

Audit Revision Notes – Part 1 – Kunal Sir

Note -sequence of this revision notes is as per my book but chapter name as per Module

Happy Learning – Kunal Sir



Chp 1

Kunal Mandhania

Objective of Audit (SA -200)

Primary



1) Collect SAAE



To obtain reasonable assurance



To express his opinion on F.S



free. From
material
mis-
statement
(M.M)

Made as
per
applicable
financial
reporting
framework
(AFRF)

Whether
it shows T
& F view
or not

2) To Communicate as per S.A

Secondary



➤ Prevention & detection of fraud & error

Note:

- 1) R.A(Reasonable Assurance) is high level of assurance but not complete assurance
- 2) Audit provides R.A
- 3) Absolute assurance cannot be obtained



i.e. cannot reduce audit risk to Zero



Because of



Inherent limitations of audit

Question

Discuss the following:

CA Jatin is the auditor of JP Ltd. The auditor expressed his opinion on the financial statements without ascertaining as to whether the financial statements as a whole were free from material misstatements. Explain w.r.t SA 200.

(MTP 3 Marks April '23)

OR

Mr. Z, auditor of the Company, Different and Capable Limited for the financial year 2022-23, explained to audit team members about the objectives of the Independent Auditor in accordance with the relevant Standard on Auditing. Explain those objectives.

(RTP Nov '23) (PYP 3 Marks May '22)

*Auditor should ensure that F.S do not misled anyone

↓
Check
↓
A²EIOU
↓

A → A/c → Drawn as per → BOA

A → A.S → comply

E → Entries → in BOA → supported by → SAAE

I → Info in FS → T & F show

O → Omission → No

U → Unambiguous & clear → info in FS

Scope of Audit

Included

DM → I.D → C.A

D → Check all disclosures → Properly disclosed

M → Mgt. Judgement → Evaluate

I → Info in F.S → relevant & reliable

D → Design audit procedure (AP)

To check all transactions & balances

C → Cover all aspects of Audit

A → Evaluate → Acc. System & I.C.S.

Not included

CID

C → which falls outside his competence

I → Investigation into alleged wrong doing

D → Documents → authenticate

Note:

Investigation is critical examination of A/cs for some special purpose

(c) The auditor should decide whether relevant information is properly disclosed in the financial statements. Explain with reference to scope of audit.

(3 Marks) MTP Mar. 24

Audit

Advantage

AB²C²DEFGHI



- 1) A → Advantage of Suggestion by auditor
- 2) B → Books → upto date
- 3) B → Banks → Loan
- 4) C → Check → Moral check on employee
- 5) C → Confidence to uses of F.S
- 6) D → Decision making help
- 7) D → Disputes → Solve
- 8) EF → Error & Fraud detect
- 9) G → to Govt. to ascertain tax liabilities
- 10) I → Insurance claim settlement

Notes:

Mater of difficulty time, cost involved



Is not a valid basis to



Omit audit procedure



Specially where there is not alternative

Limitations



Jumping from CLIF in Future



- 1) **Nature of financial reporting**
J → To prepare FS mgt. applies many Judgement
↓
Checking it covers high uncertainty
- 2) **C → Cost & Benefit balance**
To Complete check in reasonable time & cost
↓
Many times test checking needs to be adopted
↓
Leading to audit risk
- 3) **L → Legal Power** → Auditor cannot investigate, So has no legal power like search, seize, etc.
- 4) **Nature of audit procedures (AP)**
I → Information → many time mgt. do not provide complete info.
F → Fraud involves organized & sophisticated scheme
↓
A.P. may be ineffective against fraud
Future → Future uncertainties may increase Audit risk

(c) Nature of financial reporting itself is one of causes of inherent limitations of audit of financial statements. Explain.

(3 Marks) (MTP April 24)

Question 1

In case of certain subject matters, limitations on the auditor's ability to detect material misstatements are particularly significant. Explain such assertions or subject matters.

(Old SM, RTP Nov'23)

Question

There are practical and legal limitations on the auditor's ability to obtain audit evidence. Explain giving examples. Also explain the difference between audit and investigation.

(RTP Nov 22, Nov'23)

Descriptive Questions

(c) The auditor carries out his work by obtaining audit evidence through performance of audit procedures. However, there are practical and legal limitations on ability of auditor to obtain audit evidence. Give one example each for such practical and legal limitations.

(3 Marks) MTP Mar. 24

ANSWER

(c) Example of practical limitation on ability of auditor to obtain audit evidence An auditor does not test all transactions and balances. He forms his opinion only by testing samples. It is an example of practical limitation on auditor's ability to obtain audit evidence.

Example of legal limitation on ability of auditor to obtain audit evidence Management may not provide complete information as requested by auditor. There is no way by which auditor can force management to provide complete information as may be requested by auditor. In case & he is not provided with required information, he can only report. It is an example of legal limitation on auditor's ability to obtain audit evidence.

Assurance Engagement (New concept)

Meaning



Eng. In which



Practitioner expresses a
conclusion



To enhance degree of
confidence



Of intended user other than
responsible person



About outcome of evaluation
of subject matter

Elements(PACER)

P → Three Party Relationship

- Practitioner → who provides assurance
- Responsible person → who prepares subject matters
- User → form whom report is prepared

A → Appropriate subject matters ➤ Info to be examined

C → Suitable criteria

- Like standards / guidelines / laws / etc.

E → sufficient appropriate evidence

- Practitioner performs to obtain 'SAE'

R → Report (Assurance)

- Report containing conclusion provided to User

Descriptive Questions

(d) KST Limited is engaged in manufacturing business. It appoints CA T to provide it an assurance report on its financial statements prepared on the basis of historical financial information. The characteristic of such an engagement is that it involves gathering of sufficient appropriate evidence on basis of which limited conclusions can be drawn up by practitioner. Identify type of engagement. Which are two other features of such an engagement?

(3 Marks) (MTP April 24)

Distinguish between

Audit



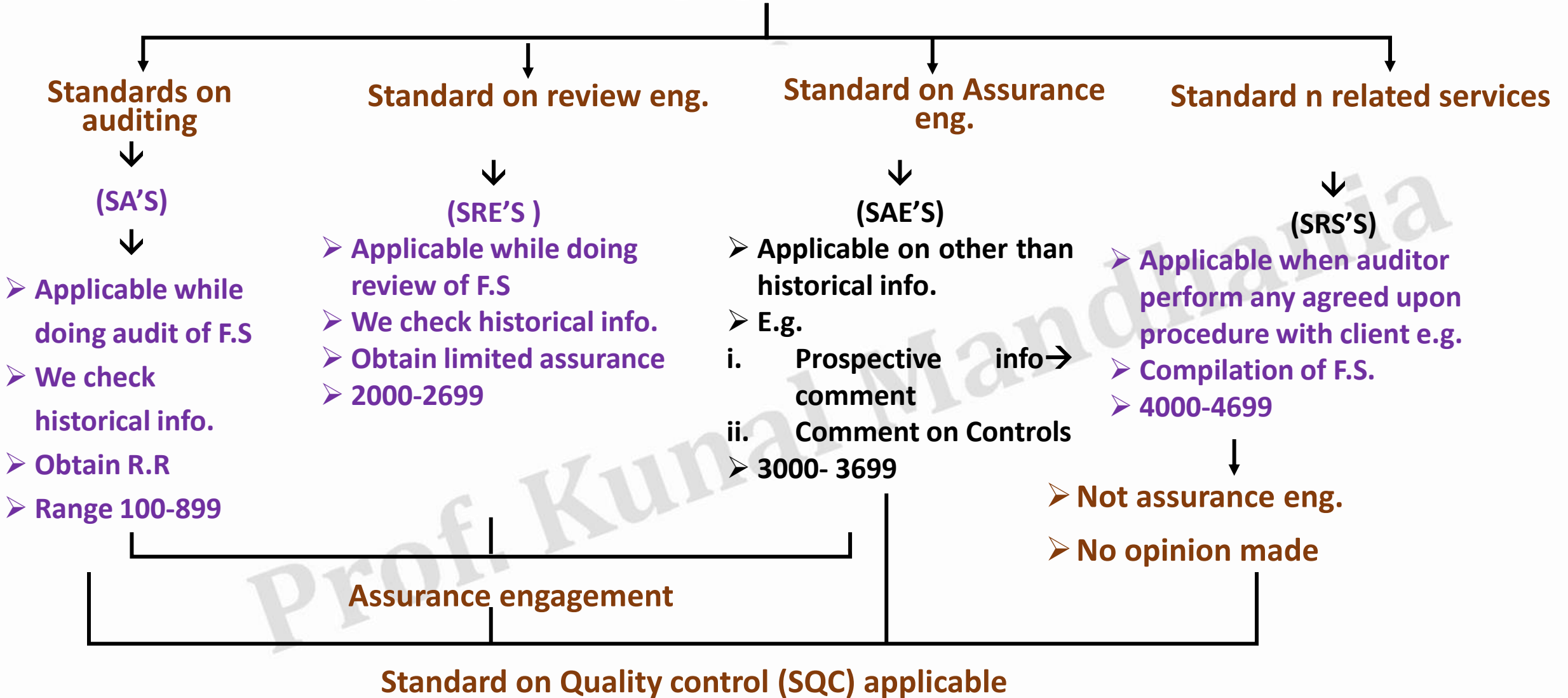
VS

VS

Review



Type of Engagement Standards



***Note : If Specific procedure in required in standards → ineffective**

(1) Document + (2) Perform alternate procedure + (3) Document reason for departure

2. Standards on Auditing (SAs) apply in “audit of historical financial information” whereas Standards on Review Engagements (SREs) apply in “review of historical financial information.” Explain in detail giving examples.

(RTP May 24)

ANSWER

2. Standards on Auditing (SAs) apply in “audit of historical financial

information” whereas Standards on Review Engagements (SREs) apply in “review of historical financial information”. Standards on auditing apply in “audit” of historical financial information which is a reasonable assurance engagement whereas Standards on Review Engagements apply in “review” of historical financial information which is a limited assurance engagement only.

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

“Audit” and “review” are two different terms. Audit is a reasonable assurance engagement, and its objective is reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement. However, “review” is a limited assurance engagement, and its objective is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement.

Standards on Auditing have been issued on wide spectrum of issues in the field of auditing including (but not limited to) overall objectives of independent auditor, audit documentation, planning an audit of financial statements, identifying and assessing risk of material misstatement, audit evidence, audit sampling, going concern and forming an opinion and reporting on financial statements.

Some examples of Standards on Auditing are:

- (i) SA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing
- (ii) SA 230 Audit Documentation
- (iii) SA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment
- (iv) SA 500 Audit Evidence
- (v) Revised SA 700 Forming an Opinion and Reporting on Financial Statements

Examples of Standards on Review engagements are

- (i) SRE 2400 (Revised) Engagements to Review Historical Financial Statements
- (ii) SRE 2410 Review of Interim Financial Information Performed by the Independent Auditor of the Entity

Question

Standards on Auditing (SAs) apply in “audit of historical financial information” whereas Standards on Review Engagements (SREs) apply in “review of historical financial information.” Explain in detail giving examples.

(RTP May '22)

Answer

It is to be understood that Standards on Auditing (SAs) apply in “audit of historical financial information” whereas Standards on Review Engagements (SREs) apply in “review of historical financial information”. Remember that Standards on auditing apply in “audit” of historical financial information which is a reasonable assurance engagement whereas Standards on Review Engagements apply in “review” of historical financial information which is a limited assurance engagement only.

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

Here, we have to broadly understand that “audit” and “review” are two different terms. Audit is a reasonable assurance engagement, and its objective is reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement. However, “review” is a limited assurance engagement, and its objective is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement,

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Question

1. The persons with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity are :

- (a) management**
- (b) Those charged with governance –**
- (c) audit committee**
- (d) board of directors**

(MTP 1 Marks March '21, Oct'23, RTP May '21, Nov'21, Nov'23)

B

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2. The Auditor of a Sole Proprietor Concern is appointed by

- (a) CAG**
- (b) Bank**
- (c) Sole Proprietor himself**
- (d) District Administration**

(MTP 1 Mark April 22)

C

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Question

3. Which of the following is Incorrect:

- (a) An auditor conducting an audit in accordance with SAs is responsible for obtaining absolute assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error.**
- (b) As described in SA 200, owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements will not be detected, even though the audit is properly planned and performed in accordance with the SAs.**
- (c) The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error.**
- (d) The risk of the auditor not detecting a material misstatement resulting from management fraud is greater than for employee fraud.**

(MTP 1 Mark March '23)

A

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Question

4. With respect to auditing, which of the following statement is correct:

- (a) Audited financial statements are absolutely free from all material misstatement due to fraud or error.**
- (b) An audit is an official investigation into alleged wrongdoing and auditor has specific legal powers to conduct investigation**
- (c) The auditor can obtain only a reasonable assurance about whether the financial statement as a whole are free from material misstatement and report on it.**
- (d) An auditor's opinion is an assurance as the future viability of the enterprise or the efficiency or effectiveness of the management.**

(MTP 1 Marks April '23)

C

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7. Which of the following is the responsibility of the auditor:

- (a) Preparation and presentation of the financial statements in accordance with applicable financial reporting**
- (b) Design, implementation and maintenance of internal controls**
- (c) Express an opinion on the Financial Statements**
- (d) To obtain limited assurance.**

(MTP1 Mark April 22)

C

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Descriptive Questions

(d) SQC 1 dwells upon engagement quality control review (EQCR) as part of system of quality control in a firm. Why is such a review required? For which type of engagements EQCR is mandatory?

What should be approach of firm for engagements for which EQCR is not mandatory?

(3 Marks) MTP Mar. 24

ANSWER

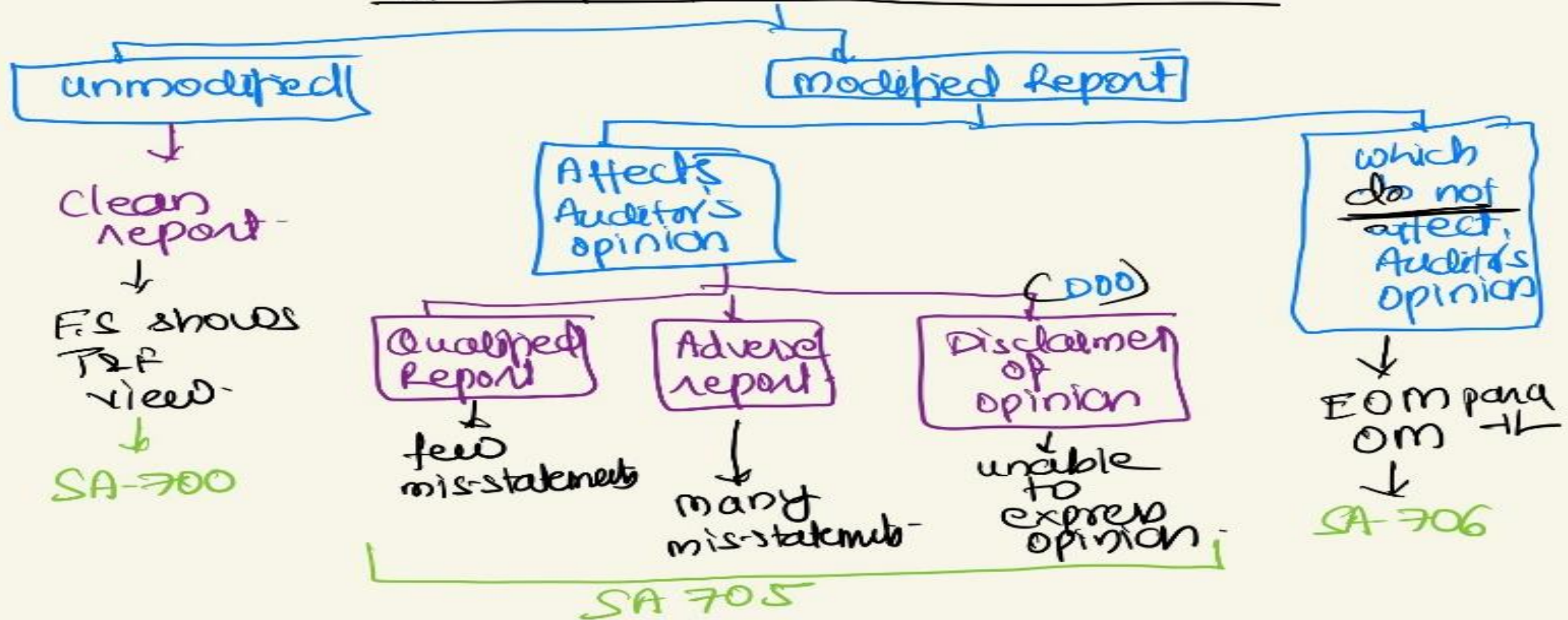
(d) Significant judgments made in an engagement should be reviewed by an engagement quality control reviewer for taking an objective view before the report is issued. Engagement quality control review is mandatory for all audits of financial statements of listed entities.

In respect of other engagements, firm should devise criteria to determine cases requiring performance of engagement quality control review.

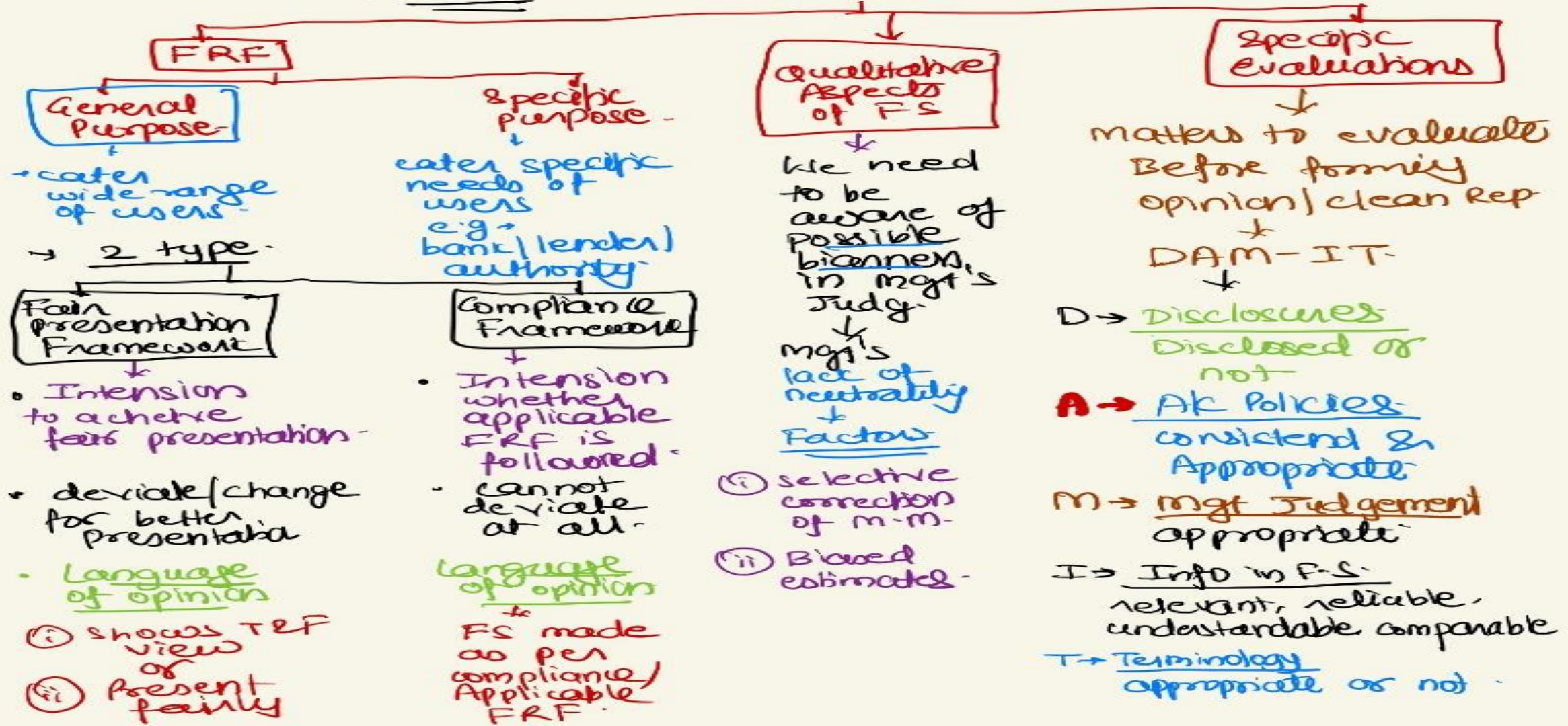
8. Audit Report

Kunal Mandhania

Types of opinion/Audit Report -



SA-700 → Basics



Question

The auditor shall evaluate whether the financial statements are prepared in accordance with the requirements of the applicable financial reporting framework. Explain stating clearly specific evaluations made by the auditor.

(RTP May '22, MTP 3 Marks Oct '21, MTP 4 Marks Apr 21 & March '23, PYP 5 Marks, Nov'18)

Question

G & Associates are the Statutory Auditors of R Ltd., a company engaged in the business of manufacturing of blankets. The auditor has completed the audit and is in the process of forming an opinion on the financial statements for the F.Y. 2022-2023. CA L, the engagement partner, wants to conclude that whether the financial statements as a whole are free from material misstatements, whether due to fraud or error. What factors he should consider to reach that conclusion? Hint – DAM-IT

(MTP 4 Marks Sep '23, PYP 4 Marks Dec '21)

Question

In considering the qualitative aspects of the entity's accounting practices, the auditor may become aware of possible bias in management's judgements. The auditor may conclude that lack of neutrality together with uncorrected misstatements causes the financial statements to be materially misstated. Explain and analyse the indicators of lack of neutrality with examples, wherever required.

(RTP May '23 & May 20, Old & New SM)

SA – 700 – Forming opinion on F.S

Contents / Elements of Audit Report

1. Title – Independent Auditor's Report

2. Addressee – To, members of Co.

3. Opinion Paragraph.

Includes

- a) Name of entity
- b) Period of Audit
- c) Name of F.S. audited
- d) Opinion

4. Basis for opinion para

- a) Followed S.A.
- b) Sec. 143(2) → Ref. to Responsibility
- c) Independence statement
- d) States whether the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's opinion.

While drafting auditor's report of LK Ltd., what are the matter to be included by auditor in Opinion Section paragraph?

(RTP Nov'22)

Question

What an auditor should state in the "Basis for opinion" section of auditor's report ? When the auditor modifies the opinion on the financial statements, explain the amendments he should make in this section?

(RTP Nov '23 , Nov '19 & Nov '20, MTP 3 Marks Oct '23)

Answer

An auditor should state in “Basis for Opinion” section of Auditor’s Report as under:

Basis for Opinion:

The auditor’s report shall include a section, directly following the Opinion section, with the heading “Basis for Opinion”, that:

- (i) States that the audit was conducted in accordance with Standards on Auditing;
- (ii) Refers to the section of the auditor’s report that describes the auditor’s responsibilities under the SAs;
- (iii) Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit and has fulfilled the auditor’s other ethical cordance with these requirements.
- (iv) States whether the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor’s opinion.

Amendments an Auditor should make:

When the auditor modifies the opinion on the financial statements, the auditor shall, in addition to the specific elements required by SA 700 (Revised):

- (i) Amend the heading “Basis for Opinion” required by para of SA 700 (Revised) to “Basis for Qualified Opinion,” “Basis for Adverse Opinion,” or “Basis for Disclaimer of Opinion,” as appropriate; and
- (ii) Within this section, include a description of the matter giving rise to the modification.

SA – 700 – Forming opinion on F.S

5. Going Concern Para –As per SA 570

6. Key audit matters (As per SA- 701)

7. Auditors Resp. for Audit of F.S

Mention

a) We can take only reasonable assurance

b) Report whether F.S is free from material misstatement

8. Mgt.'s Resp. – F.S / I,C,S / making F.s – follows going concern (refer next slide)

9. Report on other legal and Regulatory requirements [Sec. 143]

10. Date – Can be any date but after date of approval of F.s by mgt

11. Place – City where Audit report is signed

12. Signature

a) Prop firm – Signed in his own name

b) Part Firm/LLp- Sign on behalf of firm

c) Also mention membership no and Firm's registration no

Question

The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements." SA 200 explains the premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit in accordance with SAs is conducted. Explain

(MTP 4 Marks April 19, Apr'21, May'20 & April '23, RTP Nov'18, Old & New SM)

OR

The description of management's responsibilities in the auditor's report includes reference to management's responsibilities as it helps to explain to users the premise on which an audit is conducted. Explain

(RTP May '23)

Answer

Responsibilities for the Financial Statements: The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements."

SA 200 explains the premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit in accordance with SAs is conducted. Management and, where appropriate, those charged with governance accept responsibility for the preparation of the financial statements. Management also accepts responsibility for such internal control as it determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. The description of management's responsibilities in the auditor's report includes reference to both responsibilities as it helps to explain to users the premise on which an audit is conducted.

This section of the auditor's report shall describe management's responsibility for:

(a) Preparing the financial statements in accordance with the applicable financial reporting framework, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; [because of the possible effects of fraud on other aspects of the audit, materiality does not apply to management's acknowledgement regarding its responsibility for the design, implementation, and

internal control (or for establishing and maintaining effective internal control over financial reporting) to prevent and detect fraud.] and

(b) Assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern. The explanation of management's responsibility for this assessment shall include a description of when the use of the going concern basis of accounting is appropriate.

