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“The Authority shall establish auditing, reporting standards and practices that will meet the highest auditing and reporting standards”.

- Audit Act of Bhutan 2006

Mandate

The Auditor General, as the head of the Royal Audit Authority (RAA), the Supreme Audit Institution of Bhutan derives his powers and responsibilities mainly from Article 25 of the Constitution of Kingdom of Bhutan and the Audit Act of Bhutan 2006. As per the provisions of the Constitution and the Audit Act of Bhutan, the RAA shall without fear, favour or prejudice, audit the accounts of government or any of its instrumentalities including all offices under the legislature, the judiciary, constitutional bodies, armed forces, corporations and financial institutions where government has ownership interest, all entities including non-government organization whose funds are provided through or by the government, those receiving grants and subsidies directly or through the government and those whose funds are raised through lottery or public contributions. Article 45 (b) of the Audit Act empowers the Auditor General to issue statements on the generally accepted auditing standards and principles and related guidelines. The Act further stipulates that the Authority shall establish and publish auditing standards and practices that meet the highest Auditing and Reporting Standards (Articles 56 and 57).

Auditing Standards

Auditing Standards prescribe the norms of principles and practices, which the auditors are expected to follow in the conduct of audit. They provide minimum guidance to the auditor in determining the extent of auditing steps and procedures that should be applied in the audit and constitute the criteria or yardstick against which the quality of audit results are evaluated.

As required under the Audit Act, the RAA has established these standards broadly in line with INTOSAI auditing standards.

The RAA's auditing standards consist of four parts:

- (a) Basic Postulates;
- (b) General Standards;
- (c) Field Standards; and
- (d) Reporting Standards.

CHAPTER 1

Basic Postulates

The postulates for auditing standards are fundamental assumptions, consistent premises, logical and rational principles and requirements which help in developing auditing standards. These assist in forming the auditor's opinions and reports, particularly in cases where specific standards are not applicable.

The following are the basic postulates with appropriate explanations:

1.1 With increased public consciousness, the demand for public accountability of persons or entities managing public resources has become increasingly evident so that there is a need for the accountability process to be in place and operating effectively.

1.1.1 All entities managing public resources, irrespective of the manner in which they are constituted, their functions, degree of autonomy or funding arrangements, are ultimately accountable for proper usage of public resources to His Majesty the King, the Country and the People through the Parliament.

1.1.2 The Government and all public officials entrusted with the responsibilities to deal with the public funds are responsible to ensure that the funds are used for the intended purpose in accordance with the rules and regulations. The RAA as a watchdog of the public resources is responsible:

- To promote value for money in government operations and contribute towards good governance. Its broad aim is to safeguard the financial interest of the government and to uphold and promote public accountability and sound and prudent management practices.

- To assist the legislature in the exercise of financial control over the executive Government and all public officials entrusted with the responsibilities to deal with the public funds.
- To bring to light the instances of wastefulness, failures, system weaknesses, deficiencies, lapses and the circumstances leading to uneconomical, inefficient and ineffective use of public resources.
- To highlight and make recommendation to the relevant authorities on the overall improvement of the system based on the review of their accounts, operations and management reports.

1.2 Development of adequate information, control, evaluation and reporting systems within the Government will facilitate the accountability process. Management is responsible for correctness, reliability and sufficiency of the form and content of the financial reports and other information.

1.2.1 Management of the audited entity is responsible for correctness, sufficiency and reliability of the form and content of the financial reports and other information.

1.3 Appropriate authorities should ensure the promulgation of acceptable accounting standards for financial reporting and disclosure relevant to the needs of the Government, and the audited entities should develop specific and measurable objectives and performance targets.

1.3.1 The Ministry of Finance and appropriate authorities should ensure the promulgation of acceptable accounting standards and financial reporting and disclosure requirements relevant to the needs of the Government.

1.3.2 The audited entity should develop specific and measurable objectives and performance targets relevant to their needs.

1.3.3 The RAA may recommend to the Government for the promulgation of acceptable accounting standards for financial reporting and disclosure relevant to the needs of the Government and other users of financial information.

1.4 The existence of an adequate system of internal control minimizes the risk of errors and irregularities.

1.4.1 Audited entity is required to develop adequate internal control systems to protect its resources, conduct its operation in an orderly and effective manner and ensure adherence to rules and regulations.

1.4.2 The RAA shall review the adequacy of internal controls and submit recommendations to the audited entity where systems of controls are found to be inadequate, non-existent or non-operational.

1.4.3 The RAA shall report to the parliament through its report on the agencies that have not complied with its recommendations.

1.5 Legislative enactments would facilitate the co-operation of audited entities in maintaining and providing access to all relevant data necessary for a comprehensive assessment of the activities under audit.

1.5.1 The RAA has the right to access of information, records and documents relevant to the activities and transactions to be audited.

1.5.2 The following provisions require the agencies to provide requisite access of information and records to the RAA:

- (a) “Subject to the provisions of other laws, the RAA shall have the right of access to personnel records, information and premises of the entities being audited and parties involved” (*Article 50 of the Audit Act*).

- (b) “The Authority shall have right of access to the records, bank statements of agencies audited, suppliers, taxpayers and other third parties in accordance with the laws, if found relevant and material to the audit of an entity” (*Article 51 of Audit Act*).
- (c) “The RAA shall also have powers to enforce or initiate enforcement action to secure to needed records, which are not produced” (*Article 52 of Audit Act*)

1.6 Consistent application of acceptable accounting standards results in the fair presentation of the financial position and the results of operations.

1.6.1 The RAA expresses an opinion on the financial statements which are prepared by the audited entity using relevant accounting standards and principles.

1.6.2 Consistent application of acceptable accounting standards results in the fair presentation of the financial position; and the results of operations enhances comparability of financial information over a period of time thereby avoiding distortion of results of operations and financial position.

1.7 The RAA shall consider the materiality of issues involved while conducting audits.

1.8 The auditor should apply his professional judgment to the diverse situations that arise in the course of auditing.

1.8.1 It would be impracticable to establish a code of rules, sufficiently elaborate, to cater to all situations and circumstances which the auditor might encounter.

1.8.2 The auditor must exercise his professional judgment in determining the auditing procedures necessary in the circumstances to form a reasonable basis for his opinion and the content of his report.

1.8.3 The auditor should consult the supervising official(s) if the auditor is in doubt in determining his professional judgement as required under Sub-clause 1.8.2 above.

1.9 All audit activities should be within the RAA's audit mandate.

1.9.1 “There shall be a Royal Audit Authority to audit and report on the Economy, Efficiency, and Effectiveness in the use of public resources” (*Article 25.1 of the Constitution*).

1.9.2 The Audit Act provides extensive mandate to the RAA in terms of nature, jurisdiction and types of audit to be conducted (*Article 38, 39 and 41 of the Audit Act*).

1.9.3 In pursuance of the Constitutional responsibility, the Auditor General of Bhutan is empowered to decide on the nature, scope, extent and frequency of audit including the form and content of the audit reports in respect of audit to be conducted by him or on his behalf.

1.10 The RAA should work towards improving techniques and procedures for auditing.

1.10.1 The RAA may develop rules, procedures and guidelines to carry out auditing economically, efficiently and effectively.

1.10.2 The expanding audit role expected of the auditors will require them to improve and develop new techniques and methodologies.

1.10.3 Wherever practicable, the auditors should acquaint themselves with techniques and methodologies of other relevant disciplines.

1.10.4 Auditors shall undergo requisite in-house training before being assigned to the field audit upon joining the RAA.

1.11 The Auditor should avoid conflict of interest with the audited entity.

1.11.1 The RAA performs its role by carrying out audits of the various public sector entities and by reporting the results thereof without fear, favour or prejudice.

