Chapter 7

Question Bank

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Q1.	Which of the following factors is (are) considered in determining the sample size for tests of control? (a) Projected error (b) Tolerable error (c) Expected error (d) Both (b) and (c) **(Sample MCQs)**
	Correct answer: (d) Both (b) and (c) **Comments and feedback:** ● Direct and easy question
Q2.	Tolerable error, is the maximum monetary error that the auditor is prepared to accept in the population and still conclude that audit objective has been achieved, is directly related to (a) Sample size (b) Audit risk (c) Materiality (d) Expected error **(Sample MCQs)**
	Correct answer: (c) Materiality **Comments and feedback:** ● Direct and moderate question
Q3.	Which of the following is source of Non Sampling risk : (a) Human Mistakes (b) Applying audit procedures not appropriate to the objectives of audit (c) Misinterpreting the sample results (d) All of the above **(Sample MCQs)**
	Correct answer: (d) All of the above **Comments and feedback:** ● Direct and easy
Q4.	While auditing TEN Ltd., CA. Porky divided the whole population of trade receivables balances to be tested in a few separate groups called 'strata' and started taking a sample from each of them. He treated each

stratum as if it was a separate population. He divided the trade receivables balances of TEN Ltd. for the Financial Year 2017-18 into groups on the basis of personal judgment as follows:

S. No.	Particulars
1.	Balances in excess of Rs. 10,00,000;
2.	Balances in the range of Rs. 7,75,001 to Rs. 10,00,000;
3.	Balances in the range of Rs. 5,50,001 to Rs. 7,75,000;
4.	Balances in the range of Rs. 2,25,001 to Rs. 5,50,000;
5.	Balances Rs. 2,25,000 and below

From the abovementioned groups, CA. Porky picked up different percentage of items for examination from each of the groups, for example, from the top group i.e. balances in excess of Rs.10,00,000, he selected all the items to be examined; from the second group, he opted for 25 % of the items to be examined; from the lowest group, he selected 2% of the items for examination; and so on from rest of the groups. Which one of the following methods of sample selection is he following?

(a) Systematic sampling.

(b) Stratified sampling.

(c) Section sampling.

(d) Selection sampling.

(Sample MCQs)

Correct answer: (b) Stratified sampling.

Comments and feedback:
- Case study based and moderate question
- Stratified sampling involves dividing the whole population to be tested in a few separate groups called strata and taking a sample from each of them.

Q5.	Whatever may be the approach non-statistical or statistical sampling, the sample must be representative. Discuss explaining Statistical and Non Statistical sampling approaches.
	(RTP, May 2018, NA)

Audit sampling enables the auditor to obtain and evaluate audit evidence about some characteristic of the items selected in order to form or assist in forming a conclusion concerning the population from which the sample is drawn. Audit sampling can be applied using either non-statistical or statistical sampling approaches.

Statistical sampling: An approach to sampling that has the following characteristics:
- **Random selection of the sample** items; and
- The **use of probability theory to evaluate sample results,** including measurement of sampling risk.

This method is **more scientific** as it involves use of mathematical laws of probability. This method has **reasonably wide application** where a population to be tested consists of a **large number of similar items**

Non- Statistical sampling:
- A sampling approach that **does not have characteristics of random selection** and use of

probability theory is considered non-statistical sampling.
- Under this approach, the sample size and its composition are determined on the basis of the **personal experience and knowledge of the auditor.**
- This approach has been in common application for many years because of its simplicity in operation.

The decision whether to use a statistical or non-statistical sampling approach is a matter for the **auditor's judgment;** however, **sample size is not a valid criterion to distinguish between statistical and non-statistical approaches**. Sample must be representative.

Whatever may be the approach, **non-statistical or statistical sampling**, **the sample must be representative**. This means that it must be **closely similar** to the whole population although not necessarily exactly the same. The sample **must** be **large enough to provide statistically meaningful results.**

Comments and feedback:
- Direct and easy question
- Important keywords are highlighted in the above answer.

Q6. XYZ Ltd is engaged in trading of electronic goods and having huge accounts receivables. For analysing the whole accounts receivables, auditor wanted to use sampling technique. In considering the characteristics of the population from which the sample will be drawn, the auditor determines that stratification or value-weighted selection technique is appropriate. SA 530 provides guidance to the auditor on the use of stratification and value - weighted sampling techniques. Advise the auditor in accordance with SA 530

(RTP, May 2018, NA) (MTP2, May 2018, 5 Marks) (MTP1, Nov 2019, 4 Marks)

OR

In considering the characteristics of the population from which the sample will be drawn, the auditor may determine that stratification or value-weighted selection technique is appropriate. Guide the auditor on the use of stratification and value-weighted sampling techniques.

(RTP, Nov 2021, NA)

Stratification and Value-Weighted Selection:

As per SA 530 "Audit Sampling", the objective of the auditor when using audit sampling is to provide a reasonable basis for the auditor to draw conclusions about the population from which the sample is selected. In considering the characteristics of the population from which the sample will be drawn, the auditor may determine that stratification or value-weighted selection technique is appropriate.

Stratification:

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

Audit efficiency may be improved if the auditor stratifies a population by dividing it into **discrete sub-populations which have an identifying characteristic.** The objective of stratification is to **reduce the variability of items within each stratum** and therefore allow sample size to be reduced without increasing sampling risk.

