

## Chapter 3 The correspondence and permanent files

### 3.1 The correspondence file

A useful part of the planning process is the review of the correspondence file. This serves to remind the auditor of issues which have arisen during the course of the year that could have an impact on the audit. It can also provide useful information that the partner may have forgotten to pass on to the audit staff!

The auditor should carefully review the correspondence within the file, making a more detailed note on any issue that would have a significant bearing on the audit approach. Many firms summarise every piece of client correspondence, when much of it comprises routine covering letters and has little or no impact on the audit. The auditor is looking for matters which significantly affect the audit – for example:

- correspondence confirming the amount of corporation tax payments on account during the year should help the auditor to check the accuracy of the corporation tax control account entries;
- discussions with the client prior to year end regarding bonuses might influence the auditor's expectations of wages and salaries expense and accruals when undertaking preliminary analytical procedures; and
- indications that the owners are considering selling the business would affect the audit risk assessment.

In firms where separate correspondence files are maintained in each department, it is important that the auditor reviews them all.

### 3.2 The permanent file

A permanent audit file is essential, but it is even more important that it is kept up to date and maintained as a workable file. This is especially true under ISAs, as a lot of the background information which drives the planning and risk assessment is maintained here.

Many firms do not allow sufficient, or indeed any, time in the budget for updating the permanent audit file, which often then becomes merely a receptacle for old, out-of-date documents and information that staff are unsure where to file. Furthermore, people often do not spend adequate time updating the permanent file on the grounds that they have been dealing with the client for a number of years and therefore know all there is to know. A problem may then arise when, for some reason, a key partner or member of staff is no longer involved in the assignment. This can result in difficulties for the person taking over the assignment, particularly if that person no longer has access to the original partner or staff member involved.

The contents of the file should be reviewed at the start of each assignment, and any necessary amendments made. The permanent file should be organised into sections, including the following:

- client-specific background information and knowledge;
- industry or sector information;
- a register of significant laws and regulations;
- details of all related parties;
- review of accounting policies;
- accounting systems and controls;
- statutory information;

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- taxation;
- assets;
- contracts, leases and agreements;
- information of continuing interest; and
- the accounts for previous years.

Each of these areas is considered separately below, with examples given of the sorts of information that may be relevant and the possible risks arising from dealing with such information.

Whether gathering, preparing, updating or reviewing information for the permanent file, it is important to remember that the main objective of audit planning is to identify any risks that could have a material impact on the financial statements. In order to identify such risks, the auditor needs to understand the entity being audited and its environment. The information recorded on the permanent file should therefore be focused on this objective, and highlight any associated risks.

## 3.3 Client-specific background information and knowledge

As a starting point, the standing data that a practice has on its database should be incorporated within this section. This should include details of the client's name, VAT registration number, etc., together with details of the client's key members of staff and other professional advisers. In addition, in order to comply with the money-laundering regulations the file should record the steps taken by the practice to confirm that the client is a bona fide business operation.

In order to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements, and to identify potential risk areas, ISA 315 *Identifying and assessing the risks of material misstatement through understanding the entity and its environment* also specifically requires the auditor to have knowledge of the following aspects of the client's business.

### • Operations

This might include information about customers, suppliers and any other relevant information. For example, an entity that is largely dependent on one main customer or supplier may be at risk if that entity moves its business elsewhere or ceases trading.

### • Ownership and governance

An understanding of the ownership and relations between owners and other people or entities is also important in determining whether related party transactions have been identified and accounted for appropriately. See section 3.6 for further details.

### • Investments

Some clients – typically, charities – are dependent on investments to provide an income stream. A stock market downturn can put the going concern of such entities at risk. There may be a significant risk of accounting errors arising where entities are investing in complex financial instruments which need to be valued.

### • Group structure

A client may have a complex structure with subsidiaries, etc., in multiple locations. In addition to consolidation difficulties, other issues may arise, such as whether investments are joint ventures, subsidiaries, or associates.

### • Financing arrangements

The financial statements of highly geared entities may, for example, be at risk of manipulation in order to meet banking covenants, or be at risk of continuing as a going concern if interest rates rise substantially or credit is withdrawn.

## 3.3.1 Entities which do business electronically

Increasing numbers of entities are undertaking elements of their operations electronically. This might include such things as purchases and sales made via websites, online or internet banking, etc. It is important that the auditor obtains an understanding of such activities sufficient to identify any potential risks arising from those activities. This may involve consideration of the client's use of service organisations (see section 10.4.2) and looking at the IT aspects of the client's systems in more depth (see Chapter 4).