1.11.2 To fulfill this role, the RAA needs to maintain its independence and objectivity.

1.11.3 The auditor should not have any form of relationship with the audited entity which could be construed as conflict of interest.

CHAPTER 2

General Standards in Government Auditing

The General Standards in Government Auditing describe the general requirements and qualifications applicable to the individual auditor and the Royal Audit Authority as a whole. They can be seen as requirements for carrying out the audit works related to field and reporting standards in a competent and effective manner.

Independence

2.1 The Royal Audit Authority and its auditor shall be independent from the legislature, the executive, the judiciary and the audited entity.

2.1.1 The RAA shall maintain independence, objectivity and impartiality in all matters relating to the audit works.

2.1.2 Independence from the Legislature, the Judiciary and the Executive branch of government and the audited entity are essential to the conduct of audit and to the credibility of its results.

2.1.3 The following provisions from the Constitution and the Audit Act uphold the independence, the objectivity and impartiality of the auditors and the RAA:

- (a) “The Royal Audit Authority shall be an independent authority headed by the Auditor General who shall be appointed by the Druk Gyalpo from a list of eminent persons recommended jointly by the Prime Minister, the Chief Justice of Bhutan, the Speaker, the Chair Person of the National Council and the Leader of the Opposition Party” (*Article 25.2 of the Constitution*).

- (b) “The Royal Audit Authority shall without, fear, favour or prejudice audit the accounts of all departments and offices of the Royal Government including all offices in the legislature and the judiciary, all public authorities and bodies administering public funds, the armed forces as well as the revenues, public and other monies received and the advances and reserves of Bhutan” (*Article 25.4 of the Constitution*).
- (c) “The Authority shall enjoy full organizational and functional independence including programming, investigative and reporting” (*Article 15 of the Audit Act*).
- (d) “The Authority shall have full authority to determine and administer its organizational structure, budgetary and personnel requirements” (*Article 16 of the Audit Act*).
- (e) “The State shall make adequate financial provisions for the independent administration of the Authority” (*Article 17 of the Audit Act*).
- (f) “The Auditor General and its auditors shall enjoy immunity from prosecution for any lawful act arising from the due discharge of their duties under this act” (*Article 99 of the Audit Act*).

2.1.4 While the RAA must observe the laws enacted by the legislature, adequate independence requires that it should not otherwise be subject to direction by the legislature in the programming, planning and conduct of audits.

2.1.5 The RAA has discretion to set priorities and programme its work in accordance with the mandate and adopt methodologies appropriate to the audits to be undertaken.

- 2.1.6 The RAA may provide members of the Public Accounts Committee factual briefings and additional information on audit reports submitted to the Parliament, but it is important that the RAA maintains its independence from political influence, in order to preserve an impartial approach to its audit responsibilities.
- 2.1.7 The RAA shall not be responsive, nor give the appearance of being responsive, to the wishes of particular political interests.
- 2.1.8 The RAA and its auditors should not be subject to the direction or control of any other person or authority, and that no person may inhibit the Auditor General in the conduct of his or her duties.
- 2.1.9 The RAA's reports assist the executive by drawing attention to deficiencies in administration and recommending improvements. Care should be taken to avoid participation in the executive's functions of the kind that would undermine the RAA's independence and objectivity in the discharge of its mandate.
- 2.1.10 The RAA may advise the executive in such matters as accounting standards and policies and the form of financial statements. The RAA must ensure that in providing such advice it avoids any explicit or implied commitment that would impair the independent exercise of the audit mandate.
- 2.1.11 Maintenance of the RAA's independence does not preclude requests to the RAA by the executive proposing matters for audit. The RAA may accept or decline any such request.
- 2.1.12 Any imposition on resource or other restrictions by the executive, which would constrain the RAA's exercise of its mandate, would cause the RAA to report the matter to the Parliament.

- 2.1.13 The auditors should not accept any gifts, entertainments from the audited entity which would jeopardize their independence.
- 2.1.14 The RAA may co-operate with academic institutions and enter into formal relationship with professional bodies provided such relationships do not inhibit its independence and objectivity, in order to enrich itself of the advice of the experienced members of the profession at large.
- 2.1.15 The RAA may acquire the services of external experts/specialists if the successful carrying out of an audit so requires.
- 2.1.16 The RAA may outsource the auditing assignments of NGOs, CSOs and other agencies as may be appropriate to private professional auditing firms.

Conflict of Interest

2.2 The Auditor shall avoid conflicts of interest with the audited entity.

- 2.2.1 The RAA should carry out audits and report its results effectively and efficiently, by maintaining independence, impartiality and objectivity.
- 2.2.2 The following provisions from the Audit Act of Bhutan 2006 are directed towards avoiding conflict of interest with the audited entity;
 - (a) “The Auditor General shall ensure that no conflict of interest arises or appears to arise, between his public duties and his private interests, financial or otherwise” (*Article 30 of the Audit Act*).
 - (b) “All auditors, including the Auditor General, shall declare any perceived or potential conflict of

interest before undertaking any particular audit or other duties concerning a particular person or entity” (*Article 33 of the Audit Act*).

- (c) “The Auditor General may exclude an official from an audit if he considers there is a reasonable cause to doubt the existence of a conflict of interest” (*Article 35 of the Audit Act*).

2.2.3 Auditors should not become involved in instructing personnel of an audited entity as to their duties nor get involved in any decision making or approval process which is considered the audited entity’s management responsibility.

2.2.4 All auditors should subscribe to the Good Code of Conduct, Ethics and Secrecy of the Authority.

Competence and Qualification of Auditors

2.3 The Royal Audit Authority and its auditors must possess the required qualification and competence necessary for the discharge of the audit mandate.

2.3.1 The RAA has the responsibility to see that audit is conducted by its staff including auditors who are duly deputed or contracted, who collectively have the competence or the knowledge, skills and experience necessary for the effective discharge of the audit mandate.

2.3.2 The following stipulations would ensure the engagement of qualified and competent auditors by the Royal Audit Authority.

- (a) The Royal Audit Authority shall adopt policies and procedures to recruit, engage and maintain competent and motivated staff with suitable qualifications that match the various tasks mandated to the Authority.

- (b) Audits differ in purpose and scope. A variety of skills would be needed to meet the requirements of audit.
 - (c) The qualification should apply to the skills of the RAA as a whole and not necessarily to the individual auditors that comprise the audit staff. Each audit staff member or hired auditor or consultant with acceptable skills in such areas as accounting, engineering, etc, need not possess all such skills.
 - e) The individual auditors must possess adequate qualifications, skills and experience and have access to a full range of audit methodologies. All aspects of the audit work should be carried out by auditors who possess requisite competence and experience that meets the requirement as to scope and complexity of the audit assignment.
 - f) Auditors should have adequate knowledge of government administration, including financial management, Auditing Standards, Audit Manuals and Guidelines applicable to their field of work.
 - g) All audit staff must possess good knowledge of the Legal Framework covering the RAA, the Code of Ethics, as well as the policies, procedures and practices of the Royal Audit Authority.
- 2.3.3 “The RAA shall develop and implement training programmes which ensure that audit staffs remain competent to carry out their duties in accordance with the prevailing standards and practices” (*Article 45 (f) of the Audit Act*).
- 2.3.4 The RAA should encourage its personnel to become members of a professional body relevant to their field of work and to participate in that body’s activities.

- 2.3.5 The RAA should develop Audit Manuals, instructions, procedures and guidelines in line with Article 42 (a) of the Audit Act to ensure quality of audits.
- 2.3.5 Care should be taken to review and update the Auditing Standards and Manuals from time to time in line with the changes and developments in the field of auditing.
- 2.3.6 The RAA shall maintain an efficient information system covering Government orders, rules, acts, etc. through its data base and shall be made accessible to its auditors.

