

PAPER – 6 : AUDITING AND ASSURANCE

Question No.1 is compulsory.

*Attempt any **five** questions from the remaining **six** questions.*

Question 1

Discuss the following:

- (a) *Write the circumstances that indicate the possibility of fraud due to problematic or unusual relationship between the auditor and management. (5 Marks)*
- (b) *Write the steps that are taken for an audit to be carried out in a systematic and efficient manner. (5 Marks)*
- (c) *During the audit of PQR Ltd. you as an auditor requested officers of the company to have access to secretarial records and correspondence which they refused to provide. Comment. (5 Marks)*
- (d) *As per the provisions of the companies Act, 2013 the report of Board of Director on annual accounts shall also include a 'Director's Responsibility Statement'. Comment. (5 Marks)*

Answer

- (a) **Problematic or unusual relationships between the auditor and management, including:**
1. Denial of access to records, facilities, certain employees, customers, vendors, or others from whom audit evidence might be sought.
 2. Undue time pressures imposed by management to resolve complex or contentious issues.
 3. Complaints by management about the conduct of the audit or management intimidation of engagement team members, particularly in connection with the auditor's critical assessment of audit evidence or in the resolution of potential disagreements with management.
 4. Unusual delays by the entity in providing requested information.
 5. Unwillingness to facilitate auditor access to key electronic files for testing through the use of computer-assisted audit techniques.
 6. Denial of access to key IT operations staff and facilities, including security, operations, and systems development personnel.
 7. An unwillingness to add or revise disclosures in the financial statements to make them more complete and understandable.
 8. An unwillingness to address identified deficiencies in internal control on a timely basis.

9. Unwillingness by management to permit the auditor to meet privately with those charged with governance
10. Accounting Policy that appears to be variance with industry norms
11. Frequent changes in accounting estimates that do not appear to result from changed circumstances
12. Tolerance of variations in the entity's code of conduct

(b) In order that an audit may be carried out in a systematic and efficient manner, the following steps should be taken:

- (1) Work must be carried on regularly and record kept of time of arrival/departure of the staff and also of the work done each day;
- (2) As far as possible, a definite portion of the work should be completed each day so that loose ends are not left over for being tied up at a later date;
- (3) Entries should be made in the audit note book and the audit programme initialled as a routine;
- (4) Coloured pencils and different type of ticks must be employed to indicate the various audit processes which have been applied and their significance must not be disclosed to the client;
- (5) All the vouchers after examination must be immediately cancelled with an audit stamp;
- (6) Staff members should refrain from discussing the client's affairs amongst themselves and with outsiders.

(c) Right of Access to secretarial records and correspondence:

1. Section 143(1) of the Companies Act, 2013 grants powers to the auditor that every auditor has a right of access, at all times, to the books of account and vouchers of the company kept at Registered or Head Office, branches and subsidiaries in the case of a Holding Company for conducting the audit.
2. Further, he is also entitled to require from the officers of the company such information and explanations which he considers necessary for the proper performance of his duties as Auditor. Therefore, he has a statutory right to inspect the secretarial records and correspondence.
3. In order to verify actions of the company and to vouch and verify some of the transactions of the company, it is necessary for the auditor to refer to the decisions of the shareholders and/or the directors of the company. It is, therefore, essential for the auditor to refer to the secretarial records and correspondence which also includes Minute book. In the absence of the same, the auditor may not be able to vouch/verify certain transactions of the company.

4. The refusal to provide access to secretarial records and correspondence shall constitute limitation of scope as far as the auditor's duties are concerned.
 5. The auditor may examine whether by performing alternative procedures, the auditor can substantiate the assertions or else he shall have to either qualify the report or give a disclaimer of opinion.
- (d) **Director's Responsibility Statement:** According to section 134(3)(c) of the Companies Act, 2013, the report of board of directors on annual accounts shall also include a 'Director's Responsibility Statement'. However, the provisions related to Director's Responsibility Statement are provided under section 134(5) of the Companies Act, 2013 which requires to state that-
- (i) in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures;
 - (ii) the directors had selected such accounting policies and applied them consistently and made judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the profit and loss of the company for that period;
 - (iii) the directors had taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of this Act for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;
 - (iv) the directors had prepared the annual accounts on a going concern basis;
 - (v) the directors, in the case of a listed company, had laid down internal financial controls to be followed by the company and that such internal financial controls are adequate and were operating effectively.
 - (vi) the directors had devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems were adequate and operating effectively.