5. Which of following is not an element of audit report in accordance with SA 700?

(a) Title

(b) Addressee

(c) Audit strategy

(d) Auditor's opinion (MTP 1 Mark Oct '23)

C

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SA-701 → Key audit matters (KAM)

Meaning	Where required	How to determine KAM (nov 20)	Other IMP Pts.
<p>Matters</p> <p>↓</p> <p>In auditors judgement</p> <p>↓</p> <p>Were of most significance in audit</p> <p>↓</p> <p>Of F.S. of current period</p>	<ol style="list-style-type: none"> 1) Listed Co. 2) If required by law 3) Optional <ol style="list-style-type: none"> a) If entity is of significant public interest. E.g. Banks, F.I. b) Public sector entities 	<ol style="list-style-type: none"> 1) Should be from matters communication to TCWG 2) Require significant auditor attention 3) Most significant 	<ol style="list-style-type: none"> 1) Communicate in auditors report under KAM para with <ol style="list-style-type: none"> a) Separate heading b) Reason of consideration c) How matter was addressed. <p>Communicating KAM is not a Substitute to</p> <ul style="list-style-type: none"> • Disclosure in FS • Modified Opinion • Material uncertainty about Going Concern Reporting • Separate opinion individually 1) Where KAM not required <ol style="list-style-type: none"> a) Matter on which report modified b) If disclaimer- then omit KAM para (SA 705)

- 1) Higher RMM
- 2) Significant risk identified
- 3) Area requiring significant mgt. judgement.
- 4) Recent significant event occurred during period

Other important points

1. If matter highlighted in KAM no need to include it in EOM / OM para
2. Purpose [RTP-Nov. 18]
 - i) Enhance communication value of report for intended users
 - ii) Greater transparency
 - iii) Assist them in understanding significant areas , and matters requiring significant judgement

SA 705 MODIFIED OPINION

Meaning

Any opinion other than clean report is **modified report**

Eg

1. Qualified report
2. Negative report
3. Disclaimer of Opinion

Which opinion to give

Reasons	Material but not pervasive (Spread out)	Material as well as pervasive
Material Misstatement in FS	Qualified	Adverse / Negative
Unable to obtain evidence	Qualified	Disclaimer of opinion

Changes in Audit Report

1. Opinion in opinion para
2. Name of opinion para will be qualified / negative / Disclaimer of opinion
3. Name of basis of opinion para will be basis for Q / N / DOO and give reasons and effect of Modification

Question

Elucidate the circumstances when a modification to the Auditor's opinion is required. Also state the factors for making the decision regarding which type of modified opinion is appropriate.

(PYP 3 Marks May '23, Old & New SM)

Distinguish between an adverse opinion and a qualified opinion. Also draft an opinion paragraph for both types of opinion.

(MTP 4 Marks Oct'23, Old & New SM)

Answer

An auditor shall express an adverse opinion, when the auditor having obtained sufficient and appropriate audit evidence, concludes that misstatements, individually or in aggregate are both material and pervasive.

Whereas, when the auditor, having obtained sufficient and appropriate audit evidence, concludes that misstatements are material but not pervasive, shall express a qualified opinion.

SA705 – “Modifications to the Opinion in the Independent Auditor’s Report” deals with the form and content of both types of report. The following are the draft of the opinion paragraphs of the reports.

(i) Adverse Opinion

We have audited the accompanying consolidated financial statements of ABC Company Limited (hereinafter referred to as the “Holding Company”) and its subsidiaries (the Holding Company and its subsidiaries together referred to as “the Group”), its associates and jointly controlled entities, which comprise the consolidated balance sheet as at March 31, 2023, the consolidated statement of profit and Loss, (consolidated statement of changes in equity) and the consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies (hereinafter referred to as the “consolidated financial statements”). In our opinion and to the best of our information and according to the explanations given to us, because of the significance of the matter discussed in the Basis for Adverse Opinion section of our report, the accompanying consolidated financial statements do not give a true and fair view in conformity with the accounting principles generally accepted in India, of their consolidated state of affairs of the Group, its associates and jointly controlled entities, as at March 31, 2023, of its consolidated profit/loss, (consolidated position of changes in equity) and the consolidated cash flows for the year then ended.

(ii) Qualified Opinion

We have audited the standalone financial statements of ABC Company Limited (“the Company”), which comprise the balance sheet as at March 31, 2023, and the statement of Profit and Loss, (statement of changes in equity) and the statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory information (in which are included the Returns for the year ended on that date audited by the branch auditors of the Company’s branches located at (location of branches)) . In our opinion and to the best of our information and according to the explanations given to us, except for the effects of the matter described in the Basis for Qualified Opinion section of our report, the aforesaid financial statements give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the Company as at March 31st, 2023 and profit/loss, (changes in equity) and its cash flows for the year ended on that date.

SA 706 Emphasis of Matter Para & Other Matter Para

EMPHASIS OF MATTER PARA (EOM)

Meaning

Used where although matter appropriately presented and disclosed



Is of such importance



Is fundamental to users understanding of F.S

Examples where used

1. Early application of AS → disclosed by Management
2. Doubt about Going Concern → disclosed by assumption Management
3. Material Change in → Disclosed by Accounting policy Management
4. Uncertainty over pending → Disclosed by Litigation Management
5. Major amalgamation during the year
6. Many prior period items
7. Subsequent event



Occurring between Balance Sheet date & date of Audit Report

Other Important Points

1. Use EOM para where on such matter
 - He neither modifies report
 - Nor use KAM Para

Question

What is meant by Emphasis of Matter Paragraph? Give some examples of circumstances where the auditor may consider it necessary to include an Emphasis of Matter paragraph.

(MTP 4 Marks Oct'22)

OR

Discuss any four examples of circumstances where the auditor may consider it necessary to include an Emphasis of Matter paragraph in his report.

(MTP 4 Marks Sep '23)

OR

Mention the examples of circumstances where the auditor may consider it necessary to include an Emphasis of Matter paragraph.

(MTP 3 Marks Nov '21, RTP Nov'22)

SA 706 Emphasis of Matter Para & Other Matter Para

OTHER MATTER PARA (OM)

Meaning

Matter other than those in FS



Relevant to

- User's understanding

- Auditors responsibility

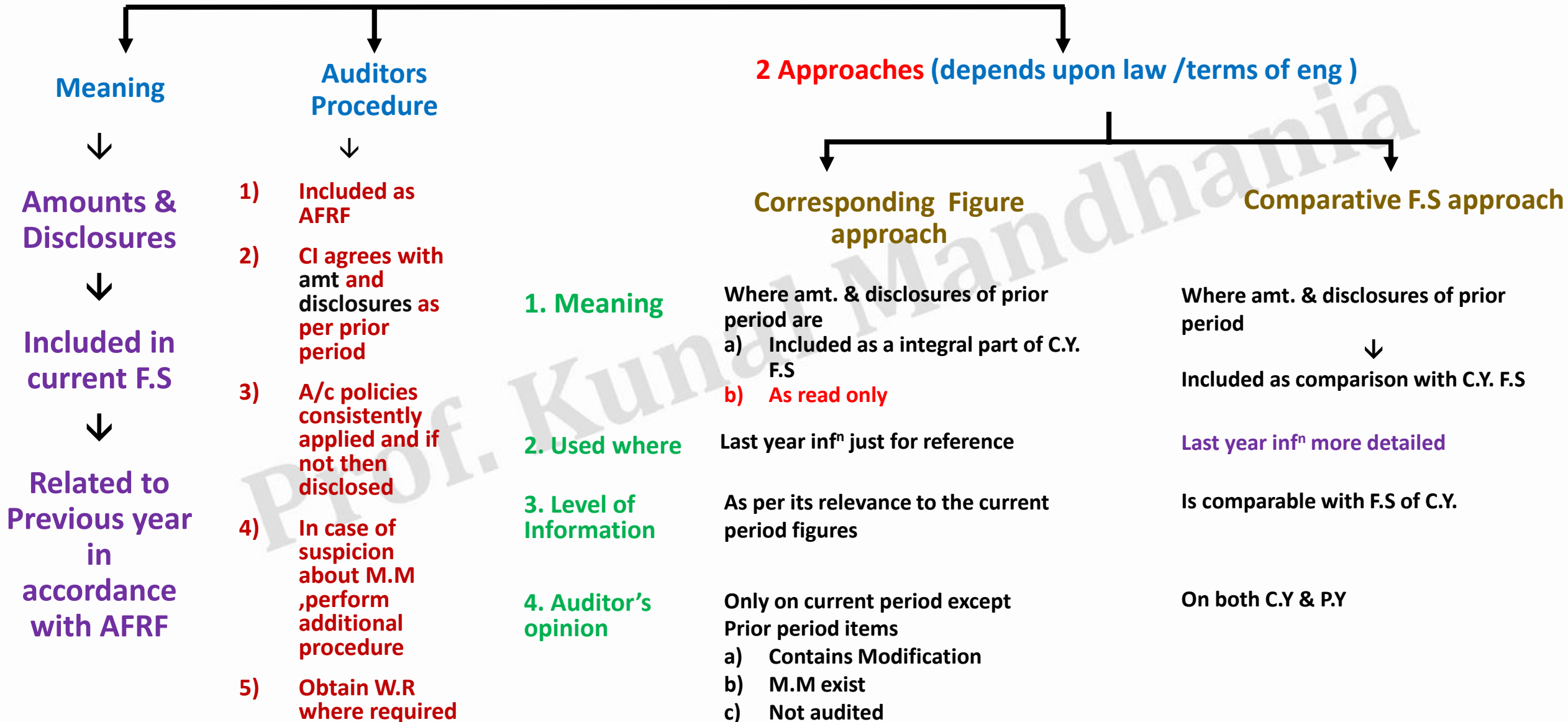
Examples where used

1. Audit not conducted in previous year (SA 510)
2. Someone else did audit during previous year (SA 510)
3. Audit of branch done by someone else (SA 600)
4. Reporting on distribution or use of audit report

Placed where

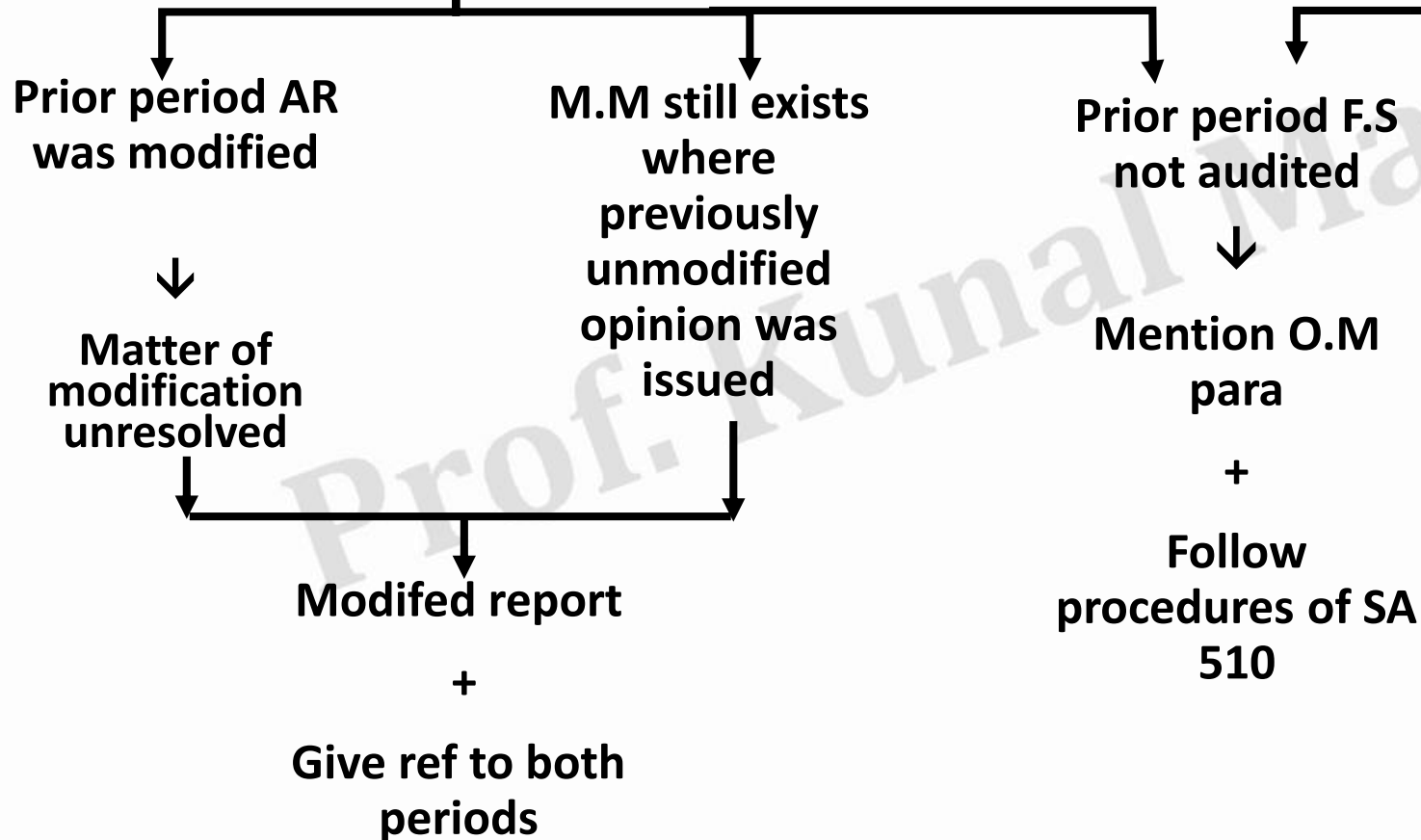
After EOM Para (if EOM present or after KAM para

SA 710 – Comparative Information corresponding figures & Comparative F.S



Decisions

Corresponding Figure approach



Comparative F.S approach

1. Previous opinion differs from current opinion
↓
Disclose reason in 'OM' para
2. Prior period F.S audited by Predecessor auditor
↓
State in OM para

Question

When corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in some circumstances. Explain those circumstances.

(MTP 5 Marks Aug '18, Sep 22, PYP 4 Marks Nov '19)

OR

The senior member of the firm Kaur & Associates, Chartered Accountants, informed to its auditing staff that at the time of audit reporting regarding corresponding figures, when corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in specified circumstances. What are those exceptional circumstances?

(PYP 4 Marks May'22)

Answer

When corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in the following circumstances.

1. If the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which gave rise to the modification is unresolved, the auditor shall modify the auditor's opinion on the current period's financial statements. In the Basis for Modification paragraph in the auditor's report, the auditor shall either:
 - (a) Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or
 - (b) In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.
2. If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements on which an unmodified opinion has been previously issued, the auditor shall verify whether the misstatement has been dealt with as required under the applicable financial reporting framework and, if that is not the case, the auditor shall express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, modified.
3. **Prior Period Financial Statements Not Audited-** If the prior period financial statements were not audited, the auditor shall state in an Other Matter paragraph in the auditor's report that the corresponding figures are unaudited. Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements

Question

NG Ltd. appointed CA N as the statutory auditor for the F.Y. 2021 -2022. Previous year's auditor gave a qualified opinion on the Comparative Financial Statements for the year ended 31.03.2021. What will be the reporting responsibility casted on CA N when he forms an opinion and prepares audit report on the Comparative Financial Statements for the F.Y. 2021-2022?

(PYP 4 Marks Nov 22)

Answer

Prior Period Financial Statements Audited by a Predecessor Auditor: As per SA 710, if the financial statements of the prior period were audited by a predecessor auditor, in addition to expressing an opinion on the current period's financial statements, CA. N, the auditor of NG Limited shall state in an Other Matter paragraph:

- (a) That the financial statements of the prior period were audited by a predecessor auditor;**
- (b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefor; and**
- (c) The date of that report, unless the predecessor auditor's report on the prior period's financial statements is revised with the financial statements.**

SA-299 Joint Audit of FS

Scope	Objective	Meaning	Other Important Points
<p>1.Deals with special consideration in carrying out audit by joint auditors</p> <p>2.This SA does not deal with relationship between principal auditor & branch / division / subsidiary / any other component auditor</p>	<p>1.To lay down board principles for conducting joint audit</p> <p>2.To give uniform approach to joint audit</p> <p>3.To identify areas of work & coverage by each auditor</p> <p>4.To identify individual & joint responsibility of joint auditors</p>	<p>Audit of company</p> <p>↓</p> <p>Performed by more than 1 CA / CA firm</p>	<p>1.JA is not compulsory</p> <p>2.If we are doing JA then for all Joint Auditors, it will be covered as 1 audit individually u/s 141(3)(g)</p>

SA-299 Joint Audit of FS

Advantages

BHAI LOGS

- 1.B –better quality
- 2.H – healthy competition
- 3.A – advantage of mutual consultation
- 4.I – improved services
- 5.L } **Lower Work load**
- 6.O }
- 7.G – greater cost savings
- 8.S – sharing of expertise

Disadvantages

CLIF

- C** – common work get neglected
- L** – lack of co-ordination
- I** – inferiority complex
- F** – fees sharing

Question

The practice of appointing Chartered Accountants as joint auditors is quite widespread in big companies and corporations. Explain stating the advantages of the joint audit.

(MTP 4 Marks April '23, RTP Nov '19, Old & New SM)

SA-299 Joint Audit of FS

Division of work

1. Division is not compulsory
2. Can be divided
 - a) periodwise
 - b) item in FS wise
 - c) areawise (regionwise)
 - d) unit wise (component wise)
3. Certain area of work which is important in nature may not be divided & carried on by all.

Responsibilities

Work divided



Specific / separate responsibility

NTE of audit procedures for work allocated to said auditor

Work not divided



Joint responsibility

1. Decisions taken by all Joint auditor together w.r.t. NTE of AP for common areas
2. Matters brought to the notice of Joint auditor by other Joint auditor & on which there is an agreement among auditors
3. Responsibility of evaluating information from management is generally a joint responsibility of all auditor

Note : Responsibility of evaluating information from management is generally a joint responsibility of all auditor

Question

HMB Limited's business has grown from one state of India to various countries of the world. Since the business has increased manifold, the management decided to appoint joint auditors for conducting the statutory audit of the company. They appointed three CA firms for it. For which audit work the joint auditors will be jointly & severally responsible?

(PYP 4 Marks Nov 22)

Requirements of SA 299

Responsibility & co-ordination among joint auditor

Co-ordination

During course of audit joint auditor shall communicate to other in writing prior to the completion of audit



Matters which are relevant to area of responsibility of other joint auditor



- 1. Require application of judgement by other joint auditor**
- 2. Deserve attention of other Joint auditor**
- 3. Require disclosure & discussion**

Requirements of SA 299

Audit Conclusion & Reporting

1. Before finalizing Audit report

JA shall discuss & communicate with other JA their respective conclusion



Audit Report

**Agreement w.r.t
opinion**



**Common
Audit report**

Disagreement w.r.t opinion



express their opinion in a separate AR



**JA is not bound by views of majority w.r.t. opinion or
matters to be covered in AR**



**Give reference under heading 'OM Para' as per SA
706**

Sec. 143(1) → Duty to enquire

- Enquire means to inquire & report only in case of discrepancy

S Security → Loan & Advance → Made by co.
 ↗ Properly secured
 ↘ Terms –prejudicial

B Mere book entries → Prejudicial to interest of Co.

I Investment in securities → Whether selling price < Purchase Price

D Deposits → Loan & Advance → Shown as deposits

P Personal expense → Charged to revenue a/c's

S Shares → Paid up → Actually cash received or not

Sec. 143(3)– Principal Assertions

I	Information & Explanation	→	Needed to be obtained	→	Has been obtained
A	A.S	→	Complied or not		
B	Books of accounts	→	Properly maintained		
B	B/s & P&L	→	In agreement with BOA		
B	Branch Audit Report	→	Timely submitted to H.A		
C	Control system	→	Adequate (financial control system)		
D	Directors	→	Disqualified	→	u/s 164(2)

Sec. 143(3)– Principal Assertions

E

Effect

→ Matters having adverse effect on functioning of company

F

Further Points (LL-Ladli Ladki – BIDA)

L-Pending **litigations**

L-Provision made

I-Delay

Company has
disclosed
impact

For material
foreseeable
losses

In transfer of
amount to **IEPF**

Holding & dealing with it

Between 15th Nov. 2016 to 30th

Dec. 2016

Amendment

After clause (d), the following clauses shall be inserted – Mnemonic -

(a)

(i)B- Whether the management has represented that, to the best of its knowledge and belief, other than as disclosed in the notes to the accounts,

- no funds have been advanced or loaned or invested (either from borrowed funds or share premium or any other sources or kind of funds) by the company
- to or in any other person(s) or entity(ies), including foreign entities (“Intermediaries”),
- with the understanding, whether recorded in writing or otherwise, that
- the intermediary shall, whether, directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the company (“Ultimate Beneficiaries”) or provide any guarantee, security or the like on behalf of the Ultimate **Beneficiaries**;

(ii) Whether the management has represented, that, to the best of its knowledge and belief, other than as disclosed in the notes to the accounts, no funds have been

- from any person(s) or entity(ies), including foreign entities (“Funding Parties”),
- with the understanding, whether recorded in writing or otherwise, that
- the company shall, whether, directly or indirectly, lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the Funding Party (“Ultimate Beneficiaries”) or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries; and

(iii) Based on such audit procedures that the auditor has considered reasonable and appropriate in the circumstances, nothing has come to their notice that has caused them to believe that the representations under sub-clause (i) and (ii) contain any material mis-statement.

(b) D- Whether the **dividend** declared or paid during the year by the company is in compliance with section 123 of the Companies Act, 2013.

(c) A-Whether the company, in respect of financial years commencing

- on or after the 1st April, 2022 has used such **accounting software** for maintaining its books of account which has a feature of recording audit trail (edit log) facility and
- the same has been operated throughout the year for all transactions recorded in the software and
- the audit trail feature has not been tampered with and the audit trail has been preserved by the company as per the statutory requirements for record retention

Question

The auditor shall make a report to the members of the company on the accounts examined by him.

Explain with reference to relevant provisions of the Companies Act, 2013.

(MTP 3 Marks March '23, RTP Nov '19, Old SM)

Question

The auditor's reporting on internal financial control will be applicable with respect to interim financial statements. Discuss

(MTP 3 Marks April '21 & April '23 PYP 2 Marks Nov

Answer

Clause (i) of Sub-section 3 of Section 143 of the Act requires the auditors' report to state whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls.

It may be noted that auditor's reporting on internal financial controls is a requirement specified in the Act and, therefore, will apply only in case of reporting on financial statements prepared under the Act and reported under Section 143.

Accordingly, reporting on internal financial controls will not be applicable with respect to interim financial statements, such as quarterly or half-yearly financial statements, unless such reporting is required under any other law or regulation.

In view of above, the given statement is incorrect.

Question

CA E was appointed statutory auditor of XYZ Private Limited in AGM held in the month of August, 2023 for the first time for audit of financial statements of the company from year 2023-24 onwards. Since he is new to the company, he wants to be sure about integrity of accounting records. In this regard, he wants to ensure that software used by company for maintenance of its books of accounts is capable of tracking user activities and changes made to entries in books of accounts, if any, during the course of year.

What CA E is looking for in the given situation? Discuss the reporting requirements for CA E in this matter to be included in audit report to be issued under the Companies Act, 2013.

(MTP 3 Marks Oct'23)

u3(12) → duty to report on Fraud: (A⁺)

- If fraud found (against the Co by officer/employee)

Attention AP

↓
Check Amt

[less than 1cr] → [Report to BOD/A-C]

[1 cr or more] → [To C.G.]

Report to Board/A-C

Report to Board/A-C
2 week for reply.

within
2 days

N → Nature of fraud
A → Amt involved
P → Parties involved

within
15 days

seek there (reply time)
reply.

Board/A-C

B.R⁺ report
to shareholder

Regd. Post
Ackn. due

Report to C.G. (MCA,
Secy)

within 15
days

form no- ADT-4.
comments - if no reply

N
A
P } same like
above.

R → Remedial
action taken.

Question

During the course of audit of PQR Ltd, the statutory auditor CA G came across payments made to various creditors aggregating to ` 75 lakhs. On verifying the same it is found that the accounts manager had accounted for fake invoices of credit purchases for ` 25 lakhs in the books of account in the name of one bogus creditor Mr. X.

Discuss the duties of auditor with reference to the provisions of Companies Act, 2013 and also the disclosure requirements in the Board's Report.

(PYP 4 Marks May '23)

Question

3. Which of the following is FALSE regarding UDIN? (Unique document identification number)

- (a) It is to be generated on UDIN portal.**
- (b) Its basic objective is to help ICAI in keeping and maintaining an online registry of different services provided by all of its members.**
- (c) It has to be generated and stated for each audit report signed by a Chartered Accountant.**
- (d) It has to be generated and stated for each certificate signed by a Chartered Accountant. (MTP 1 Marks Oct'22)**

B

Prof. Kunal Handhania

Question

4. UDIN (Unique Document Identification Number) is required to be stated by practising Chartered Accountant on: -

- (a) Each audit report only**
- (b) Each audit report and each certificate**
- (c) Each audit report issued under Companies Act, 2013 only**
- (d) Each audit report issued under Companies Act, 2013 only and each certificate (MTP 1 Mark Oct '23)**

B

Prof. Kunal Handhania

Teachers Note

- SA 600 – branch Audit in next revision Part

Prof. Kunal Mandhania

Chp 11-Ethics

A close-up photograph of a person's hand in a dark suit, holding a black fountain pen with gold accents and writing on a white document. To the left, a stack of three books is visible, with the top one having a grey cover. The background is softly blurred, showing a light-colored wall and a desk.

Kunal Mandhania

Professional Ethics

Meaning



Moral
principles



Governing



Person's
behavior or his
activity

Need



TRP



T → Trust creation
R → Create Respect &
confidence on
profession
P → Protect interest of
profession

Approaches



Principle based

- Comply with spirit of ethics
- Exercise professional judgement
- Flexible



Rules based

- Comply with established rules
- Exercise what written in rule
- Rigid.

Ethical Requirement / Fundamental principles of prof. ethics / Code of Conduct for Professionals

O → IC³ → P.B.

O → Objectivity →

➤ Don't compromise because of bias, conflict of interest or undue influence.