Due Professional Care and Objectivity

- 2.4 The RAA and the auditors must exercise due professional care and objectivity when conducting audits**
 - 2.4.1 All auditors must exercise due professional care and objectivity in specifying, gathering and evaluating audit evidence and in reporting findings, conclusions and recommendations.
 - 2.4.2 All auditors shall be guided by applicable laws, rules and regulations, Auditing Standards as well as the Generally Accepted Accounting Principles and sound management practices.
 - 2.4.3 The RAA must be, and be perceived to be, objective and impartial in its audits and exercise due professional care in all its audit work. It must be fair in its evaluations and in its reporting of the outcomes and results of audits.
 - 2.4.4 All audit findings, conclusions and recommendations submitted should be based on the audit evidence gathered
 - 2.4.5 Due care imposes a responsibility upon each auditor of the RAA to observe all applicable standards in conducting the

government audits. The following should be considered while choosing the tests, procedures etc.

- a) What is necessary to achieve the audit objectives?
 - b) Materiality of matters to which the test procedures and methodology will be applied.
 - c) Effectiveness of internal control mechanism.

 - d) Cost and extent of audit work to be done, as well as the benefits that may be derived therefrom.
 - e) The audit time allotted to complete the work including the report preparation.
- 2.4.6 Where an authorized or recognized entity sets standards or guidelines for accounting and reporting by public enterprises, the RAA may use such guidelines in the course of its examination.
- 2.4.7 If the RAA employs external experts as consultants it must exercise due care to assure it of the consultants' competence and aptitude for the particular tasks involved.
- 2.4.8 Obtaining advice from an external expert does not relieve the RAA of responsibility for the opinions formed or conclusions reached on the audit task.
- 2.4.9 Information about an audited entity acquired in the course of the auditor's work must not be used for purposes outside the scope of the audit and the Audit Act.
- 2.4.10 "The Authority may rely on the audits performed by other organizations including internal auditors if it has reasonable assurance through such means as prior experience, tests or other indicators that the audits and other reports on those audits are accurate, reliable and meet its standards" (*Article 59 of the Audit Act*).

- 2.4.11 When the RAA uses the work of another auditor(s), it must apply adequate procedures to provide assurance that the other auditor(s) has exercised due care and complied with relevant auditing standards, and may review the work of the other auditor(s) to satisfy itself as to the quality of work done.
- 2.4.12 The RAA should assess any certification or authorizations held by the other auditor or external expert and seek to assess his or her independence and objectivity.

Fraud and corruption

2.5 When planning, performing audits, evaluating and reporting on the results of these audits, the auditor should consider the risk of fraud and corruption.

- 2.5.1 When planning the audit, the auditor should consider the risk of fraud and corruption. Accordingly the auditor should develop investigative auditing procedures designed to increase the likelihood of detection of fraud and corruption thereby reducing the incidence of their occurrences. (*Article 42(d) of the Audit Act*).
- 2.5.2 When the auditor discovers instances of fraud and corruption, such instances should be reported instantly to the Auditor General through the supervisor who will then consider for further appropriate action, and should also, if appropriate, report the issue to the management of the audited entity.
- 2.5.3 Cases of fraud and corruption should also be reported to the appropriate authorities, such as the Anti Corruption Commission who shall carry out further investigation if deemed appropriate.

Quality Assurance

2.6 The Royal Audit Authority should have an appropriate Quality Assurance system in place.

- 2.6.1 The RAA should establish adequate quality assurance programmes to improve quality of audit performance and results. The benefits to be derived from such programmes make it essential for appropriate resources to be made available for this purpose.
- 2.6.2 The RAA should establish systems and procedures to:
- (a) Confirm that internal quality control processes have operated satisfactorily;
 - (b) Ensure the quality of the audit report; and
 - (c) Secure improvements and avoid repetition of weaknesses.
- 2.6.3 The quality of the work done by the RAA can be enhanced by strengthening internal review and by the independent appraisal of its work
- 2.6.4 The RAA should ensure that applicable standards have been followed in the conduct of audits and any deviations from the standards are justified and documented.
- 2.6.5 “The Authority may undertake a peer review by a member of peer organization or other professional bodies from time to time to ensure consistency and high standard of auditing” (Article 86 of the Audit Act).
- 2.6.6 The RAA shall evaluate its performance through periodic survey involving all stakeholders, which shall assist in improving its function.

Chapter 3

Field Standards

The field standards are the auditing framework established for conducting and managing audit work. It establishes the criteria and overall framework for the purposeful, systematic and balanced steps and actions that the auditor has to follow in the planning and execution of audits.

Field standards are related to the general auditing standards, which set out the general requirements and preconditions for undertaking the tasks covered in the field standards. They also relate to the reporting standards, which cover the communication aspects of auditing, as the results from audits carried out in accordance with the field standards constitute the source for the content of the audit opinion or report.

The field standards applicable to all types of audit are:

- (a) The auditor should plan the audit in a manner, which ensures that an audit of high quality is carried out in an economic, efficient and effective way and in a timely manner.
- (b) The work of the audit staff at each level and audit phase should be properly supervised during the audit; and a senior member of the audit staff should review documented work.
- (c) The auditor, in determining the extent and scope of the audit, should study and evaluate the reliability of internal control.
- (d) In conducting financial audits, a test should be made of compliance with applicable laws and regulations. The auditor should design audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, and illegal acts that could have a direct and material effect on the financial statement amounts or the results of regularity audits. The auditor also should be aware of the possibility of illegal acts that could have an indirect and material effect on the financial statements or results of regularity audits.

In conducting performance audits, an assessment should be made of compliance with applicable laws and regulations when necessary to satisfy the audit objectives. The auditor should design the audit to provide reasonable assurance of detecting illegal acts that could significantly affect audit objectives. The auditor also should be alert to situations or transactions that could be indicative of illegal acts that may have an indirect effect on the audit results.

Any indication that an irregularity, illegal act, fraud or error may have occurred which could have a material effect on the audit should cause the auditor to extend procedures to confirm or dispel such suspicions.

The regularity audit is an essential aspect of government auditing. One important objective, which this type of audit assigns to the RAA, is to make sure, by all the means put at its disposal, that the Government budget and accounts are complete and valid. This will provide Parliament and other users of the audit report with assurance about the size and development of the financial obligations of the Government. To achieve this objective the RAA will examine the accounts and financial statements of the government with a view to assuring that all operations have been correctly undertaken, completed, passed, paid and registered.

- (e) Competent, relevant and reasonable evidence should be obtained to support the auditor's judgment and conclusions regarding the organization, programme, activity or function under audit.
- (f) In regularity (financial) audit and in other types of audit when applicable, auditors should analyse the financial statements to establish whether acceptable accounting standards for financial reporting and disclosure are complied with. Analysis of financial statements should be performed to such a degree that a rational basis is obtained to express an opinion on financial statements.

Planning

3.1 The auditor should plan the audit in a manner which ensures that an audit of high quality is carried out in an economic, efficient and effective way, and in a timely manner.

3.1.1 The Audit Plan is the document in which the auditor describes the planned strategy and approach for an audit based on their established knowledge of the business and assessed risk and materiality.