## 3.3.2 Objectives, strategies and related business risks

ISA 315 goes on to require that the auditor obtains an understanding of the client's objectives and strategies, and the related business risks that may result in material misstatement of the financial statements. Business risks result from significant conditions, events, circumstances, actions or inactions that could adversely affect the entity's ability to achieve its objectives and execute its strategies, or through the setting of inappropriate objectives and strategies.

This is an area that many auditors struggle with. Some clients, especially smaller ones, may not have a formal business plan or written plans and objectives for the business, which absence often results in the auditor not considering this issue. However, the absence of any sort of strategy or plan for the business may in itself be a risk, particularly in certain industries which, for example, depend heavily on fashions, trends or the latest technology, or are highly competitive. Such issues can have a significant impact on the going concern of an entity if not adequately addressed by the directors.

As well as affecting going concern directly, the objectives and strategies of the client can lead to other risk factors. For example, consider a manufacturing client moving production abroad to save costs. This might give rise to following situations.

- There will be a foreign exchange risk when the overseas costs are converted back into Sterling.
- Inadequate local knowledge of the country in question may result in an increased risk of falling foul of local laws and regulations, giving rise to fines and penalties, etc.
- New staff with no experience of the company or particular product(s) may result in production problems and give rise to quality control issues, with adverse knock-on effects on the company's reputation and customer goodwill.
- Overseas tax may need to be considered, possibly including transfer-pricing regulations.

This area is one of the most important to consider when planning an audit, due to the wide-ranging impact that strategic decisions can have on a business. It is vital that such issues are discussed with the directors, especially where there is no formal business plan.

## 3.3.3 Measurement and review of the entity's financial performance

The ISA also requires the auditor to understand the measurement and review of the entity's financial performance. This is not the equivalent of simply printing out some figures and ratios and putting them on the permanent file! It requires the auditor to consider what specific performance measures are important to the entity, and whether any risks arise from these measures – risks such as those exemplified below.

- In a business where turnover growth is the most important factor, sales staff may be pressurised into doing business with uncreditworthy customers, or even to generate fictitious sales, especially if their remuneration is based – at least in part – on reaching sales targets.
- Key measures for many charities include the amount of administrative expenses and/or fundraising costs compared to the income generated, as funding bodies often look at these ratios when making decisions about funding. This might result in pressure to manipulate income recognition or to not account for all expense invoices.

### 3.4 Industry or sector information

This should give some background detail on the type of trade, major products of the client, technological developments and competition in the market. In addition to the above the auditor might want to include details of any other factors that could affect the business. Where clients have some form of brochure, it is useful to place a copy on file and to highlight the important areas. But simply placing a copy of the brochure on file and doing nothing with it is not sufficient!

Where the business does not have a brochure, auditors should seek, through enquiry and their own knowledge of the business, to make some useful comments on the file on the nature of the trade and industry sector. The internet is always a good place to start, as a wealth of information can be found here. Trade magazines and publications are also a good source of knowledge.

This type of information is useful in identifying external risks affecting the client, and often these will impact in some way on going concern risk. For example, clients in industries where technology advances rapidly must run effective research and development programmes to avoid being 'left behind' by their competitors.

### 3.5 Register of significant laws and regulations

The permanent file should include details of significant laws and regulations applicable to the client. ISA 250 Section A - *Consideration of laws and regulations in an audit of financial statements* requires the auditor to obtain a general understanding of the legal and regulatory framework applicable to the client and its industry sector, and how the entity is complying with that framework, including the procedures followed by the client to ensure compliance.

Again, the objective here is to identify those laws or regulations that may give rise to business risks that have a fundamental effect on the client's operations, and to consider their impact. For example, non-compliance with certain laws and regulations may cause the client to cease operations or call into question the client's continuance as a going concern.

Laws and regulations can be divided into:

- laws and regulations governing accounts;
- general business laws and regulations; and
- other specific laws and regulations.

#### 3.5.1 Laws and regulations governing accounts

Relevant laws may include such things as the Companies Act or Charities Act, while relevant regulations would include the choice of GAAP used (for example, the FRSSSE, full UK GAAP or IFRS). Paragraph 8a of ISA 540 *Auditing accounting estimates, including fair value accounting estimates, and related disclosures* specifically requires the auditor to understand how the applicable financial reporting framework relates to accounting estimates, including related disclosures in the financial statements. All members of the audit team should ensure that they are familiar with the relevant requirements.