I → Integrity →

➤ SSH → Sincere, Straight forward, honest

➤ Fair dealing, truthful

➤ Don't associate with report, return, commⁿ



If info → false / misleading / omission

C → Competence →

➤ Professional knowledge & skill

C → Care →

➤ Act diligently → as per standards

C → Confidentially →

➤ Not disclose into to 3rd party except

➤ Law permission

➤ Client permits

PB → Professional behaviors →

➤ Avoid that discredits profession

➤ Don't engage → where integrity, objectives, reputation of profession can be questioned

Question

The IESBA Code establishes the fundamental principles of professional ethics relevant to the auditor when conducting an audit of financial statements. Discuss and also explain the meaning of ethics.

(RTP May '22)

(d) Professional Behaviour is one of the fundamental principles governing professional ethics. Explain its meaning. Also, give example of a situation where a Chartered Accountant fails to follow this principle.

(3 Marks) MTP Mar. 24

ANSWER

(d) The Principle of Professional Behaviour requires an accountant to comply with relevant laws and regulations and avoid any conduct that the accountant knows or should know might discredit the profession. A professional accountant shall not knowingly engage in any employment, occupation or activity that impairs or might impair the integrity, objectivity or good reputation of the profession, and as a result would be incompatible with the fundamental principles.

Example

A Chartered Accountant has conducted audit of accounts of an entity for a particular year. ICAI has issued a letter to him relating to certain matters concerning audit. He didn't even bother to reply to the letter despite reminders. Failure to reply to professional body smacks of lack of courtesy and professional responsibility. In the given case, Chartered accountant has not followed principle of Professional Behaviour.

(i) CA didn't
bother to reply

➤ Professional behavior

(ii) CA issue
wrong
certificate
specifying
wrong amt.

➤ Integrally

(iii) Signing. False
audit report
knowingly

➤ Integrity

Independent Audit

Meaning



➤ Judge of auditor



Is not subordinate to will / wishes of another person



Who has engaged him/ in his own interest

➤ Indep. Of mind & physical appearance (personal) (inter-linked)

Threats to independence



SSAFI



- 1) S → Self interest threat fin-interest
- 2) S → Self- review threat - previous eng. With client
- 3) A → Advocacy threat - Promote opinion
- 4) F → Familiarity threat too sympathetic
- 1) I → Intimidation defer from acting objectively

Approaches



WE-CID



- W → Work to eliminate threat
- E → Ethic Req. Practice
- C → Consider all threats
- I → Independence maintain
- D → Do not accept audit
- ↓
- If threats exist

Descriptive Questions

(d) CA Tripad (engagement partner) based at New Delhi is external auditor of Lap of Nature, a firm, since last three years. The firm is engaged in business of providing tourism services including holiday packages to its club members. It has also provided auditor including his team members free holiday for a week every year in one of its premium resorts in Ooty in the State of Tamil Nadu. The company has also booked free air travel for engagement team members during all these years. Discuss why Chartered Accountant is not acting ethically. How are familiarity threats created in above situation?

(3 Marks) MTP Mar. 24

ANSWER

(d) The firm is providing free hospitality to engagement team members including engagement partner. In such circumstances, fundamental principles governing professional ethics are violated. Such acts of free hospitality are capable of impairing objectivity of auditor.

The situation given in the question signifies that auditors have formed relationships with client where they may end up being too sympathetic to the client's interests. Due to free hospitality enjoyed by engagement team members, they may take a sympathetic view to issues which may have arisen during course of audit. In this way, familiarity threats are created in the situation.

SA 210- Agreeing upon terms of Audit Eng.

Objective



- i. Check whether pre-condition exist
- ii. Common understanding



Between client & auditor

Pre- condition of audit



- i. Mgt's FRF → should be acceptable to
- ii. Mgt. should accept it's responsibilities
- a) FS → Prepare & Present
- b) I.C.S → Design & Implement
- c) Provide Auditor with
 - i. All into rel. for audit
 - ii. Addⁿ into asked by auditor
 - iii. Unrestricted access to person within entity

AEL – Aud. Eng. Letter



1) Basics

- Prepare by Auditor
- Sent to client
- Compulsory

2) Purpose → (DATA)

- D → Define obj. & Scope
- A → Audit fees → base form
- T → Time for completion → decide
- A → Avoid mis-understanding

3) Mandatory Content (FOAAM)

- F → Form & content of A.R.
- O → Obj. & Scope of Audit
- A → AFRF → identify
- A → Auditor's Resp.
- M → Mgt.'s Resp.

Descriptive Questions

(d) The auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate. The agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement. Who gives engagement letter to whom and what is included in such a letter?

(3 Marks) (MTP April 24)

Discuss preconditions for an audit as per SA 210. Explain how would an auditor proceed to establish the presence of preconditions for an audit.

(RTP May '21, MTP 4 Marks Sep'22, PYP 4 Marks Dec'21)

Question

“An auditor who before the completion of the engagement is requested to change the engagement to one which provides a lower level of assurance should consider the appropriateness of doing so.” Discuss.

**(RTP May'18 & Nov '23, MTP 4 Marks
Mar'22)**

Answer

Acceptance of a Change in Engagement: An auditor who, before the completion of the engagement, is requested to change the engagement to one which provides a lower level of assurance, should consider the appropriateness of doing so. A request from the client for the auditor to change the engagement may result from a change in circumstances affecting the need for the service, a misunderstanding as to the nature of an audit or related service originally requested or a restriction on the scope of the engagement, whether imposed by management or caused by circumstances. The auditor would consider carefully the reason given for the request, particularly the implications of a restriction on the scope of the engagement, especially any legal or contractual implications. If the auditor concludes that there is reasonable justification to change the engagement and if the audit work performed complied with the SAs applicable to the changed engagement, the report issued would be appropriate for the revised terms of engagement. In order to avoid confusion, the report would not include reference to-

- (i) the original engagement; or
- (ii) any procedures that may have been performed in the original engagement, except where the engagement is changed to an engagement to undertake agreed-upon procedures and thus reference to the procedures performed is a normal part of the report. The auditor should not agree to a change of engagement where there is no reasonable justification for doing so.

If the terms of the audit engagement are changed, the auditor and management shall agree on and record

the new terms of the engagement in an engagement letter or other suitable form of written agreement. If the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted by management to continue the original audit engagement, the auditor shall-

- (i) Withdraw from the audit engagement where possible under applicable law or regulation; and
- (ii) Determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators.

Re- Curring
audit



New → NO →
AEL
???

When
AEL

➤ Misunderstanding

➤ Change

- Mgt.
- Owners
- AFRF
- Nature of business
- Legal Req.
- Rep. Req.

Question

An auditor who, before the completion of the engagement, is requested to change the engagement to one which provides a lower level of assurance, should consider the appropriateness of doing so. Explain the circumstances which may contribute towards a request from the client for the auditor to change the engagement.

(RTP Nov'22, Nov'19)

Professional & Skepticism

Meaning

Attitude

Questioning mind
Or
Being alert to sitⁿ
That shows
suspicion about
possible M.M

For critical
Assessment of
A.E

When / examples

- 1) Contradictory evidence
- 2) Doubt
 - a) Reliability of documents
 - b) Response to inquiry
- 3) fraud indications
- 4) S.A requirements to perform procedures

Purpose

To reduce audit risk

Not to

- Overlook unusual circumstances
- Over generalizing conclusion
- Inappropriate assumptions

Response

CIA

- i. C → Critical Assessment A.E.
- ii. I → Investigate partner
- iii. A → Audit procedures

Modify

Question

The auditor cannot be expected to disregard past experience of the honesty and integrity of the entity's management and those charged with governance. Nevertheless, a belief that management and those charged with governance are honest and have integrity does not relieve the auditor of the need to maintain professional skepticism. Explain.

(RTP Nov'22)

OR

Professional skepticism refers to an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence. The auditor shall plan and perform an audit with professional skepticism recognising that circumstances may exist that cause the financial statements to be materially misstated. Explain giving examples.

(MTP 4 Marks Sep '23, RTP Nov'20, PYP 4 Marks, Nov' 19)

SQC -1 & SA - 220

Basic



SQC -1 & SA – 220
both deals with
quality control
SQC -1 deals with
all types of
engagement



At firm level
(entire firm)



When we follow
such quality
measures &
particular audit i.e.
eng. Level



SA 220 applies

Req. of SQC-1



➤ Conduct audit using



- Standards
- Laws



Issue appropriate
report

➤ Assemble documents
& file



Within 60 days from A.R
date

➤ Audit documentation
is properties of
auditor

➤ Preserve for 7 yrs
from date of A.R

Elements of Q.C. System



LE – CHEM



- 1) L → Leadership
resp.
- 2) E → Ethical Req.
- 3) C → CCR (client
Continuous
Relationship)
- 4) H → H.R.
- 5) E → Eng.
Performance
- 6) M → Monitory

Difference of opinion between Eng .partners & reviewer



See What is
firm's policy to
take such
differences

Elements of Quality control system

Leadership Respon

➤ Policy & procedure

↓
To ensure that firm has inner culture to maintain quality

- Requires firm's
- Partners
- CEO to take responsibility for quality control system
- Such person shall have
 - Experience
 - Ability
 - Authority

Ethical Req.

- Policy & procedure that
 - Firm
 - It's personnel

↓
Are maintaining independence

- Requires to
 - **Communicate independence requirements**
 - **Identify threats to independence**
 - **Elements threats**
 - **Breach to be notified**
 - **Obtain confirmation about independence annually**

Client Continuance relationship

- Accept audit only after checking CCR

↓
ICES

- I → Integrity of Mgt. / ICMP/ TCWG.
- C → Competency of team
- E → whether team can comply ethical req.
- S → significant event happened recently

Human Resources

↓
Firm should have policies & procedure

↓
That it has sufficient personnel's with capability competency & commitment to ensure quality

↓
Addressed by

- P → Performance education
- P → Promotions
- RO → Recruitment
- C → Capable
- C → career development
- C → Compensation
- E → Estimation of personal (process) needs

Human Resources

↓
Policy & procedure to ensure quality measures are consistently applied

↓
By making

- M → manuals
- S → Software
- D → Documents
- G → Guidance notes

↓
To address matters

- BOSS DRS
- B → Briefing team
- S → Supervise team
- D → Document appropriates
- R → Review work
- S → Complying Standards

Eng. Performance

- Policy & Procedures to ensure that quality control system is

- ↓
- R → Relevant
- A → Adequate
- O → Operates Effectively
- Ongoing activity including periodic evaluation to evaluate quality control system
- Purpose

- ↓
- Evaluation of
- 1) Adherence to standards / legal requirements
- 2) Q.C System
 - a) Designed
 - b) Properly implemented
 - c) Applied effectively
- 3) Reports → Accurate

Question

Discuss the following:

The firm should establish policies and procedures designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, operating effectively and complied with in practice. Explain the purpose of monitoring compliance with quality control policies and procedures.

(MTP 4 Marks Oct'22, RTP Nov '19 & Nov '20)

SA – 220 : Maintany Qualets of Audit of F.S

Basis



- Premised on the basis that from is subject to SQC -1
- Deals & eng-level

Definition



- 1) **Eng-partner**
 - Firm partner
 - Other person (CA+COP)

↓

Responsible for audit
- 2) **Eng- team all personnel**
dairy audit includes expert
- 3) **Q.C. Review**
Process to evaluate judgement & opinion of eng-team
- 4) **Q.C reviswer**
 - Person (CA +COP)
 - Team (leader CA +COP)

↓

Appointed to do review

Responsibility of Eng. Partner

1) Leadership Resp.

- Primarily responsible to maintain quality of audit of F.S.

2) Ethical Requcurst

- Ensure team is independent
- Take action to eliminate threats to independents

3) Client continuar is retitonty

- Accept audit only after checking C.C.R

4) Human Resources

- Responsible to appoint team
- Ensure team is competent ,capable to do audit

5) Eng. Perf.

- DRS (direct, supervise review their work)
- Consult in care of difficult
- Ensure following standard, legal & profess req

6) Monitority

- Ensure reviewer appⁿ
- Ensure review conducted as per firms policy
- Proper monitory activity
- Not to sign A.R till review is performed

(e) An engagement partner takes overall responsibility for maintaining audit quality in an audit engagement in accordance with SA 220. What are his objectives in taking and emphasizing such responsibility?

(3 Marks) MTP Mar. 24

Question

As per SA 220, the engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned. While taking responsibility for the overall quality on each audit engagement, analyse and explain the emphasis of the actions of the engagement partner and appropriate messages to the other members of the engagement team . Also define engagement partner.

(MTP 5-Marks Aug '18, RTP Nov'20 & May '23, PYP 3 Marks Nov'19)

Question

4. _____requires firms to establish policies and procedures for the retention of The retention period for audit engagements ordinarily is no shorter than from the date of the auditor's report, or, if later, the date of the group auditor's report

(RTP May '22)

- (a) SA 220, audit evidence, six years**
- (b) SA 200, audit documentation, seven years**
- (c) SQC 1, engagement documentation, seven years**
- (d) SA 230, documentation, six years**

C

Prof. Kuldeep Mandhania

25. “SA 220 is premised on the basis that the firm is subject to SQC 1”. What do you understand by given statement in context of audit quality?

(RTP May 24)

ANSWER

25. Audit quality is essential to maintain confidence in the independent assurance provided by the auditors. It is responsibility of auditor to maintain high audit quality. SQC 1 and SA 220 both deal with quality control. SQC 1 applies to entire firm. However, SA 220 applies to a particular audit engagement.

Based upon quality control system of firm established in accordance with requirements of SQC 1, quality control policies pertaining to audit engagements are decided by engagement teams. Engagement partner of a team is responsible for quality control procedures of a particular audit engagement in accordance with SA 220.

Therefore, SA 220 is premised on the basis that the firm is subject to SQC 1. Within the context of the firm's system of quality control, engagement teams have a responsibility to implement quality control procedures that are applicable to the audit engagement.

2. Audit strategy , Audit Planning

Kunal Mandhania



Audit Strategy

Meaning



Setting

S :- Scope

T :- Timing

D :- Direction

Of Audit

Benefits



Resources



Q :- Quality

Q :- Qty.

T :- Timing

M :- Manger

Factors Consider



RESPONCE

R :- Reporting objective → time table ,meeting, types of report

E :- Eng. Characteristic → Components Segments location

S :- Sign Factors → Imp to direct teams effort

P :- PEA → Consider results

N :- NTE → Resources

Question

In establishing overall audit strategy, the auditor shall ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required. Elucidate those cases by which auditor can ascertain the reporting objectives of the engagement.

(MTP 4 Marks Nov '21 & April '23, RTP Nov'23, PYP 4 Marks Nov '19)

Answer

In establishing the overall audit strategy, auditor shall ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required. The cases by which auditor can ascertain the reporting objectives of the engagement are:

- (i) The entity's timetable for reporting, such as at interim and final stages.
- (ii) The organization of meetings with management and those charged with governance to discuss the nature, timing and extent of the audit work.
- (iii) The discussion with management and those charged with governance regarding the expected type and timing of reports to be issued and other communications, both written and oral, including the auditor's report, management letters and communications to those charged with governance.
- (iv) The discussion with management regarding the expected communications on the status of audit work throughout the engagement.

Question

In establishing the overall audit strategy, the auditor shall identify the characteristics of the engagement that define its scope. Explain with example.

(RTP May '23)

Answer

In establishing the overall audit strategy, the auditor shall Identify the characteristics of the engagement that define its scope.

For Example:

- The expected audit coverage, including the number and locations of components to be included.**
- The nature of the business segments to be audited, including the need for specialized knowledge.**
- The expected use of audit evidence obtained in previous audits, for example, audit evidence related to risk assessment procedures and tests of controls.**



Audit Plan

Meaning

Overall plan

Includes

NTE of Audit procedures

- More detailed than strategy

Factors to be considered in developing plan

TRAINING DAYS

- T :- Terms of Aud. Eng.
- R :- Result of RAP
- A :- App. Laws
- I :- Involvement of other auditor
- N :- NTE of AP
- I :- Identification of Key check
- N :- NTE of reporting
- G :- Get knowledge of Client's business
- D :- Degree of reliance on ACC Sys. & ICS
- A :- Allocation of Stock

Benefits of plan/planning

P-SCAMS

- P- potential problems – identify and resolve
- S- Select right team members
- C- Coordination
- A- Attention to key areas
- M- Manage Audit efficiently and effectively
- S- Supervise team

Other IMP Points

- Benefits → P – SCAMS
- Continuous = ✓
Discrete = ✗
- Change TQ[CUE]
 - Change in Circumst
 - U :- Unexpected event
 - E :- Evidences
- Document = Planning memorandum
- Plan → NTE of DSR = Factors (Size of CAR)
 - Size of Entity
 - Complexing of Fronsection
 - Area of audit
 - Romm

**"An adequate planning benefits the audit of financial statements."
Discuss.**

**(MTP 4 Marks Sep'22 & March '23,
PYP 5 Marks, Nov '18, RTP May '19,
May '23, Nov '19, Nov '21, May '18)**

Question

The nature, timing and extent of the direction and supervision of engagement team members and review of their work vary depending on many factors. Discuss those factors.

(RTP Nov'22, Nov '21, Old & New SM)

Knowledge Of Clients Business

Factors



State of Economy

Nature of Industry

Regulatory Requirement

Ownership & Structure

Financing & Structure

types of Investments

Nature of operations

Financial Reporting
Framework

Selection & Application
of Accounting Policies

Financial Performance
Objectives.

Shortcut :- From Macro to Micro

Question

“The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client’s business” Discuss stating clearly the broad points you would be covering in framing plan to conduct audit in an efficient and effective manner.

(MTP 4 Marks March), (19, MTP 5 Marks March '18), (RTP Nov 18, Nov 19 & May '19, May'23)

Audit Programme

Meaning

Seres of verification
procedure on A/c's
& F.S

➤ Detaied plan of
how to do audit

➤ List of
examination
procedure

➤ 3 golden rules

- i) One prog. Not for
all client
- ii) Assistant keep
open mind
- iii) Periodic review

Rules / Pts. To be kept in
mind to develop a A Prog.

Written SCOPE

- i) Always in writing
- ii) **S** :- Stay within scope &
limitation
- iii) **C** :- Co-ordinate all
procedure
- iv) **O** :- Only useful steps to
be perf.
- v) **P** :- Possibilities of error
consider
- vi) **E** :- Best evidence

Advantage

COVER – Shortcut

- 1) Kya :- work to be
performed (**Checklist**)
- 2) Kaise :- AP to be
performed
(**Perspective**)
- 3) Kaun :- Allocation of
staff (**Staff select &
Resp. Fix**)
- 4) Kab :- Time Frame
(**Timely complete**)
- 5) General Point
 - i. Evidence against
Ehage. Of Neglieness
 - ii. Basis of report
 - iii. Future Audits helpful

Disadvantage

- i) Mechanical
- ii) Rigd.
- iii) Efficient staff
↓
Lack of initiative
- iv) Inefficient staff
↓
Shelter

Question

XYZ & associates are appointed as the statutory auditors of Fisco Ltd. for the FY 2021 -22. While constructing the audit programme, the engagement partner, CA X, should keep in mind various points. List such points.

(MTP 4 Marks Oct'22)

OR

Arpan Hospitals Ltd having Gross Professional Charges of ` 50 crores are engaged in providing healthcare services. STP & Co., a firm of auditors is appointed as its auditors.

Advise what special points to be kept in mind for the purpose of construction of an Audit programmer. Explain.

(RTP May '18 & Nov '22, PYP 3 Marks, May '19)

OR

Discuss the points to be considered by auditor for the purpose of constructing an audit program me. (PYP 4 Marks Nov,19)

Question

CA Vikas Jain discussed with his audit team about advantages and disadvantages of audit programme. He explained to his team that –“work may become mechanical” as disadvantage of the audit programme. Discuss explaining the disadvantages of an audit programme

(MTP 4 Marks March 22)

Question

As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan. Explain

(RTP Nov '19 & Nov '18, PYP 2 Marks May 22)

Question

Explain what do you mean by documentation of audit plan. Discuss the purpose served by it and also elaborate the tools used by the auditor to reflect the particular engagement circumstances.

(RTP Nov'22)

Answer

The documentation of the audit plan is a record of the planned nature, timing and extent of risk assessment procedures and further audit procedures at the assertion level in response to the assessed risks. It also serves as a record of the proper planning of the audit procedures that can be reviewed and approved prior to their performance.

The auditor may use standard audit programs and/or audit completion checklists, tailored as needed to reflect the particular engagement circumstances

Question

The agreed terms of the audit engagement shall be recorded in an audit engagement letter or other

suitable form of written agreement and shall include:

- (i) The objective and scope of the audit of the financial statements;
- (ii) The responsibilities of the auditor;
- (iii) The responsibilities of management;
- (iv) Identification of the applicable financial reporting framework for the preparation of the financial statements; and
- (v) Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

Which of the following is correct?

- (a) (i),(ii),(iii)
- (b) (i),(ii),(iii), (iv), (v)
- (c) (iz), (ii), (iv), (v)
- (d) (i),(ii),(iii), (iv)

(MTP (1 Marks March 22))

B

Prof. Kunal Mandal

Question

sets the scope, timing & direction of the audit and guides the development of the more detailed plan.

- (a) Audit Programme**
- (b) Overall Audit Strategy**
- (c) Completion Memorandum**
- (d) Audit Plan**

(MTP 1 Mark April 22)

B

Prof. Kunal Mandal

Question

The overall audit strategy and the audit plan remain the responsibility.

- a) auditor's**
- b) management's**
- c) those charged with governance.**
- d) both management and those charged with governance.**

(MTP 1 Mark March '23)

A

Prof. Kunal Mandal

Question

Which of the following statements is MOST APPROPRIATE?

- (a) Audit programme is a detailed plan of audit strategy**
- (b) Audit programme cannot be reviewed**
- (c) Audit programme is a detailed plan of applying audit procedures**
- (d) Audit programme is relevant for year for which it is prepared, it is useless for subsequent years.**

(RTP Nov'22)

C

Prof. Kunal Mandhania

6. Documentation

A close-up photograph of a person's hand in a dark suit, holding a black fountain pen with gold accents, writing on a white document. To the left, a stack of several books is visible, slightly out of focus. The background is a soft, blurred indoor setting.

Kunal Mandhania

SA – 230 : Audit Documentation

Meaning

Record of

- ✓ Planning
- ✓ Procedure performed
- ✓ Evidences collected &
- ✓ Opinion formed
- Physical / electronic form / other media
- Audit file

One or more folder

Physical electronic

Maintaining record

- Prepare simultaneously as audit progress
- Can show to client

At his discretion

- Cannot show to 3rd party

Violates confidentiality

IMP Pts.

➤ Property of Auditor

➤ Retention period

7 yrs from date of
A.R.

➤ Assembly period

60 days from date of
A.R

Advt. / Function / Utility / purpose

IPFADE²

I → Inspection

Internal or external

P → Plan & perform audit

Help

F → Future audit

Reference

A → Accountability

Held

D → DSR (help)

E → Evidence

plan & performed as per
SQC/SA'S / COC

E → Evidence

Against charge of negligence

Assembly of Audit file

SQC -1

➤ Administrative process

➤ Within 60 days from date of
A.R.

➤ Here, no new procedure
performed, no new evidence
collected, no change in A.R.

➤ Mainly done for
CDS

C → Collate

C → Cross reference

D → Delete

D → Discard

S → Supersede

S → Sort

The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis. Explain in detail.

(RTP Nov '23, May'23, Nov '18 & May '22)

Question

CAM is the engagement partner of S Ltd. He has instructed his audit team to maintain proper audit documentation. The audit team members are not sure about the purpose for which the documentation should be made. Explain the various purposes of audit documentation with reference to SA 230.

(PYP 3 Marks Nov 22)

Audit Documentation refers to the record of three items. Explain stating clearly the objective and nature of audit documentation. (RTP Nov '23)

Hint - Functions

Descriptive Questions

14. Rajni, a CA student, has understood that SA 230 requires auditor to prepare audit documentation on a timely basis. While reading about SQC 1, she notices that time limit for completion of final audit file is ordinarily not more than 60 days after the date of auditor's report. She finds it to be puzzling. Unable to comprehend, she seeks your guidance. Guide her.

(RTP May 24)

ANSWER

14. SA 230 requires that the auditor shall prepare audit documentation on a timely basis. Preparing sufficient and appropriate audit documentation on a timely basis helps to enhance the quality of the audit and facilitates the effective review and evaluation of the audit evidence obtained and conclusions reached before the auditor's report is finalized.

SQC 1, however, requires auditor to complete assembly of final audit file in ordinarily not more than 60 days after the date of the auditor's report. The completion of the assembly of the final audit file after the date of the auditor's report is only an administrative process that does not involve the performance of new audit procedures or the drawing of new conclusions.

Therefore, auditor shall prepare documentation on a timely basis. However, for completion of assembly of final audit file which is an administrative process, time period of 60 days after the date of auditor's report has been required in SQC 1.

SA – 230 : Audit Documentation

Completion Memorandum



- 1) **Summary of**
 - Significant matters found during audit &
 - How they were addressed
- 2) **Purpose**
 - i. **Effective & efficient**
↓
Review & inspection
 - ii. **Consider all significant matters**
 - iii. **Help in formally right conclusion as per SA.**

Form, content & extent of documentation

Factors



Size & nature of CARE²



- 1) **Size of entity**
- 2) **Nature of A.P. performed**
- 3) **C – complexity of transaction**
- 4) **A – Audit tools & methodologies used**
- 5) **R – ROMM**
- 6) **E – Evidence – obtained**
- 7) **E – Exceptions**

Examples of significant matters



DREAM

- 1) **D → Difficulty in performing A.P.**
- 2) **R → Risk – high**
- 3) **E → EOM para invoice**
- 4) **A → Audit procedure result**
↓
 - a) MM can exist
 - b) Revise risk assessment
- 5) **M → Matters → modify opinion**

15. Discussing meaning of completion memorandum, elaborate upon its importance.
(RTP May 24)

(d) What is meant by audit documentation? What are objectives of an independent auditor in accordance with SA 230?