3.1.2 The auditor should prepare and develop detailed audit programme prior to taking up the audit. In planning an audit, the auditor should:

- (a) Identify important aspects of the environment in which the audited entity operates.
- (b) Develop an understanding of the accountability relationships;
- (c) Specify the audit objectives and the tests necessary to meet them;
- (d) Identify key management systems and controls and carry out a preliminary assessment to identify both their strengths and weaknesses;
- (e) Consider the form, content and users of audit opinions, conclusions or reports;
- (f) Determine the materiality of matters to be considered;
- (g) Review the internal audit of the audited entity and its work programme;
- (h) Assess the extent of reliance that might be placed on other auditors, for example, internal audit;
- (i) Determine the most efficient and effective audit approach;

- (j) Provide for a review to determine whether appropriate action has been taken on previously reported audit findings and recommendations; and
 - (k) Provide for appropriate documentation of the audit plan and for the proposed fieldwork.
- 3.1.3 The audit planning also includes defining audit objectives, setting up procedures ideally for each audit objective, determining the nature and scope of audit including the audit period, setting the audit time or time frame for conducting the audit and preparing the audit report, and assigning specific responsibilities for audit execution, supervision and review.
- 3.1.4 The audit plan should be flexible enough to respond to situation prevailing at the time of audit. Necessary changes occasioned thereby should be integrated in the audit plan
- 3.1.5 Proper supervision in planning involves appropriate guidance in the preparation of audit priorities and the audit programme, including determination of adjustments and changes to be made, and assignment of audit responsibility, as well as development, maintenance, and encouragement of individual involvement, commitment and morale.

Knowledge of the Entity

- 3.2 **The auditor should obtain sufficient knowledge of the entity to enable him/her to identify and understand the organization, events, transactions and practices that may have a significant effect on the audit results.**
- 3.2.1 The first step in the planning process is to collect information about the audited entity to assess risk and determine materiality levels. Obtaining the required knowledge of the entity is a continuous and cumulative process that involves gathering and assessing information

from various sources and relating the resulting knowledge to the planning of the audit and audit evidence collected in the course of the audit.

- 3.2.2 The information gathered may cover information on organizational structures, the environment it operates in and the nature of the entity's operations, internal control systems, internal audit function etc.
- 3.2.3 The auditor should understand the audited entity by familiarizing with the entities' financial and accounting, and management information systems; laws, rules and regulations pertaining to the entities' operations, objectives, policies affecting the entities including their internal and external environment and linkages.
- 3.2.4 The auditor should be able to identify key areas within the audited entity, particularly in its internal control system, priority areas in its operations and critical decision points in its information system.
- 3.2.5 The auditor should, in the process of obtaining the necessary knowledge of the entity, update and re-evaluate information gathered previously, including audit documentation from previous years and information in the permanent files.

Internal Controls

3.3 The auditor should assess and evaluate the existence, functioning and reliability of the internal control system.

- 3.3.1 All agencies shall be responsible to establish proper working systems and procedures including transparent and well defined controls and checks within the respective agencies for achieving, as far as practicable, the financial management and accountability objectives of the Government (*Chapter III, 3.3 E, clause 3.3.9 of the Financial Management Manual of the FRR 2001*).

- 3.3.2 The auditors should review the existence of internal control system and evaluate it (*internal control*) not only to determine the extent of audit work required, but also to determine weakness therein and to recommend measures to improve controls.
- 3.3.3 The auditor may use the work of the internal auditors depending on the reliability of the work performed to prevent duplication of effort and to save on audit time.
- 3.3.4 Internal control devices that the auditor decides to rely on must always be tested to assess its effectiveness and reliability. The study and evaluation of internal control should be carried out according to the type of audit undertaken.
- 3.3.5 In the case of financial audit, study and evaluation are made mainly on controls that assist in safeguarding assets and resources, and assure the accuracy and completeness of accounting records.
- 3.3.6 In the case of compliance audit, study and evaluation are made mainly on controls that assist management in complying with laws and regulations.
- 3.3.7 In the case of performance audit, study and evaluation are made on controls that assist in conducting the business of the audited entity in an economic, efficient and effective manner, ensuring adherence to management policies, and producing timely and reliable financial and management information.
- 3.3.8 Where accounting or other information systems are computerized, the auditor should determine whether internal controls are functioning properly to ensure the integrity, reliability and completeness of the data.

Audit Risk

3.4 The auditor should exercise sound professional judgment in assessing the audit risk and carry out the necessary audit tests to reduce risk to an acceptable level.

- 3.4.1 Audit risk consists of three components: inherent risk, control risk and detection risk. Inherent and control risk differs from detection risk in that they are determined within the audited entity and the environment it operates in. Detection risk on the other hand, is determined by the auditor and is dependent on the extent and timing of the auditor's procedures. It is through the auditor's control of detection risk that the auditor can seek to secure an acceptably low audit risk.
- 3.4.2 "Risk Assessment" refers to the systematic analysis of the various aspects of the audited entity's operations, internal control systems and environment, in order to identify potential risk areas.
- 3.4.3 Risk assessments, and the results thereof, should be the most important determinant in choosing the areas to be prioritized within an entity.
- 3.4.4 Risk assessments should be carried out at both division and individual assignment level. The exercise of professional judgment is essential in making risk assessments.
- 3.4.5 The auditor should evaluate the risks and document the understanding and assessment of the audit risks for every audit assignments.
- 3.4.6 The audit risks documented should be evaluated by the supervisor and assess the impact on the audit assignments and its outcome.

- 3.4.7 In designing steps and procedures to test or assess compliance, auditors should evaluate the entity's internal controls and assess the risk that the control structure might not prevent or detect non-compliance.

Materiality

3.5 The auditor should assess the materiality in order to determine the level of acceptable errors in the financial statements.

- 3.5.1 Materiality is often measured in monetary value, but does not have to be so. Irregularities and non-compliance with laws and regulations could for instance render a matter material even if the amounts involved were “immaterial”.
- 3.5.2 “Assessment of Materiality” refers to the establishment of criteria for what is considered to be a material error. The auditor should specify the criteria for materiality on the basis of his/her professional judgment and with due regard for factors that affect financial statements and other information in a way that will have an impact on the decisions and conclusions of the users of the information.
- 3.5.3 Auditors need to be knowledgeable on the steps required to determine the materiality on the entity being audited. As the laws, regulations and the internal control function that may be instituted are often different; the auditors need to exercise professional judgment in determining risks that might have a significant impact on the audit objectives and outcomes.
- 3.5.4 When determining materiality levels, the auditor should consider the following factors:
- a) The size (monetary value) of an account or an item in an account;

- b) Omission of information in documents that form the basis for decision making;
- c) Failure to submit information or the submission of incorrect information to decision making authorities regarding, for instance the appropriation of funds;
- d) Unbudgeted expenditure; and
- e) Breach of any law, regulation or statutes applicable to the audited entity or the decisions and intentions of the Parliament.

Audit Programme

3.6 The auditor should develop and document a detailed audit programme for each audit assignment. The audit should incorporate the audit objective, information on the timing and organization of the audit and the tests that are to be carried out.

- 3.6.1 The auditor should prepare a detailed audit programme for each audit assignment undertaken. The audit programme should also always contain the objectives of the audit, and the planned audit tests for each audit area.
- 3.6.2 While preparing the audit programme, the auditor should consider the risk and materiality assessments and the required level of assurance to be provided by substantive tests.
- 3.6.3 The auditor should also consider the timing of tests of controls and substantive tests, and the need for involvement and assistance from the audited entity, and if appropriate, other auditors and experts.
- 3.6.4 Those planning the audit need to be knowledgeable of the compliance requirements that apply to the entity being audited.

- 3.6.5 The audit programme should be revised as necessary during the audit. Planning is a continuous process and should be flexible enough to respond to situations prevailing at the time of audit. The reasons for significant changes to the audit programme should be recorded in working papers.

