

1. NATURE, OBJECTIVE AND SCOPE OF AUDIT

QUESTION - WISE ANALYSIS OF PREVIOUS EXAMINATIONS

Question No.	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)
4.	-	-		-	-	-	-	-	-	-	5	-	-
6.	-	-	-	5	-	-	-	-	-	-	-	-	-
17.	-	-	5	-	-	-	-	-	-	-	-	-	-

CHAPTER OVERVIEW

SECTION	TOPIC	STARTING PAGE NO.
1.	THEORY FOR CLASSROOM DISCUSSION	1.1
2.	QUESTIONS FOR ACADEMIC INTEREST – FOR STUDENTS SELF STUDY	1.12

SECTION 1: THEORY FOR CLASSROOM DISCUSSION

Q.No.1. Define the term “Audit” and also explain the points that an Auditor has to satisfy himself before expression of opinion? (A) (NEW SM)

- 1) **DEFINITION:** An audit is an independent examination of financial information of any entity, whether profit oriented or not, and irrespective of its size or legal form, when such an examination is conducted with a view to expressing an opinion thereon.
- 2) **PURPOSE OF AN AUDIT:** Audit enhances degree of confidence of users of financial statements as they are verified for its validity and accuracy by an independent competent person.
- 3) **POINTS TO BE CONSIDERED:** The auditors need to ensure the following during the audit:
 - a) The Information in the financial statements are in conformity with books of accounts.
 - b) The journal entries in the books of accounts are supported by sufficient and appropriate (Proper) evidence.
 - c) Ensure that there are no omissions or duplications or fictitious entries in the financial statements.
 - d) The information conveyed by financial statements is clear and unambiguous (without confusion).
 - e) The amounts, classification, presentation and disclosures are as per accounting standards.
 - f) The financial statements are prepared as per applicable financial reporting framework.
 - g) The accounting policies are applied consistently.
 - h) Accounting estimates are reasonable.
- 4) **IMPLICATIONS OF AUDIT OPINION:**
 - a) The auditor’s opinion does not guarantee regarding:
 - i) Future viability of the entity
 - ii) Efficiency and effectiveness of management.
 - b) The audit is just an opinion on historical financial information as to whether they are reliable or not.

SIMILAR QUESTIONS:

- 1) Explain clearly meaning of Auditing. How would you as an auditor perform the audit? SM-TYK
 A. Write about Definition of audit and Point C
- 2) Definition of an audit? Purpose of an audit?
 A. Write - Point A & B
- 3) Various confirmations the auditor shall obtain in an audit. Explain?
 A. Write about Definition of audit and Point C
- 4) What are the implications of an audit opinion?
 A. Write about Definition of audit and Point D
- 5) Audit opinion cannot be construed as a guarantee for future viability of an entity. Comment.
 A. Write about Definition of audit and Point D

Q.No.2. Explain the objectives of an auditor as per SA 200.

(A) (NEW SM)

AS PER SA-200 THE OVERALL OBJECTIVES OF THE AUDITOR ARE:

- 1) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatements; and
- 2) To report on the financial statements as per relevant SA's based on the auditor's findings.

NOTE: The SA 200 deals with "Overall Objectives of the Independent Auditor and conduct of an audit in accordance with Standards of auditing".

SIMILAR QUESTIONS:

- 1) The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements". Explain stating the objectives of audit as per SA 200. RTP M17
 A. Refer above answer
- 2) State the objectives of Audit according to SA 200 SM – TYK
 A. Refer above answer
- 3) Explain the overall objective of auditor as contained in SA 200. RTP-M19
 A. Write above answer.

Q.No.3. Write a short note on Scope of Audit?

(B) (NEW SM)

The auditor should consider the following while determining scope of audit:

- 1) **COVER ALL ASPECTS OF FINANCIAL STATEMENTS:** The audit should cover all aspects of the enterprise relevant to the financial statements.
- 2) **RELIABILITY OF SOURCE DATA:** The auditor should confirm whether the financial statements are prepared based on a reliable source data i.e., Underlying records.
- a) The reliability of source data can be verified by evaluation of accounting systems and internal controls and
- b) By performing test checks. (Audit Sampling)
- 3) **PRESENTATION AND DISCLOSURE:** The auditor shall ensure that the information presented and disclosed in financial statements is as per the relevant statute. This can be done by:
- a) Comparing the financial statements with the underlying accounting records to see that the transactions and events recorded properly;
- b) Considering the judgments (Assumptions and estimates) that management has made to determine their reasonableness.
- c) Verify the selection and consistency of accounting policies followed.
- d) Whether the classification, presentation and disclosure of information is appropriate.