(3 Marks) MTP Mar. 24

ANSWER

(d) Audit documentation refers to the record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached. The objective of the auditor in accordance with SA 230 is to prepare documentation that provides: -

(i) A sufficient and appropriate record of the basis for the auditor's report and

(ii) Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.

(d) One of the factors affecting the form, content and extent of audit documentation relates to size and complexity of the entity. State six other factors in this respect.

(3 Marks) (MTP April 24)

Question

The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor to understand significant matters arising during the audit. Explain the above statement and also give examples of significant matters.

(RTP Nov'22)

4. Judging the significance of a matter requires _____ of the facts and circumstances.

- (a) objective analysis**
- (b) subjective analysis**
- (c) Both subjective and objective analysis**
- (d) qualitative analysis (MTP 1 Mark April 22, RTP Nov'19)**

A

Prof. Kunal Mandal

Question

5. CA Amar is the statutory auditor of XYZ Ltd. for the FY 2020-21. During the process of assembling the audit

file, CA Amar briefed his team as to what all changes can be made to the audit documentation at that stage. Which of the following changes cannot be made to the audit documentation during the final assembly process?

- (a) Sorting, collating & cross referencing of working papers.**
- (b) Signing off completion checklists relating to the file assembly process.**
- (c) Deleting or discarding superseded documents.**
- (d) Recalculation of Depreciation. (MTP 1 Mark March '23)**

D

Prof. Kuldeep Sandhania

Question

6. The auditor may consider it helpful to prepare and retain as part of the audit documentation a summary (sometimes known as a completion memorandum) that describes-

- (a) evidence identified during the audit**
- (b) the significant matters identified during the audit and how they were addressed**
- (c) the significant evidence identified during the audit**
- (d) the significant matters identified during the audit**

(MTP 1 Marks April '23)

B

Prof. Kunal Mandal

Question

8. A company has started its manufacturing operations from a newly constructed building. CA Z is statutory auditor of company. Which of following is not likely to be an example of audit documentation?

- (a) E-mail correspondence with CFO of company concerning significant matters**
- (b) Audit programme**
- (c) Response to external confirmation requests**
- (d) Structural engineer's report on strength of building (MTP 1 Mark Oct '23)**

D

Prof. Kuldeep Sandhania

Question

9. refers to the record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached.

- (a) Audit Techniques**
- (b) Audit evidence**
- (c) Audit Documentation**
- (d) Audit Procedures record (MTP 1 Mark March '23)**

C

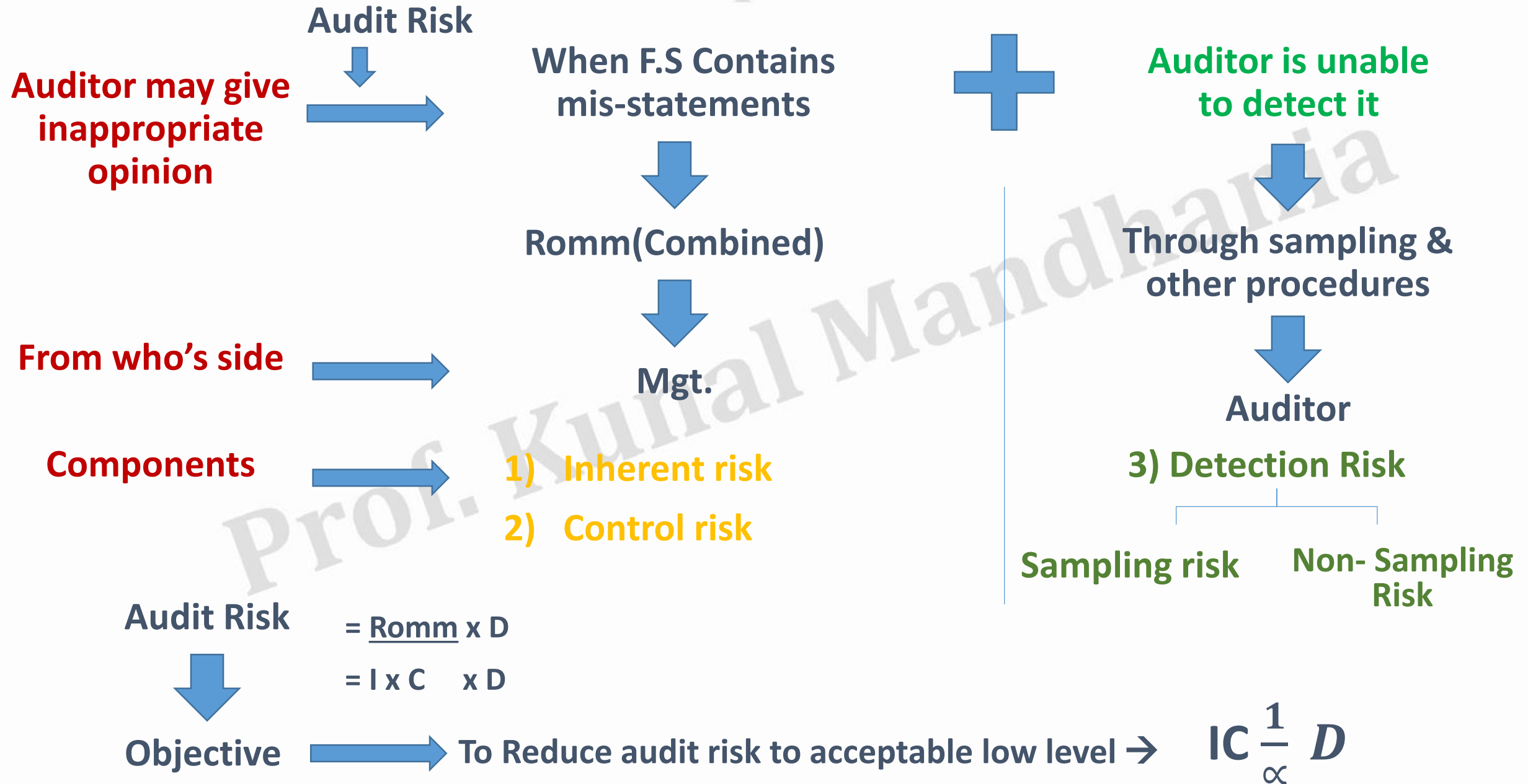
Prof. Kunal Mandhania

3. Risk assessment and Internal Controls

Kunal Mandhania



Risk assessment and Internal Controls



Audit Risk

(Risk that auditor may give inappropriate opinion → when F.S. is materially misstated → Auditor is unable to detect it)

Components (CID)

Risk that FS are materially misstated before (prior) to Audit

Inherent Risk

→ Romm

Control Risk

Detection Risk

Meaning

↓
Basic Susceptibility
↓
Of Mis-Statements (Amt. Classification, Prese, disclosure)
↓
In F.S
↓
Assuming there is no I.C.S.

↓
When I.C.S is unable to
P :- Prevent
D :- Detect
C :- Correct
↓
Mis-Statements

↓
That auditor's procedures
↓
Will not be able to detect mis-statements in F.S.

Reasons

1. Nature of entity
2. Mgt. Integrity & Knowledge
3. Wrong application of a/c policies

Inherent limitation of I.C.S.

Inherent limitation of audit

Question

You are appointed as an auditor of Gama Ltd. Your audit assistant wants to understand the meaning of Audit Risk. Explain him the meaning of Audit Risk with example. Also guide him as to what is not included in Audit Risk.

(PYP 4 Marks May '23)

Descriptive Questions

5. Satranga Foods Private Limited is engaged in manufacturing of pickles. The auditors of the company have planned audit procedures in respect of recognition of revenues of the company. Despite that, there is a possibility that misstatements in revenue recognition are not identified by planned audit procedures. Identify and explain that particular risk in detail.

(RTP May 24)

ANSWER

5. There is a possibility that planned audit procedures may not achieve desired result and fail to detect misstatements in revenue recognition. Such a risk is referred to as “detection risk”.

SA 200 defines detection risk as the risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

For example, auditor of a company uses certain audit procedures for the purpose of obtaining audit evidence and reducing audit risk, but still there will remain a risk that audit procedures used by the auditor may not be able to detect a misstatement which by nature is material, then that risk is known as detection Risk.

Detection risk comprises sampling and non-sampling risk.

(a) 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. It simply means that the sample was not representative of the population from which it was chosen.

(b) Non-sampling risk is the risk that the auditor reaches an erroneous conclusion for any reason not related to sampling risk. Like an auditor may reach an erroneous conclusion due to application to some inappropriate audit procedure.

SA 315 : Identify and assess → Romm through understanding entity and its environment

Objective	How to Identify and assess Romm	Risk assessment procedure	Understanding entity & its environment
<p>↓</p> <p>Identify and assess</p> <p>↓</p> <p>Romm</p> <p>@</p> <p>i) F.S level</p> <p>ii) Assertion level</p>	<p>(I-ARC)</p> <p>↓</p> <p>1) I-Identify Risk</p> <p>Through</p> <ul style="list-style-type: none">- Understanding entity & environment- I.C.S study <p>2) A-Assess risk</p> <p>Related</p> <ul style="list-style-type: none">- F.S level- Assertion level <p>3) R-Relate risk to what can go wrong</p> <p>4) C-Consider likelihood of mis-statement or multiple misstatement</p>	<p>Meaning</p> <p>↓</p> <p>A.P.</p> <p>↓</p> <p>To obtains</p> <p>↓</p> <p>- understanding of entity & environment &</p> <p>- I.C.S</p> <p>↓</p> <p>to identify & assess r Romm</p> <p>↓</p> <p>Due to fraud or error</p> <p>↓</p> <p>i) F.S Level</p> <p>ii) Assertion level</p> <p>Includes</p> <p>↓</p> <p>O :- ICAI</p> <p>↓</p> <p>OI :- Observation and Inspection</p> <p>O :- Entity's operation</p> <p>O :- Visit premises/ plant</p> <p>I :- Inspect Documents , records, control manually</p> <p>I :- Inspect - Reports by Mgt. TCWG</p> <p>A :- ARP → Analytical review procedure</p> <p>Identify unusual or unreasonable transaction</p> <p>↓</p> <p>Help to asses Romm specially fraud</p> <p>I :- Inquiry</p> <p>i) Mgt.</p> <p>ii) TCWG</p> <p>iii) Internal Auditor</p> <p>iv) Other auditor legal counsel</p> <p>v) Employee</p>	<p>↓</p> <p>Factor check</p> <p>↓</p> <p>i) Study economic environment, nature of industry, AFRR, regulatory req. (laws)</p> <p>ii) Check ownership / financial / investment structure</p> <p>iii) Operations → nature</p> <p>iv) Select and apply a/c policies</p> <p>v) Study fin. Performance Budgets/ credit agency report, F.S</p> <p>vi) Objectives, strategies, risk mgt. process.</p>

(b) The objective of an auditor in accordance with SA 315 is to identify and assess risks of material misstatement at financial statement level and assertion level. Which specific activities an auditor is required to perform for the purpose of identifying and assessing risks of material misstatement?

(4 Marks) MTP Mar. 24

Question

Discuss the steps to be taken by the auditor for the purpose of Identifying and assessing the risks of material misstatement as per SA 315. (MTP 4 Marks Sep'22)

Hint - IARC

Question

As per SA-315, “Identifying and Assessing the Risk of Material Misstatement through Understanding the Entity and Its Environment”, the auditor shall obtain an understanding of the relevant industry, regulatory and other external factors including the applicable financial reporting framework. Explain giving examples.

(MTP 4 Marks Sep ‘23)

Question

Risks of material misstatement may be greater for significant non-routine transactions arising from matters such as complex calculations. Also, risks of material misstatement may be greater for significant judgmental matters that require the development of accounting estimates, arising from matters such as accounting principles for accounting estimates may be subject to differing interpretation etc. Explain in detail.

(MTP 3 Marks Oct'23, RIP Nov '21)

Answer

Risks of Material Misstatement– Greater for Significant Non-Routine Transactions

Risks of material misstatement may be greater for significant non-routine transactions arising from matters such as the following:

- Greater management intervention to specify the accounting treatment.
- Greater manual intervention for data collection and processing.
- Complex calculations or accounting principles.
- The nature of non-routine transactions, which may make it difficult for the entity to implement effective controls over the risks.

Risks of material misstatement– Greater for Significant Judgmental Matters

Risks of material misstatement may be greater for significant judgmental matters that require the development of accounting estimates, arising from matters such as the following:

- Accounting principles for accounting estimates or revenue recognition may be subject to differing interpretation.
- Required judgment may be subjective or complex, or require assumptions about the effects of future events, for example, judgment about fair value.

Descriptive Questions

6. (a) Auditor of Sunshine Ltd. is of the view that due to greater management intervention to specify accounting treatment, the risk of material misstatement is greater for non-routine transactions. Is view of the auditor correct? Specify the other matters due to which the risk of material misstatement is greater for significant non-routine transactions.

(4 Marks) (MTP April 24)

Risk of material misstatement refers to the risk that the financial statements are materially misstated prior to audit. Discuss the levels at which this risk exists.

(RTP Nov '23 & Nov 20)

Internal Controls

Meaning

Process



D:- Designed

I :- Implemented

M- Maintained



By mgt. TCWG, personnel



To obtain R.A.



That entity's objective has been achieved



With regards to (RAEES)

R:- Reliability of F.R.

A: Applicable laws →
comply

EE:- Efficient & Effectively
conduct of operations

S :- Safeguarding of assets

Purpose objective of I.C.S



Basic

+

2 3 4 5

RAEES

P :- Prevention

D :- Detect

C-Correct of
misstatement

+

RAEES

Benefits of understanding



i) Identify

Romm

ii) Identify

potential

misstatement

iii) Decide NTE

of Further

A.P.

Limitations of I.C.S



1. Cost effective

Cost > Benefit

When we apply best system

2. Small entities

- Less employees

- Owner's interference is more

- ↓

- Good system not req.

3. Human error

Humans is system bound to make errors

4. Collusion among employees

Segregation of duty fails if employees

collude & over rides control

5. Abuse of authority

Authority abuses their power can over

ride controls

6. Manipulation of mgt.

7. System can give only R.A.

8. Lack of understanding the purpose

Components of I.C.S



CRIME



1) Control

activity

2) RAP

3) Into System

4) Monitoring

of controls

5) Control

environment

Question

The division of internal control into five components provides a useful framework for auditors to consider how different aspects of an entity's internal control may affect the audit. Mention those components of internal control.

(MTP 4 Marks Oct '20, Oct '21, MTP 3 Marks Mar'23, RTP May 23)

Briefly discuss the limitations of Internal Control.

(MTP 4 Marks April 19, PYP 6 Marks May '18, RTP May '23)

Component of I.C.S

Control Environment



3a



Attitude, action & awareness



Of mgt. & TCWG



Regarding I.C.S . It's importance

Elements of Control Environment
(T.Q)(B)



Hope → TCA



- 1) H :- H.R Policies
- 2) O :- Org. Structure
- 3) P :- Mgt. philosophy & Operating style
- 4) E :- Ethical values, integrity of mgt / TCWG
- 5) T :- TCWG .
Knowledge, exp. Involvement
- 6) C :- Commitment to competence
- 7) A :- Assignment of Authority

Risk Assessment Procedure within entity



Process to

I :- Identify risk

D :- Decide action on risk

E :- Estimate significant of risk

A :- Assess likelihood of occurrence

Into system (A/c System)



Transactions

initiate, record process correct



records maintains



Capturing event which are significant for F.S



Prepare F.S

Monitoring



Ongoing activity to evaluate effectiveness of I.C.S and take remedial action

Control Activity



✓ Policy & procedure to ensure mgt's directive are followed.

✓ Directives related to

- Performance analysis
- Info processing
- Physical controls (Stock / Assets)
- Segregation of duties

Question

The auditor shall obtain an understanding of the information system, including the related business processes, relevant to financial reporting, including the classes of transactions in the entity's operations that are significant to the financial statements, controls surrounding journal entries etc. Explain the other considerations in this regard.

(MTP 4 Marks April 22 & Sep '23, RIP May '21)

Answer

The auditor shall obtain an understanding of the information system, including the related business processes, relevant to financial reporting, including the following are as under:

- (a) The classes of transactions in the entity's operations that are significant to the financial statements;
- (b) The procedures by which those transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements;
- (c) The related accounting records, supporting information and specific accounts in the financial statements that are used to initiate, record, process and report transactions;
- (d) How the information system captures events and conditions that are significant to the financial statements;
- (e) The financial reporting process used to prepare the entity's financial statements;
- (f) Controls surrounding journal entries.

Question

Explain what understanding should an auditor obtain regarding an entity's risk assessment process (one of the components of the internal control of the entity).

(MTP 3 Marks Oct'22)

***Risk which are significant or require special attention or consideration TQ (A)**



FORCED



- 1) **F** :- Fraud
- 2) **O** :- Outside normal course of business
- 3) **R** :- Related Party transaction (RPT)
- 4) **C** :- Complex or unusual transactions
- 5) **E** :- Estimation uncertainty high
E.g. warranty obligation
- 6) **D** :- New Developments

Question

In exercising judgment as to which risks are significant risks, the auditor shall consider various factors. Explain.

(MTP 4 Marks Oct'22, RTP May '18)

OR

As a part of Risk assessment, the auditor shall determine whether any of the risks identified are in the auditor's judgement a significant risk. Mention any three guiding factors to judge as to which risks are significant risks?

(PYP 3 Marks May '23)

OR

Significant risks often relate to significant non- routine transactions or judgmental matters. Non-routine transactions are transactions that are unusual, due to either size or nature, and that therefore occur infrequently. Judgmental matters may include the development of accounting estimates for which there is significant measurement uncertainty.

In context of significant risk, explain the factors to be considered by the auditor in exercising judgment as to which risks are significant risks.

(MTP 4 Marks Sep '23, RTP Nov 21)

*Which Controls are relevant for Audit



Size and Nature of CARE matters



- 1) Size of entity
- 2) Nature of business
- 3) C :- Complexity of operations
- 4) A : - Applicable laws
- 5) R :- ROMM
- 6) E :- Established components of I.C.S.
- 7) Matter → Materialities

Question

Factors relevant to the auditor's judgment about whether a control, individually or in combination with others, is relevant to the audit may include such matters as materiality, size of the entity etc. Explain the other relevant considerations in the above context.

(MTP 3 Marks March 22, RTP May 21, RTP Nov'22)

Question

The auditor's responsibility includes reporting on Internal Financial Controls over Financial Reporting which includes an understanding IT environment of the company and relevant risks and controls. Mention the situations where IT will be relevant to an audit.

(RTP May '23)

Evaluate → 4 tools / methods

Tools	Meaning	Advt.	Disad.
1. Narrative Record	Complete and exhaustive description of system found by auditor/ audit staff.	i) Suitable for small business ii) Suitable where no formal system is made	i) Weakness in fin system cannot be easily located ii) Comprehension and summarization requires skill iii) Time consuming
2. Check List	Series of questions ↓ Prepared by Auditor ↓ Answer by audit staff	i) Weakness can be entity located ii) Saver time	It requires skill to & experience to prepare questions
3. Internal control Questionnaire	Series of questions ,prepared by auditor ↓ Answer by client / employee	i) Weakness can be easily located ii) Time saver	-----” -----
4. Flowchart	Graphical representation of each part of I.C.S	i) Concise view ii) Bird eye view iii) No need to read narrative or reply again	<ul style="list-style-type: none"> Weakness cannot be easily located Time consuming to prepares flowchart

Descriptive Questions

(d) Internal Control Questionnaire is a comprehensive series of questions concerning internal control. A company is engaged in business of manufacturing of chemicals. It has two plant locations in city “A” and one plant location in city “B” involving huge value of assets. Building at three locations is owned by the company. The company earns handsome profits and does not want to suffer losses due to business interruptions. It has a dedicated department for looking after insurance matters. As an auditor, prepare an internal control questionnaire concerning this department for obtaining staff responses.

(3 Marks) (MTP April 24)

SA 320 : Materiality

Meaning

- Information which can influence the economic decision of user of F.S
- Check materiality in
 - a) Planning
 - b) Performing audit
- Can be qualitative or quantitative
- Can be individually or combination

Determination

- Matter of professional judgement (T/F) (MCQ)
- Assumptions

User he is not **financial** kid

- i) Users understand **F.s**
- ii) K :- Knowledge of A/c economic activity
- iii) I :- Inherent limitation
- iv) D :- decision
User can make reasonable decisions

Calculation

$$\begin{array}{r} \text{Mat} = \text{Benchmark} \\ \text{(Base)} \\ \times \\ \hline \% \\ \hline = \text{Amount} \\ \text{MM More than amt} \\ \text{Material} \\ \hline \text{Less} \\ \hline \text{Immaterial} \end{array}$$

Benchmark can be sales, Profit assets, equity

Depend 5 factors

EUROS

E :- Element of FS
U :- User need/ attention
R :- Relative Volatility (less)
O :- Ownership Structure
S :- Stage / Cycle of entity

Other imp pts

- i) Performance materiality
Less amt. than actual materiality
↓
To cover judgment error of even a lesser amt's uncorrected or undetected MM
- ii) Materially → Audit Risk
Inverse Relationship Revision of Materiality (TQ)
↓
Depending upon CUE
C :- Change in conditions
U :- Unexpected event
E :- Evidences obtained

Question

An auditor has to exercise professional judgement in determining materiality. Explain the factors that may affect the identification of an appropriate benchmark in determining materiality for the financial statements as whole.

(PYP 3 Marks May '23)

Automated Environment

Meaning



Business environment



D → Decision makers

O → Operation

P → Processing

A → A/cing



With the help of computer system

E.g. Banks

- more (T/F) automated
- Less manual intervention
- More complex
- Difficult to audit

Obtain understanding of automated environment



Understand

A → IPL paid version



A → Architecture (desktop, cloud, client – based boned, server)

I → Info system used (e.g. tally, ERP)

P → Purpose (Financial, non-financial)

L → Location of I.T system (local / Global)

P → Person (key) → CIO, CISO administrator)

A → Activities → Outsourced

I → Interface

D -> Developer (Inhouse / prepackaged)

Advantage



FAF- DU- PLESIS



F → Faster business operation

A → Accurate data processing

F → Faster data processing

P → Process → large volume of transaction

L → Latest info. Provide

E → Errors → Less

S → Security → better

I → Integration between operation

S → system connectivity and networking

Question

Understanding the entity and its automated environment involves understanding how IT department is organised, IT activities, the IT dependencies, relevant risks and controls. Explain stating the points that an auditor should consider to obtain an understanding of the company's automated environment.

(MTP 4 Marks Oct 19, MTP 3 Marks Sep '23, RTP May '18)

OR

List any five points that an auditor should consider to obtain an understanding of the Company's automated environment.

(MTP 4 Marks Oct '21, Mar'22, Old SM)

Question

List the points that an auditor should consider to obtain an understanding of the Company's automated environment.

(RTP Nov'22, Nov'19 & Nov '23, PYP 5 Marks, May '18)

Automated Environment

Disadvt. / Risk



FAILED



- F** → Fail to update
- A** → Unauthorized access
- I** → Inaccurate data processing
- L** → Lack of segregations of duties
- L** → loss of data
- E** → Excessive access/ privileged access (super user)



Abuse

- D** → Direct data change (back and charge) - misuse

Risk → Impact

Controls



- Cannot rely
- More substantive procedure (FAP)

Substantive Procedure



- More evidence to be collected
- Cannot rely on data

Audit Report



- Audit risk
- Erroneous Audit report
- Report → modify

6. IT related risks can have an impact on audit. In what different ways, such risks can have an impact on audit of financial statements?

(RTP May 24)

Question

Describe how risks in IT systems, if not mitigated, could have an impact on audit.

(MTP 3 Marks March '23 & Nov '21, RTP Nov'21, Old SM)

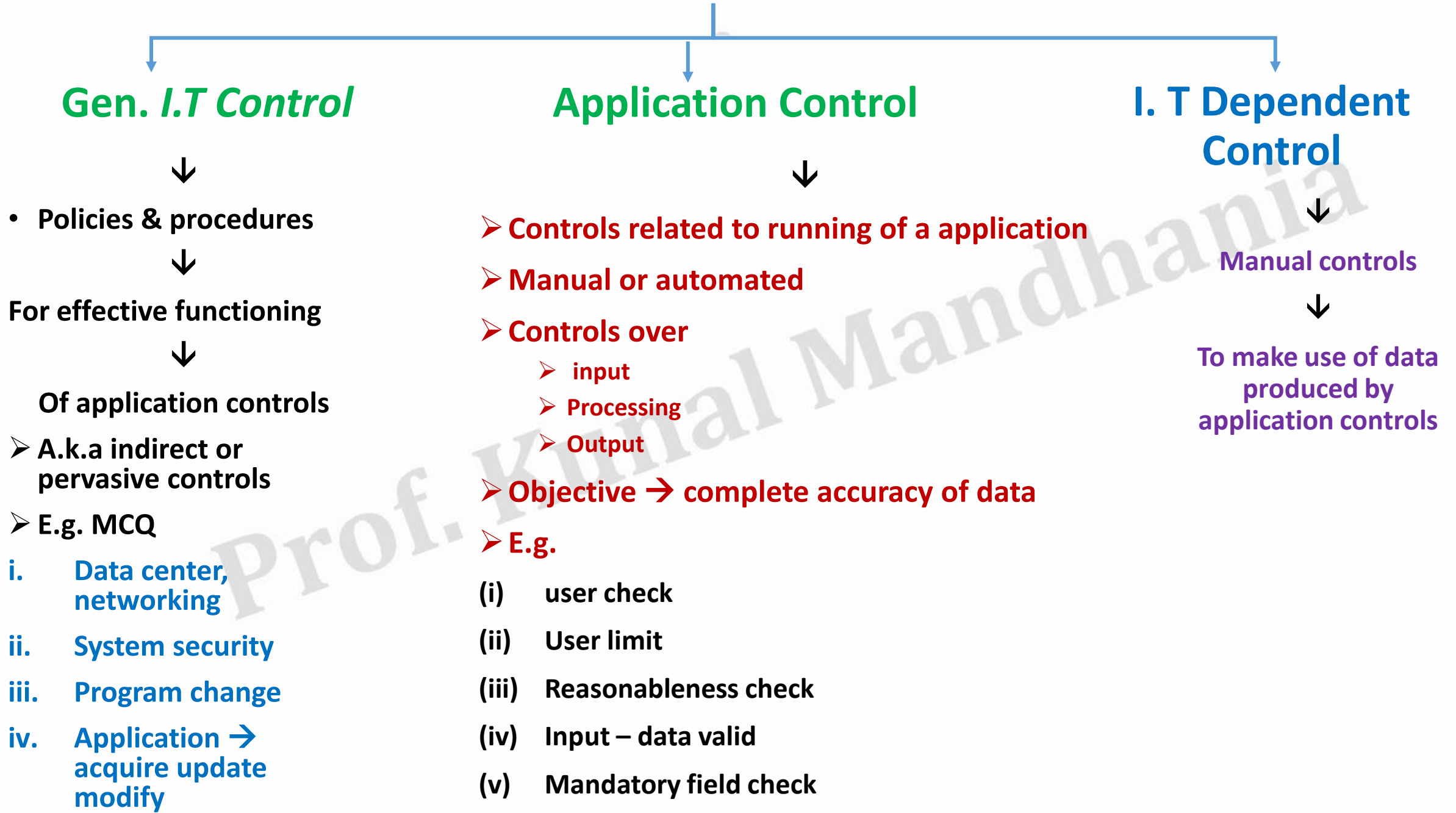
OR

Analyse how risks in the IT system if not mitigated could have an impact on the audit.