#### 3.5.2 General business laws and regulations

This might include things such as health and safety, employment legislation and planning regulations. The extent to which these may present significant risks may depend on the type of sector the client is in, as instanced below.

- Health and safety might be a minor issue in an office, but a significant risk in a factory where heavy machinery is operated or toxic chemicals are used. A serious breach of health and safety legislation can lead to large fines for the entity, possible legal action and a loss of reputation.

- Employment legislation has become increasingly complex in recent years, and a failure to comply can have a significant effect on entities of all sizes – for example, unfair dismissal claims in employment tribunals. Certain industry sectors are also more at risk from the working time or minimum wage regulations, where non-compliance can result in heavy fines.
- Obtaining planning permission is a critical issue for many businesses such as housebuilders, supermarkets, etc.

#### 3.5.3 Other specific laws and regulations

The auditor should also ascertain details of specific laws and regulations which could have an impact on the business, for example:

- Financial Services and Markets Act for financial services business;
- food hygiene regulations and licensing laws for restaurants and pubs; and
- child protection legislation for schools, charities, etc.

It is not sufficient to just list the relevant acts or regulations. The auditor should then consider whether, as a result of non-compliance with any laws or regulations, there are any potential contingent liabilities (for example, warranty claims, legal action, fines or penalties, etc) or any issues that would have a material impact on the financial statements, in particular the client's ability to continue as a going concern – for example, bad publicity leading to a critical loss of customer and/or supplier goodwill.

Many small entities are only governed by general business regulations, which would not have a significant impact on their ability to continue as a going concern, nor would they result in material contingent liabilities should they not comply. However, a significant minority of such entities will be governed by additional laws and regulations, which could have a significant impact on the entity's operations. Where this is the case, it is essential that the auditor has an understanding of such laws and regulations. The auditor does not need to become a legal expert, but some understanding is necessary to ascertain the nature of the relevant laws and regulations and to determine, through investigation and discussion with the client, the types of situation that could result in significant risks.

When seeking to determine whether there are any specific laws and regulations which could have a significant impact on the client, the auditor should consider the following questions:

- Does the entity make payments or returns to a separate licensing agency?
- Is the entity subject to regular or potential reviews of its operations by an external agency?
- Does the entity deal with hazardous material or machinery?

An affirmative answer to one or more of the questions above is an indicator that there could be laws or regulations that could have a significant impact on the client if they are not complied with.

### 3.6 Register of related parties

The permanent file should contain details of all known related parties, plus details of any regular or past transactions with them. In fact, documentation of all related parties and their relationships with the client is now a formal requirement of paragraph 28 of ISA 550 *Related parties*. The ISA acknowledges that due to their nature, related parties and transactions may not always be easy to identify, and lists the following documents or records that could be inspected to search for information about related parties and transactions therewith:

- a) third party confirmations (in addition to bank and legal confirmations);
- b) tax returns;
- c) information supplied by the client to regulatory authorities;
- d) shareholder records (to determine the names of principal shareholders);

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- e) statements of conflict of interest of directors;
- f) records of investments and those of the client's pension schemes.
- g) directors' contracts and/or agreements;
- h) specific invoices and correspondence from the client's professional advisors;
- i) life assurance policies acquired by the client;
- j) significant contracts renegotiated during the period under audit; and
- k) internal auditors' reports.

The clarified ISA 550 also contains a number of mandatory procedures for assessing risk in relation to related party transactions at the planning stage, namely:

- l) discussion of the risk of material misstatement arising from related party transactions at the audit team planning meeting (see section 7.3);
- m) asking management about the existence and identification of related parties, their relationships to the client and the nature and purpose of any transactions therewith; and
- n) obtaining details of the controls (if any) operating over related party transactions, including those over the identification of related parties and authorising of related party transactions.

Care needs to be taken when making inquiries of management and/or those charged with governance, particularly with small clients, as the directors may not have a thorough understanding of who or what is included within the definition of a related party. Auditors therefore need to be specific about what needs to be disclosed so that the directors can provide complete answers to the auditor's inquiries.

The disclosure of related party transactions is important, and the risk of incomplete disclosure may be high for certain clients. However, the register of related parties is often incomplete or out of date. It is important that the register is kept relevant and up to date, and that the risk of undisclosed related party transactions existing is carefully considered.