When performing **tests of details**, the population is often **stratified by monetary value.** This allows greater audit effort to be directed to the larger value items, as these items may contain the greatest potential misstatement in terms of overstatement. Similarly, a population may be stratified according to a particular characteristic that indicates a higher risk of misstatement, **for example, when testing the allowance for doubtful accounts in the valuation of accounts receivable, balances may be stratified by age.**

Dividing a population into discrete sub population which have identifying characteristics is called as Stratification. Each **Sub population is called as Stratum** and **units under those sub population are referred to as Strata.**

The results of audit procedures applied to a sample of items within a stratum can only be projected to the items that make up that stratum. To draw a conclusion on the entire population, the auditor will need to consider the **risk of material misstatement** in relation to whatever other strata make up the entire population.

The results of samples from the units drawn under each sub population are projected to that **respective stratum.** In order to draw an opinion on the overall population, the auditor needs to combine the results of all the stratum to check for **possible deviation or risk of material misstatement.**

Projected misstatements of each stratum will be combined together to consider the possible effect of misstatement in the account balances and class of transactions.

For example, 20% of the items in a population may make up 90% of the value of an account balance. The auditor may decide to examine a sample of these items. The auditor evaluates the results of this sample and reaches a conclusion on the 90% of value separately from the remaining 10% (on which a further sample or other means of gathering audit evidence will be used, or which may be considered immaterial).

<u>**Value-Weighted Selection**</u>: When performing **tests of details** it may be efficient to identify the sampling unit as the **individual monetary units** that make up the population. Having selected specific monetary units from within the population, **for example, the accounts receivable balance, the auditor may then examine the particular items, for example, individual balances, that contain those monetary units.**

One benefit of this approach to defining the sampling unit is that audit effort is directed to the larger value items because they have a greater chance of selection, and can result in smaller sample sizes.

This approach may be used in **conjunction with the systematic method of sample selection** and is **most efficient when selecting items using random selection.**

In value weighted selection, the **sample size, its selection and evaluation will result in a conclusion in monetary amounts.**

Comments and feedback:
- Direct and moderate question
- Important keywords are highlighted in the above answer

Q7.	CORRECT/INCORRECT

CORRECT/INCORRECT

When statistical sampling is used to select a sample, sample need not be representative because the statistical sampling takes care of the representation.

(SA, May 2018, 2 Marks)

The statement is Incorrect.

Whatever may be the approach, **non-statistical or statistical sampling**, the sample **must be representative**. This means that it must be **closely similar** to the whole population although not necessarily exactly the same. The sample **must be large enough to provide statistically meaningful results.**

Comments and feedback:
- Direct and moderate question
- **Important keywords:** non-statistical or statistical sampling, must be representative, closely similar, must be large enough to provide statistically meaningful results.

Q8.	CORRECT/INCORRECT
	According to SA 530 "Audit sampling", 'audit sampling' refers to the application of audit procedures to 100% of items within a population of audit relevance.
	(MTP1, May 2018, 2 Marks) (MTP1, May 2019, 2 Marks)

The statement is Incorrect.

According to **SA 530 "Audit sampling",** 'audit sampling' refers to the application of audit procedures to **less than 100% of items within a population** of audit relevance such that **all sampling units have a chance of selection** in order to provide the auditor with a **reasonable basis** on which to **draw conclusions about the entire population.**

Comments and feedback:
- Direct and easy question
- **Important keywords:** SA 530 "Audit sampling, less than 100% of items within a population, all sampling units have a chance of selection, reasonable basis, draw conclusions about the entire population.

Q9.	The level of sampling risk that the auditor is willing to accept affects the sample size required. The lower the risk the auditor is willing to accept, the greater the sample size will need to be. Explain Stating the examples of factors that the auditor may consider when determining the sample size for tests of controls.
	(MTP1, May 2018, 5 Marks)
	OR
	The sample size can be determined by the application of a statistically-based formula or through the exercise of professional judgment. When circumstances are similar, the effect on sample size of factors will be similar regardless of whether a statistical or non-statistical approach is chosen. Explain Stating the examples of factors (any four) that the auditor may consider when determining the sample size for tests of controls.
	(MTP 2, Nov 2018, 5 Marks) (MTP1, May 2019, 4 Marks) (MTP1, May 2020, 3 Marks)

The level of sampling risk that the auditor is willing to accept affects the sample size required. The **lower the risk the auditor is willing to accept, the greater the sample size** will need to be.

The sample size can be determined by the application of a statistically-based formula or through the exercise of professional judgment. When circumstances are similar, the effect on sample size of factors will be similar regardless of whether a statistical or non-statistical approach is chosen.

Examples of Factors Influencing Sample Size for <u>Tests of Controls</u>: The following are factors that the auditor may consider when determining the sample size for tests of controls. These factors, which need to be considered together, assume the auditor does not modify the nature or timing of tests of controls or otherwise modify the approach to substantive procedures in response to assessed risks.

- When there is an **increase in the extent to which the auditor's risk assessment** takes into account relevant controls. The **more assurance** the auditor intends to obtain from the **operating effectiveness of controls**, the **lower the auditor's assessment of the risk of material misstatement will be, and the larger the sample size will need to be**. When the auditor's assessment of the risk of material misstatement at the assertion level includes an expectation of the operating effectiveness of controls, the auditor is required to perform tests of controls. Other things being equal, the **greater the reliance the auditor places on the operating effectiveness of controls** in the risk assessment, the greater is the extent of the auditor's tests of controls (and therefore, the sample size is increased). Thus, **sample size will increase.**
- If there is an **increase in the tolerable rate of deviation.** Then **sample size will decrease**, as lower the tolerable rate of deviation, larger the sample size needs to be.