Question 2

*State with reasons (in short) whether the following statements are correct or incorrect: (Answer any **Eight**)*

- (a) *Audit notes can serve as a guide in framing Audit programme.*
- (b) *Procedures and Techniques are often used interchangeably in an audit.*
- (c) *For auditor's opinion, reasonable assurance is an absolute level of assurance.*
- (d) *The results of all cases of surprise checks are included in auditor's report on the accounts.*
- (e) *General CIS controls may have pervasive effect on the processing of transactions in application system.*
- (f) *Any item of income or expenditure which exceeds 1% of the net profit of the company or ₹ 2 lakh whichever is lower, is required to be disclosed in Profit & Loss A/c.*

- (g) *Internally generated Goodwill can be recognized as an asset.*
- (h) *Sample size is not a valid criterion to distinguish between statistical and non-statistical approaches.*
- (i) *A government company which is in existence since 5 years cannot make political contributions.*
- (j) *The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error.* **(8 x 2 = 16 Marks)**

Answer

- (a) **Correct:** Audit notes can serve as a guide in framing audit programme in the future as they indicate the weaknesses in the system of the client which specially need to be watched.
- (b) **Correct:** The two terms, procedure and techniques, are often used interchangeably. However, a distinction does exist. Procedure may comprise a number of techniques and represents the broad frame of the manner of handling the audit work; techniques stand for the methods employed for carrying out the procedure.
- (c) **Incorrect:** Reasonable assurance is a high level but not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive.
- (d) **Incorrect:** It is not necessary in all cases for the results of the surprise checks to be included in the auditors' report on the accounts. They should, however, be included if in the opinion of the auditor they are material and affect a true and fair view of the accounts on which he is reporting.
- (e) **Correct:** The general CIS controls may have a pervasive effect on the processing of transactions in application systems. If these controls are not effective, there may be a risk that misstatements might occur and go undetected in the application systems.
- (f) **Incorrect:** A Company shall disclose by way of notes additional information regarding any item of income or expenditure which exceeds one per cent of the revenue from operations or ₹ 1,00,000, whichever is higher;
- (g) **Incorrect:** As per AS-26, internally generated goodwill is not recognized as an asset because it is not an identifiable resource controlled by the enterprise that can be measured reliably at cost.
- (h) **Correct:** The decision whether to use a statistical or non-statistical sampling approach is a matter for the auditor's judgment; however, sample size is not a valid criterion to distinguish between statistical and non-statistical approaches.

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

- (i) **Incorrect:** Section 182 of the Companies Act 2013 deals with prohibition and restriction regarding political contributions. According to this section, a government company or any other company which has been in existence for less than three financial years cannot contribute any amount directly or indirectly to any political party.
- (j) **Correct:** The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error. This is because fraud may involve sophisticated and carefully organized schemes designed to conceal it, such as forgery, deliberate failure to record transactions, or intentional misrepresentations being made to the auditor. Such attempts at concealment may be even more difficult to detect when accompanied by collusion.

Question 3

How will you vouch/verify the following?

- (a) *Recovery of Bad debts written off*
- (b) *Receipt of Insurance claims*
- (c) *Payment of Taxes*
- (d) *Sale proceeds of scrap material* **(4 x 4 = 16 Marks)**

Answer

- (a) **Recovery of Bad Debts written off:** Recovery of bad debts written off is verified with reference to relevant correspondence and proper authorisation.
- (i) Ascertain the total amount lying as bad debts and verify the relevant correspondence with the trade receivables whose accounts were written off as bad debt.
- (ii) Ensure that all recoveries of bad debts have been properly recorded in the books of account.
- (iii) Examine notification from the Court or from bankruptcy trustee. Letters from collecting agencies or from account receivables should also be seen.
- (iv) Check Credit Manager's file for the amount received and see that the said amount has been deposited into the bank promptly.
- (v) Vouch acknowledgement receipts issued to account receivables or trustees.
- (vi) Review the internal control system regarding writing off and recovery of bad debts
- (b) **Receipt of Insurance Claims:** Insurance claims may be in respect of fixed assets or current assets. While vouching the receipts of insurance claims-
- (i) The auditor should examine a copy of the insurance claim lodged with the insurance company correspondence with the insurance company and with the insurance agent should also be seen. Counterfoils of the receipts issued to the insurance company should also be seen.