#### 3.6.1 Pension schemes

Pension schemes are worthy of a specific mention at this stage, for two reasons. Firstly, it is often the case with entities that have schemes such as Small Self Administered Schemes ('SSASs'), that there will also be loans and other transactions between the entity and the scheme which will need disclosure in the financial statements.

Secondly, entities with defined benefit pension schemes will fall under the accounting requirements of FRS 17 (there are similar rules in the FRSSSE for small entities). Obtaining the figures for the accounts will generally require the input of an actuary, and the process will necessitate careful planning and organisation by both the entity's management and the auditor, and should therefore be considered at as early a stage as possible. The reliance on the work of the actuary as an expert will need to be considered (see section 10.4.5).

The auditor should obtain a copy of the scheme's trust deed and rules, to identify obligations to pay retirement benefits. However, there might also be benefits payable that are not recorded in the rules. For example, there might be:

- legal obligations to pay retirement benefits, which arise from informal agreements rather than from a formal contract;
- constructive obligations (for example, where pension benefits are regularly enhanced beyond the minimum required by statute); or
- statutory requirements that override the original provisions of a scheme.

A thorough understanding of the scheme is therefore needed to be able to identify any such risk factors.

### 3.7 Significant accounting estimates

The auditing of significant accounting estimates is one area which has changed substantially on the changeover to clarified ISAs. This is now covered by ISA 540 *Auditing accounting estimates, including fair value accounting estimates, and related disclosures*. At the outset of the audit, the auditor needs to have a good understanding of how management identifies areas where accounting estimates may be needed. In order to do this, the auditor should make inquiries of management, which should specifically include any changes in circumstances that may give rise to new, or the need to revise existing, accounting estimates.

The auditor should also understand how estimates are determined by management, as well as an understanding of the data on which they are based. This includes:

- The method, including where applicable the model, used in making the accounting estimate. Models are more likely to arise in relation to fair value estimates, but may also be found in other accounting estimates such as calculation-driven provisions.
- Relevant controls. In many cases, especially with smaller clients, it is likely that there will be few or no controls in relation to many accounting estimates.
- Whether management has used an expert (see section 10.4.6). This is common in connection with the valuation of tangible fixed assets (especially property) and FRS 17 figures for defined benefit pension schemes.
- The assumptions underlying the accounting estimates.
- Whether there has been or ought to have been a change from the prior period in the methods for making the accounting estimates, and if so, why.
- Whether and, if so, how management has assessed the effect of estimation uncertainty (see section 6.5.8).

An additional and new mandatory audit procedure is the requirement for the auditor to review the outcome of accounting estimates included in last year's financial statements, or, where applicable, their subsequent re-estimation for the purpose of the current period (for example, if a litigation provision is still needed in the following year's accounts as the case has still not been resolved).

The point of this exercise is to help identify and assess the risk of material misstatement of accounting estimates in the year under audit. For example, if it was noticed that the actual bad debt expense in the year in relation to the previous year's debts was materially higher than the brought forward bad debt provision, the auditor might conclude there to be a risk of material understatement of the bad debt provision in the current year. However, the review is not intended to call into question the judgments made in prior periods that were based on information available at the time.

An accounting estimate that may be material on many audits is depreciation. However, care needs to be taken when undertaking this review in relation to depreciation. The purpose of depreciation is to spread the cost of a fixed asset across its useful economic life, not to maintain the asset's net book value close to net realisable value. Thus, looking at profits or losses on sale of assets may not be a very good indicator. A better approach might be to look at the disposal proceeds for fully depreciated assets in the year. This may indicate whether useful economic lives and/or residual values are inappropriate.

### 3.8 Review of accounting policies

Again, the aim here is to identify risks that arise from the accounting policies applied by the client. This involves more than simply photocopying the accounting policies note from the financial statements and placing it on the permanent file. ISA 315 notes that the review needs to consider the client's accounting policies for appropriateness and consistency with:

- its business;
- the applicable financial reporting framework (for example, the FRSSSE, UK GAAP or IFRS); and

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- the client's industry. Certain industries have industry-specific policies which, generally, should be followed unless there is a good reason not to do so. One way to check this is to compare the client's accounting policies with those of a competitor or other entity in the same industry sector. These can be obtained either from Companies House or, in the case of a listed company, for free from its website.

The ISA requirement also encompasses the methods the client uses to account for significant and unusual transactions and the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Consideration should also be given to any new Accounting Standards which are relevant to the client, and consider when and how the client will adopt such requirements. Where the client has changed its selection of, or method of applying, a significant accounting policy, the auditor should consider the reasons for the change and whether it is appropriate and consistent with the applicable financial reporting framework.