- 4) **LIMITATION ON SCOPE:** If there is a limitation on the auditor's scope then he can report the same in his audit report.
- 5) **TECHNICAL DUTIES ARE EXCLUDED:** The auditor is not expected to perform duties which fall outside the scope of his competence.

SIMILAR QUESTIONS:

- 1) Audit is restricted to examination of financial statements and books of accounts alone. It has no control over other areas of the entity. Comment.
A. Refer above answer
- 2) What are the factors the auditor should consider while determining the scope of the audit?
A. Refer above answer

Q.No.4. what are the principal aspects to be covered in Audit?

(B) (NEW SM)

1) **EXAMINATION OF INTERNAL CONTROL SYSTEM:**

- a) Ascertain whether the accounting and internal control system is commensurate (matching) with the nature and size of business of the entity.
- b) Examine the system to identify the weaknesses that may give an opportunity for fraud or error.

2) **AUTHENTICITY AND ARITHMETICAL ACCURACY:**

- a) Verify the arithmetical accuracy of the books of accounts by verifying postings, balances, etc.
- b) Verification of validity of transaction entered by scrutinizing books and supporting documents.

3) **ACCOUNTING PRINCIPLES:**

- a) Verify whether capital and of revenue items are properly classified and
- b) Verify whether the incomes and expenses are accounted in proper financial year. (Cut-off)

4) **SUBSTANTIVE AUDIT PROCEDURES:**

- a) Verify the incomes and expenses recorded in Profit and Loss A/c are true and fair.
- b) Verify the assets and liabilities shown in balance sheet are true and fair.
- c) Verify that the financial statements are in conformity with books of accounts.

5) **STATUTORY COMPLIANCES:**

For corporate entities the auditor has to verify the compliances with various laws and regulations such as Income tax, GST, Companies Act, 2013 and any other applicable laws.

6) **REPORTING:**

On Completion of audit, the auditor shall express opinion on financial statements in accordance with Standards on Auditing (SA 700).

SIMILAR QUESTIONS:

- 1) GST & Co., a firm of Chartered Accountants has been appointed to audit the accounts of XYZ Ltd. The partner wanted to cover principal aspects while conducting its audit of financial statements. Advise those principal aspects. RTP M18(N)
A. Refer above answer
- 2) Principal aspects to be considered by an auditor while conducting an audit of final statements of accounts. M18(N) - 5M
A. Refer above answer
- 3) SWM is proprietorship firm engaged in the manufacturing of different kind of yarns. It sells its finished products both in the domestic as well as in the international market. The company is making total turnover of Rs. 30 crores. It has also availed cash credit limit of Rs.3 crores from Dena Bank. In the year 2018-19. Proprietor of the firm is worried about the financial position of the company and is under the impression that since he is out of India, therefore firm might not run well. He approaches an Internal Auditor about as to what would be covered in Audit. Advise regarding principal aspects (any four) to be covered in getting accounts audited. MTP-M19(N)
A. Write any 4 points from the above.

- 4) State the principal aspects which the statutory auditor shall look into before framing an opinion on finalization of audit of accounts. QP-M19(O)-4M

A. Write above answer. (Any 4 Points)

Q.No.5. Discuss various types of Audits.

(B) (NEW SM)

Audit is not mandatory for all forms of organisations. Depending on requirements of law the audits are classified into two types:

- 1) Statutory audit - Audit mandatory under any Law for time being in force.
- 2) Non-Statutory audit - Voluntary audit.

1) STATUTORY AUDIT:

- a) The organisation which requires compulsory audit under law is known as statutory audit.

E.g.: Company audit u/s 139 of companies act, 2013. Tax audit u/s 44AB of Income tax Act, 1961, Bank audit under Banking regulation act, 1949 etc.

- b) The auditor shall be independent in case of statutory audits. (Both Mind and Appearance)
 c) The rights and duties of the auditor are determined under the law and terms of engagement.

2) NON - STATUTORY AUDIT / VOLUNTARY AUDIT:

- a) The Appointment of auditors even though, is not mandatory under the law is known as Non statutory audit. Also known as VOLUNTARY AUDIT. Eg: Audit of sole proprietary concern, audit of partnership firms.
 b) The auditor need not be independent in terms of appearance but the audit process may be carried out independently (Mind).
 c) The rights and duties are determined as per the terms of engagement by the appointing authority.

