilities.

Provisions for Claims and Losses

24. Provision has been made in the accounts for all known losses and claims of material amounts.

25. There have been no events subsequent to the balance sheet date which require adjustment of, or disclosure in, the financial statements or notes thereto.

Profit and Loss Account

26. Except as disclosed in the financial statements, the results for the year were not materially affected by:

(a) transactions of a nature not usually undertaken by the company;

(b) circumstances of an exceptional or non-recurring nature;

(c) charges or credits relating to prior years;

(d) changes in accounting policies.

General

27. The following have been properly recorded and, when appropriate, adequately disclosed in the financial statements:

(a) Losses arising from sale and purchase commitments.

(b) Agreements and options to buy back assets previously sold.

(c) Assets pledged as collateral.

28. There have been no irregularities involving management or employees

who have a significant role in the system of internal control that could have a material effect on the financial statements.

29. The financial statements are free of material misstatements, including omissions.

30. The company has complied with all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance. There has been no non-compliance with requirements of regulatory authorities that could have a material effect on the financial statements in the event of non-compliance.

31. We have no plans or intentions that may materially affect the carrying value or classification of assets and liabilities reflected in the financial statements.