- (ii) The auditor should also determine the adjustment of the amount received in excess or short of the value of the actual loss as per the insurance policy.
- (iii) The copy of certificate/report containing full particulars of the amount of loss should also be verified.
- (iv) The accounting treatment of the amount received should be seen particularly to ensure that revenue is credited with the appropriate amount and that in respect of claim against asset, the Statement of Profit and Loss is debited with the short fall of the claim admitted against book value, if the claim was lodged in the previous year but no entries were passed, entries in the Statement of Profit and Loss should be appropriately described.

(c) Payment of Taxes:

- (i) Obtain the computation of taxes prepared by the auditee and verify whether it is as per the Income Tax Act/ Rules/ Notifications/ Circulars etc.
- (ii) Examine relevant records and documents pertaining to payment of advance income tax and self assessment tax.
- (iii) Payment on account of income-tax and other taxes like GST consequent upon a regular assessment should be verified by reference to the copy of the assessment order, notice of demand and the receipted challan acknowledging the amount paid.
- (iv) The penal interest charged for non-payment should be debited to the interest account.
- (v) Nowadays, electronic payment of taxes is also in trend. Such electronic payment of taxes by way of internet banking facility or credit or debit cards shall also be verified.
- (vi) The assessee can make electronic payment of taxes also from the account of any other person. Therefore, it should be verified that the challan for making such payment is clearly indicating the PAN No./TAN No./TIN No./GSTIN etc. of the assessee on whose behalf the payment is made.

(d) Sale Proceeds of Scrap Material:

- (i) Review the internal control on scrap materials, as regards its generation, storage and disposal and see whether it was properly followed at every stage.
- (ii) Ascertain whether the organisation is maintaining reasonable records for the sale and disposal of scrap materials.
- (iii) Review the production and cost records for determination of the extent of scrap materials that may arise in a given period.
- (iv) Compare the income from the sale of scrap materials with the corresponding figures of the preceding three years.
- (v) Check the rates at which different types of scrap materials have been sold and compare the same with the rates that prevailed in the preceding year.

- (vi) See that scrap materials sold have been billed and check the calculations on the invoices.
- (vii) Ensure that there exists a proper procedure to identify the scrap material and good quality material is not mixed up with it and sold as scrap
- (viii) Make an overall assessment of the value of the realisation from the sale of scrap materials as to its reasonableness.

Question 4

Answer *all* questions:

- (a) *What are the provisions prescribed under Companies Act, 2013 in respect of ceiling on number of audits in a company to be accepted by an auditor?* **(4 Marks)**
- (b) *What are the considerations for an auditor regarding the operating effectiveness of controls using audit evidence obtained in previous audits?* **(6 Marks)**
- (c) *As an auditor, how would you consider the acceptance of a change in audit engagement?* **(6 Marks)**

Answer**(a) Ceiling on number of Audits:**

1. Section 141(3)(g) of the Companies Act, 2013 prescribes that a person shall not be eligible for appointment as an auditor of a company namely – a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such person or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies other than one person companies, dormant companies, small companies and private companies having paid-up share capital less than ₹ 100 crore.
2. In the case of a firm of auditors, it has been further provided that 'specified number of companies' shall be construed as the number of companies specified for every partner of the firm who is not in full time employment elsewhere. This limit of 20 company audits is per person. In the case of an audit firm having 3 partners, the overall ceiling will be $3 \times 20 = 60$ company audits.
3. Sometimes, a chartered accountant is a partner in a number of auditing firms. In such a case, all the firms in which he is partner or proprietor will be together entitled to 20 company audits on his account. Subject to the overall ceiling of company audits, how they allocate the 20 audits between themselves is their affairs.