Compliance with Applicable Laws and Regulations

3.7 The auditors should ascertain compliance to applicable laws, rules and regulations in force.

- 3.7.1 Government agencies and entities are created by law or orders and are governed by laws, rules and regulations in their operations. Hence, the auditors should determine whether the agencies/entities have complied with applicable laws, rules and regulations.
- 3.7.2 In conducting any regularity audits, a test should be made of compliance with applicable laws and regulations.
- 3.7.3 The auditor should design audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, and illegal acts that could have a direct and material effect on the financial statement amounts or the results of regularity audits. The auditor also should be aware of the possibility of illegal acts that could have an indirect and material effect on the financial statements or results of regularity audits.
- 3.7.4 Reviewing compliance with laws and regulations is especially important when auditing government programmes because decision-makers need to know if the laws, rules and regulations are being followed, whether they are having the desired results, and if not, what revisions are necessary.
- 3.7.5 The auditor's study should also include review of related legislative history, relevant charters, legal opinions,

administrative and court decisions, other regulatory requirements, agreements, contracts, sub-contracts and pertinent documents. Additionally government organizations, programmes, services, activities, and functions are created by laws and are subject to more specific rules and regulations.

- 3.7.6 One of the important objectives of the regularity audit is to ascertain that the government budget and accounts are complete and valid. To achieve this objective, the RAA will examine the accounts and financial statements of the government with a view to assuring that all transactions and operations have been correctly undertaken, approved, paid and properly recorded.
- 3.7.7 In performance audit, review will focus mainly on the laws and regulations pertaining to the objectives of the agency/entity, its programmes or activities. The auditor should do sufficient testing to determine whether the agency/entity carries out programmes and activities in conformity with such legal and regulatory requirements.
- 3.7.8 The auditor also should be alert to situations or transactions that could be indicative of illegal acts that may indirectly impact the results of the audit. When audit steps and procedures indicate that illegal acts have or may have occurred, the auditor needs to determine the extent to which these acts affect the audit results.

Audit Evidence

- 3.8 The auditor should obtain competent, relevant and reasonable audit evidence to draw and support conclusions regarding the entity, programme, activity or function being audited.**

- 3.8.1 The auditor should obtain sufficient, competent and reliable audit evidence to support his audit findings, judgment conclusions, audit certificate or opinion and recommendations.
- 3.8.2 Since auditor seldom has the opportunity of considering all information about the audited entity, it is crucial that the data collection and sampling techniques are carefully chosen.
- 3.8.3 When computer-based system data are an important part of the audit and the data reliability is crucial to accomplishing the audit objective, auditor needs to satisfy himself that the data are reliable and relevant.
- 3.8.4 Auditor should have a sound understanding of techniques and procedures and should obtain evidence through inspection, inquiry, confirmation, physical count and inventory, comparison reconciliation and other audit techniques.
- 3.8.5 The RAA should ensure that the techniques employed are sufficient to reasonably detect all quantitatively material errors and irregularities.
- 3.8.6 In choosing approaches and procedures, consideration should be given to the quality of evidence, i.e. the evidence should be competent, relevant, reasonable and as direct as possible so as to reduce the need for inferences to be made.

Documentation

3.9 The auditor should document all audit evidence that is used to support audit conclusions, opinions and recommendations.

- 3.9.1. “Documentation” encompasses all the auditor’s working papers and all other source material assembled and collected during the audit. Working papers” refer to documentation

of the planning of the audit work, the performance of audit procedures (execution), and the conclusions drawn on the basis of the audit evidence.

- 3.9.2 Auditors should adequately document the audit evidence in working papers, including the basis and extent of the planning, work performed and the findings of the audit.
- 3.9.3 Working papers should contain sufficient information to enable an experienced auditor having no previous connection with the audit to ascertain from them the evidence that supports the auditor's significant findings, conclusions and quality of work performed.
- 3.9.4 The auditor should bear in mind that the content and arrangement of working papers reflect the degree of the auditor's proficiency, experience, and knowledge.
- 3.9.5 Documentation may be stored on a variety of media such as paper, film, electronic or other media.
- 3.9.6 Retention of working papers is of paramount importance for any legal issues resulting from the audit, as well as being an important source of information for follow-up and future audits of the entity.

Supervision and Review

3.10 The work of the audit staff at each level and audit phase should be properly supervised during the audit, and documented work should be reviewed by a senior member of the audit staff.

- 3.10.1 Supervision of audit is essential to ensure the fulfilment of audit objectives and the quality of work. Proper supervision from planning till the final issuance of audit report is necessary for all audits regardless of the competence of the individual auditor or the audit team.

- 3.10.2 All audit work should be properly supervised and quality assured at each stage of the audit, and a senior member of staff/supervisor should review documented work.
- 3.10.3 Supervision should be directed both to the substance and to the method of auditing. It involves ensuring that:
- (a) The members of the audit team have a clear and consistent understanding of the audit plan;
 - (b) The audit is carried out in accordance with the auditing standards and practices of the RAA;
 - (c) The audit plan and procedures specified in the audit plan are followed unless a variation is authorized;
 - (d) Working papers contain evidence adequately supporting all conclusions, recommendations and opinions;
 - (f) The auditor achieves the stated audit objectives; and
 - (g) The audit report includes the audit conclusions, recommendations and opinions, as appropriate.
- 3.10.4 All audit works should be reviewed by supervisors at appropriate level. “Reviews” refer to quality controls carried out after working papers etc. have been prepared. It is done to ensure that the documentation collected supports the conclusions and recommendations. Reviews can be done either before the audit results are reported, as a means of ensuring the quality of the results that are to be reported, or be in the form of a “post-audit review” where it serves as a tool for measuring the quality of work and compliance with the Standards and Audit Manuals to facilitate future training and improvements.
- 3.10.5 Audit reviews for all audits regardless of the competence of the individual auditor or audit team is essential to ensure the fulfilment of audit objectives and the quality of work.

- 3.10.6 The RAA should adopt policies and procedures to review the efficiency, effectiveness and quality of audit work and the compliance with Auditing Standards and Audit Manuals.
- 3.10.7 Article 86 of the Audit Act requires peer reviews from time to time to ensure consistency and high standard of auditing in the RAA. The purpose of these reviews is to:
- (a) Ensure that the audit work performed in the RAA is of the desired quality;
 - (b) Assess and ensure compliance with the Auditing Standards and Audit Manuals;
 - (c) Identify training needs to improve audit quality; and
 - (d) Ensure a uniform audit approach in the RAA Office.
- 3.10.8 “Post audit” reviews of audit work shall be carried out annually by a designated Review Team.

Analysis of Financial Statements

3.11 The auditor shall carry out the analysis of Financial Statements of the audited entity.

- 3.11.1 In regularity (financial) audit, and in other types of audit when applicable, auditor should analyse the financial statements to establish whether acceptable accounting standards for financial reporting and disclosure are complied with.
- 3.11.2 Analysis of financial statements should be performed to such a degree that a rational basis is obtained to express an opinion on financial statements.
- 3.11.3 Financial statement analysis aims at ascertaining the existence of the expected relationship within and between

the various elements of the financial statements, identifying any unexpected relationships and any unusual trends. The auditor should therefore thoroughly analyse the financial statements and ascertain whether:

- (a) Financial statements are prepared in accordance with acceptable accounting standards;
- (b) Financial statements are presented with due consideration to the circumstances of the audited entity;
- (c) Sufficient disclosures are presented about various elements of financial statements; and
- (d) The various elements of financial statements are properly evaluated, measured and presented.

3.11.4 The methods and techniques of financial analysis depend to a large degree on the nature, scope and objective of the audit, and on the knowledge and judgment of the auditor.