SIMILAR QUESTIONS:

- 1) Discuss the types of audits required under law.
 A. Refer above answer
- 2) What are differences between statutory audit and non-statutory audit?
 A. Refer above answer
- 3) Write about Statutory audit? Who will decide the scope of audit under statutory audit?
 A. Write about - Point A and conclusion saying the scope is determined by law.

Q.No.6. What are the advantages of an Independent audit?

(A) (NEW SM, M15 - 5M)

- 1) It safeguards the financial interest of persons who are not associated with the management of the entity, whether they are partners or shareholders, bankers, FIS, Public at large etc.
- 2) It acts as a moral check on the employees from committing frauds or errors.
- 3) For negotiating loans from lenders.
- 4) For determining the purchase consideration for a business in case of amalgamations.
- 5) For detection of weakness in internal controls those are leading to wastages and losses.
- 6) To help in the settlement of accounts at the time of admission or death of partner.
- 7) Government may require audited and certified statement before it gives assistance or issues a license for a particular trade.
- 8) To ascertain whether the necessary books of account and allied records have been properly kept.
- 9) Also helps to settle insurance claims in case of any catastrophe.

SIMILAR QUESTION:

- 1) The chief utility of audit lies in reliable financial statements on the basis of which the state of affairs may be easy to understand. Apart from this obvious utility, there are other advantages of audit. Some or all of these are of considerable value even to those enterprises and organisations where audit is not compulsory. Explain. RTP M19 (N&O), MTP N18 (N)
- A. Refer above answer

Q.No.7. Write a short note on Inherent Limitations of Audit.**(A) (NEW SM)**

The opinion expressed by auditor can only be a reasonable assurance. He cannot obtain absolute assurance. Further the audit risk cannot be reduced to zero but can only be minimized through a proper conduct of audit in accordance with standards on auditing.

Reasonable assurance is a high level of assurance but not absolute assurance.

- 1) **NATURE OF FINANCIAL REPORTING:** The financial statements preparation involves many judgements and assumptions which may vary considerably from entity to entity. In addition, many financial statement items involve subjective decisions or assessments or a degree of uncertainty
- E.g.: Accounting estimates such as life of assets, provision for doubtful debts, Net realisable value for inventory.

2) **NATURE OF AUDIT PROCEDURES:**

- a) Further due to legal and practical constraints the auditor could not obtain required evidence.
- b) Normal audit procedures may not be effective to detect frauds which are sophisticatedly carried out.
- c) The nature of audit process is determined by using the auditor's professional judgement.

3) **TIME, COST-BENEFIT COMPARISON:**

- a) The auditor cannot escape saying time and cost as a reason for not obtaining sufficient appropriate audit evidence even where there is no alternative.
- b) However due to certain external factors, the audit shall be completed within a limited period of time. Eg: Legal or regulatory requirements.
- c) Unless the auditor properly plans and perform the audit, the objective cannot be achieved.

4) **OTHER LIMITATIONS:**

The following are various other events or transactions that cause limitations on audit.

- a) Frauds involving senior management.
- b) Entity's ability to be a going concern.
- c) Extent of related party transactions.
- d) The occurrence of non-compliance with laws and regulations.

SIMILAR QUESTIONS:

- 1) The matter of difficulty, time, or cost involved is not in itself a valid basis for the auditor to omit an audit procedure for which there is no alternative or to be satisfied with audit evidence that is less than persuasive. Explain. RTP N18 (N), M18(O)
- A. Refer above answer
- 2) The process of auditing is such that it suffers from certain limitations which cannot be overcome irrespective of the nature and extent of audit procedures." Explain. RTP N17
- A. Refer above answer
- 3) Distinguish between absolute assurance and reasonable assurance. Identify the type of assurance that is expected in an audit of financial statements, clearly outlining the reasons to justify your point of view. RTP M19 (O)
- A. Refer above answer
- 4) Audit procedures used to gather audit evidence may be ineffective for detecting an intentional misstatement that involves, for example, collusion to falsify documentation which may cause the auditor to believe that audit evidence is valid when it is not. Explain SM
- A. Refer above answer

- 5) MNO Ltd requested the auditor CA P to provide for absolute assurance in respect of its ten branches scattered in Delhi and confirm that the financial statements are free from material misstatement due to fraud or error. Advise. SM
- A. The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is 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.
- In view of the above, CA P cannot provide audit absolute assurance to MNO Ltd in respect of its branches.
- 6) DEF & Co. Chartered Accountants successfully carried out the audit of Shree Garments for the f.y. 2015-2016. After the completion of the audit, there were found material misstatements due to fraud in the financial statements which were not noticed and reported by the auditor. Management alleges that it is failure on the part of auditor. Comment SM

Q.No.8. What are the qualities of an ideal auditor?