- (b) Using Audit Evidence Obtained in Previous Audits:** 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, including whether it is manual or automated;
- (iii) The effectiveness of general IT-controls;
- (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 affect the application of the control;
- (v) Whether the lack of a change in a particular control poses a risk due to changing circumstances; and
- (vi) The risks of material misstatement and the extent of reliance on the control.

If the auditor plans to use audit evidence from a previous audit about the operating effectiveness of specific controls, the auditor shall establish the continuing relevance of that evidence by obtaining audit evidence about whether significant changes in those controls have occurred subsequent to the previous audit.

(c) Acceptance of a Change in Engagement:

1. 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.
2. 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.
3. 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:
 - (1) the original engagement; or
 - (2) 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.

4. The auditor should not agree to a change of engagement where there is no reasonable justification for doing so.
5. 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.
6. 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:
 - (a) Withdraw from the audit engagement where possible under applicable law or regulation; and
 - (b) 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.

Question 5

Answer *all* questions:

- (a) *The Auditor is fully satisfied with the audit of an entity in respect of its systems and procedures and wants to issue a report without any hesitation. What type of opinion can be give and state give reasoning. (4 Marks)*
- (b) *A junior accountant of a limited company has not separated transactions of one period from those in the ensuing period. As an Auditor, state the correct procedure to be followed and the areas in which it can be applied. (6 Marks)*
- (c) *During the course of audit of an entity, the Auditor ascertains that the internal control system is not effective and rather weak with certain lapses. Give in detail the communication in this regard the Auditor will have with the management. (6 Marks)*

Answer

(a) Unqualified Opinion:

1. An unqualified opinion should be expressed when the auditor concludes that the financial statements give a true and fair view in accordance with the financial reporting framework used for the preparation and presentation of the financial statements.
2. An unqualified opinion indicates, implicitly, that any changes in the accounting principles or in the method of their application, and the effects thereof, have been properly determined and disclosed in the financial statements.
3. An unqualified opinion also indicates that:
 - (i) the financial statements have been prepared using the generally accepted accounting principles, which have been consistently applied;

- (ii) the financial statements comply with relevant statutory requirements and regulations; and
- (iii) there is adequate disclosure of all material matters relevant to the proper presentation of the financial information, subject to statutory requirements, where applicable.

(b) Cut-off Arrangement:

1. Accounting is a continuous process because the business never comes to halt. It is, therefore, necessary that transactions of one period would be separated from those in the ensuing period so that the results of the working of each period can be correctly ascertained. The arrangement that is made for this purpose is technically known as "cut-off arrangement".
2. It essentially forms part of the internal control system of the organisation.
3. Accounts, other than sales, purchase and inventory are not usually affected by the continuity of the business and therefore, this arrangement is generally applied only to sales, purchase and inventory.
4. The auditor satisfies by examination and test-checks that the cut-off procedures are adequately followed and ensure that:
 - (i) Goods purchased, property in which has already been passed on to the client, have in fact been included in the inventories and that the liability has been provided for in case credit purchase.
 - (ii) Goods sold have been excluded from the inventories and credit has been taken for the sales. If the value of sales is to be received, the concerned party has been debited.
5. The auditor may examine a sample of documents, evidencing the movement of inventory into and out of stores, including documents pertaining to period shortly before and after the cut-off date and check whether inventories represented by those documents were included or excluded as appropriate during inventory taking for perfect and correct presentation in the financial statements.

(c) Communication of Weaknesses in Internal Control:

1. **Weakness in Internal Control:** As a result of obtaining an understanding of the accounting and internal control systems and tests of control, the auditor may become aware of weaknesses in the systems. The auditor should make management aware, as soon as practical and at an appropriate level of responsibility, of material weaknesses in the design or operation of the accounting and internal control systems, which have come to the auditor's attention. The communication to management of material weaknesses would ordinarily be in writing. However, if the auditor judges that oral communication is appropriate, such communication would be documented in the audit working papers. It is important to indicate in the communication that only

weaknesses which have come to the auditor's attention as a result of the audit have been reported and that the examination has not been designed to determine the adequacy of internal control for management purposes.