3.11.5 The RAA is required to report on the execution of the budgetary norms. The audit should include:

- a) For revenue accounts - ascertaining whether forecasts are those of initial budget, and whether the audits of taxes and duties recorded, and imputed receipts, can be carried out by comparison with the annual financial statements of the audited activity;
- b) For expenditure accounts - verifying credits to assist budgets, adjustment laws, and the previous year's financial statements in the case of carryovers.

Chapter 4

Reporting Standards

The purpose of these standards is to establish requirements concerning the reporting of audit work in connection with the performance of all types of audits in the Royal Audit Authority.

The RAA issues the following types of reports:

- (a) Audit reports on the accounts and operations of agencies/entities;
- (b) Management Appraisal Report;
- (c) Audit report on the certification of donor funded projects;
- (d) Audit report on Performance Audit/Systems Audit;
- (e) Statutory Audit Report;
- (f) Auditor General's Advisory Series;
- (g) Auditor General's Occasional Papers;
- (h) Audit report on the certification of Consolidated Annual Financial Statements of the Government;
- (i) Annual Audit Report; and
- (j) Follow up Report.

The audit report may be presented on other media that are retrievable by all users. Retrievable audit reports include those, which are in electronic formats and may be posted on the Internet.

Chapter 6, Article 67 of the Audit Act stipulates that the RAA shall submit copies of audit report to the Druk Gyalpo, the Prime Minister and the Chairperson of the Royal Civil Service Commission or Chairperson of the Anti-Corruption Commission, where offences are serious and require urgent attention.

- 4.1 The auditor shall prepare a written report setting out the audit observations, conclusions and recommendations in an appropriate form. Its content should be easy to understand, free from ambiguity and supported by sufficient, competent and relevant audit evidence and be independent, objective, fair, complete, accurate, constructive and concise.**
- 4.1.1 The auditors shall prepare and submit promptly an audit report for the audit work completed. Timeliness of the report shall be strictly observed.
- 4.1.2 The report shall conform to specific standards of report content, presentation, language and style.
- 4.1.3 The report should be clear and easy to understand and free from ambiguity. The findings should be supported by sufficient, competent and relevant audit evidence. The recommendations must flow logically from the observations and conclusions and should be practicable prompting actions by the entity.
- 4.1.4 The audit report should be complete containing all pertinent information needed to satisfy the audit objectives, and to promote an adequate and correct understanding of the matter reported. It also means including appropriate background information.
- 4.1.5 Accuracy requires that the evidence presented is true and the conclusions be correctly portrayed. The conclusions should flow from the evidence. The need for accuracy is based on the need to assure the users that what is reported is credible and reliable.
- 4.1.6 The report should include only information, findings and conclusions that are supported by competent and relevant evidence. Reported evidence should demonstrate the correctness and reasonableness of the matters reported.

- 4.1.7 Correct portrayal means describing accurately the audit scope and methodology and presenting findings and conclusions in a manner consistent with the scope of audit work.
- 4.1.8 Objectivity requires that the presentation throughout the report to be balanced in content and tone. The audit report should be fair and not be misleading and should place the audit results in proper perspective. This means presenting the audit results impartially and guarding against the tendency to exaggerate or over-emphasize deficient performance. In describing shortcomings in performance, the auditor should present the explanation of the audited entity and stray instances of deviation should not be used to reach broad conclusions.
- 4.1.9 The tone of reports should encourage decision-makers to act on the auditor's findings and recommendations. Although findings should be presented clearly and forthrightly, the auditor should keep in mind that one of the objectives is to persuade and this can best be done by avoiding language that generate defensiveness and opposition.
- 4.1.10 Being convincing requires that the audit results to be presented persuasively and the conclusions and recommendations followed logically from the facts presented. The information presented should be sufficient to convince the readers to recognise the validity of the findings and reasonableness of audit conclusions. A convincing report can help focus the attention of management on matters that need attention and help stimulate correction.
- 4.1.11 Clarity requires that the report be easy to read and understand. Use of non-technical language is essential. Wherever technical terms and unfamiliar abbreviations are used, they should be clearly defined. Both logical organization of the material and precision in stating the facts

and in drawing conclusions significantly contribute to clarity and understanding. Appropriate visual aids (such as photographs, charts, graphs and maps etc.) should be used to clarify and summarize complex material.

- 4.1.12 Being concise requires that the report is not longer than necessary to convey the audit opinion and conclusions. Complete and concise reports are likely to receive greater attention.
- 4.1.13 Being constructive requires that the report also includes well thought out suggestions, in broad terms, for improvements, rather than how to achieve them. In presenting the suggestions due regard should be paid to the requirements of rules and orders, operational constraints and the prevailing milieu. The suggestions should be discussed with sufficiently high level functionaries of the entities and as far as possible, their acceptances obtained before these are incorporated in the report.
- 4.1.14 Timeliness requires that the audit report should be made available promptly to be of utmost use to all users, particularly to the audited entities and/or Government who have to take requisite action.
- 4.1.15 The RAA should make a balanced reporting. To maintain a balanced perspective in audit the auditor should not only report on the negative issues like shortfalls, deficiencies, and lapses but also report on noteworthy accomplishments made by agencies/entities.
- 4.1.16 Improvements made by the agencies/entities should be acknowledged and given due cognizance. Besides, the views and comments of the management should be properly evaluated and considered while framing further comments and recommendations.

- 4.1.17 The RAA shall require prompt and proper follow up action by the entity on the individual audit report issued by it in order to enhance the effectiveness of audit and promote public accountability.
- 4.1.18 The RAA shall ensure proper distribution of audit reports to the agencies and authorities as specified in Articles 65 to 67 of the Audit Act.
- 4.1.19 The Annual Audit Report is submitted to the Druk Gyalpo, the Prime Minister and the Parliament. The copies of the Annual Audit Report are endorsed to the Lhengye Zhungtsho, concerned heads of audited entities, the Chairperson of the Anti-Corruption Commission and the Chairperson of the Public Accounts Committee as per *(Article 72 & 73 of the Audit Act)*.
- 4.1.20 The form and content of all audit opinions and reports are founded on the following general principles:
- (a) **Title:** The opinion or report should be preceded by a suitable title or heading, helping the reader to distinguish it from statements and information issued by others.
 - (b) **Signature and date:** The opinion or report should be properly signed. The inclusion of a date informs the reader that consideration has been given to the effect of events or transactions about which the auditor became aware up to that date (which, in the case of financial audits, may be beyond the period of the financial statements).
 - (c) **Objectives and scope:** The opinion or report should include reference to the objectives and scope of the audit. This information establishes the purpose and boundaries of the audit.

- (d) **Completeness:** The report should be complete in all material respect. Opinions should be appended to and published with the financial statements to which they relate, but performance reports may be free standing. Where, for reasons of National interest some items are required to be excluded from the report thereby rendering the report incomplete, the Auditor General may communicate such matters separately.
- (e) **Addressee:** The opinion or report should identify those to whom it is addressed, as required by the circumstances of the audit engagement and the Audit Act or other legislation.
- (f) **Identification of subject matter:** The opinion or report should identify the financial statements in the case of financial audits or area in the case of performance audits to which it relates. This includes information such as the name of the audited entity, the date and period covered by the financial statements and the subject matter that has been audited.
- (g) **Legal basis:** Audit opinions and reports should identify the legislation or other authority providing for the audit.
- (h) **Compliance with standards:** Audit opinions and reports should indicate the auditing standards or practices followed in conducting the audit, thus providing the reader with an assurance that the audit has been carried out in accordance with generally accepted procedures.
- (i) **Timeliness:** The audit opinion or report should be available promptly to be of greatest use to readers and users, particularly those who have to take necessary action.