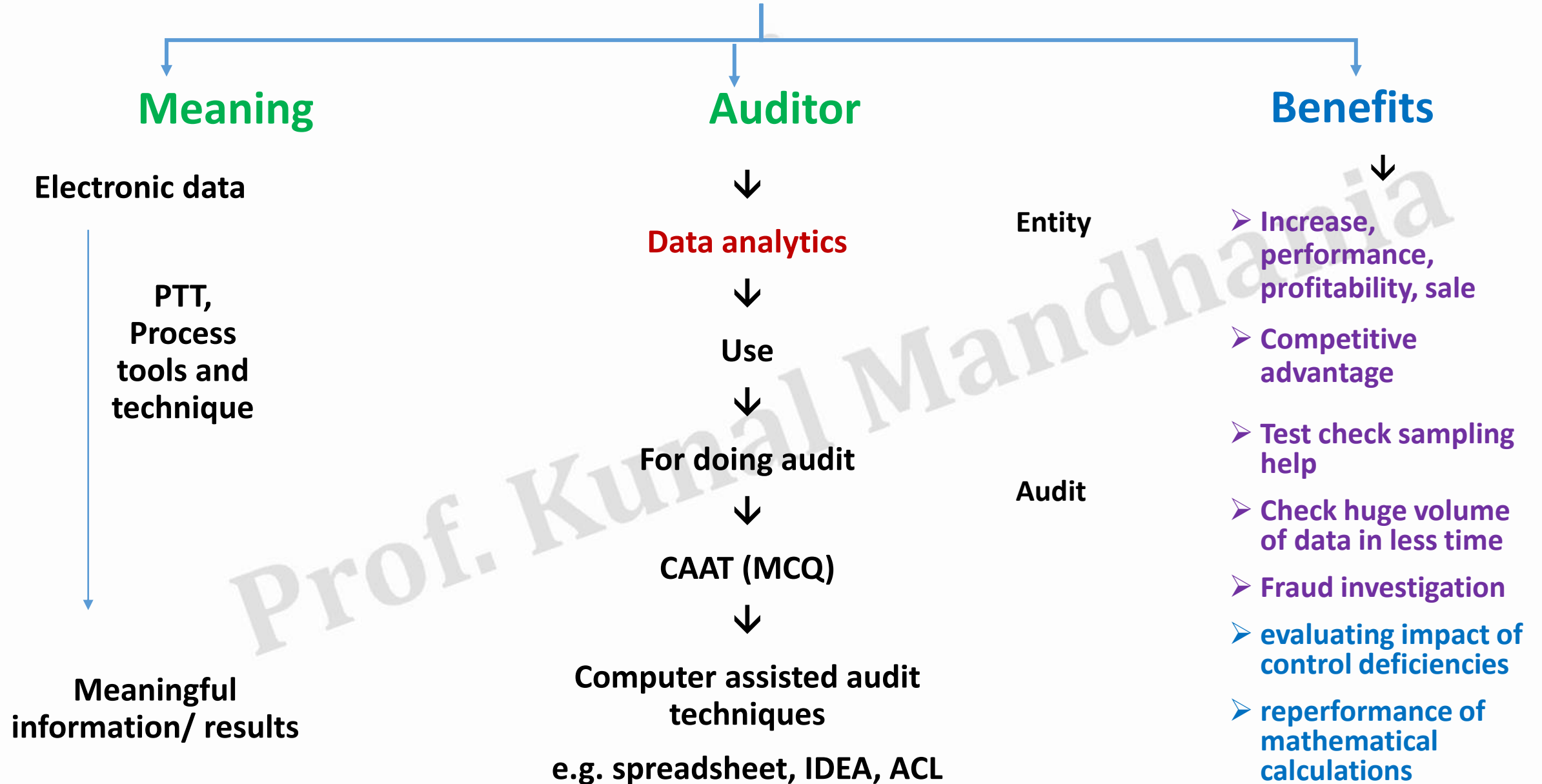
(MTP 3 Marks

Sep'22, PYP 3 Marks Nov '20)

3 types of controls



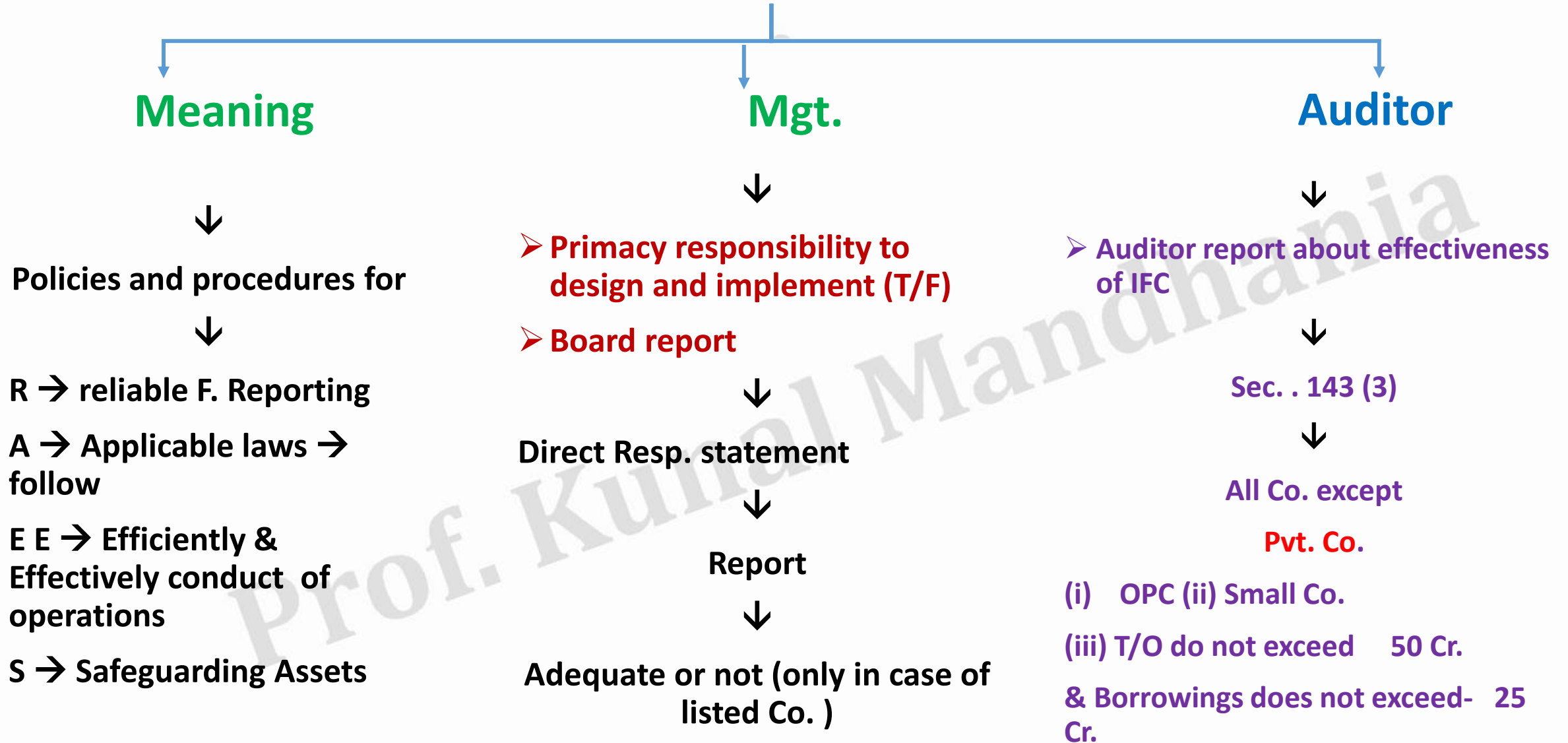
Data Analytics



While auditing in an automated environment, how data analytics can be used in testing electronic records and data residing in IT systems using spread sheets and specialised audit tools?

(PYP 3 Marks May '23)

Internal Financial control system



Question

Explain the meaning of Internal Financial Controls clearly stating reporting requirement (with reference to audit) on adequacy of internal financial controls. Also discuss about its (reporting requirement on adequacy of internal financial controls) applicability on various types of Companies.

(RTP May '22)

Question

With respect to audit in an automated environment, explain the following: (any four)

(i) CAATs

(ii) Data Analytics

(iii) Database

(iv) Information Systems

(v) Privileged access

(vi) (MTP 4 Marks May 20, RTP May'23, PYP 5 Marks Nov'18, Old SM)

OR

With respect to audit in an automated environment, explain the following:

(i) CAATs

(ii) Data Analytics

(iii) Database

(MTP 3 Marks Oct'22)

Answer

- (i) **CAATs:** Short form for Computer Assisted Audit Techniques, are a collection of computer based tools and techniques that are used in an audit for analysing data in electronic form to obtain audit evidence.
- (ii) **Data Analytics:** A combination of processes, tools and techniques that are used to tap vast amounts of electronic data to obtain meaningful information
- (iii) **Database:** A logical subsystem within a larger information system where electronic data is stored in a predefined form and retrieved for use.
- (iv) **Information Systems:** Refers to a collection of electronic hardware, software, networks and processes that are used in a business to carry out operations and transactions.
- (v) **Privileged access:** A type of super user access to information systems that enforces less or no limits on using that system.

Question

Discuss the various points which auditor needs to consider in determining whether it is appropriate to use audit evidence about operating effectiveness of controls obtained in previous audit, and if so, the length of the time period that may elapse before retesting a control.

(MTP 4 Marks April '23, PYP 4 Marks Nov '19)

Answer

In determining whether it is appropriate to use audit evidence about the operating effectiveness of controls obtained in previous audits, and, if so, the length of the time period that may elapse before retesting a control, the auditor shall consider the following:

- i. The effectiveness of other elements of internal control, including the control environment, the entity's monitoring of controls, and the entity's risk assessment process;
- ii. The risks arising from the characteristics of the control, i automated;
- iii. The effectiveness
- iv. The effectiveness of the control and its application by the entity, including the nature and extent of deviations in the application of the control noted in previous audits, and whether there have been personnel changes that significantly affects the application of the control;
- v. Whether the lack of a change in a particular control poses a risk due to

Question

11. Owing to the limitations of an audit, there is risk that some material misstatements of the financial statements will not be detected, even though the audit is properly planned and performed in accordance with the SAs.

- (a) Inherent, unavoidable**
- (b) Inherent, complete**
- (c) Management, unavoidable**
- (d) Regulatory, control**

(MTP 1 Marks March 22)

A

Prof. Kunal Mandal

Question

A company is engaged in manufacturing of wooden furniture. The auditor of company notes that company has identified emerging risks pertaining to probable reduction in demand of company's products due to procurement of imported furniture from South East Asian nations. It has also estimated how significant are those risks and their possibility of happening. Besides, it has also formulated an action plan to deal with the situation, in case these risks materialize.

Which of the following options would be most appropriate to describe above situation?

- (a) An example of audit risk for auditor
- (b) An example of component of internal control of company
- (c) An example of control risk of company
- (d) An example of inherent risk for auditor (MTP 1 Marks Oct'22)

B

Prof. Kunal Mandal

Question

Which of the following is incorrect-

For the purpose of Identifying and assessing the risks of material misstatement, the auditor shall :

- (a) Identify risks throughout the process of obtaining an understanding of the entity and its environment, including relevant controls that relate to the risks, and by considering the classes of transactions, account balances, and disclosures in the financial statements;**
- (b) Assess the identified risks, and evaluate whether they relate more pervasively to the financial statements as a whole and potentially affect many assertions;**
- (c) Relate the identified risks to what can go wrong at the assertion level, taking account of relevant controls that the auditor intends to test; and**
- (d) Not consider the likelihood of misstatement, including the possibility of multiple misstatements, and whether the potential misstatement is of a magnitude that could result in a material misstatement.**

(MTP 1 Mark March '23)

D

Prof. Kunal Mandal

Question

To evaluate the Internal Control of Kingsway Limited, a team member of the auditors used a method according to which, number of questions relating to internal control of the company were required to be answered by the employees of the company. After obtaining the answers there was a discussion relating to those answers between team member of the auditor and employees of the company for a clear picture. State the method of evaluation of internal control as discussed above.

- (a) Narrative record
- (b) Check List
- (c) Internal Control questionnaire
- (d) Flow chart

(MTP 1 Mark Sep '23)

C

Prof. Kunal Mandhania

Question

15. The term Internal Financial Controls (IFC) basically refers to the policies and procedures put in place by companies for ensuring:

- (i) Reliability of financial reporting**
 - (ii) Compliance with applicable laws and regulations**
 - (iii) Safeguarding of assets.**
 - (iv) Effectiveness and efficiency of operations**
 - (v) Prevention and detection of frauds**
- Which statement is correct?**
- (a) (i),(ii)and (iv)**
 - (b) (i),(iii) (v) and(ii)**
 - (c) (i),(ii),(iii) and (iv)**
 - (d) (i), (ii),(iii),(iv)and (v)**

(MTP 1 Mark Sep '23)

D

Prof. Kuldeep Sandhania

Question

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

- (i) How the controls were applied at relevant times during the period under audit.**
- (ii) The consistency with which they were applied.**
- (iii) By whom or by what means they were applied. Which of the following is correct?**

- (a) (i) and (ii)**
- (b) (ii) and (iii)**
- (c) (i),(ii) and (iii)**
- (d) (i) and (iii)**

(MTP 1 Marks March 22)

C

Prof. Kunal Mandhania

Question

Consider the following statements pertaining to nature and meaning of “assertions”:-

Statement I—-Assertions are representations by the management which are present in financial statements.

Statement II —-The assertions have to be necessarily explicit. Which of the following is correct?

- (a) Only Statement I is true.**
- (b) Only Statement II is true.**
- (c) Both statements I and II are true.**
- (d) Both statements I and II are false. (MTP 1 Marks March 22)**

A

Prof. Kunal Mandal

20. are needed to support the functioning of

(a) General IT Controls; Application Controls

(b) Application Controls; General IT Controls

(c) IT Dependent Controls; General IT Controls

(d) Application Controls; IT Dependent Controls

(MTP 1 Marks April '23)

A

Prof. Kunal Mandal

Question

24. refer to the audit procedures performed to obtain an understanding of the entity and its environment, including the entity's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.(RTP May '22)

- (a) Internal control assessment procedures**
- (b) Risk assessment procedures**
- (c) substantive procedures**
- (d) analytical procedures**

B

Prof. Kunal Mandal

27. A type of super user access to information systems that enforces less or no limits on using that system is known as: (RTP May '22)

- (a) Super access.**
- (b) Super user access.**
- (c) Unlimited access.**
- (d) Privileged access**

D

Prof. Kuldeep Sandhania

Question

Tools and techniques that auditors use in applying the principles of data analytics are known as-

- (a) Computer Aided Audit Technique**
- (b) Computer Aided Audit Tools**
- (c) Computer Accounting and Auditing Technique**
- (d) Computer Assisted Audit Technique (RTP May '23)**

D

Prof. Kuldeep Sandhania

4. Audit Evidence

A close-up photograph of a person's hand in a dark suit jacket, holding a black pen with gold accents and writing on a white document. To the left, a stack of several books is visible, slightly out of focus. The background is a soft, blurred office setting.

Kunal Mandhania

SA-500 Audit Evidence

Meanings

Any information

Obtained by

Auditor

To express his opinion on
FS

AE includes

i. Financial information

- * initial accounting entries
- * supporting records EFT, invoices, contracts, ledgers.

ii. Other information

- * minutes
- * written confirmations
- * manuals of ICS

Why AE is required

- Auditing is logical process
- Auditor assesses + review FS & give expert opinion on them
- Objective examination & scrutiny of accounting statement of undertaking with view of assessing how far the statement present actual state of affairs
- Hence, he needs evidence to arrive at his judgement

Types of AE

On the basis of NATURE

1. WRITTEN

Documentary evidences

2. ORAL

information & explanation obtained by client / employees

3. VISUAL

observing somebody else performing procedures (physical verification)

On the basis of SOURCE

1.INTERNAL

which originates within the entity being audited
eg. Sales, Invoice, Challan, GRN, etc.

2.EXTERNAL

evidence that originates outside the clients entity
eg. Purchase Invoice, Quotations, etc.

On the basis of IMPACT

PERSUASIVE

Most likely to be true

CONCLUSIVE

True

Corroborative AE

Support other A.E

Question

Auditing is a logical process. An auditor is called upon to assess the actualities of the situation, review the statements of account and give an expert opinion about the truth and fairness of such accounts. This he cannot do unless he has examined the financial statements objectively. He needs evidence to obtain information for arriving at his judgment. Discuss explaining clearly the meaning of audit evidence in detail.

(MTP 4 Marks Oct'23, RTP Nov '19)

Question

SA 500 – “Audit Evidence”, explains what constitutes audit evidence in an audit of financial statements. A combination of tests of accounting records and other information is generally used by the auditor to support his opinion on the financial statements. Explain and discuss the meaning of Audit Evidence in detail.

(RTP Nov '23)

SA-500 Audit Evidence

Relevance & reliability

RELEVANCE

- Deals with
- ❑ Logical connection Bearing upon the purpose of audit procedures
 - ❑ And assertions under consideration

RELIABILITY

1. Written Documentary evidence $\xrightarrow{\text{more reliable than}}$ Oral AE
2. External AE $\xrightarrow{\text{more reliable than}}$ Internal AE
3. If ICS is satisfactory Internal AE $\xrightarrow{\text{more reliable than}}$ External AE
4. Original AE $\xrightarrow{\text{more reliable than}}$ Duplicate / Xerox Copies
5. Evidence obtained directly by auditor $\xrightarrow{\text{more reliable than}}$ Obtained indirectly

Sufficiency & appropriateness

Sufficiency of AE

- Measure of quantity
- Depends upon (FACTORS)(MARS)
 1. Materiality
 2. ROMM
 3. Size Of Population (less for homogenous and more for heterogenous)

Appropriateness of AE

- Measure of Quality i.e. its relevance & reliability

Factors determining SAAE

MNEMONIC – PRITAM

P – Previous experience of auditor

R – Risk of Mis-statement

I – if any fraud detected by auditor

T – trends shown by accounting ratio

A – available information

M – Materiality of items

Question

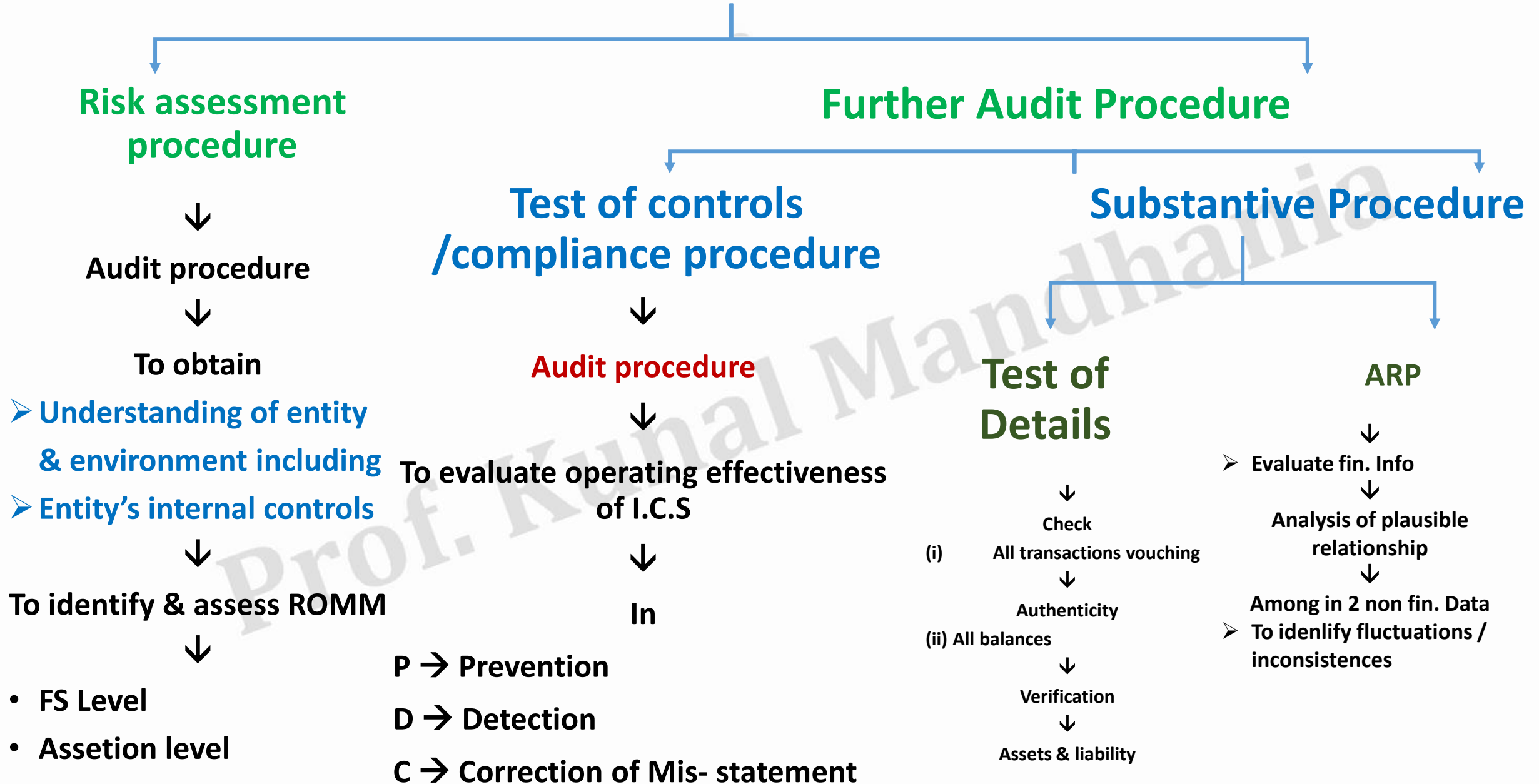
The reliability of information to be used as audit evidence, and therefore of the audit evidence itself, is influenced by its source, its nature and the circumstances under which it is obtained. Explain and elucidate the guiding principles which are useful in assessing the reliability of audit evidence.

(MTP 3 Marks March 22, RTP May 18)

What is meant by sufficiency of Audit Evidence? Explain the factors affecting the auditor's judgement as to the sufficiency of audit evidence.

(MTP 3 Marks April '23, RTP Nov 20 & May 23, Old & New SM)

Audit Procedures



Gen Procedures done through

O	Observation observing a process being performed by others
R	Re-performance Means performing some work which had already been performed by the mgt. (e.g. Preparing BRS)
E	<i>External Confirmation</i> audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party)
I	Inspection examining documents or Physical examination of tangible assets
C	Re-calculation Checking arithmetical accuracy
A	Analytical Review Analytical review consists of studying significant ratios and trends and investigating unusual fluctuation and item.
I	Inquiry seeking appropriate information from knowledgeable persons inside or outside the entity.

Question

The objective of auditing is to design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion. This can be obtained by performing which procedures? Name the types of audit procedures the auditor can perform to obtain audit evidence?

(PYP 4 Marks Nov 22)

AUDIT Trail

- **An audit trail is a documented flow of a transaction**
- It is a **step-by-step record** by which accounting, trade details, or other financial data can be **traced to their source**
- **Benefits**
- **I- investigate**
- **R-record & Fix responsibility**
- **C- Controls – verify**
- **T – Keep track record of all transactions**
- **C-Controls – and data security – enhance**

Question

2. Audit evidence includes

- (a) information contained in the accounting records underlying the financial statements**
- (b) both information contained in the accounting records underlying the financial statements and other information.**
- (c) other information.**
- (d) information contained in the accounting records underlying the financial statements or other information.**

(MTP 2 Marks MTP-Oct'19-MTP-APRIL-2019 , April '21 , Nov '21 & April '23)

B

Prof. Kunal Mandal

Question

4. Audit evidence is necessary to support the auditor's opinion and report. It is_____in nature and is primarily obtained from audit procedures performed during the course of the audit.