- When there is an **increase in the expected rate of deviation** of the population to be tested then **sample size will increase**, as higher the expected rate of deviation, larger the sample size needs to be so that the auditor is in a position to make a reasonable estimate of the actual rate of deviation. Factors relevant to the auditor's consideration of the expected rate of deviation include the **auditor's understanding of the business** (in particular, **risk assessment procedures** undertaken to obtain an understanding of internal control), changes in personnel or in internal control, the results of audit procedures applied in prior periods and the results of other audit procedures. High expected control deviation rates ordinarily warrant little, if any, reduction of the assessed risk of material misstatement.
- An **increase in the auditor's desired level of assurance** that the **tolerable rate of deviation is not exceeded by the actual rate of deviation** in the population will increase the sample size. Thus, the **greater the level of assurance** that the auditor desires that the results of the sample are in fact indicative of the actual incidence of deviation in the population, the **larger the sample size** needs to be.
- In case of large populations, the actual size of the population has little, if any, effect on sample size. For small populations however, audit sampling may not be as efficient as alternative means of obtaining sufficient appropriate audit evidence. Therefore, there will be **negligible effect** on sample size due to **increase in the number of sampling units in the population.**

Comments and feedback:
- Direct and moderate question
- Important keywords are highlighted in the above answer
- For a student's understanding:
  - ➢ Factors Influencing Sample Size for **Tests of Details** : Auditor's desired level of assurance, Tolerable misstatement, Expected rate of misstatement, Stratification of the population, Sample units, Auditor's assessment of the risk of material misstatement, Other substantive procedures applied.
  - ➢ In case of any mistakes found during control testing (Test of controls), it is known as deviation. However, any mistakes found during detailed testing (Test of Details), it is known as a misstatement. The word "deviation" is used in case of Test of controls and the word "misstatements" is used in case of Test of Details.

Q10.	With the emergence of test check procedure, discipline of statistics has come quite close to auditing as the auditor is also expected to have the knowledge of statistical sampling so as to arrive at meaningful conclusions. Analyse **(MTP2, May 2018, 5 Marks)**
	Statistics and Auditing: With the passage of time, test check procedures in auditing have become part of generally accepted auditing procedures. With the emergence of test check procedure, discipline of statistics has come quite close to auditing as the auditor is also expected to have the knowledge of statistical sampling so as to arrive at meaningful conclusions. The knowledge of mathematics is also required on the part of auditor particularly at the time of verification of inventories. The use of data analytics is advancing rapidly in auditing where many organizations are using continuous auditing and continuous monitoring of data to identify risks as part of their system of internal control.
Q11.	While planning the audit of S Ltd. you want to apply sampling techniques. What are the risk factors you should keep in mind? **(RTP, Nov 2018, NA) (MTP2, May 2019, 3 Marks)**
	OR
	"Sampling risk can lead to erroneous conclusions". Justify **(SA, May 2019, 4 Marks) (MTP2, May 2021, 3 Marks)**

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Risk Factors while applying Sampling Techniques: As per **SA 530 "Audit Sampling"**, sampling risk is the risk that the **auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure**. This risk will always be in existence when auditor uses sampling technique in conducting his audit. Sampling risk can lead to two types of erroneous conclusions-

- ➢ In the case of a **test of controls**, that **controls are more effective than they actually are**, or in the **case of tests of details**, that a **material misstatement does not exists when in fact it does.** The auditor is primarily concerned with this type of erroneous conclusion because it affects **audit effectiveness** and is more likely to lead to an **inappropriate audit opinion.** This is because of **over reliance on the internal controls**

- ➢ In the case of **test of controls**, the **controls are less effective than they actually are**, or in the case of **tests of details**, that a **material misstatement exists when in fact it does not.** This type of erroneous conclusion affects **audit efficiency** as it would usually lead to **additional work** to establish that initial conclusions were incorrect. This is because of **under reliance on the test of controls** and detailed substantive procedures performed by the auditor. Here the risk of giving wrong opinion is **minimum** but it will lead to more detailed checking which is time consuming.

Comments and feedback:
- Direct and moderate question
- Important keywords are highlighted in the above answer

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<td>Q12.</td>
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The auditor shall evaluate the results of the sample and whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested. Explain

(RTP, Nov 2018, NA) (MTP1, Nov 2018, 5 Marks)

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The auditor shall evaluate-

- The **results of the sample**; and
- Whether the use of audit sampling has provided a **reasonable basis for conclusions** about the population that has been tested.

For tests of controls, an unexpectedly **high sample deviation rate** may lead to an **increase in the assessed risk of material misstatement**, unless further audit evidence substantiating the initial assessment is obtained. For **tests of details**, an **unexpectedly high misstatement** amount in a sample may cause the auditor to believe that a class of transactions or account balance is materially misstated, in the absence of further audit evidence that no material misstatement exists.

In the case of **tests of details,** the **projected misstatement plus anomalous misstatement, if any, is the auditor's best estimate of misstatement in the population.** When the projected misstatement plus anomalous misstatement, if any, **exceeds tolerable misstatement, the sample does not provide a reasonable basis for conclusions** about the population that has been tested. The closer the projected misstatement plus anomalous misstatement is to tolerable misstatement, the more likely that actual misstatement in the population may exceed tolerable misstatement.

Also, if the **projected misstatement is greater than the auditor's expectations of misstatement** used to determine the sample size, the auditor may conclude that there is an **unacceptable sampling risk** that the actual misstatement in the population exceeds the tolerable misstatement. Considering the results of

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other audit procedures helps the auditor to assess the risk that actual misstatement in the population exceeds tolerable misstatement, and the risk may be reduced if additional audit evidence is obtained.