Examples of potential risks arising from accounting policies include:

- Those arising from whether research and development costs should be capitalised or expenses, and if the former, from what point and over what period should they be amortised?
- Non-depreciation of buildings on the grounds that the depreciation charge and accumulated depreciation are immaterial. This is in accordance with FRS15, but many clients forget to consider the accumulated depreciation, and this can become material over time.

#### 3.8.1 Revenue recognition

ISA 240 notes that material misstatements due to fraudulent financial reporting often result from an overstatement of revenue (for example, premature revenue recognition or recording fictitious revenues) or from an understatement of revenue (for example, improperly shifting revenues to a later period). Therefore, the auditor ordinarily presumes that there are risks of fraud in revenue recognition and considers which types of revenue, revenue transactions or assertions may give rise to such risks. If the auditor has not identified, in a particular circumstance, revenue recognition as a risk of material misstatement due to fraud, the reasons for arriving at this conclusion should be documented.

### 3.9 Accounting systems and controls

The permanent file should contain a record of the client systems and controls, including the key business processes. This is considered in more detail in Chapter 4.

Irrespective of whether or not the auditor wishes to try to place reliance on the client's systems and controls, these must be documented in accordance with the requirements of ISA 315, and the design and implementation of controls must be checked. Further guidance on this can be found in Chapter 4. The adequacy of the books and records should also be assessed as the basis for preparing the accounts and, where appropriate, their compliance with the requirements of the Companies Act for maintaining adequate accounting records.

#### 3.10 Statutory information

The permanent file should contain some basic statutory information about the client. This should include such things as a list of shareholders, details of any current mortgages and charges, directors' interests in the shares and debentures, as well as a copy of the latest annual return and any elective resolutions. A copy of the memorandum and articles of association or other governing document, such as a trust deed, should also be placed on the file. The auditor should highlight any issues relating to these items that are of particular interest, particularly if they are different to the norm (that is, standard Table A provisions) – for example, restricted borrowing powers or the treatment of gains and losses on the disposal of investment properties.

The permanent file should be a workable file containing information relevant to the audit. It should not be treated as an archive. It is very common for audit practices to incorporate too much information in this

section. For example, it is not unusual to see three or four years' worth of annual returns on the file. The more superfluous information that is kept on the file, the less likely it is that the file will be used properly. Information that is not of immediate relevance to the audit should be placed on a separate file or archived.

The permanent file should also contain a copy of the most recent letter of engagement. Whilst some firms do not issue engagement letters for other services, they are mandatory for audit engagements under paragraph 10 of ISA 210 *Agreeing the terms of audit engagements*. The letter should be reviewed annually, not only to ensure that it is the most up-to-date version from a technical viewpoint, but also that it reflects all of the work to be undertaken for the client. The letter of engagement is a contract between the auditor and client, and if it does not reflect the actual work being undertaken, it will not be valid in the event of any dispute. Products such as the *Engagement Letters Toolkit*, also published by Wolters Kluwer, ensure that the auditor always has the latest wording.

It is essential that the terms of engagement are reviewed at the beginning of the assignment, as well as at the end. If they are reviewed on starting the audit, then at least there is an opportunity to issue an updated letter to the client and to ensure that this is signed and returned before the audit is completed.

All firms should ensure that a copy of the letter of engagement is actually retained. Many firms do not have a system for following up letters once they have been despatched to the client. In addition, they often print only two copies, both of which are sent to the client, one for the client to keep and one to return. With the frequent changes that occur to engagement letters, it is essential that the auditor maintains a record of what has been sent to the client.

### 3.11 Taxation

Most firms keep separate tax files so only information of direct relevance to the audit (such as copies of any PAYE dispensations) should be on the permanent file.

#### 3.12 Assets

Details of any major assets, properties, etc. should be maintained on the permanent file. Where the practice maintains the client's fixed asset register, a copy is usually kept on the permanent file. However, the filing of numerous copies or scanned images of purchase invoices should be avoided.

### 3.13 Contracts, leases and agreements

There should be a section in the permanent file containing copies of any contracts, leases and agreements that could have an impact on the audit. This may include details of bank overdrafts and loan facilities, securities, covenants, finance and operating leases, etc. It is not sufficient to simply place copies of the contracts or agreements on file. The auditor should review each document and note or highlight any key points that could be of relevance to the audit – for example:

- the banking facility letter may contain details of banking covenants, which if broken may result in withdrawal of funding, giving rise to a going-concern risk;
- covenants and guarantees may need to be disclosed in the financial statements; and
- lease agreements should contain details of the amounts to be paid and the period of the lease, including any break clauses, options to purchase, etc. These will materially affect the accounting for and disclosure of leases.