2. **Identification of weakness:** The auditor shall determine whether, on the basis of the audit work performed, the auditor has identified one or more deficiencies in internal control. If the auditor has identified one or more deficiencies in internal control, the auditor shall determine, on the basis of the audit work performed, whether, individually or in combination, they constitute significant deficiencies.
3. **Communication to the management -** The auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis.

The auditor shall also communicate to management at an appropriate level of responsibility on a timely basis:

- (1) In writing, significant deficiencies in internal control that the auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances; and
 - (2) Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties and that, in the auditor's professional judgment, are of sufficient importance to merit management's attention.
4. **Content of communication of weakness:** The auditor shall include in the written communication of significant deficiencies in internal control:
 - (1) A description of the deficiencies and an explanation of their potential effects; and
 - (2) Sufficient information to enable those charged with governance and management to understand the context of the communication. In particular, the auditor shall explain that:
 - (i) The purpose of the audit was for the auditor to express an opinion on the financial statements;
 - (ii) The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control; and
 - (iii) The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance.

Question 6

Answer *all* questions:

- (a) A limited company has disclosed Trade Receivables in its Balance Sheet as Gross receivable less provision for Bad debts. Mention disclosure requirements of the same in its financial statements as per Companies Act, 2013. **(4 Marks)**
- (b) What is the basis on which the judgement is formed by Auditor to express his opinion after the audit? **(6 Marks)**
- (c) At the time of scrutiny of General Ledger the Auditor observes that certain expenses essentially of a revenue nature are wrongly treated as capital expenditure. State examples of such expenses and the duties of auditor in this regard. **(6 Marks)**

Answer**(a) Disclosure requirement of Trade Receivables as per the Companies Act, 2013:**

- (i) Aggregate amount of Trade Receivables outstanding for a period exceeding six months from the Date they are due for payment should be separately stated.
- (ii) Trade receivables shall be sub-classified as:
- (a) Secured, considered good;
- (b) Unsecured considered good;
- (c) Doubtful.
- (iii) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.
- (iv) Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

(b) Process of Judgement Formation by Auditor:

1. After the audit, the opinion that the auditor expresses is the result of exercise of judgement on facts, evidence and circumstances which he comes across in the course of audit.
2. The judgement is formed on the following basis-
 - a. Identification of the assertions to be examined.
 - b. Evaluation of the assertion as to relative importance.
 - c. Collection of the information or evidence about the assertions to enable him to give an informed opinion.

- d. Evaluation of evidence as valid or invalid, pertinent or not pertinent, sufficient or insufficient.
- e. Formulation of judgement as to the fairness of the assertions under consideration.

(c) Revenue expenses wrongly treated as capital expenditure

Expenses which are essentially of a revenue nature, if incurred for non-creation of an asset or which do not result in achieving higher productivity of the existing asset, are to be treated as revenue, and not as capital expenditure.

Examples of such revenue expenses which may be wrongly treated as capital expenditure are as under

- (i) Material and wages – Expenses which are incurred on the normal repairs of a building or machinery
- (ii) Legal expenses – Expenses incurred to protect existing assets
- (iii) Freight – Transport expenses incurred for repairing the machinery at the manufacturer's site.
- (iv) Repair – Repairs to existing plant & machinery which do not increase its productivity
- (v) Wages – Wages paid for regular repair to plant & machinery
- (vi) Interest – Interest paid on loan for the construction of a building after the qualification period as per AS-16 i.e. after the building is constructed

Auditor's duty: Whenever, therefore, a part of the expenditure ostensibly of a revenue nature is wrongly capitalized, it is the duty of the auditor to assess the implications on the financial statements and include it in his report.

Question 7

Write short notes on any **four** of the following:

- (a) *Techniques of suppressing cash receipts.*
- (b) *Monitoring of controls.*
- (c) *Performance audit under government accounting system.*
- (d) *Physical verification of Fixed assets "at reasonable intervals".*
- (e) *External confirmation as audit procedure.*

(4 x 4 =16 Marks)

Answer

- (a) Techniques of Suppressing Receipts:** Few Techniques of how receipts are suppressed are:

- (1) Teeming and Lading: Amount received from a customer being misappropriated; also to prevent its detection the money received from another customer subsequently

being credited to the account of the customer who has paid earlier. Similarly, moneys received from the customer who has paid thereafter being credited to the account of the second customer and such a practice is continued so that no one account is outstanding for payment for any length of time, which may lead the management to either send out a statement of account to him or communicate with him.