4.1.21 An audit opinion is normally in a standard format, relating to the financial statements as a whole, thus avoiding the need to state at length what lies behind it but conveying by its nature a general understanding among readers as to its meaning. The nature of these words will be influenced by the legal framework for the audit, but the content of the opinion will need to indicate unambiguously whether it is unqualified or qualified and, if the latter, whether it is qualified in certain respects or is adverse or a disclaimer of opinion.

An unqualified opinion is given when the auditor is satisfied in all material respects that:

- (a) The financial statements have been prepared using acceptable accounting bases and policies which have been consistently applied;
- (b) The statements comply with statutory requirements and relevant regulations;
- (c) The view presented by the financial statements is consistent with the auditor's knowledge of the audited entity; and
- (d) There is adequate disclosure of all material matters relevant to the financial statements.

4.1.22 **Emphasis of Matter:** In certain circumstances the auditor may consider that the reader will not obtain a proper understanding of the financial statements unless attention is drawn to unusual or important matters. As a general principle the auditor issuing an unqualified opinion does not make reference to specific aspects of the financial statements in the opinion in case this should be misconstrued as being a qualification. In order to avoid giving that impression, references that are meant as "emphasis of matter" are contained in a separate paragraph from the opinion.

However, the auditor should not make use of an emphasis of matter to rectify a lack of appropriate disclosure in the financial statements, nor as an alternative to, or a substitute for, qualifying the opinion.

- 4.1.23 **Adverse Opinion:** Where the auditor is unable to form an opinion on the financial statements taken as a whole due to disagreement which is so fundamental that it undermines the position presented to the extent that an opinion which is qualified in certain respects would not be adequate, an adverse opinion is given. The wording of such an opinion makes clear that the financial statements are not fairly stated, specifying clearly and concisely all the matters of disagreement. Again, it is helpful if the financial effect on the financial statements is quantified where relevant and practicable.
- 4.1.24 **Disclaimer of Opinion:** Where the auditor is unable to arrive at an opinion regarding the financial statements taken as a whole due to an uncertainty or scope restriction that is so fundamental that an opinion, which is qualified in certain respects, would not be adequate, a disclaimer is given. The wording of such a disclaimer makes clear that an opinion cannot be given, specifying clearly and concisely all matters of uncertainty. It is customary to provide a detailed report amplifying the opinion in circumstances in which it has been unable to give an unqualified opinion.
- 4.1.25 In addition, regularity audits often require that reports are made where weaknesses exist in systems of financial control or accounting (as distinct from performance audit aspects). This may occur not only where weaknesses affect the audited entity's own procedures but also where they relate to its control over the activities of others. The auditor should also report on significant irregularities, whether perceived or potential, on inconsistency of application of regulations or on fraud and corrupt practices.

- 4.1.26 In reporting on irregularities or instances of non-compliance with laws or regulations, the auditors should be careful to place their findings in the proper perspective. The extent of non-compliance can be related to the number of cases examined or quantified monetarily.
- 4.1.27 Reports on irregularities may be prepared irrespective of a qualification of the auditor's opinion. By their nature they tend to contain significant criticisms, but in order to be constructive they should also address future remedial action by incorporating statements by the audited entity or by the auditor, including conclusions or recommendations.
- 4.1.28 In contrast to regularity audit, which is subject to fairly specific requirements and expectations, performance audit is wide-ranging in nature and is more open to judgement and interpretation; coverage is also more selective and may be carried out over a cycle of several years, rather than in one financial period; and it does not normally relate to particular financial or other statements. As a consequence performance audit reports are varied and contain more discussion and reasoned argument.
- 4.1.29 The performance audit report should state clearly the objectives and scope of the audit. Reports may include criticism (for example where, in the public interest or on grounds of public accountability, matters of serious waste, extravagance or inefficiency are drawn to attention) or may make no significant criticism but give independent information, advice or assurance as to whether and to what extent economy, efficiency and effectiveness are being or have been achieved.
- 4.1.30 The auditor is not normally expected to provide an overall opinion on the achievement of economy, efficiency and effectiveness by an audited entity in the same way as the opinion on financial statements. Where the nature of the

audit allows this to be done in relation to specific areas of an entity's activities, the auditor should provide a report which describes the circumstances and arrives at a specific conclusion rather than a standardised statement. Where the audit is confined to consideration of whether sufficient controls exist to secure economy, efficiency or effectiveness, the auditor may provide a more general opinion.

- 4.1.31 Auditors should recognise that their judgements are being applied to actions resulting from past management decisions. Care should therefore be exercised in making such judgements, and the report should indicate the nature and extent of information reasonably available (or which ought to have been available) to the audited entity at the time the decisions were taken. By stating clearly the scope, objectives and findings of the audit, the report demonstrates to the reader that the auditor is being fair. Fairness also implies the presentation of weaknesses or critical findings in such a way as to encourage correction, and to improve systems and guidance within the audited entity. Accordingly the facts are generally agreed with the audited entity in order to ensure that they are complete, accurate and fairly presented in the audit report. There may also be a need to include the audited entity's responses to the matters raised, either verbatim or in summary, especially where the SAI presents its own views or recommendations.
- 4.1.32 Performance reports should not concentrate solely on criticism of the past but should be constructive. The auditor's conclusions and recommendations are an important aspect of the audit and, where appropriate, are written as a guide for action. Generally these recommendations suggest what improvements are needed rather than how to achieve them, though circumstances sometimes arise which warrant a specific recommendation, for example to correct a defect

in the law in order to bring about an administrative improvement.

- 4.1.33 While formulating and following up recommendations, the auditor should maintain objectivity and independence and thus focus on whether identified weaknesses are corrected rather than on whether specific recommendations are adopted.
- 4.1.34 In formulating the audit opinion or report, the auditor should have regard to the materiality of the matter in the context of the financial statements (regularity (financial) audit) or the nature of the audited entity or activity (performance audit).
- 4.1.35 For regularity (financial) audits, if the auditor concludes that, judged against the criteria most appropriate in the circumstances, the matter does not materially affect the view given by the financial statements, the opinion should not be qualified. Where the auditor decides that a matter is material the opinion should be qualified, having determined the type of qualification (paragraphs 174 – 177).
- 4.1.36 In the case of performance audits that judgment will be more subjective as the report does not relate so directly to financial or other statements. Consequently the auditor may find that materiality by nature or by context is a more important consideration than materiality by amount.

Glossary of Terms

Accounting System

A series of tasks and records of an entity by which transactions are processed as a means of maintaining financial records. Such a system should identify, assemble, analyze, calculate, classify, record, summarize and report transactions.

Audit Mandate

The auditing responsibilities, powers, discretions and duties conferred on the Royal Audit Authority under the constitution or other lawful authority.

Audited Entity

The organisation, program, activity or function subject to audit by the Royal Audit Authority.

Audit Objective

A precise statement of what the audit intends to accomplish and/or the question the audit will answer. This may include financial, regularity or performance issues.

Audit Procedures

Tests, instructions and details included in the audit program to be carried out systematically and reasonably.

Audit Scope

The framework or limits and subjects of the audit

Auditing Standard

Auditing Standards provide minimum guidance for the auditor that helps determine the extent of the audit steps and procedures that should be applied to fulfill the audit objective. They are the criteria against which the quality of the audit results is evaluated. Auditing Standards can be complemented by more detailed Auditing Manuals.

Audit Risk

“Audit Risk” is the probability that the auditor unknowingly expresses an inappropriate audit opinion on financial statements and general financial management.

Audit Programme

The audit programme is a detailed description of the procedures that are to be followed in the implementation and execution of the audit plan. It serves as a set of instructions to the auditor, and as a measure to control and record the efficient and effective execution of the audit works.