### 3.14 Information of continuing interest

Copies of selected correspondence and other information of continuing interest that the auditor may wish to refer to during the course of the audit should be placed on file. This will include, for example, copies of any letters of comment sent to the client and details of the client's responses. It is not necessary to copy or scan every audit-related letter sent to the client!

### 3.15 Previous years' accounts

The auditor may wish to maintain copies of the signed accounts within the permanent file. However, on the basis that most firms will incorporate a copy of the previous year's accounts on the current file, it is probably more appropriate to retain signed accounts on a separate dedicated file. Retaining these on the permanent file will very quickly make it an unwieldy tool. Obviously, it is important for the auditor to retain a signed copy of the accounts; the issue is simply where these should be kept.

### 3.16 Access to information by successor auditors

If the firm is undertaking the audit of a new client, one of the most time-consuming activities is the gathering of background information for the permanent file, as this usually has to be done from scratch.

Schedule 10 of the Companies Act 2006 permits a successor auditor access to relevant information held by the predecessor auditor. The Audit Regulations (regulation 3.09) have now been amended to give effect to this requirement. Therefore, whilst the requirement to provide information to a successor auditor originates in the Companies Act, it now applies to all audits carried out under the audit regulations, whether for companies or not, in respect of appointments for the audits of financial years starting on or after 6 April 2008. Auditors of new clients should therefore give due consideration to requesting access to the predecessor auditor's working papers.

Technical Release AAF 01/08 *Access to Information by Successor Auditors* repeats the requirements and gives further practical guidance to both successor and predecessor auditors. The main points to note are set out below.

- Information is for the purposes of the successor's audit and must not be disclosed to a third party, unless the successor is required to do so by a legal or professional obligation. The term 'third party' includes the client, although the successor may discuss the information with the client where to do so is a necessary part of the audit work. Because the auditor is complying with a mandatory requirement, providing access to relevant information will not breach professional confidentiality or data protection laws. However, because of the danger of tipping off, any money-laundering report and papers recording the predecessor's related consideration of apparently suspicious activities should not be provided by the predecessor to any person (including the successor) unless the predecessor has clear advice that to do so would be lawful.
- The new right does not alter the existing liability of each auditor in relation to its respective audit.
- The request can only be made after formal appointment of the successor auditor. The provision of information should be on a timely basis.
- The request must be in writing and should not include unnecessary information. It should be as specific as possible and should avoid, wherever possible, a request for 'all relevant information'. It does not matter whether those working papers are filed on the current audit file, a permanent file or a systems file.
- The predecessor should be prepared to assist the successor by providing oral or written explanations on a timely basis.
- The period for which information is requested would normally be the period in respect of the last audit report signed by the predecessor and would include any subsequent interim review. If the successor considers that it needs information relating to an earlier period, then the successor should be prepared to

list precisely what information is required and give reasons that demonstrate why such additional information is 'relevant' in accordance with the regulations.

- It would be usual for the basis on which the information is to be provided to be documented in writing by an exchange of letters between the two auditors, copied to the audited entity. Guidance on suitable wording, including example letters, is provided in the Technical Release.

#### 3.16.1 Practicalities of access

Where working papers are held electronically, the predecessor will need to consider how to provide access to the relevant audit documentation without putting at risk the confidentiality of the firm's audit methodologies or confidential information of other clients.

It is reasonable for the successor to make notes of the review but there is no obligation to allow copying of audit working papers. The Technical Release states that it would be reasonable to allow, as a minimum, the copying of extracts of the books and records of the client. It would also be reasonable and helpful to allow copying of papers such as breakdown of analyses of financial statement figures and documentation of the client's systems and processes.

If the successor does ask to copy documents, it would be sensible to check them and to keep a record of which items were copied.

The Technical Release also suggests that it would be reasonable for the predecessor auditor to seek to recover costs, but without any element of profit. However, there is no obligation on the successor to make any payment and therefore the predecessor may wish to look to the client for recovery of costs.

### 3.17 Conclusion

A properly maintained permanent file is essential in performing an effective audit under ISAs, and it is important that it is treated as such. Some audit systems use checklists to help the auditor consider relevant issues. An example of such a checklist is shown below.