- (a) cumulative**
- (b) regressive**
- (c) selective**
- (d) objective**

(MTP 1 Mark Oct 19, Apr'22, RTP Nov'19)

A

Prof. Kunal Mandal

Question

6. In relation to completed engagements, procedures designed to provide evidence of compliance by engagement teams with the firm's quality control policies and procedures is known as:

- (a) Monitoring**
- (b) Inspection**
- (c) Subsequent Audit procedures**
- (d) Compliance procedures**

(MTP 1Mark Sep'22)

B

Prof. Kunal Mandal

Question

7. Mr. H and his team members in detail checked and evaluated the books of accounts and relevant documents of WT Limited. This is an example of which audit procedure:

- (a) Inspection.**
- (b) Re-performance.**
- (c) Recalculation.**
- (d) Observation.**

(MTP 1Mark Sep'22)

A

Prof. Kunal Mandal

Question

8. Statement 1: Audit procedures consist of Risk Assessments Procedures and other procedures.

Statement 2: Substantive procedures consist of test of details and analytical procedures.

- (a) Only Statement 1 is correct**
- (b) Only Statement 2 is correct**
- (c) Both 1 & 2 are correct**
- (d) Both 1 & 2 are incorrect**

(MTP 1Marks Sep'22, RTP May'20)

C

Prof. Kunal Mandhania

Question

9. CA X, auditor of Green Shoots Private Ltd. is going through financial statements of the company. On perusing notes to accounts, he finds ageing of trade payables reflecting in accordance with requirements of Schedule III of Companies Act, 2013. He wants to be sure that ageing of trade payables forming part of notes of accounts is proper and carries out ageing independently to confirm its veracity.

Identify audit procedure(s) being performed by CA X.

- (a) Analytical procedures**
- (b) Recalculation**
- (c) Re-performance**
- (d) Observation**

(MTP 1 Marks Oct'22)

C

Prof. Kunal Mandhania

Question

10. may be defined as the information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. It includes both information contained in the accounting records underlying the financial statements and other information.

- (a) Audit procedure**
- (b) Audit evidence**
- (c) Audit plan**
- (d) Audit programme**

(MTP 1 Mark Sep '23)

B

Prof. Kunal Mandal

Question

11. While auditing the books of accounts of Mehra Limited for the financial year 2022-23, the auditor of the company used an audit procedure according to which complete documents and records of the company were checked in detail in order to obtain audit evidence. Explain the audit procedure used by the auditor of company.

- (a) Recalculation**
- (b) Analytical Procedures**
- (c) Inquiry**
- (d) Inspection**

(MTP 1 Mark Sep '23)

D

Prof. Kuldeep Sandhania

Question

12. CA Tarini is in process of formulating audit plan for conducting audit of a company engaged in business of dealing in commodity futures. Which of the following is not likely to be an appropriate audit procedure to be included in audit plan for the abovesaid company?

- (a) Verification of turnover of company**
- (b) Verification of cost of raw material consumed**
- (c) Examination of company's accounting policy for revenue recognition**
- (d) Verification of contract notes with brokers**

(MTP 1 Mark Oct '23)

B

Prof. Kunal Mandal

Question

1. CA M is internal auditor of Crayon Products Limited. Which of the following is not TRUE about scope of internal audit?

- (a) Internal audit is an independent assurance activity.**
- (b) Internal audit helps in improving internal control of the company.**
- (c) Internal audit cannot review non-financial activities of company.**
- (d) Internal audit can review compliance of company with various laws and regulations.**

(MTP 1 Marks Oct'22)

C

Prof. Kunal Mandhania

Descriptive Questions

7. CA Kanika audited books of accounts of Engineering Ltd. for the financial year 2022-2023. The auditor used an audit procedure according to which all the documents and records maintained by the company were checked in detail to obtain audit evidence. Explain the audit procedure used by the auditor. Comment on reliability of audit evidence obtained by performing such an audit procedure in some situations.

(RTP May 24)

ANSWER

7. Audit Procedure:

Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset. In view of above, it can be concluded that CA Kanika used Inspection as an audit procedure.

Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production.

Example of inspection used as a test of controls is inspection of records for evidence of authorisation.

Some documents represent direct audit evidence of the existence of an asset, for example, a document constituting a financial instrument such as a inventory or bond. Inspection of such documents may not necessarily provide audit evidence about ownership or value. In addition, inspecting an executed contract may provide audit evidence relevant to the entity's application of accounting policies, such as revenue recognition. Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity's rights and obligations or the valuation of the assets. Inspection of individual inventory items may accompany the observation of inventory counting.

SA 501- Audit Evidence – Special Consideration for selected Items

Scope

Deals with specific consideration by auditor to obtain SAAE w.r.t. inventory, litigation & claims and segment information

Objectives

To obtain SAAE regarding :

- a) **Existence and condition** of inventory
- b) **Completeness** of litigation and claims involving the entity
- c) **Presentation and disclosure** of segment information as per AFRF

Specific/ selected items

1. **Inventory**
2. **Litigations & Claims**
3. **Segment information**

Inventory

Auditors Procedure

- When inventory is material
- He shall obtain sufficient appropriate evidence
- W.r.t. existence and condition of inventory by

Attendance at
physical
inventory count

&

Examining
Entity's final
inventory
records &
comparing
them with
actual count
result

1. Evaluate management instructions for controlling inventory
2. Observe mgt. count procedure
3. Inspect inventory
4. Perform test count

Decision 1

If auditor could not attend physical verification on B/s Date

1. Attend some other day (Count Date)
2. Check inventory as on count date
3. Check intermediary transactions (from 1st April to count date)
4. If unable to obtain AE, then modify the report

Decision 2

It is not practical for auditor at all to attend verification

1. Perform alternate procedures; eg. Inspect documents of subsequent sale of inventory prior to counting
2. If unable to obtain SAAE; then modify the report (SA-705)
3. Matter of general inconvenience to auditor; is not sufficient to support that attendance is impracticable
4. Matter of difficulty, cost, time not valid basis to omit audit procedures

Decision 3

If verification is held by stockiest (3rd party)

1. Confirmation from 3rd party
2. Perform inspection
3. Other audit procedure:
 - a) Attending or arranging for another auditor
 - b) Another auditors report or a service auditors report (SA 402)
 - c) Inspecting documentation
 - d) Confirmation from other parties when inventory has been pledged as collateral.

Matters relevant in planning attendance at physical inventory counting

CRICKET

- i. C → Completion Stage of WIP**
- ii. R → RMM**
- iii. I → I.C.S related to it**
- iv. C → Counting procedure**
- v. K → Knowledge about nature of inventory**
- vi. E → Ensure location of inventory**
- vii.T → Timing of verification**

Descriptive Questions

(b) While performing statutory audit of Contra Industries Private Limited, a company engaged in manufacturing and assembling of LED lights, CA Varun has decided to attend physical inventory count process of the company on 30th and 31st March, 2024. The inventories are lying at three different locations - two such locations A and B are in one city and third location C is in another city. Further, company also sends inventories to some service providers for quality control and testing as such facilities are not available with the company.

CA Varun is well-versed with this type of industry and has prepared a list of following matters which could be relevant to him in planning attendance at physical inventory count process for discharging his responsibilities in accordance with SAs: -

- **Nature of inventories i.e. LED light components, parts, circuits, panels, body, WIP and finished packed LED lights**
- **Materiality of inventories at different locations A, B and C**
- **Stage of completion of work-in-progress**
- **Maintenance of perpetual inventory system by company**
- **Materiality of inventories lying with service providers**
- **Timing of physical inventory counting i.e. year end**

There are two important matters which do not find place in above list. Without considering these crucial matters, it would be difficult for the auditor to properly plan his attendance at inventory count process in accordance with relevant SA. Discuss such matters.

(4 Marks) MTP Mar. 24

ANSWER

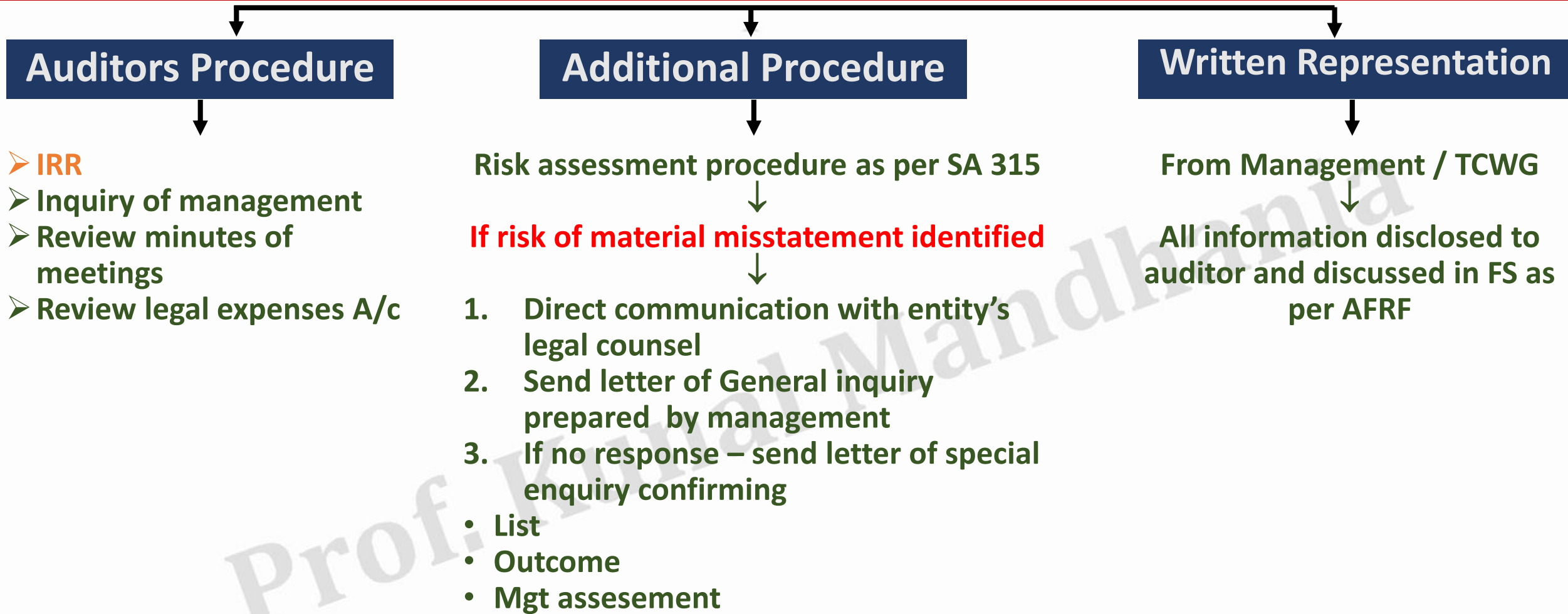
(b) The list given in the question does not contain following important matters: -

)> Whether adequate procedures are expected to be established and

proper instructions issued for physical inventory counting. The auditor has to evaluate management's instructions for recording and controlling physical inventory counting. It is important for the auditor to know beforehand how the inventory count will be conducted so as to assess its effectiveness.

> The nature of internal control related to inventories at different locations. It is possible that inventories at one location have unsatisfactory control leading to higher risk of material misstatement related to inventories at that particular location.

Completeness of Litigation & claims



Question

Pachranga International Ltd is manufacturer of pickles, ginger garlic paste, jams etc having its plant at Jaipur. Being in food industry, the company is facing many litigations in various courts across India. Auditors SPV & Co. wants to identify such litigations and claims involving the company which may give rise to risk of material misstatement. Guide the auditor as to how they should proceed for the purpose.

(RTP May '22, Old & New SM)

Question

35. The auditor shall design and perform audit procedures in order to identify litigation and claims involving the entity which may give rise to a risk of material misstatement, including:

- (a) Inquiry of management and, where applicable, others within the entity, including in-house legal counsel.**
- (b) Reviewing minutes of meetings of those charged with governance and correspondence between the entity and its external legal counsel.**
- (c) Reviewing legal expense accounts.**
- (d) All of the above**

Answer

D

Prof. Kunal Mandhania

Question

36. If the auditor is unable to obtain sufficient appropriate audit evidence

regarding the opening balances, the auditor shall express :

- (a) a disclaimer opinion**
- (b) a qualified opinion**
- (c) a qualified opinion or a disclaimer of opinion, as appropriate, in accordance with SA 705.**
- (d) unmodified opinion**

Answer

C

Prof. Kunal Mandhania

SA 505 External Confirmation

Meaning	Process to obtain	Examples	Types of Confirmation letter		
<p>Audit Evidence obtained by auditor</p> <p>↓</p> <p>From 3rd party</p> <p>↓</p> <p>As a DIRECT WRITTEN RESPONSE</p> <p>↓</p> <p>In paper form / electronic / other medium</p>	<p>Shortcut – DS DS</p> <p>1. Decide - Matters on which confirmation required <u>Factor to be considered while deciding items:</u></p> <ul style="list-style-type: none"> a. Materiality of a/c balance b. Assessment of inherent & Control risk c. Particular FS assertion <p>2. Select - Party from which confirmation required</p> <p>3. Design – Confirmation Letter <u>Factor to be considered while designing confirmation letter (ALAA-CFP)</u></p> <ul style="list-style-type: none"> Assertions being addressed Layout & presentation of confirmation request Management's Authorization to confirming parties to respond Ability of confirming party to provide request information Method of Communication Identified RMM, including Fraud risk Prior experience on audit or similar engagement <p>4. Send – To the appropriate party</p>	<p>Shortcut – ABCD of SIP (Systematic Investment plan)</p> <ul style="list-style-type: none"> A– Account Balance & transaction details B– Bank Balances & transaction Details C– Creditor Balance confirmation D – Debtor Balance Confirmation S– Stock held by 3rd party I – Investments details P– Related Party transaction confirmation 	<div> <div>Positive</div> <div>↓</div> <div>Situation where auditor require answer in all agreements & disagreements</div> <div>↓</div> <div>More persuasive</div> <div>↓</div> </div> <div> <div>Negative</div> <div>↓</div> <div>Situation where auditor require ans. Only in case of disagreement</div> <div>↓</div> <div>Less persuasive</div> <div>↓</div> </div>		
			ICS is -	Weak	Strong
			RMM is-	High	Low
			Materiality is –	more	Less
			Expected error –	more	Less

Question

External confirmation procedures frequently are relevant when addressing assertions associated with account balances and their elements but need not be restricted to these items. Apart from confirmations for bank balances and accounts receivables, what are the other situations where external confirmation procedures may provide relevant audit evidence in responding to assessed risks of material misstatement?

(MTP 3 Marks April 22, RTP Nov'22)

Question

28. Statement 1: A response that indicates a difference between information

requested to be confirmed and information provided by confirming party is Negative Confirmation.

Statement 2: A failure of the confirming party to respond, or fully respond, to a positive confirmation request, or a confirmation request returned undelivered is exception.

- (a) Statement 1 is correct**
- (b) Statement 2 is correct**
- (c) Both 1 & 2 are incorrect**
- (d) Both 1 & 2 are correct**

Answer

C

Prof. Kunal Mandhania

SA 505 External Confirmation

Decisions

1. In case of Non-response

- perform alternate procedure
- still AE not obtained → modify AR

2. Unreliable Response

- perform additional procedures
- if not satisfied, alternate procedure
- AE not obtained → Modify AR

3. Managements Refusal

Check whether it is justified

Yes



Perform alternate procedure



Still AE not obtained – modify

No



Communicate with TCWG (SA 260)



modify AR (SA 705)

Descriptive Questions

8. CA J is conducting statutory audit of Gemini Ltd engaged in manufacturing of pharma products. The company is fairly large one and has a well-functioning internal audit department. While considering sending out external confirmation requests to trade receivables outstanding as on date of financial statements, CA J has delegated the process of choosing trade receivables, designing requests and receiving responses from customers to internal audit department. The responses are also received on the mail id of internal audit department. Is the approach of CA J proper?

(RTP May 24)

ANSWER

8. When using external confirmation procedures, the auditor shall maintain control over external confirmation requests, including:

- (a) Determining the information to be confirmed or requested;**
- (b) Selecting the appropriate confirming party;**
- (c) Designing the confirmation requests, including determining that requests are properly addressed and contain return information for responses to be sent directly to the auditor; and**
- (d) Sending the requests, including follow-up requests when applicable, to the confirming party.**

In the given case, it appears that external auditor has delegated entire work of sending out external confirmation requests to internal audit department over which he has no control. Further, responses to external confirmation requests are received on mail id of internal audit department. All these acts are not in line with requirements under SA 505.

SA 510 'Initial Audit Engagement – Opening Balance'

Meaning	Procedure for Opening Balances	Consistency of Accounting Policy	Predecessor's Audit Report
<p>Engagement in which either FS for the prior period</p> <p>a) Not audited OR b) Audited by Predecessor auditor</p>	<p>a) Read prior year's Financial Statements & Audit Reports.</p> <p>b) Whether correctly brought forward.</p> <p>c) Any adjustment disclosed as Prior Period Adjustment.</p> <p>d) Co-relate opening balance with procedures performed in current year.</p> <p>e) Obtain additional evidence for opening balances. If doubt as to misstatement in opening balance, then communicate with management and TCWG.</p> <p style="text-align: center;">↓</p>	<p>Obtain SAAE whether:</p> <p>a) Accounting Policies applied appropriately and consistently</p> <p>b) If any change; properly disclosed by management in notes to account as per AFRF</p> <p style="text-align: center;">↓</p>	<p>If modification in predecessor's AR, then evaluate the effect of modification in assessing RMM in Current period F.S.</p> <p style="text-align: center;">↓</p> <p style="text-align: center;">Decision</p> <p>If balance of current FY still contain effect of that misstatement → modify AR (SA 705 & 710)</p>
	<p style="text-align: center;">Decision</p> <p>a) Unable to obtain AE: modify AR (SA 705)</p> <p>b) If misstatement in Opening Balance ask mgt to rectify</p> <p style="margin-left: 150px;">→ Yes – EOM para</p> <p style="margin-left: 150px;">→ No – Modify AR</p>	<p>Whether disclosed:</p> <p>→ Yes – Clean Report (EOM para)</p> <p>→ No – modify the AR (SA 705)</p>	<p>Note:</p> <p>Use OM para to mention that last year we have not audited the FS</p>

Descriptive Questions

9. The newly appointed auditor of BTN Limited wants to obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements. What audit procedures should he perform for this purpose?

(RTP May 24)

Descriptive Questions

(c) In an initial audit engagement, in the case of inventories, the current period's audit procedures on the closing inventory balance provide little audit evidence regarding inventory on hand at the beginning of the period. Therefore, in such a case, additional audit procedures become necessary so that auditor may obtain sufficient appropriate audit evidence. Discuss those additional audit procedures.

(3 Marks) (MTP April 24)

What is the objective of the auditor with respect to the opening balances when conducting an initial audit engagement as per the relevant SA?

(RTP May '23, Old & New SM)

Answer

In conducting an initial audit engagement, the objective of the auditor with respect to opening balances is to obtain sufficient appropriate audit evidence about whether:

- (a) Opening balances contain misstatements that materially affect the current period's financial statements; and
- (b) Appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are properly accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

ARP → SA - 520

Meaning

↓
**Evaluation of
financial
Information**

↓
**Through analysis
of relationship**

↓
**Among financial &
non –financial
data**

Benefits

↓
PROF

- ↓
- i. **P** → Planning (Help in)
 - ii. **R** → Risk Assesement (Help)
 - iii. **R** → Reasonableness (judge)
 - iv. **O** → Overall review to draw conclusion
 - v. **F**raud → Existence (to confirm)

Techniques /types

↓
Trend analysis

comparison of current data with the prior period

Ratio analysis

Reasonableness test

non-financial data

**structure
(statistical)model**

Budget to actual

Factors to asses reliability

↓
SINC

- ↓
- i. **Source of data**
 - ii. **Information → Comparable**
 - iii. **Nature of Information**
 - iv. **Controls over preparation of information**

1. CA D, during the course of audit of a company engaged in export business, notices that credit facilities taken by company during the year from a bank for `10 crores have almost been fully utilized during the year. On going through sanction letter provided by bank to company, it is observed that rate of interest stipulated in sanction letter is 8% p.a. Financial statements of company show bank interest amounting to `60.00 lacs. Which type of substantive analytical procedure is being used by CA D?

- (a) Trend analysis
- (b) Ratio analysis
- (c) Reasonableness tests
- (d) Structural modelling

(MTP April 24)

Question

While applying the Substantive Analytical Procedures what techniques can be used by the statutory auditor of a company to obtain sufficient and appropriate audit evidence?

(MTP 4 Marks March 22, RTP May'23, Old & New SM)

ARP can be applied

Decision in case of inconsistency in data

(1) Planning



Benefits



- i. Understand entity's business
- ii. Risk assessment
- iii. Designing NTE of further audit procedure

(2) Substantive procedure



Factors/pts to be considered



(SAP, AND, I)



S → Source
A → Available Info'
P → Predictability
A → A/c Types
N → Nature of Assertion
D → Disaggregation
I → Inherent Risk

Pls to see considered

(3) Overall Review

Steps



- i. Determine Suitability
- ii. Evaluate reliability
- iii. Develop expectation
- iv. Compare & conclude

1. Inquire with Mgt.
2. If still inconsistent, perform additional procedure to confirm

Question

Explain the aspects to be considered by an auditor when designing and performing substantive analytical procedures, either alone or in combination with test of details, as substantive procedures in accordance with SA 330.

(RTP Nov'22)

Question

Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. Explain.

**(MTP 4 Marks April 19 & April '22, RTP
Nov 18)**

Answer

Substantive Analytical Procedure: Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. The application of planned analytical procedures is based on the expectation that relationships among data exist and continue in the absence of known conditions to the contrary. However, the suitability of a particular analytical procedure will depend upon the auditor's assessment of how effective it will be in detecting a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated. In some cases, even an unsophisticated predictive model may be effective as an analytical procedure. For example, where an entity has a known number of employees at fixed rates of pay throughout the period, it may be possible for the auditor to use this data to estimate the total payroll costs for the period with a high degree of accuracy, thereby providing audit evidence for a significant item in the financial statements and reducing the need to perform tests of details on the payroll. The use of widely recognised trade ratios (such as profit margins for different types of retail entities) can often be used effectively in substantive analytical procedures to provide evidence to support the reasonableness of recorded amounts.

Question

If analytical procedures performed in accordance with SA 520 identify fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount, how would the auditor investigate such differences.

(MTP 3 Marks Oct'23, RTP May '23, May'22, May'19)

Answer

If analytical procedures performed in accordance with SA 520 identify fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount, the auditor shall investigate such differences by:

- (i) Inquiring of management and obtaining appropriate audit evidence relevant to management's responses: Audit evidence relevant to management's responses may be obtained by evaluating those responses taking into account the auditor's understanding of the entity and its environment, and with other audit evidence obtained during the course of the audit.
- (ii) Performing other audit procedures as necessary in the circumstances: The need to perform other audit procedures may arise when, for example, management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate.

Question

5. Statement I: As per the Standard on Auditing (SA) 520 “Analytical Procedures”, the term “analytical procedures” means evaluations of financial information through analysis of plausible relationships among financial data.

Statement II: Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

- (a) Only Statement I is correct**
- (b) Only Statement II is correct**
- (c) Both statements are correct**
- (d) Both Statements are incorrect (MTP 1 Mark April 22, Sept 22)**

B

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6. Auditor Compares Gross Profit Ratio with that of Previous year and it is discovered that there has been a fall in the ratio. This is an example of:

- (a) Analytical Procedure**
- (b) Test of Controls**
- (c) Walk Through Test**
- (d) Audit Sampling**

(MTP 1 Mark April 22 & April '23)

A

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Question

7. The auditor of Vishwas Ltd wants to know from you which of the following methods are analytical procedures

- I. Comparison of client and industry data**
 - II. Comparison of client data with similar prior period data**
 - III. Comparison of client data with client-determined expected results**
 - IV. Comparison of client data with auditor-determined expected results**
- (a) I, II and III only**
 - (b) I & II only**
 - (c) III & IV only**
 - (d) I, II, III and IV**

(MTP 1 Marks, Sep'22)

D

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SA 530 – Audit Sampling

Scope	Definitions	Population	Other Imp points
<p><u>This standard deals with the auditor's use of</u></p> <p>=</p> <p>A. <u>Statistical and</u></p> <p>B. <u>Non-statistical sampling</u></p> <p><u>when designing and selecting the-</u></p> <ul style="list-style-type: none"> <u>audit sample,</u> <u>performing tests of controls and tests of details, and</u> <u>evaluating the results from the sample.</u> 	<ol style="list-style-type: none"> <u>Sampling:</u> Checking less than 100% data in entire population <u>Population:</u> entire set of data from which sample is selected <u>Sampling Unit</u> The individual items that make up the population <u>Sampling Risk:</u> Risk that auditors conclusion on sample may be different if entire population was checked (dealt in detail further) <u>Non-sampling risk:</u> Risk that auditor reaches erroneous conclusion for reason other than sampling risk 	<p>Sample selected must be representative of the population</p> <p>Characteristics:((CAR)</p> <ol style="list-style-type: none"> <u>Completeness:</u> population needs to include all relevant items throughout the entire period <u>Appropriateness:</u> for particular audit objective. <u>Reliable</u> complete & accurate 	<ol style="list-style-type: none"> Sample must be true representative of data Sampling perform on Test of Controls (to identify deviations in expected controls) and test of details (to identify mis-statements) While designing sample – auditor includes specific purpose to be achieved and procedures which give best results . Size of entity has no effect on sample size Anamoly is mis-statement and deviation not representing mis-statement in population

SA 530 – Audit Sampling

Techniques / types/Approaches

Judgmental / Traditional / non-statistical

Auditor use experience / judgement

Advantages

- **Simple to operate**
- **TIME SAVING**

Disadvantages

- Less scientific & Objective
- Narrow application
- Personal biasness
- **LESS RELIABLE**

Statistical

Auditor use **random selection** of samples and use probability theory / mathematical Calc/Statistics

Advantages:

- More scientific and Objective
- Widely acceptable
- No personal biasness
- Results can be projected in more reliable way

Disadvantages

- **Complex to operate**
- **Time consuming exercise**

Method to pick Sample

1. Random Sampling:

equal chance of selection & may involve use of random number tables

Simple random – data homogenous (for similar units)

Stratified sampling – data heterogenous – divide into strata and take sample from each

2. Systematic / Interval Sampling:

Divide the Population into Strata of **EQUAL Size** called **INTERVAL Size**. Here Strata are known as **INTERVALS**.