In case the auditor concludes that audit sampling has not provided a reasonable basis for conclusions about the population that has been tested, the **auditor may request management to investigate misstatements that have been identified** and the potential for further misstatements and to make any **necessary adjustments;** or tailor the **nature, timing and extent of those further audit procedures** to best achieve the required assurance. For example, in the case of tests of controls, the auditor might extend the sample size, test an alternative control or modify related substantive procedures.

Comments and feedback:
- Direct and moderate question
- Important keywords are highlighted in the above answer

Q13.	Discuss the factors that should be considered for deciding upon the extent of checking on a sampling plan. **(SA, Nov 2018, 5 Marks) (RTP, May 2019, NA) (RTP, Nov 2020, NA)**

The factors that should be considered for deciding upon the extent of checking on a sampling plan are following:

➢ **Size of the organisation** under audit.
➢ State of the **internal control.**
➢ **Adequacy and reliability** of books and records.
➢ **Tolerable error range.**
➢ Degree of the **desired confidence.**

Comments and feedback:
- Direct and easy question
- **Important keywords:** Size of the organisation, internal control, Adequacy and reliability, Tolerable error range, desired confidence

Q14.	CORRECT/INCORRECT Stratified Sampling involves dividing the whole population to be tested in a few separate groups called strata and taking a sample from each of them. **(MTP 2, Nov 2018, 2 Marks)**

The statement is correct.

Stratified Sampling involves **dividing the whole population to be tested in a few separate groups called strata and taking a sample from each of them**. Each stratum is treated as if it was a **separate population** and if proportionate of items are selected from each of these stratum. The number of groups into which the whole population has to be divided is determined on the basis of **auditor judgment.**

Comments and feedback:
- Direct and easy question
- **Important keywords:** dividing the whole population to be tested in a few separate groups called strata and taking a sample from each of them, separate population, auditor judgment.

Q15.	The auditor is required to project misstatements for the population to obtain a broad view of the scale of misstatement. Explain **(RTP, May 2019, NA)** **OR** The auditor is required to project misstatements for the population to obtain a broad view of the scale of

misstatement but this projection may not be sufficient to determine an amount to be recorded. Explain **(RTP, May 2020, NA)**

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OR

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It is imperative for the auditor to project misstatements for the population while performing audit procedures through sampling. Comment. **(SA, Nov 2020, 3 Marks)**

- As per SA 530 "Audit Sampling", the auditor is required to project misstatements for the population to obtain a broad view of the scale of misstatement but this projection may not be sufficient to determine an amount to be recorded.
- When a misstatement has been established as an **anomaly,** it may be **excluded when projecting misstatements** to the population. However, the effect of any such **misstatement, if uncorrected, still needs to be considered in addition to the projection of the non-anomalous misstatements.**
- For **tests of details,** the auditor shall **project misstatements** found in the sample to the population whereas for **tests of controls, no explicit projection of deviations is necessary since the sample deviation rate is also the projected deviation rate** for the population as a whole.

Comments and feedback:
- Direct and moderate question
- **Important keywords:** anomaly, excluded when projecting misstatements, misstatement, if uncorrected, still needs to be considered in addition to the projection of the non-anomalous misstatements, tests of details, project misstatements, tests of controls, no explicit projection of deviations is necessary since the sample deviation rate is also the projected deviation rate

Q16.	In the case of tests of details (a) the projected misstatement plus anomalous misstatement, if any, is the auditor's best estimate of misstatement in the population. (b) the projected misstatement is the auditor's best estimate of misstatement in the population. (c) the anomalous misstatement is the auditor's best estimate of misstatement in the population. (d) the projected misstatement plus anomalous misstatement, if any, cannot be the auditor's best estimate of misstatement in the population. **(MTP1, May 2019, 1 Mark)**
	Correct answer: (a) the projected misstatement plus anomalous misstatement, if any, is the auditor's best estimate of misstatement in the population. **Comments and feedback:** - Direct and moderate question
Q17.	Which of the following is correct : (a) When the projected misstatement exceeds tolerable misstatement, the sample does not provide a reasonable basis for conclusions about the population that has been tested. (b) When the projected misstatement plus anomalous misstatement, if any, exceeds tolerable misstatement, the sample does not provide a reasonable basis for conclusions about the population that has been tested. (c) When the anomalous misstatement exceeds tolerable misstatement, the sample does not provide a reasonable basis for conclusions about the population that has been tested. (d) When the projected misstatement plus anomalous misstatement, if any, exceeds tolerable misstatement, the sample provides a reasonable basis for conclusions about the population that has been

	tested. **(MTP1, May 2019, 1 Mark)**
	Correct answer: (b) When the projected misstatement plus anomalous misstatement, if any, exceeds tolerable misstatement, the sample does not provide a reasonable basis for conclusions about the population that has been tested. **Comments and feedback:** ● Direct and moderate question
Q18.	It is a type of value-weighted selection in which sample size, selection and evaluation results in a conclusion in monetary amounts : (a) Haphazard sampling (b) Monetary Unit Sampling (c) Stratified Sampling (d) Interval sampling **(MTP2, May 2019, 1 Mark)**
	Correct answer: (b) Monetary Unit Sampling **Comments and feedback:** ● Direct and easy question
Q19.	CORRECT/INCORRECT Sample size is not a valid criterion to distinguish between statistical and non-statistical approaches. **(MTP2, May 2019, 2 Marks)**
	The statement is correct. The decision whether to use a statistical or non-statistical sampling approach is a matter for the **auditor's judgment**; however, sample size is **not a valid criterion** to distinguish between statistical and non-statistical approaches. Whatever may be the approach, **non-statistical or statistical sampling,** the sample **must be representative.** This means that it must be **closely similar** to the whole population although not necessarily exactly the same. The sample **must be large enough to provide statistically meaningful results.** **Comments and feedback:** ● Direct and moderate question ● **Important keywords:** auditor's judgment, not a valid criterion, non-statistical or statistical sampling, must be representative, closely similar, must be large enough to provide statistically meaningful results.
Q20.	There is a growing realisation that the traditional approach to audit is economically wasteful because all efforts are directed to check all transactions without exception. Explain **(RTP, Nov 2019, NA)**
	● No conscious effort in human society is divested of economic considerations and auditing is no exception. There is a growing realisation that the traditional approach to audit is economically wasteful because all efforts are directed to check all transactions without exception. ● In the traditional approach more emphasis is placed on routine **checking,** which often is not