- (2) Adjusting unauthorised or fictitious rebates, allowances, discounts, etc. to customer' accounts and misappropriating amount paid by them.
- (3) Writing off as debts in respect of such balances against which cash has already been received but has been misappropriated.
- (4) Not accounting for cash sales fully.
- (5) Not accounting for miscellaneous receipts, e.g., sale of scrap, quarters allotted to the employees, etc.
- (6) Writing down asset values in entirety, selling them subsequently and misappropriating the proceeds.

(b) Monitoring of Controls:

1. The auditor shall obtain an understanding of the major activities that the entity uses to monitor internal control over financial reporting, including those related to those control activities relevant to the audit, and how the entity initiates remedial actions to deficiencies in its controls.
2. Monitoring of controls is a process to assess the effectiveness of internal control performance over time. It involves assessing the effectiveness of controls on a timely basis and taking necessary remedial actions. Management accomplishes monitoring of controls through ongoing activities, separate evaluations, or a combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of an entity and include regular management and supervisory activities.
3. Management's monitoring activities may include using information from communications from external parties such as customer complaints and regulator comments that may indicate problems or highlight areas in need of improvement.
4. In case of small entities, management's monitoring of control is often accomplished by management's or the owner-manager's close involvement in operations. This involvement often will identify significant variances from expectations and inaccuracies in financial data leading to remedial action to the control.

(c) Performance audit -

1. The scope of audit has been extended to cover efficiency, economy and effectiveness audit or performance audit, or full scope audit.
2. Efficiency audit looks into whether the various schemes/projects are executed and their operations conducted economically and whether they are yielding the results

expected of them, *i.e.*, the relationship between goods and services produced and resources used to produce them; and examination aimed to find out the extent to which operations are carried out in an economical and efficient manner.

3. Economy audit looks into whether government have acquired the financial, human and physical resources in an economical manner, and whether the sanctioning and spending authorities have observed economy.
4. Effectiveness audit is an appraisal of the performance of programmes, schemes, projects with reference to the overall targeted objectives as well as efficiency of the means adopted for the attainment of the objectives. Efficiency-cum-performance audit, wherever used, is an objective examination of the financial and operational performance of an organisation, programme, authority or function and is oriented towards identifying opportunities for greater economy, and effectiveness. The procedure for conducting performance audit covers identification of topic, preliminary study, planning and execution of audit, and reporting. While the trend towards a comprehensive approach for conducting performance of full scope audit is visible, the coverage and depth of evaluation vary according to the statutory limitations, and the organisational constraints of C&AG.

(d) Physical verification of Fixed Assets at Reasonable Intervals:

1. Physical verification of fixed assets is primarily a responsibility of the management. The management is required to carry out physical verification of fixed assets at appropriate intervals in order to ensure that they are in existence.
2. However, the auditor should satisfy himself that such verification was done by the management wherever possible and by examining the relevant working papers. The auditor should also examine whether the method of verification was reasonable in the circumstances relating to each asset. The reasonableness of the frequency of verification should also be examined by the auditor in the circumstances of each case.
3. The auditor should test check the book records of fixed assets with the physical verification reports. He should examine whether discrepancies noticed on physical verification have been properly dealt with.
4. Further, it is duty of the auditor to report as per clause 1(b) of Para 3 of CARO 2016 that whether these fixed assets have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account. What constitutes 'reasonable interval' depends on the circumstances of each case.

(e) External Confirmation as audit procedure:

1. An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.

2. External confirmation procedures frequently are relevant when addressing assertions associated with certain account balances and their elements. However, external confirmations need not be restricted to account balances only.
3. For example, the auditor may request confirmation of the terms of agreements or transactions an entity has with third parties; the confirmation request may be designed to ask if any modifications have been made to the agreement and, if so, what the relevant details are.
4. External confirmation procedures also are used to obtain audit evidence about the absence of certain conditions, for example, the absence of a "side agreement" that may influence revenue recognition.