2. Monetary unit sampling/ Value weighted selection :

Conclusions are drawn in monetary amount

3. Haphazard Sampling:

- without following a structured technique.

2. Block Sampling –

This method is applicable when the population is clearly divided into **homogeneous blocks of contiguous items (connected items)**.

SA 530 – Audit Sampling

Sampling Risk

Test of Control

1.Over reliance
↓
erroneous/insufficient AR

2.Under Reliance
↓
**no error in AR
additional work**

Test of Detail

1.Incorrect Acceptance
↓
**erroneous /
insufficient AR**

2.Incorrect Rejection
↓
**no error in AR
additional work**

NON SAMPLING RISK (**HEMA**)

H- Human Mistakes
E- Erroneous information
M - Misinterpreting the sample results
A- Applying audit procedures not appropriate to the objectives of audit

FACTORS INFLUENCING SAMPLE SIZE

Factors Influencing Sample Size for Tests of Controls (TOC)

Factor	Effect on Sample Size
An increase in the extent to which the auditor's risk assessment takes into account relevant CONTROLS	Increase
An increase in the TOLERABLE rate of deviation	Decrease
An increase in the EXPECTED rate of deviation of the population to be tested	Increase
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	Increase
An increase in the number of sampling units in the POPULATION	Negligible Effect

Factors Influencing Sample Size for Tests of Details

Factor	Effect on Sample Size
An increase in the auditor's ROMM assessment	Increase
An increase in the use of other substantive procedures directed at the same assertion	Decrease
An increase in the auditor's DESIRED LEVEL OF ASSURANCE that tolerable misstatement is not exceeded by actual misstatement in the population	Increase
An increase in TOLERABLE misstatement	Decrease
An increase in EXPECTED misstatement	Increase
STRATIFICATION of the population when appropriate	Decrease
The number of sampling units in the POPULATION	Negligible Effect

Factors affecting EXTENT OF CHECKING ON A SAMPLING PLAN

SIR-TC

S	Size of the organisation under audit.
I	State of the internal control .
R	Adequacy & reliability of books & records.
T	Tolerable error range.
C	Degree of the desired confidence .

Factors that should be considered for deciding upon the extent of checking on a sampling plan. (5 Marks) (Nov 2018) (RTP-Nov 2020) (Module)

SA 550 Related Parties

Scope	Meaning	Exception	Nature	Gen Responsibility
Deals with Auditor's responsibility regarding RP relationship and transactions when performing audit of FS	<p>Party that is either</p> <ol style="list-style-type: none"> A RP as per AFRF, or Where AFRF is silent, its as per SA 550 <ol style="list-style-type: none"> Person / Entity having control / significant influence; directly or indirectly over reporting entity Entity over which Rep.entity has significant influence or control directly / indirectly Entity under common control with client through <ul style="list-style-type: none"> Common controlling ownership Owners who are close family members Common key management 	<p>Entities that are under common control of government (CG or SG)</p> <p>→ Not considered related unless they engage in significant transactions or share resources to significant extent amongst themselves</p>	<ol style="list-style-type: none"> Many RPT are in normal course of business & carry no RMM But, nature of RPT in some cases, give rise to higher RMM of FS.(module) This include: <ul style="list-style-type: none"> RP may operate through complex range of structures Weak ICS to identify o/s balance between entity & RP May not be conducted as per normal market T&C 	<ol style="list-style-type: none"> Whether disclosed as per AS 18 Perform AP to identify & assess RMM arising as a result of RPT Obtain understanding of entity's RPT & ensure whether <ol style="list-style-type: none"> FS show T&F view FS are not misleading Evaluate fraud risk factor as per SA 240 Due to inherent limitations, auditor may not be able to detect RMM because of: <ol style="list-style-type: none"> Mgt - unaware of all RPT collusion & manipulation among RP & mgt

Teacher Note – SA 610 is next part

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7. Completion and Review

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SA 560 Subsequent Events

Scope	Objective	Definitions	Types of Subsequent Event
Deals with Auditor's responsibility relating to Subsequent Events in audit of FS	<ul style="list-style-type: none"> ■ To obtain SAAE ■ To respond Appropriately 	<ol style="list-style-type: none"> 1. Subsequent Events: events between date of FS & date of AR; fact becomes known to auditor after date of AR 2. Date of FS: last date of period covered by FS 3. Date of Approval of FS: date on which recognized authority takes responsibility of FS 4. Date of AR: as dated by auditor in his report 5. Date the FS are issued: date on which audited FS & AR are made available to 3rd parties 	<p>As per AS 4</p> <ol style="list-style-type: none"> 1. Adjusting Event (TYPE - I) provide additional evidence w.r.t. condition existed on B/s date. Adjustment to be done in FS eg. Settlement of dispute before date of AR; which arose before B/s date 2. Non Adjusting Event (TYPE - II) conditions that did not exist on B/s date but arose subsequent to it. No adjustment required in FS. Eg. Purchase of business, sale of shares.

SA 560 Subsequent Events



Events occurring after B/s Date but before date of AR



&



Facts that become known to auditor after the date of AR

Before FS issued

After FS issued

Since auditor has signed AR, so he has no obligation. However, if the facts are so material, had it been known earlier to auditor, he would have modified report

Discuss with Management / TCWG & ask him to amend FS

Discuss with Management / TCWG & ask them to issue New FS

Management

Management

Amends FS

Does not Amend FS

Issue new FS

Does not Issue new FS

Issue new AR

1. Dual Dating
2. Altogether new AR + EOM / OM para

Check whether AR already issued to mgt:

- a) No – modify as per SA 705
- b) Yes – ask them not to give it to 3rd party – if gave then take step to prevent reliance on wrong AR

- Issue new AR
1. Dual Dating
 2. Altogether new AR + EOM / OM para

Take step to prevent reliance on wrong FS

- ☐ Auditor shall Prform RAP which includes
 - Obtain understanding of **Procedure** established by mgt.
 - Reading **minutes**
 - **Inquiry** mgt or TCWG where appropriate
 - Reading latest subsequent **interim FS** if any
- ☐ Perform SAAE whether Such event can be
 - a) Adjusting event → FS**OR**
 - b) Disclosing Event → Board Report
- ☐ Perform procedure to cover period from as date of FS to date of AR
- ☐ Since, yet we have not signed AR in case of any modification → we can modify AR

Question

38. The auditor has no obligation to perform any audit procedures regarding the financial statements after the date of the auditor's report. However, when, after the date of the auditor's report but before the date the financial statements are issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of the auditor's report, may have caused the auditor to amend the auditor's report, the auditor shall:

- (a) Discuss the matter with management and, where appropriate, those charged with governance.
- (b) Determine whether the financial statements need amendment.
- (c) Inquire how management intends to address the matter in the financial statements.
- (d) All of the above**

Answer

D

Prof. Kunal Mandhania

Question

SA 560, “Subsequent Events” deals with the auditor’s responsibilities relating to subsequent events in an audit of financial statements. Financial statements may be affected by certain events that occur after the date of the financial statements. Many financial reporting frameworks specifically refer to such events. Explain those events and also define subsequent events.

(MTP 3 Marks Sep '23, RTP Nov '21)

Answer

SA 560, “Subsequent Events” deals with the auditor’s responsibilities relating to subsequent events in an audit of financial statements.

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

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

SA 700 explains that the date of the auditor’s report informs the reader that the auditor has considered the effect of events and transactions of which the auditor becomes aware and that occurred up to that date.

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

Question

- 1. The auditor has no obligation to perform any audit procedures regarding the financial statements after the date of the auditor's report. However, when, after the date of the auditor's report but before the date the financial statements are issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of the auditor's report, may have caused the auditor to amend the auditor's report, the auditor shall:**
- (a) Discuss the matter with management and, where appropriate, those charged with governance.**
 - (b) Determine whether the financial statements need amendment.**
 - (c) Inquire how management intends to address the matter in the financial statements.**
 - (d) All of the above (MTP 1 Mark March '23, MTP 1 Mark Apr'19)**

D

Prof. Kuldeep Sandhania

SA 570 (Revised) Going Concern (w.e.f. 1st April, 2009)

Indicators

Financial indicators – A2neg 2 no2 RCB

1. **A**- Arrears / discontinuance of Dividends
2. **A**- Adverse Financial ratio
3. **Negative** - Negative Net worth/ working capital
4. **Negative**- Negative cash flow from operations
5. **No**- No payment to creditors on due date.
6. **No**- Non compliance with terms in loan agreement
7. **RC** – Rearrangement with Creditors for reduction in liability
8. **B**- Borrowings approaching maturity without any chance of renewal/ repayment.

Operating indicators

1. **L** – Loss of key management and no replacement available.
2. **L** – Loss of major market or supplier
3. **L** – Labour unrest, strikes etc.
4. **L** – Loss or major licence, franchise, etc.
5. Emergence of a highly successful competitor.
6. Management intentions to liquidate the entity or to cease operations.
7. Shortages of important supplies.

2. (a) Mention any four financial events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as going concern.

(4 Marks) MTP Mar. 24

Other Indicators

1. Uninsured or underinsured catastrophes when they occur. (*Law related matters*)
2. Non-compliance with capital or other statutory requirements. (*CAR in Banks*)
3. Changes in law or regulation or government policy expected to adversely affect the entity.
4. Pending legal or regulatory proceedings against the entity that may, if successful, result in claims that the entity is unlikely to be able to satisfy.

Question

S Ltd., a large textile manufacturing company, due to heavy recession in the market was unable to collect amount of huge receivables in time and also holding large amounts of stock of raw materials and finished goods since last 9 months of the Financial Year 2022-23.

From your primary observations of audit evidence, you feel that there is a material uncertainty existing about going concern.

How will you deal in your audit report?

What will be the effect on your audit opinion in the following situations?

- (i) If adequate disclosure of such material uncertainty is already made in the financial statements.**
- (ii) If adequate disclosure of such material uncertainty is not made in the financial statements. (PYP 4 Marks May '23)**

Answer

Use of the Going Concern Basis of Accounting is Appropriate but a Material Uncertainty Exists

The identification of a material uncertainty is a matter that is important to users' understanding of the financial statements. The use of a separate section with a heading that includes reference to the fact that a material uncertainty related to going concern exists alerts users to this circumstance.

(a) Adequate Disclosure of a Material Uncertainty is Made in the Financial Statements

If adequate disclosure about the material uncertainty is made in the financial statements, the auditor shall express an unmodified opinion and the auditor's report shall include a separate section under the heading "Material Uncertainty Related to Going Concern."

(b) Adequate Disclosure of a Material Uncertainty is Not Made in the Financial Statements If adequate disclosure about the material uncertainty is n

auditor shall:

(i) Express a qualified opinion or adverse opinion, as appropriate, in accordance with SA 705 (Revised); and

(ii) In the Basis for Qualified (Adverse) Opinion section of the auditor's report, state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter.

Question

3. Following are examples of events or conditions that may cast significant doubt on an entity's ability to continue as a going concern. Which of following is an example of operating event/conditions?

- (a) Adverse key financial ratios**
- (b) Inability to pay creditors on due dates**
- (c) Indications of withdrawal of financial support by creditors**
- (d) Shortages of important supplies (MTP 1 Mark Oct '23)**

D

Prof. Kuldeep Sandhania

SA 580 Written Representation

Scope	Meaning	Features of WR	Types of WR		Date of WR & Period Covered
Deals with auditors responsibility to obtain WR from those responsible for F.S (mostly mgt, sometimes TCWG)	Written statement by Management ↓ Provided to auditor ↓ To confirm certain matters or support audit evidence	<ol style="list-style-type: none"> Not a substitute to audit procedures Corroborative audit evidence Evaluate reasonableness & consistency of WR Person representing on behalf of management is well informed Sometimes WR may be the only evidence with auditor 	WR about Mgt's responsibility	Other WR	<ul style="list-style-type: none"> As near as practicable but not after the date of AR on FS for period referred to in AR
Objective <ol style="list-style-type: none"> To obtain WR from Management To support other evidence To respond appropriately 	<p><u>Note - Not a sufficient & Appropriate A.E by itself.</u></p> <p>Addressed to Auditor</p>		<ul style="list-style-type: none"> Compulsory Managements Responsibility: <ol style="list-style-type: none"> Preparation & presentation of FS As per AFRf Designing & implementation of ICS Management has provided all information relevant for audit to auditor Any other matter auditor wants to confirm 	<p>Other SA's require auditor to request WR →</p>	

SA 580 Written Representation

Management from whom WR requested	Decision	Form of WR	Communication	WR about Specific assertions
<p>Requested from those responsible for preparation & presentation of FS</p> <p>↓</p> <p>Such individual may vary as per governance structure of entity (generally – management)</p> <p>Hence WR requested from entity's CEO/ CFO/ other equivalent persons / TCWG</p> <p>However management may inquire others who have expertise relating to matters on which WR required. Such individuals include:</p> <ul style="list-style-type: none"> a) Actuary b) Staff Engineers c) Legal Counsels 	<p><u>Decision-1</u></p> <p><u>W.R not Provided</u></p> <p>↓</p> <ul style="list-style-type: none"> a) Discuss with Mgt. b) Re-evaluate reliability & integrity of mgt. c) Modify report – if unable to obtain A.E. <p><u>Decision-2</u></p> <p><u>Doubt about reliability of W.R.</u></p> <p>Perform additional procedure to resolve matter</p> <p>If W.R not reliable</p> <p>↓</p> <p>Reconsider reliability on other W.R.</p> <p>+</p> <p>Modify report where unable to obtain A.E.</p>	<ul style="list-style-type: none"> 1. In form of representation letter addressed to auditor 2. If law requires management to make written public statement about its responsibility → if such responsibility as required by auditor is included in public statement – no need to include it in WR 	<p>Communicate with TCWG about the WR which auditor has requested from management (SA-260)</p>	<p>Auditor may consider:</p> <ul style="list-style-type: none"> a) entity's past history in carrying out its stated intentions b) Entity's reason for choosing a particular course of action c) Entity's ability to pursue a specific course of action d) Lack of other information or information obtained during course of audit which is inconsistent with management's intention

2. (a) Written representation about management's responsibilities involves confirmation of fulfilment of management's responsibilities in the preparation of the financial statements providing the relevant information and also informing about completeness of transactions. Explain.

(4 Marks) (MTP April 24)

Question

Akash & Associates are the statutory auditors of Deluxe Ltd. for the FY 2020 -21. During the course of audit, CA Akash, the engagement partner requested the management of the company to provide written representation with respect to valuation of a transaction. The management, however does not provide the same to CA Akash. What course of action should CA Akash follow in such situation?

(MTP 3 Marks March '23, RTP May'23)

Answer

If management of Deluxe Ltd. does not provide one or more of the requested written representations, CA Akash should:

- (a) Discuss the matter with management;
- (b) Re-evaluate the integrity of management and evaluate the effect that this may have on the reliability of representations (oral or written) and audit evidence in general; and
- (c) Take appropriate actions, including determining the possible effect on the opinion in the auditor's report in accordance with SA 705.

Written representations are to be provided by the management to the auditor when requested. Explain
(RTP Nov '23)

Prof. Kunal Manchanda

Answer

Management from Whom Written Representations Requested: SA-580, “Written Representations”, the auditor shall request written representations from management with appropriate responsibilities for the financial statements and knowledge of the matters concerned.

Written representations are requested from those responsible for the preparation and presentation of the financial statements. Those individuals may vary depending on the governance structure of the entity, and relevant law or regulation; however, management (rather than those charged with governance) is often the responsible party. Written representations may therefore be requested from the entity’s chief executive officer and chief financial officer, or other equivalent persons in entities that do not use such titles. In some circumstances, however, other parties, such as those charged with governance, are also responsible for the preparation and presentation of the financial statements.

If management does not provide one or more of the requested written representations, the auditor shall-

- (i) discuss the matter with management;
- (ii) re-evaluate the integrity of management and evaluate the effect that this may have on the reliability of representations (oral or written) and audit evidence in general; and
- (iii) take appropriate actions, including determining the possible effect on the opinion in the auditor’s report.

The auditor shall disclaim an opinion on the financial statements if management does not provide the written representations.

Students Note

- 3 standards SA 450,260,265 will be sent in Next part

Prof. Kunal Mandhania

10.BANK AUDIT

A close-up photograph of a person's hand in a dark suit jacket, holding a black pen with gold accents and writing on a white document. To the left, a stack of several books is visible, slightly out of focus. The background is a soft, out-of-focus office setting with warm lighting.

Kunal Mandhania



Types of Banks

1) Commercial Banks	<ul style="list-style-type: none">▪ Most wide spread▪ Provide many product and services▪ Two main functions<ul style="list-style-type: none">a) Accepting depositsb) Granting Advances	
2) Regional Rural Banks	<ul style="list-style-type: none">▪ IN Rural Areas▪ To cater basic banking and financial needs of rural communities <p>Eg.: Punjab Gramin Bank</p>	
3) Co-Operative Banks	<ul style="list-style-type: none">▪ Set-Up under co-operative principles▪ Regd. under co-operative Act or MSCS Act. <p>Eg. : Gujrat State Co-operative Bank Ltd.</p>	
4) Payment Banks Eg.: PayTm , Bharat Pe, Airtel Bank	Can	Cannot
	<ul style="list-style-type: none">▪ Open A/cs▪ ATM Services▪ Internet and Mobile banking▪ Accept deposits	<ul style="list-style-type: none">▪ Loan facility▪ Credit card facility
5) Development Banks	<ul style="list-style-type: none">▪ Funds for infra facility▪ Imp for economic growth of country▪ Eg.: IFCI, IDBI, SIDBI etc.	
6) Small Finance Banks	<ul style="list-style-type: none">▪ Basic financial and banking facility▪ For unorganised sectors like formers, small and micro business	



RBI

Basics



- **Regulatory body of all banks**
- **Central Bank of India**

Responsibilities



DDR



(Develop, Determine, Regulate)

- Develop**
Indian financial system
- Determine**
Monetary and credit policies of India
- Regulate**
Activities of all banks

Functions



Licence from R²B²I²

- Licence → Issuing licence to commence banking business**
- R → Regulate → Currency notes**
- R → Regulate → Banks**
- B → Banker to C.G | S.G**
- B → Banker to other banks**
- I → Inspect → Banks**
- I → Issue currency**



Peculiarities involved in banking system

Mnemonic → STATES

- i. **S → Strict Vigilance by RBI**
- ii. **T → Too many transactions**
- iii. **A → Area → Huge Area covered under banking network**
- iv. **T → Transactions → Complex**
- v. **E → Extensive use of technology**
- vi. **S → Services → many services and product offered**



Types of Reports in Banks

Mnemonic → LIST by CA²S

***Reports on :-**

- i. **L → Long form Audit Report (LFAR)**
- ii. **I → Income Recognition**
- iii. **S → SLR requirement compliance**
- iv. **T → Treasury operations**
- v. **C → Compliance of conducted as per RBI guidelines**
- vi. **Ghosh Committee → Fraud / Malpractices**
Jilani Committee → Internal Controls and credit system
- vii. **A → Adverse credit : deposit ratio in rural areas**
- viii. **A → Adequacy of internal financial controls**
- ix. **S → Serious irregularity notice in working of bank**

Different Enactments (Act). Applicable to Bank.

P²RES³C²RIB²E

- P** → Prevention of money laundering Act, 2002.
- P** → Payment and settlement systems Act, 2007
- RE** → Regional Rural Bank Act, 1976

S → SARFAESI, 2002 → Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002

S → SBI Act, 1955

S → SBI (Subsidiary banks) Act, 1959

C → Companies Act, 2013


C → Credit information companies regulation act, 2005

R → RBI Act, 1934

I → I. T Act, 2000

B → Banking Regulation Act, 1949

B → Banking Companies (Acquisition and transfer of undertaking) Act, 1970 & 1980
(this governs nationalise banks)

 → END

Appointment of Auditor

Type of Commercial Bank	Appointment by	Remuneration fixed by
SBI	By C & AG in consultation with CG	By RBI in consultation with CG
Subsidiaries of State Bank of India	By the SBI	By the SBI
Nationalized Banks	By BOD of the Bank with prior approval of RBI	By RBI in consultation with CG
Regional Rural Banks	By the Bank with prior approval of CG	By RBI in consultation with CG
Banking Companies	By shareholders of the Bank with prior approval of RBI	By shareholders

Understanding risk management process

Requirement of adequate Risk Mgt Process (**C R I M E**)

C → **Control activities** – to manage risk including SOD, contingency planning, approval of transaction, setting limits, etc.

R → **Reliable information system** – TCWG / Mgt needs risk management information that is easily understood & assess dynamic nature of risk

I → **Identification, measurement & monitoring of Risk** – risk that could impact banks goals must be identified

M → **Monitoring activities** – risk management models, methodologies, assumptions must be assessed & updated regularly

E → **Ensure proper risk assessment policies / strategies made by TCWG** – whether TCWG approves written risk management policies that are consistent with banks objective

Question

What are the general requirements of an effective Risk Management System in Banks?

(MTP Sep'22 4 Marks)

OR

Mr Rishikesh, the Bank Manager develops controls to assist in managing key business and financial risks. Discuss the various requirements for an effective risk management system in a bank.

(RTP May '23, PYP 4 Marks May '19)

The discussion between members of the engagement team members and the audit engagement partner during Planning (Paper)

1. P- Need to maintain professional skepticism throughout the audit engagement;
2. A - Need to alert for information or other conditions that indicates that a material misstatement may have occurred
3. P – Personnels can adopt which method to do fraud
4. E- Errors that may be more likely to occur;/Errors which have been identified in prior years;
5. R- Audit responses to Risk

Part 3 – Reporting Requirements & other points

Bank Auditors Report

Format of Audit Report

Format – Comply SA 700, 701, 705, 706, 710 + 143 (if bank company)

True & Fair View – state whether B/s, P&L, Cash Flow St. show true & Fair View or not

Unaudited Branches – Provide information about unaudited branches

Reporting to RBI – RBI issued circular on implementation of recommendations of Committee on legal aspect of bank **frauds** – applicable to all scheduled commercial banks (excluding RRB's)

SA-250 – Report under SA 250

Sec. 143(12) & SA 240 – Comply with its requirements as required

LFAR

- Public / Private Sector Bank & Foreign Banks & their Branches
- Matters specified by RBI
- By 30 th june every year

Additional Matters to be reported to CG in Case of Nationalized Banks & SBI

Sec. 30(3) of Banking Regulation Act, requires to state the following:

- T- True and Fair view** – F.s shows
- R- Return** from branch office – adequate
- I- Information & explanation** – satisfactory or not
- P- Transaction** – within **power** of banking company

Note:

1. In banking company, AR should also cover matters u/s 143 of Companies Act, 2013. Also mention that CARO is NA u/s 143(11)
2. In addition to reports, auditors have to furnish 'Certificates' as required by RBI & other regulations

- 1. Long Form Audit report is to be submitted by:
- a. 30th April every year
- b. **30th June every year**
- c. 30th Sep. every year
- d. None of the above

1. The matters which the banks require their auditors to deal with in the long form audit report have been specified by the

a. Central Government

b. State Bank of India

c. Board of Directors of respective banks

d. Reserve Bank of India

Advances Classification as per security

As per Security

1. Primary Security:

Security offered by borrower for bank finance against which credit is extended

1. Collateral Security:

Additional Security, it can be in any form tangible / intangible or movable / immovable assets

Modes of Creating Security (MP HASLE)

- 1. Mortgage- Registered:** affected by mortgage deed signed by mortgager
- **equitable:** affected by mere delivery of title deeds or other documents of title with intention to create Security
- 2. Pledge-** bailment or delivery of goods by borrower to lending bank. Ownership remains with pledger. Pledge of goods is a fixed charge
- 3. Hypothecation-** created for moveable security. Borrower holds physical possession of goods
- 4. Assignment-** transfer of existing / future debts, right or property in favour of another person
- 5. Set-off-** statutory right of creditor to adjust, wholly or partly, the debit balance of debtors account against any credit balance lying in another account of debtor
For purpose of set off, all branches of bank are treated as one single entity can be exercised for time barred debt also
- 6. Lien-** creation of legal charge with consent of owner, which gives lender a right to seize and dispose / liquidate the asset under lien

Explain hypothecation and assignment as the modes of creation of security with respect to advance granted by a bank.

(MTP 4 Marks Oct'22)

Question

Explain pledge and set off as the modes of creation of security with respect to advance granted by a bank.

(MTP 4 Marks March '23)

Types of Advances

FUNDED

- Where actual transfer of funds from bank
- e.G – term loan ,cc, demand loan

NON FUNDED

- Facilities which does not involve transfer
- e.G letter of credit , bank guarantee

Which of the following is fund based advance?

- a. Term loans
- b. Cash credits
- c. Demand Loans
- d. All of the above**

Classification of Advances as per RBI Prudential Norms

Standard Loans

SMA Special Mention A/cs

SMA-0

(A/c showing stress signals but not overdue for more than 30 days)

SMA-1

(overdue between 31 to 60 days)

SMA-2

(overdue between 61 to 90 days)

NPA Loans

1. Sub-standard Assets

NPA for period less than or equal to 12 months

	<u>Secured</u>	<u>Unsecured</u>
<u>Provision</u>	15%	25%
Infrastructure	→ 20%	

2. Doubtful Assets

Sub-standard for 12 months

Doubtful upto	<u>Secured</u>	<u>Unsecured</u>
<1 yr – D1	25%	+ 100%
1-3 yr – D2	40%	+ 100%
> 3 yr – D3	100%	+ 100%

3. Loss Assets

loss identified by Bank / Auditor / RBI Provision
→ 100%

Question

While verifying provisions of advances of a branch of MCO Bank as part of statutory branch audit, CA Z notices that credit facilities consisting of term loan to KRT Enterprises have been classified under doubtful asset (D1) category.