	necessary in view of the **time and the cost involved**. In routine checking, auditor considers **extensive checking and vouching of all entries** ● With the shift in favour of **formal internal controls** in the management of affairs of organisations, the possibilities of routine **errors and frauds have greatly diminished** and auditors often find extensive routine checking **as nothing more than a ritual because it seldom reveals anything material.** ● Now the approach to audit and the extent of checking are undergoing a progressive change in favour of more attention towards the **questions of principles and controls** with a curtailment of non-consequential routine checking. **Comments and feedback:** ● Indirect and moderate question ● **Important keywords:** routine checking, time and the cost involved, formal internal controls, errors and frauds have greatly diminished, as nothing more than a ritual because it seldom reveals anything material, questions of principles and controls, extensive checking and vouching of all entries ● Many students do not attempt this question properly
Q21.	The extent of the checking to be undertaken is primarily a matter of judgment of the auditor. It is in the interest of the auditor that if he decides to form his opinion on the basis of a part checking, he should adopt standards and techniques which are widely followed Explain **(RTP, Nov 2019, NA)**
	● The auditor is required to express an opinion on the financial statements. For this purpose, the auditor is required to decide the extent of the checking to be performed. The extent of the checking to be undertaken is primarily a **matter of judgment** of the auditor, there is **nothing statutorily stated** anywhere which specifies **what work is to be done, how it is to be done and to what extent**. It is also **not obligatory** that the **auditor must adopt the sampling technique.** ● To ensure a good and reasonable standard of work, he should adopt **standards and techniques** that can lead him to an **informed professional opinion**. On a consideration of this fact, it can be said that it is in the interest of the auditor that if he decides to form his opinion on the basis of a part checking, he should adopt standards and techniques which are widely followed and which have a recognised basis. ● Since **statistical theory of sampling is based on a scientific law**, it can be relied upon to a greater extent **than any arbitrary technique which lacks in basis and acceptability.** This enables the auditor to make conclusions and express fair opinion without having to check all of the items within the financial statements. **Comments and feedback:** ● Indirect and moderate question ● **Important keywords:** matter of judgment, nothing statutorily stated, what work is to be done, how it is to be done and to what extent, not obligatory, auditor must adopt the sampling technique, standards and techniques, informed professional opinion, statistical theory of sampling is based on a scientific law, than any arbitrary technique which lacks in basis and acceptability ● Many students do not attempt this question properly
Q22.	CORRECT/ INCORRECT The non-statistical sampling is criticized on the grounds that it is neither objective nor scientific. **(SA, Nov 2019, 2 Marks)**

The statement is correct.

The non-statistical sampling is criticized on the grounds that it is **neither objective nor scientific**. The **expected degree of objectivity** cannot be assured in non-statistical sampling because the **risk of personal bias in selection of sample items cannot be eliminated.** The closeness of the qualities projected by the sample results with that of the whole population cannot be measured because the sample has not been selected in accordance with the **mathematically based statistical techniques.**

Comments and feedback:
- Direct and easy question
- **Important keywords:** neither objective nor scientific, expected degree of objectivity, risk of personal bias in selection of sample items cannot be eliminated, mathematically based statistical techniques

Q23.	CORRECT/ INCORRECT
	The method which involves dividing the population into groups of items is known as block sampling.
	(MTP1, Nov 2019, 2 Marks)

The statement is incorrect.

The method which involves dividing the population into groups of items is known as **cluster sampling** whereas **block sampling involves the selection of a defined block of consecutive items.**

Comments and feedback:
- Direct and moderate question
- Important keywords: cluster sampling, block sampling involves the selection of a defined block of consecutive items.

Q24.	CORRECT/ INCORRECT
	Statistical sampling has narrower application where a population to be tested consists of a large number of similar items.
	(RTP, May 2020, NA)

The statement is Incorrect.

Statistical sampling has **reasonably wide application** where a population to be tested consists of a large number of similar items and more in the case of transactions involving **compliance testing, trade receivables' confirmation, payroll checking, vouching of invoices and petty cash vouchers.**

Comments and feedback:
- Direct and easy question
- Important keywords: reasonably wide application, compliance testing, trade receivables' confirmation, payroll checking, vouching of invoices and petty cash vouchers.

Q25.	Explain the sampling method which involves selection of a block(s) of contiguous items from within the population. Also give example.
	(RTP, May 2020, NA)

Block Sampling: This method involves **selection of a block(s) of contiguous items from within the population**. Block selection **cannot ordinarily be used in audit sampling** because most populations are structured such that items in a sequence can be expected to have similar characteristics to each other, but

different characteristics from items elsewhere in the population. Although in some circumstances it may be an appropriate audit procedure to examine a block of items, it **would rarely be an appropriate sample selection technique** when the auditor intends to draw **valid inferences about the entire population** based on the sample.