(C) (NEW SM)

- 1) **TECHNICAL QUALITIES: (PROFESSIONAL):** The auditor should possess specific knowledge of the following:
- Accountancy - Its principles, procedures and standards (AS).
 - Auditing - Its principles, procedures and standards (SA)
 - Direct and Indirect taxation laws such as income tax and GST.
 - General principles of law of contracts, partnership;
 - Specific statutes and provisions applicable, **E.g.** Companies Act, 2013, Banking regulation act, etc.
- 2) **PERSONAL QUALITIES:**
- Apart from the knowledge acquired by the auditor in a formal manner, the auditor should also possess certain personal qualities such as, tact, caution, firmness, good temper, judgement, patience, clear headedness and common sense, reliability and trust.
 - All those qualities that make a good person contribute to make a good auditor.

SIMILAR QUESTIONS:

- 1) Lord Justice Lindley in the course of the judgment in the famous London & General Bank case had succinctly summed up the overall view of what an auditor should be as regards the personal qualities. Explain stating also the qualities of Auditor. RTP M19 (N)
- A. Refer above answer
- 2) All those personal qualities required to make a good person contribute to the making of a good auditor. Explain stating the qualities of an Auditor. RTP N17
- A. Refer above answer
- 3) "The auditor should possess specific knowledge of accountancy, auditing, taxation, etc. which are acquired by him during the course of his theoretical education". Explain stating briefly the qualities of Auditors. MTP N18 (O)
- A. Refer above answer

Q.No.9. Write a short note on Ethical Requirements Relating to an Audit of Financial Statements?

(B)(NEW SM)

The auditor shall comply with the relevant ethical requirements as prescribed below:

- INTEGRITY:** He should be honest, sincere and straight-forwarded in his approach to the professional work.
- OBJECTIVITY:** He should be fair without any bias or prejudice. He should maintain an impartial attitude.
- INDEPENDENCE:**
 - The term independence means that the judgment of auditor should not be made subordinate to the wishes and directions of management or any other person.
 - The audit decisions should be taken without giving importance to personal wishes.

- 4) **CONFIDENTIALITY:** The auditor should not disclose the information collected by him, during the course of his professional work, to any third party without specific authority from the client, unless there is a legal or regulatory requirement
- 5) **PROFESSIONAL COMPETENCE & DUE CARE:** The auditor requires specialized skill and competence which are acquired through a combination of general education, training and practical experience.

SIMILAR QUESTIONS:

- 1) In order to achieve the objectives of the accountancy profession, professional accountants have to observe a number of prerequisites or fundamental principles. Explain. RTP M19(O)
A. Refer above answer
- 2) "While auditing the entity, an auditor is expected to maintain secrecy over the affairs of the entity and should not disclose any information to outsiders without the permission of client concerned." What are the minimum ethical requirements every auditor has to follow while conducting the audit of any entity?
A. Refer above answer
- 3) Relevant ethical requirements ordinarily comprise the code of ethics for professional accountants (IESBA code) related to an audit of financial statements. Discuss with reference to those fundamental principles of professional ethics. RTP M19(N)
A. Refer above answer
- 4) Auditor's professional responsibilities are governed by basic principles which should be complied with whenever an audit is carried out. Comment. OLD PM
A. Refer above answer
- 5) The auditor shall comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements. MTP-M19
A. Refer above answer.
- 6) The auditor shall comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements. Relevant ethical requirements ordinarily comprise the Code of Ethics for Professional Accountants (IESBA Code) related to an audit of financial statements. The Code establishes the fundamental principles of professional ethics relevant to the auditor when conducting an audit of financial statements. Explain MTP-M20
A. Refer above answer.

Q.No.10. "The code of ethics for professional accountants prepared by the international federation of accountants (IFAC) identifies five types of threats." Explain? (C) (NEW SM)

INDEPENDENCE:

- 1) The term independence means that the judgment of auditor should not be made subordinate to the wishes and directions of management or any other person.
- 2) The audit decisions should be taken without giving importance to personal wishes.