The outstanding balance in above term loan account as on 31.3.2023 is ₹ 50 lakhs. Value of security held in account is ₹ 40 lakhs. The branch has made provision of ₹7.50 lakhs. Is provision made by branch proper? Discuss.

(MTP 4 Marks Sep '23) (RTP May 24)

Answer

The provision for advances falling in D1 category is required @ 25% of secured portion and 100% of unsecured portion. Therefore, provision in above case is arrived as under: -

Outstanding balance as on 31.3.23 ₹ 50 lakhs

Less: Value of security ₹ 40 lakhs

Unsecured portion ₹ 10 lakhs

Therefore, outstanding balance of ₹50 lakhs is secured to the tune of ₹40 lakhs and balance ₹ 10 lakhs is unsecured. Provision calculation

25% of secured part i.e., 25% of ₹40 lakhs ₹ 10 lakhs

100% of unsecured part i.e., 100% of ₹10 lakhs ₹ 10 lakhs

Required provision ₹ 20 lakhs

Therefore, provision made by branch is not proper. It should have made provision of ₹20 lakhs instead of ₹ 7.50 lakhs.

Non-performing Assets (NPA)

a) Term Loan / Bills Discounted

Overdue > 90 days → NPA

b) Credit Cards – atleast Min amt overdue for more than 90 days

c) Cash Credit / OD

NPA if Out of Order > 90 Days

Out of Order

- i. Amount withdrawn is more than drawing power or sanctioned limit**
- ii. when $Crs < Drs$ or no Credit**

Agricultural Advances

d)

Agricultural Advances



Short Duration Crops

Crop Season ≤ 1 yr

NPA –

if overdue > 2 CS

Long Duration Crops

Crop Season > 1 yr **Crop Season** = time from

sowing to harvesting

NPA -

if overdue > 1 CS

Note:

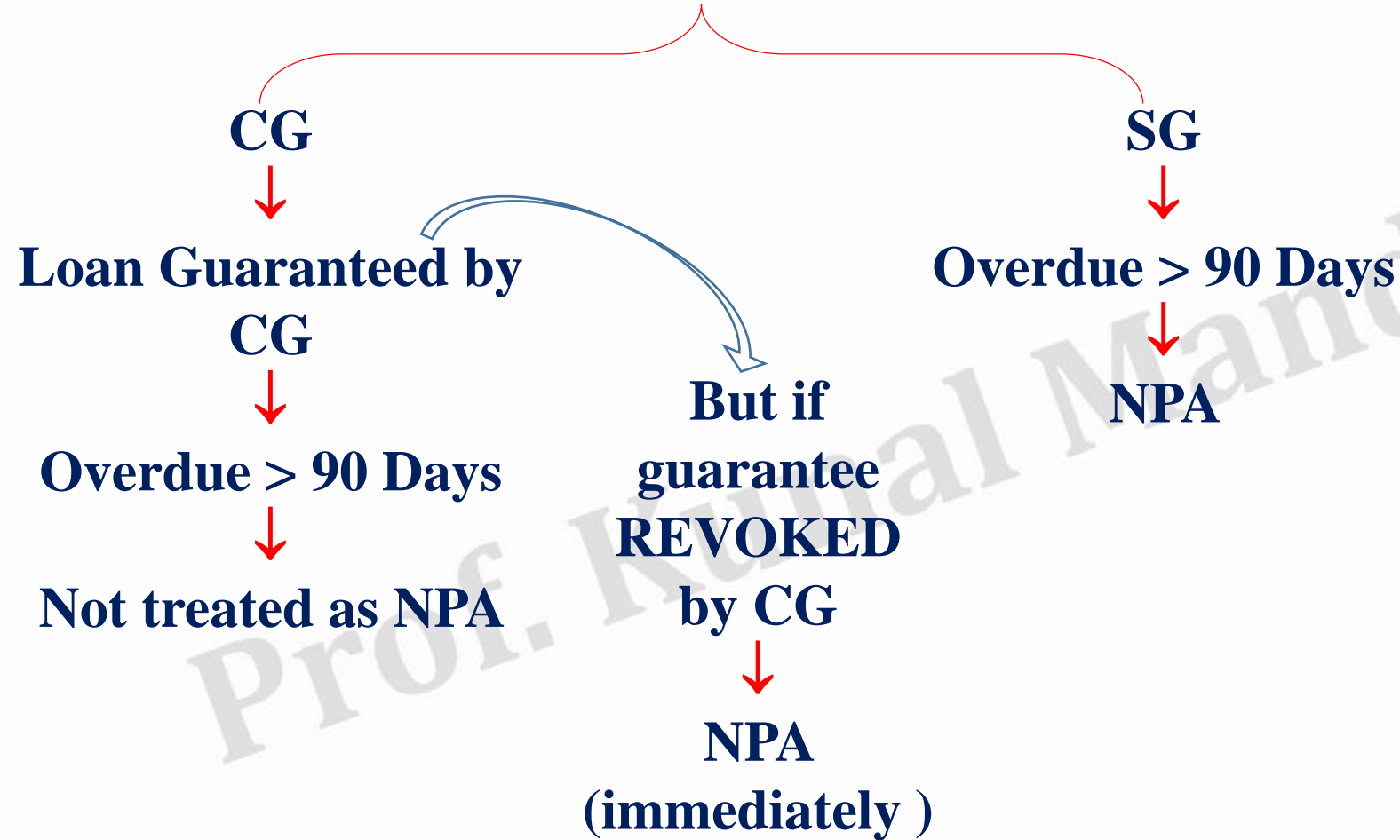
Agriculture advance affected by natural calamities \rightarrow NPA as per new T&C

When is an agricultural advance considered as non performing as per the RBI guidelines?

(MTP 4 Marks Oct'22, MTP 4 Marks March 22)

Non-performing Assets (NPA)

e) Government Guaranteed Advances



Question

**When are following considered as non performing as per the RBI guidelines? (i) Government guaranteed advances
(ii) Advances to staff**

(MTP 4 Marks March '23)

Prof. Kunal Mandhania

Answer

Government Guaranteed advances:

Central Govt. guaranteed Advances, where the guarantee is not invoked/ repudiated would be classified as Standard Assets, but regarded as NPA for Income Recognition purpose.

The situation would be different if the advance is guaranteed by State Government, where advance is to be considered NPA if it remains overdue for more than 90 days for both Provisioning and Income recognition purposes.

Advances to Staff

Interest-bearing staff advances as a banker should be included as part of advances portfolio of the bank. In the case of housing loan or similar advances granted to staff members where interest is payable after recovery of principal, interest need not be considered as overdue from the first quarter onwards. Such loans/advances should be classified as NPA only when there is a default in repayment of installment of principal or payment of interest on the respective due dates. The staff advances by a bank as an employer and not as a banker are required to be included under the sub-head 'Others' under the schedule of Other Assets.

Non-performing Assets (NPA)

f) NPA classification is borrower wise & not facility wise



→ BUSINESS LOAN →

→ CC/OD →

→ LOAN FOR TRANSPORT VEHICLE →

NPA

**Then all other loans
will also be NPA**

→ COMMENT

AB took loan → HDFC Bank

- Car Loan → **NPA**

- Home loan

- Education Loan → **other loans also NPA**

→ ICICI Bank

- Personal Loan → **loans from other banks**

- Credit Card **not NPA**

Non-performing Assets (NPA)

g) Advances under consortium



→ Loan

- SBI
- HDFC
- ICICI
- Axis
- PNB

→ Lead Bank

→ Member banks

→ Borrower repaid the loan

→ Lead Bank

→ Lead bank → Failed to Distribute

→ member bank

overdue > 90 days → NPA

NPA treatment is based on record
of recovery in bank books

Explain "Advances under Consortium" in the context of Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances.

(MTP 4 Marks Nov '21 & MTP 3 Marks Sep '23, PYP 4 Marks Jan '21)

Answer

Advances under Consortium: Consortium advances should be based on the record of recovery of the respective individual member banks and other aspects having a bearing on the recoverability of the advances. Where the remittances by the borrower under consortium lending arrangements are pooled with one bank and/or where the bank receiving remittances is not parting with the share of other member banks, the account should be treated as not serviced in the books of the other member banks and therefore, an NPA.

The banks participating in the consortium, therefore, need to arrange to get their share of recovery transferred from the lead bank or to get an express consent from the lead bank for the transfer of their share of recovery, to ensure proper asset classification in their respective books.

1. Drawing Power in case of a Consortium advance is computed and allocated to member banks by the

a) Bank members proportionately

b) Lead bank

c) Borrower

d) Reserve Bank of India

Non-performing Assets (NPA)

h) Regularization near B/s Date

**Kunal
Mandhania**

→ Home loan → due on 30th April (overdue > 90 days) → NPA

→ Even though the loan a/c
is regularized it is deemed
as NPA

→ VIP
customer of
bank

→ Called
manager

→ Grant
OD / CC

→ Utilized this amount
to pay home loan

2. Non-performing Assets (NPA)

i) On take out finance



AB
ROI = 12%

Take out

During the transfer of
loan to HDFC it
became overdue for >
90 days
→ NPA



Scheme 'Restructure your
loan with us'

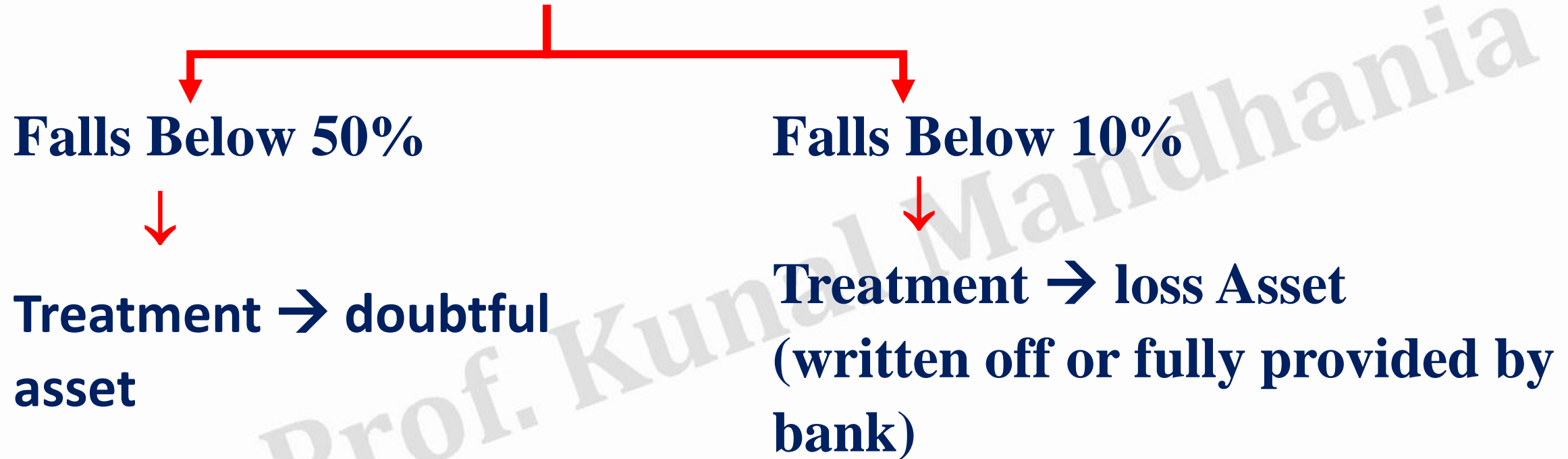
ROI = 10.5%

HDFC will classify it as NPA

**k) Advances against KVP/IVP/NSC/LIP/FD/etc –
Surrender value will be considered**

Non-performing Assets (NPA)

j) Erosion in value of security



CC/OD granted based on stock

CC/OD granted based on stock



thus latest stock statement is required



But it is impossible to provide stock statement as on date



**Hence stock statement for period of 3 months is acceptable
but not older than that**



**If such statement older than
3 months → the account becomes irregular → if irregular >
90 days → NPA**

**Note Where CC/OD limit is 5cr or more bank should
conduct stock audit instead of stock statement**

Type of Loan

When NPA

1) Term Loan / Bill Discount	→	Over Due > 90 days
2) Credit card	→	Minimum <u>Amt</u> > Over due > 90 days due
3) CC/OD	→	Out of order > 90 days
4) Agriculture Advance		
Long Crop	→	Overdue > 1 crop. Season
Short Crop	→	Overdue > 2 crop. Season
5) Govt. Guarantee		Out of order > 90 days
CG	→	Only if CG revokes guarantee
SG	→	Over > 90 days
6) Consortium	→	If lead bank don't rent member bank > 90 days
7) Take out finance	→	If lending bank Take out institution → NPA
8) Loan against LIP / KUP/ IVP	→	Surrender value < loan and overdue > 90 days

Note:- Classify Borrower wise not facility wise → use bank se 1 loan NPA hua to bank uske baki loan ko bhi NPA declare kar

1. The auditors should classify Credit card accounts as NPA, if _____ amount due, as mentioned in the credit card statement is not paid fully within _____ days from next statement date.

a) Total, 90

b) Minimum, 90

c) Minimum, 30

d) Minimum, 60 **(MTP Mar. 22) (1 Mark)**

Income Recognition Rules

i. Standard Assets : accrual basis

ii. NPA - Cash Basis

Note- Income already booked of those Npa assets in previous yrs on accrual but not realized should be reversed

Descriptive Questions

22. While conducting statutory audit of branch of a nationalized bank, it is noticed by CA Z that credit facilities granted to a borrower consisting solely of term loan have been classified as “Sub-standard Asset” during the year 2022-23 due to failure of borrower to pay EMIs on time. Such EMIs were outstanding for more than 90 days and account was, therefore, classified as “Sub-Standard Asset”. CA Z has also agreed to above asset classification made by branch management.

What are CA Z’s responsibilities regarding verification of compliance with income recognition norms by branch in respect of above credit facilities?

(RTP May 24) (MTP 3 Marks Oct’23)

ANSWER

22. RBI norms stipulate that if any advance account becomes NPA as at close of any year, the entire interest accrued or credited to income account in past periods should be reversed or provided for, if the same is not realized.

Further, in respect of NPAs, fees, commission and other similar income that have accrued should cease to accrue in the current period and should be reversed or provided for with respect to past periods, if uncollected.

In the given case, account has turned Sub-standard asset which is a type of NPA. Therefore, auditor should make compliance of above norms relating to income recognition.

Computation of Drawing Power

- a) Generally for CC facility
- b) Limit upto which company or firm can withdraw from working capital limits
- c) Sanctioned limit means total exposure that a bank can take for facilities like C,c , O.D , etc
- d) DP is always less than sanctioned limit
- e) Is amt calculated as per Primary security – margin
- f) Normally it is based on current assets of a client
 - i. STOCK → Stock at NRV
 - (-) Unpaid Stock = paid for stocks
 - (-) Margin %
 - ii. Debtors → Total Debtors
 - (-) Ineligible debtors = eligible debtors
 - (-) Margin

Question

In a bank, all accounts should be kept within the drawing power and the sanctioned limit. The accounts which exceed the sanctioned limit or drawing power should be brought to the notice of the management regularly. Analyse the following points to be considered in the computation of drawing power in case of bank audit.

- (i) Bank's Duties**
- (ii) Auditor's concern**
- (iii) Computation of DP**
- (iv) Stock audit (MTP 4 Marks April '23, PYP 4 Marks Dec '21)**

Answer

Computation of Drawing Power:

- (i) **Bank's Duties:** Banks should ensure that drawings in the working capital account are covered by the adequacy of the current assets. Drawing power is required to be arrived at based on current stock statement. However, considering the difficulties of large borrowers, stock statements relied upon by the banks for determining drawing power should not be older than three months. The outstanding in the account based on drawing power calculated from stock statements older than three months is deemed as irregular.
- (ii) **Auditor's Concern:** The stock statements, quarterly returns and other statements submitted by the borrower to the bank should be scrutinized in detail. The audited Annual Report submitted by the borrower should be scrutinized properly. The monthly stock statement of the month for which the audited accounts are prepared and submitted should be compared and the reasons for deviations, if any, should be ascertained.
- (iii) **Computation of DP:** It needs to be ensured that the drawing power is calculated as per the extant guidelines formulated by the Board of Directors of the respective bank and agreed upon by the concerned statutory auditors. Special consideration should be given to proper reporting of sundry creditors for the purposes of calculating drawing power.
- (iv) **Stock Audit:** The stock audit should be carried out by the bank for all accounts having funded exposure of more than 5 crores. Auditors can also advise for stock audit in other cases if the situation warrants the same. Branches should obtain the stock audit reports from lead bank in the cases where the Bank is not leader of the consortium of working capital. The report submitted by the stock auditors should be reviewed during the course of the audit and special focus should be given to the comments made by the stock auditors on valuation of security and calculation of drawing power.

1. The term “Drawing Power” is associated with which of the following facilities as sanctioned by any Bank:

- a. Letter of Credit
- b. Term Loan
- c. Staff Advances
- d. Cash Credit Limit** (RTP Mar 23)

Large advances

- What constitutes a '**LARGE ADVANCE**' would need to be determined in the context of volume of operations of the branch. As a general rule, however, an advance may be considered to be a large advance if the year-end balance is **in excess of Rs. 2 crore or 5% of the aggregate year- end advances of the branch, whichever is less.**
- **In carrying substantive procedures, auditor should examine all large advances while other advances may be examined on sampling basis**

6. Audit of Advances

Audit is concerned with obtaining evidence about the following:
(Shortcut – A to S)

- A** – Adequate Margin kept – to secure – future risk
- B** – Borrowing / Drawing power – properly calculated
- C** – Calculations – Correct
- D** – Disclosure requirements in B/s – Complied
- E** – Physical Enquiry – Timely basis
- F** – Figures – Accurate

6. Audit of Advances

G – Guarantee / security – Properly documented

H – x

I – Interest on N.P.A taken only when received

J – x

K – x

L – Laws (Acts) – Complied & Examine all large advances

M – Mortgage deeds & other docs properly maintained

6. Audit of Advances

- N** – N.P.A properly classified
- O** – Overall systems is adequate
- P** – Provisions properly made
- Q** – x
- R** – Recording of Advances - Correct
- S** – Sanctioning Rules - Followed

Question

a) Advances generally constitute the major part of the assets of the bank. There are large number of borrowers to whom variety of advances are granted. The audit of advances requires the major attention from the auditors. In carrying out audit of advances, the auditor is primarily concerned with obtaining evidence about, among other points, the amounts included in balance sheet in respect of advances are outstanding at the date of the balance sheet. Explain.

(RTP Nov '23, RTP Nov '19, RTP May 21, RTP Nov'22)

Descriptive Questions

(b) Following is the extract from Schedule no. 10 of Advances as appearing in financial statements of branch of a nationalized bank for year ending 31st March, 2024.

Schedule 10 – Advances

S. No.	Particulars	Amount (In ` Crores) rounded off
1.	Bills Purchased and Discounted	50.00
2.	Cash credits, overdrafts and loans repayable on demand	150.00
3.	Term Loans	75.00
	Total	275.00

In carrying out audit of above advances as part of statutory audit of branch, a statutory auditor would obtain evidence about certain matters.

State those matters.

(4 Marks) (MTP April 24)

- In carrying out audit of advances, the auditor is primarily concerned with obtaining evidence about amounts included in balance sheet in respect of advances which are outstanding. Explain stating clearly all the considerations in this context.(RTP Nov. 22)

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7. Evaluation of Internal Controls over Advances

Internal Controls should include: (**AD**vance **G**iven to **CREDITOR**)

- A** – adequate margin kept against securities, check its availability at regular intervals
- D** – Documents to be executed by parties before giving loans
- G** – goods in possession of bank, the content of it must be checked at time of receipt
- C** – credit worthiness of borrower to be satisfied before sanctioning any advance by proper authority
- R** – registration of securities in name of bank or equivalent document sufficient to give title to bank if security on basis of security
- E** – end use of funds & compliance of T&C be ensured
- D** – drawing power register should be updated every month
- I** – irregular a/c to be brought to notice of controlling authority regularly
- O** – ownership of securities in nature of shares / debentures must be transferred to bank & shall be documented
- R** – review operation of each advance atleast once in a year & more frequent intervals in large advances

Question

The auditor should examine the efficacy of various internal controls over advances to determine the nature, timing and extent of his substantive procedures. Explain this statement.

(MTP 4 Marks March 22, Old SM, MTP 4 Marks April 19, RTP Nov '18 & May '19, PYP 5 Marks Nov '18)

Audit of Income → Interest Income

- 1) **RBI Direction** = Material Income (51% of total income) → Accrual basis
- 2) **Material (on Accrual basis)** = Non material income = Cash basis
- 3) **Certainly recovery** = Accrual basis
- 4) **NPA** = Cash basis
- 5) **Leased Asset** → Interest → reverse if NPA → (Check)
- 6) **Bill discounted** → commission → Properly apportion to duration of bill
- 7) **Re-negotiation** → Commission → Properly apportion to duration of loan
- 8) **Reversal of Income** → in case of NPA → Properly done
- 9) **Secured advances** → Interest (income) → on accrual basis
- 10) **Partial recovery** → in case of NPA → cash basis enter
 - No upgration to standard amount
 - No provisional universal
- 11) **Memorandum a/c** → Calculation purpose → interest on NPA

REVERSAL OF INCOME

- If any advance, including bills purchased & discounted, becomes NPA as at the close of any year, the entire interest accrued & credited to income account in the past periods, should be **reversed or provided for** if the same is not realised. This will apply to Government guaranteed **accounts also**.
- In respect of NPAs, fees, commission & similar income that have accrued should cease to accrue in the current period & should be **reversed or provided for** with respect to past periods, if uncollected.
- Further, in case of banks which have wrongly recognised income in the past should **reverse** the interest if it was recognised as income during the current year or make a **provision for an equivalent amount** if it was recognized as **income in the previous year(s)**.

MEMORANDUM ACCOUNT

- On an account turning NPA, banks should reverse the interest already charged & not collected by debiting Profit & Loss account, & stop further application of interest. However, banks may continue to record such **accrued interest in a Memorandum account** in their books for control purposes. For the purpose of computing Gross Advances, interest recorded in the Memorandum account should not be taken into account.

Income from Investment

1) Interest Income

- Includes all income except from subsidiary / TV abroad / India
- Broken Period Interest paid & Amortisation of Premium on SLR investment to net all from Income

2) Profit on sale of Investment

3) Profit /Loss on Revaluation of Investment

- Valued at period Interval
- Depreciation / appreciation to be taken to P & L A/c

Expense Audit

Interest Expense

Check RAVI



R → Reasonableness check ratios on diff. types to average interest liability

A → ARP

- Trend analysis – Check with P.Y
- Check budgeted with Actual

VI → Verification of interest calculation



Test check



- ✓ Calculation
- ✓ Excess/short
- ✓ Regulation
- ✓ Classification savings / F.D

Operating Expenses

Check DIVA



D → Divergent trend check whether change in trend

I → Check Internal controls check system including authorisation

V → Vouch & verify with supportive document

A → ARP

✓ Check ratio of expense to total operating expenses

✓ Check trends of previous year

Shortcut → G.F ki saheli Check



Baat Karo

→ 1) Check compliance of law



Samjho

→ 2) Understand computation / calculation



Firt Karo

→ 3) Sample loan classification verification



Break up

→ 4) Obtain detailed break up of types of substandard / NPA & compare with o/s balance



Lapak lo бага

→ 5) Re-computation



Old G.F se Harzana Bhugatha Padega

→ 6) Re-compute Provision for tax

Explain the audit approach you would follow to check the Operating Expenses of a Bank.

**(MTP 4 Marks Sep'22 & April '23,
RTP May '23, RTP May'22, Old SM)**

Question

Your firm of Chartered Accountants has been appointed as auditor of a Nationalised bank. Explain how will you proceed to carry out audit of provisions and contingencies.

(MTP 4 Marks Oct 20, RTP May'22, Old & New SM)

- **Explain the audit approach you would follow to check the Operating Expenses of a Bank. (4 Marks) (MTP Sep. 22)**

Which of the following does not constitute “Other income” in the profit and loss account of branch of a bank?

- a) Discount on Bills purchased**
- b) Commission on Bills sent for collection
- c) Loan processing fees
- d) Credit card fees(2 Marks) (MTP Oct. 22)

-

Descriptive Questions

(b) CA B is statutory auditor of Boom Payments Bank for year 2023-24. During the year, banking regulator has imposed restrictions on Bank from accepting new deposits due to non-compliance in conducting KYC in large number of accounts and violation of rules aimed at preventing money laundering. There is material uncertainty regarding probable outcome of such restrictions on ability of Bank to continue as going concern. However, for year 2023-24, auditor has concluded that use of going concern basis of accounting is appropriate. The financial statements of Bank do not make adequate disclosure of material uncertainty due to above events in financial statements. What are implications for auditor's report for year 2023-24 in view of above?

(4 Marks) MTP Mar. 24

ANSWER

(b) As described in the situation given in the question, banking regulator has

imposed restrictions due to non-compliance with regulatory requirements and there is material uncertainty of such events or conditions which may cast a significant doubt on ability of Bank to continue as going concern. However, the financial statements of Bank do not make adequate disclosure of material uncertainty due to above events in financial statements.

If adequate disclosure about the material uncertainty is not made in the financial statements, the auditor shall:

- (i) Express a qualified opinion or adverse opinion, as appropriate, in accordance with SA 705.**
- (ii) In the Basis for Qualified (Adverse) Opinion section of the auditor's report, state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter.**

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