Audit Report

The auditor’s written opinion and other remarks on a set of financial statements or any other information as the result of a Financial Audit, IT Audit or Investigative Audit, or the auditor’s findings on completion of a Performance Audit.

Audit Opinion

The auditor’s written conclusion on a set of financial statements as a result of a financial or regularity audit.

Audit Evidence

Information that forms the foundation which supports the auditor’s or RAA’s opinions, conclusions or reports. The audit evidence should be competent, relevant and reasonable.

Competent: information that is quantitatively sufficient and appropriate to achieve the auditing results; and is qualitatively impartial such as to inspire confidence and reliability.

Relevant: information that is pertinent to the audit objectives.

Reasonable: information that is economical in that the cost of gathering it is commensurate with the result which the auditor or the SAI is trying to achieve.

General Auditing Standards

Describe the qualifications and competence, the necessary independence and objectivity, and the exercise of due care, which shall be required of the auditor to carry out the tasks related to the field and reporting standards in a competent, efficient and effective manner.

Control Risk

The risk that internal controls within the audited entity will fail to prevent or detect material irregularities and errors.

Detection Risk

The risk that any material irregularities or errors that have not been discovered and corrected by the entity's internal controls will not be detected by the auditor.

Documentation

All working papers and all other source material collected and retained during the audit.

Due Care

The appropriate element of care and skill which a trained auditor would be expected to apply having regard to the complexity of the audit task, including careful attention to planning, gathering of evidence, and forming opinions, conclusions and making recommendations.

Economy

Minimising the cost of resources used for an activity, having regard to the appropriate quality

Effectiveness

The extent to which objectives are achieved and the relationship between the intended impact and the actual impact of an activity

Efficiency

The relationship between the output, in terms of goods, services or other results, and the resources used to produce them.

Error

An unintentional mistake in the accounting records and financial statements

Expert

A person or organization that is in possession of specific skills, knowledge and expertise that is used by the RAA to perform a particular task

Executive

The branch of government which administers the law

Field Standards

The framework for the auditor to systematically fulfill the audit objective, including planning and supervision of the audit, gathering of competent, relevant and reasonable evidence, and an appropriate study and evaluation of internal controls.

Financial Audit

Examination and evaluation of financial and other records in order to secure competent, relevant and reasonable audit evidence and compliance with applicable laws and regulations to enable expression of opinions on financial statements. It is sometimes referred to as “Regularity Audit”.

Findings, Conclusions and Recommendations

Findings are the specific evidence gathered by the auditor to satisfy the audit objectives; conclusions are statements deduced by the auditor from those findings; recommendations are courses of action suggested by the auditor relating to the audit objectives.

Financial Systems

The procedures for preparing, recording and reporting reliable information concerning financial transactions

Fraud

Fraud is a deliberate misrepresentation which causes another person or entity to suffer damages, usually monetary losses.

Independence

The freedom of the Royal Audit Authority in auditing matters to act in accordance with its audit mandate without external direction or interference of any kind

Inherent Risk

The risk of material irregularities and errors occurring due to the nature of the entity, its activities and the environment in which it operates

Internal Audit

The functional means by which the managers of an entity receive an assurance from internal sources that the processes for which they are accountable are operating in a manner which will minimise the probability of the occurrence of fraud, error or inefficient and uneconomic practices. It has many of the characteristics of external audit but may properly carry out the directions of the level of management to which it reports.

Internal Control System

The whole system of financial and other controls, including the organisational structure, methods, procedures and internal audit, established by management within its corporate goals, to assist in conducting the business of the audited entity in a regular economic, efficient and effective manner; ensuring adherence to management policies; safeguarding assets and resources; securing the accuracy and completeness of accounting records; and producing timely and reliable financial and management information.

INTOSAI

The International Organization of Supreme Audit Institutions (INTOSAI) is an international and independent body which aims at promoting the exchange of ideas and experience between Supreme Audit Institutions in the sphere of public financial control.

Legislature

The law making authority of a country, for example a Parliament

Irregularity

Intentional acts by one or more persons that are in breach of relevant legislation and regulations. It covers both fraud and corruption.

Knowledge of the Entity

The auditor's knowledge of the environment within which the entity operates and a more particular knowledge of how the entity operates.

Materiality and Significance

In general terms, a matter may be judged material if knowledge of it would be likely to influence the user of the financial statements or the performance audit report. Materiality is often considered in terms of value but the inherent nature or characteristics of an item or group of items may also render a matter material--for example, where the law or some other regulation requires it to be disclosed separately regardless of the amount involved. In addition to materiality by value and by nature, a matter may be material because of the context in which it occurs. For example, considering an item in relation to the overall view given by the accounts; the total of which it forms a part; associated terms; the corresponding amount in previous years. Audit evidence plays an important part in the auditor's decision concerning the selection of issues and areas for audit and the nature, timing and extent of audit tests and procedures.

Methodology

Approaches, techniques and tools that are used to plan and perform the audit

Performance Auditing

Performance Auditing is concerned with the audit of economy, efficiency and effectiveness, and embraces:

- a) Audit of the economy of administrative activities in accordance with sound administrative principles and practices, and management policies
- b) Audit of the efficiency of utilization of human, financial and other resources, including examinations of information systems, performance measures and monitoring arrangements, and procedures followed by audited entities for remedying identified weaknesses; and
- c) Audit of the effectiveness of performance in relation to the achievement of the audited entity, and audit of the actual impact of activities compared with the planned impact.

Planning

Defining the objectives, setting policies and determining the nature, scope, extent and timing of the procedures and tests needed to achieve the objectives.

Postulates

Basic assumptions, consistent premises, logical principles and requirements which represent the general framework for developing auditing standards

Public Accountability

The obligations of persons or entities, including public enterprises and corporations, entrusted with public resources to be answerable for the fiscal, managerial and program responsibilities that have been conferred on them, and to report to those that have conferred these responsibilities on them

Quality Assurance

The various procedures for supervision and review that are put in place to ensure the quality of the audit

Regularity Audit

Attestation of financial accountability of accountable entities, involving examination and evaluation of financial records and expression of opinions on financial statements; attestation of financial accountability of the government administration as a whole; audit of financial systems and transactions, including an evaluation of compliance with applicable statutes and regulations; audit of internal control and internal audit functions; audit of the probity and propriety of administrative decisions taken within the audited entity; and reporting of any other matters arising from or relating to the audit that the RAA considers should be disclosed.

Reporting Standards

The framework for the auditor to report the results of the audit, including guidance on the form and content of the auditor's report

Review

Quality controls carried out after working papers etc. have been prepared, to ensure that the documentation collected supports the conclusions and recommendations.

Sampling

Sampling involves the application of audit procedures to less than 100% of items within an account such that all sampling units have a chance of selection.

Substantive testing

Substantive testing (or substantive procedures) are tests performed to obtain audit evidence to detect material misstatements in a set of financial statements or other information. There are two types of substantive testing:

- a) Test of details of transactions
- b) Analytical procedures

Supervision

An essential requirement in auditing which entails proper leadership, direction and control at all stages to ensure a competent, effective link between the activities, procedures and tests that are carried out and the aims to be achieved

Supreme Audit Institution (SAI)

The public body of a State which, however designated, constituted or organised, exercises by virtue of law the highest public auditing function of that State. The Royal Audit Authority is the Supreme Audit Institution of Bhutan.

Tests of Control

Tests of control are performed to obtain audit evidence about the effectiveness of the:

- a) Design of the accounting and internal control systems, that is, whether they are suitably designed to prevent and correct material errors and irregularities; and
- b) Operations of the internal controls throughout the period

Working papers

Documentation of the planning of the audit work, the performance of audit procedures (execution), and the conclusions drawn on the basis of the audit evidence.