Example

Take the first 300 sales invoices from the sales day book in the month of August; alternatively take any five blocks of 50 sales invoices. Therefore, once the first item in the block is selected, the rest of the block follows items to the completion.

Comments and feedback:
- Direct and easy question
- Important keywords are highlighted in the above answer
- Do write example also

Q26. Sampling risk is the risk that the auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. Sampling risk leads to erroneous conclusions. Explain in detail distinguishing it from nonsampling risk with examples.

(RTP, Nov 2020, NA)

OR

In the context of SA 530 'Audit Sampling', explain the terms 'Sampling Risk' and 'NonSampling risk'.

(SA, Jan 2021, 4 Marks)

Sampling Risk. The risk that the **auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure**. Sampling risk can lead to two types of erroneous conclusions:

➢ In the case of a **test of controls**, that **controls are more effective than they actually are**, or in the case of a **test of details**, that a **material misstatement does not exist when in fact it does**. The auditor is primarily concerned with this type of erroneous conclusion because it affects **audit effectiveness** and is more likely to lead to an **inappropriate audit opinion.**

➢ In the case of a **test of controls**, that **controls are less effective than they actually are**, or in the case of a **test of details**, that a **material misstatement exists when in fact it does not**. This type of erroneous conclusion affects **audit efficiency** as it would usually lead to **additional work** to establish that initial conclusions were incorrect.

Non-Sampling Risk. The risk that the auditor reaches an erroneous conclusion for **any reason not related to sampling risk.** Non sampling risk can **never be mathematically measured.**

Example

Examples of non-sampling risk include use of inappropriate audit procedures, or misinterpretation of audit evidence and failure to recognize a misstatement or deviation.

Sources of Non Sampling risk are :
- **Human Mistakes**
- Applying **audit procedures not appropriate** to the objectives of audit
- Relying on **erroneous informatio**n e.g. erroneous confirmation
- **Misinterpreting the sample results**

Comments and feedback:
- Direct and moderate question

	● Important keywords are highlighted in the above answer
Q27.	Audit testing done through Statistical sampling is more scientific than testing based entirely on the auditor's own judgment because it involves use of mathematical laws of probability in determining the appropriate sample size in varying circumstances. Explain and also state advantages of Statistical sampling. **(MTP1, Nov 2020, 4 Marks)** **OR** What are the advantages of Statistical sampling technique in auditing **(RTP, May 2022, NA)**

Audit testing done through this approach is **more scientific** than testing based entirely on the auditor's own judgment because it involves use of **mathematical laws of probability** in determining the appropriate sample size in varying circumstances. Statistical sampling has **reasonably wide application** where a population to be tested consists of a **large number of similar items** and more in the case of transactions involving **compliance testing, trade receivables' confirmation, payroll checking, vouching of invoices and petty cash vouchers.**

The advantages of statistical sampling may be summarized as follows -
- The amount of testing (sample size) **does not increase in proportion to the increase in the size of the area (universe) tested.**
- The sample selection is **more objective and thereby more defensible.**
- The method provides a means of estimating the **minimum sample size associated with a specified risk and precision.**
- It provides a means for deriving a **"calculated risk"** and **corresponding precision (sampling error)** i.e. the probable difference in result due to the use of a sample in lieu of examining all the records in the group (universe), using the same audit procedures.
- It may provide a **better description of a large mass of data than a complete examination of all the data**, since non-sampling errors such as processing and clerical mistakes are not as large.

Comments and feedback:
- Direct and easy question
- **Important keywords:** more scientific, mathematical laws of probability, reasonably wide application, large number of similar items, compliance testing, trade receivables' confirmation, payroll checking, vouching of invoices and petty cash vouchers, does not increase in proportion to the increase in the size of the area (universe) tested, more objective and thereby more defensible, minimum sample size associated with a specified risk and precision, "calculated risk", corresponding precision (sampling error), better description of a large mass of data than a complete examination of all the data

Q28.	_____ in which the auditor selects the sample without following a structured technique. (a) Haphazard selection, (b) Monetary Unit Sampling (c) Block Sampling (d) Structured Sampling **(RTP, May 2021, NA)**
	Correct answer: (a) Haphazard selection

	Comments and feedback:
	● Direct and easy question

Q29.	Explain the following terms with reference to Audit Sampling :
	(i) Stratification (ii) Tolerable misstatement (iii) Tolerable rate of deviation
	(RTP, May 2021, NA)

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

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

iii) **Tolerable rate of deviation** – A rate of deviation from prescribed **internal control procedures** set by the auditor in respect of which the auditor seeks to obtain an **appropriate level of assurance** that the rate of deviation set by the auditor is **not exceeded by the actual rate of deviation** in the population.

Comments and feedback:
● Direct and easy question
● Important keywords are highlighted in the above answer

Q30.	In most of the circumstances, the evidence available is not conclusive and the auditor always takes a calculated risk in giving his opinion. Even by undertaking hundred percent checking of the transactions, the auditor does not derive absolute satisfaction. This state of uneasiness led pragmatic auditors to adopt the statistical theory of sampling to derive the necessary satisfaction about the state of affairs by checking only a part of the total population of entries. Explain in detail.
	(RTP, May 2021, NA)

In most of the circumstances, the evidence available is **not conclusive** and the auditor always takes a **calculated risk** in giving his opinion. Even by undertaking hundred percent checking of the transactions, the auditor does not derive absolute satisfaction. This **state of uneasiness led pragmatic auditors to adopt the statistical theory of sampling** to derive the necessary satisfaction about the state of affairs by checking only a part of the total population of entries.

Auditors realised that they can derive good satisfaction by undertaking a much lesser checking by adoption of this technique in the auditing process. It is a **mathematical truth** that the sample, if picked purely on a random basis would reveal the features and characteristics of the population.

By adopting the sampling technique, the auditor only checks a part of the whole mass of transactions. The satisfaction he used to derive earlier, by checking all the transactions, can be derived by a sample checking provided he can put **reliance on the internal controls** and checks within the client's organisation because they provide the reliability of the records. Sampling is used as a part of the **Test of controls.** Auditors will check a few internal controls and their **operating effectiveness. Based on the conclusion derived, he can then design the sample size for test of details** (i.e checking of transactions and balances)

If the **internal control is satisfactory** in its design and implementation, a much **smaller sample** can give the auditor the necessary reliability of the result he obtains. On the other hand, if in certain areas **controls are slack or not properly implemented,** the auditor may have to take a much **larger sample** for getting satisfactory result.

Another truth about the sampling technique should be noted. It **can never bring complete reliability; it cannot give precisely accurate results.** It is a **process of estimation.** It may have some **errors.** What error is tolerable for a particular matter under examination is a **matter of the individual's judgment** in that

particular case.

Comments and feedback:
- Direct and moderate question
- Important keywords are highlighted in the above answer.

Q31.	CORRECT/INCORRECT In stratified sampling, the conclusion drawn on each stratum can be directly projected to the whole population **(SA, July 2021, 2 Marks)**

The statement is incorrect.

In case of stratified sampling, the **conclusions are drawn on the stratum**. The combination of all the conclusions on stratum together will be used to determine the **possible effect of misstatement or deviation**. Hence the samples are used to derive conclusions **only on the respective stratum** from where they are drawn and **not the whole population.**

Comments and feedback:
- Direct and moderate question
- **Important keywords:** conclusions are drawn on the stratum, possible effect of misstatement or deviation, only on the respective stratum, not the whole population**.**

Q32.	CA B is appointed as an auditor of M/s. Divine Pharmacy, a wholesale medicine supplier. While auditing for the financial year 2020-21, CA B wants to use test checking technique. Advise CA B, what kind of precautions should be taken by him in this regard. **(SA, July 2021, 4 Marks)**

While auditing the accounts of Divine Pharmacy, CA B wanted to use Test Checking technique. The following Precautions should to be taken by CA B while applying test check techniques:
- Thorough **study of accounting system** should be done before adopting sampling
- Proper study of **internal control systems.**
- **Areas which are not suitable for sampling** should be carefully considered. eg: compliance with statutory provisions, transactions of unusual nature etc.
- **Proper planning** for Sampling methods to be used and explaining the staff,
- **Transactions and balances have to be properly classified** (stratified)
- **Sample size should be appropriately determined**.
- Sample should be chosen in **unbiased way,**
- **Errors** located in the sample should be **analyzed properly.**

Comments and feedback:
- Direct and easy question
- Important keywords are highlighted in the above answer

Q33.	When designing an audit sample, the auditor shall consider the purpose of the audit procedure and the characteristics of the population from which the sample will be drawn. Explain in detail. **(RTP, Nov 2021, NA)**

- Audit sampling enables the auditor to obtain and evaluate audit evidence about some characteristic of the items selected in order to form or assist in forming a conclusion concerning

the population from which the sample is drawn. Audit sampling can be applied using **either non-statistical or statistical sampling approaches.**

- When designing an audit sample,
  - ➢ the auditor's consideration includes the **specific purpose** to be achieved and the **combination of audit procedures** that is likely to best achieve that purpose.
  - ➢ Consideration of the **nature of the audit evidence** sought and possible deviation or misstatement conditions or other characteristics relating to that audit evidence will assist the auditor in defining what constitutes a **deviation or misstatement** and what **population to use for sampling.**
  - ➢ In fulfilling the requirement of relevant portion (paragraph 8) of **SA 500,** when performing audit sampling, the auditor performs audit procedures to obtain evidence that the population from which the **audit sample is drawn is complete.**
- The auditor's consideration of the purpose of the audit procedure includes a clear understanding of what constitutes a deviation or misstatement so that all, and only, those conditions that are relevant to the purpose of the audit procedure are included in the evaluation of deviations or projection of misstatements.
- For example, in a test of details relating to the existence of accounts receivable, such as confirmation, payments made by the customer before the confirmation date but received shortly after that date by the client, are not considered a misstatement. Also, a misposting between customer accounts does not affect the total accounts receivable balance.
- Therefore, it may not be appropriate to consider this a misstatement in evaluating the sample results of this particular audit procedure, even though it may have an important effect on other areas of the audit, such as the assessment of the risk of fraud or the adequacy of the allowance for doubtful accounts.
- In considering the characteristics of a population, **for tests of controls,** the auditor makes an **assessment of the expected rate of deviation** based on the auditor's understanding of the **relevant controls** or on the examination of a small number of items from the population. This assessment is made in order to design an audit sample and to determine sample size.
- For example, if the **expected rate of deviation is unacceptably high, the auditor will normally decide not to perform tests of controls.**
- Similarly, **for tests of details,** the auditor makes an assessment of the expected misstatement in the population. If the **expected misstatement is high**, **100% examination or use of a large sample size may be appropriate** when performing tests of details.
- In considering the characteristics of the population from which the sample will be drawn, the auditor may determine that **stratification or value-weighted selection is appropriate.**
- The **decision whether to use a statistical or non-statistical sampling** approach is a matter for the **auditor's judgment**; however, sample size is **not a valid criterion** to distinguish between statistical and non-statistical approaches.

Comments and feedback:
- Direct and moderate question
- Important keywords are highlighted in the above answer

Q34.	State the requirements relating to audit sampling, sample design, sample size and selection of items for testing. **(MTP1, Nov 2021, 4 marks)**
	__Meaning of Audit Sampling:__ As per **SA 530 on "Audit Sampling"**, the meaning of the term Audit Sampling is – the application of audit procedures to **less than 100% of items within a population** of audit relevance such that **all sampling units**

have a chance of selection in order to provide the auditor with a **reasonable basis** on which to **draw conclusions about the entire population.**

The requirements relating to sample design, sample size and selection of items for testing are explained below

- *Sample design:*

  When designing an audit sample, the auditor shall consider the **purpose of the audit procedure and the characteristics of the population** from which the sample will be drawn.

- *Sample Size:*

  The auditor shall determine a sample size **sufficient to reduce sampling risk to an acceptably low level.**

- *Selection of Items for Testing:*

  The auditor shall select items for the sample in such a way that **each sampling unit in the population has a chance of selection.**

Comments and feedback:
- Direct and easy question
- Important keywords are highlighted in the above answer

Q35.	CA X is not sure about the kind of Sampling method to be used for audit of a company. Advise him about the choice of methods (name of methods only) of Sampling to be used in various circumstances. Also explain briefly the advantages of the Sampling to be used by him in auditing. **(MTP2, Nov 2021, 3 marks)**

Sample Selection:

CA. X should obtain the knowledge before using the sampling methods. The principal methods are as follows:

- **Random selection.**
- **Systematic selection.**
- **Monetary Unit sampling.**
- **Haphazard selection.**
- **Block selection.**

Advantages of Statistical Sampling in Auditing:
- The amount of testing (sample size) **does not increase in proportion to the increase in the size of the area (universe) tested.**
- The sample selection is **more objective and thereby more defensible.**
- The method provides a means of estimating the **minimum sample size associated with a specified risk and precision.**
- It provides a means for deriving a **"calculated risk"** and **corresponding precision (sampling error)** i.e. the probable difference in result due to the use of a sample in lieu of examining all the records in the group (universe), using the same audit procedures.
- It may provide a **better description of a large mass of data than a complete examination of all the data,** since non-sampling errors such as processing and clerical mistakes are not as large.

Comments and feedback:
- Direct and easy question
- Important keywords are highlighted in the above answer

Q36.	CORRECT/INCORRECT
	Statistical sampling being more scientific and without personal bias bias will always be appropriate to use under all circumstances
	(SA, Dec 2021, 2 marks)

The statement is Incorrect.

Statistical sampling is a widely accepted way of sampling as it is more scientific, without personal bias and the result of sample can be evaluated and projected in more reliable way.

Under some audit circumstances, **statistical sampling methods may not be appropriate.** The auditor should not attempt to use statistical sampling when **another approach is either necessary or will provide satisfactory information in less time or with less effort.** For instance, when exact accuracy is required or in case of legal requirements etc

Comments and feedback:
- Direct and easy question
- Important keywords are highlighted in the above answer

Q37.	With reference to SA 530 "Audit Sampling", explain briefly the following factors that the auditor may consider when determining the sample size for the Test of Details –
	(i) The desired level of assurance (ii) Stratification of the pollution
	(SA, Dec 2021, 3 marks)

Examples of factors influencing Sample Size for Test of Details:

(i) **Desired Level of Assurance:** An **increase in the auditor's desired level of assurance that tolerable misstatement is not exceeded by actual misstatement in the population will increase the sample size**. Hence, greater the level of assurance that the auditor requires that the results of the sample are in fact indicative of the actual amount of misstatement in the population, the larger the sample size needs to be.

(ii) **Stratification of population:** When stratification of the population is **appropriate then sample size will decrease** as when there is a **wide range** (variability) in the monetary size of items in the population, it may be useful to stratify the population. When a population can be appropriately stratified, the aggregate of the sample sizes from the strata generally will be less than the sample size that would have been required to attain a given level of sampling risk, had one sample been drawn from the whole population.

Comments and feedback:
- Direct and easy question
- Important keywords are highlighted in the above answer

Q38.	ABC Ltd is a Large Company with huge purchase and sales transactions. Which sampling approach is recommended in such a company? Explain giving features of such sampling approach along with example
	(MTP1, May 2022, 3 Marks)

In larger organisations, with huge transactions, statistical sampling is always rec ommended as it is unbiased, and the samples selected are not prejudged.

Features/Characteristics of Statistical Sampling:
1) Audit testing done through this approach is **more scientific** than testing based entirely on the auditor's own judgment because it involves **use of mathematical laws of probability** in determining the appropriate sample size in varying circumstances.
2) Statistical sampling has **reasonably wide application** where a population to be tested consists of a

large number of similar items and more in the case of transactions involving **compliance testing, trade receivables' confirmation, payroll checking, vouching of invoices and petty cash vouchers.**

3) There is **no personal bias** of the auditor in case of statistical sampling. Since it is scientific, the results of sample can be evaluated and projected on the whole population in a more reliable manner.

   For Example: An auditor while verifying the Purchases during the year realised that the purchase transactions in that year are more than 50,000 in number, then in such case, statistical sampling will be highly recommended in the audit programme.

Comments and feedback:
- Direct and easy question
- Important keywords are highlighted in the above answer