THREATS TO INDEPENDENCE: The International Federation of Accountants (IFAC) had identified five types of threats:

- 1) **SELF-INTEREST THREATS:** Occurs when an auditing firm or any partner benefiting from a financial interest in the audit client.
E.g.: Shares in the company, loan or guarantee to or from the concerned client, close business relationship with an audit client etc.
- 2) **SELF-REVIEW THREATS:** Occurs when auditor is reviewing the work which is performed by him during previous assignments.
E.g.: When an auditor having recently been a director or senior officer of the company, and when auditors perform services that are themselves subject matters of audit like accounting services.
- 3) **ADVOCACY THREATS:** Occurs when the auditor promotes a client's opinion without a reasonable basis.
E.g.: Auditor becomes the client's advocate (representative) in litigation and third party disputes.

4) **FAMILIARITY THREATS:** Occurs when auditor has some association or relation with the clients either directly or indirectly.

E.g.: Close relative of the auditor working in a senior position in the client company, long association between auditors and client. (Creates Sympathy)

5) **INTIMIDATION THREATS:** Occurs when auditors are prevented from acting objectively / independently. (Blackmailing or Bribing)

E.g.: Threat of replacement or pressure to disproportionately reduce work in response to reduced audit fees.

SIMILAR QUESTIONS:

1. "The Code of Ethics for Professional Accountants, prepared by the International Federation of Accountants (IFAC) identifies five types of threats." Explain. SM - TYK
- A. Refer above answer
2. You have been appointed as auditor of Ram Ltd for financial year 2018-19. During the financial year 2018-19, you are also the person involved in management of Ram Ltd. Discuss the threat, if any, as an auditor you may face while auditing Ram Ltd and also state the other threats that were identified by IFAC.
- A. Refer above answer
3. Familiarity threats are self-evident, and occur when auditors form relationships with the client where they end up being too sympathetic to the client's interests. Explain. MTP - M19
- A. Write above 4 Points (Familiarity threat is Must).

Q.No.11. Write a short note on Professional Skepticism.

(A) (NEW SM)

MEANING: Professional skepticism refers to an attitude of questioning mind, being alert to unusual situations and a critical assessment of audit evidence.

Professional skepticism includes being alert to the following situations:

- 1) Conflicts between multiple audit evidences.
- 2) Doubts as to reliability of audit evidence.
- 3) Situations of possible fraud.
- 4) Also maintaining professional skepticism throughout the audit is necessary to reduce the risks of:
 - a) Overlooking unusual circumstances.
 - b) Over generalizing while taking decisions from audit observations.
 - c) Taking inappropriate decisions regarding nature, timing, and extent of the audit procedures.

CRITICAL ASSESSMENT OF AUDIT EVIDENCE:

- 1) Is evidence obtained from reliable source
- 2) Is evidence obtained sufficient
- 3) Is evidence obtained appropriate i.e., relevant
- 4) Is there a requirement for an alternative or additional evidence

SIMILAR QUESTIONS:

- 1) The auditor is responsible for maintaining an attitude of professional skepticism throughout the audit. Do you agree with the statement? RTP N18(O), MTP M18(O)
- A. Refer above answer
- 2) 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. RTP NOV 20, NOV 19 (4M)
- A. Refer above answer

Q.No.12. Write a short note on Professional Judgment as per SA 200. (OR) Professional judgment is essential to the proper conduct of an audit (A) (NEW SM)

MEANING: It refers to taking decisions by the auditor during the course of his audit by using his knowledge, training and experience. Judgment includes assumptions and estimations made by auditor.

Professional judgment is used throughout planning and performing of an audit.

CIRCUMSTANCES WHERE EXERCISING OF PROFESSIONAL JUDGMENT IS REQUIRED:

- 1) Materiality and audit risk.
- 2) Nature, timing and extent of audit procedures.
- 3) Evaluating whether sufficient appropriate audit evidence has been obtained.
- 4) Drawing of conclusions based on the audit evidence obtained.

Q.No.13. Mention any four points which assists the auditor in accepting and continuing of relationship with the client as per SA 220. (A) (NEW SM)

SA 220 “**Quality Control for an Audit of Financial Statements**” requires the firm to consider the following information before accepting an engagement:

- 1) The integrity of the key management and those charged with governance of the entity;
- 2) Whether the engagement team is competent to perform the audit engagement and has the necessary capabilities, including time and resources;
- 3) Whether the engagement team can comply with relevant ethical requirements; and
- 4) Significant matters that have arisen during the previous audit engagement.

SIMILAR QUESTIONS:

1. The firm’s system of quality control should include policies and procedures addressing each element. Explain RTP N18(N)
A. Refer above answer
2. As per SA 220, “Quality Control for an Audit of Financial Statements” the auditor should obtain information considered necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement and when considering acceptance of a new engagement with an existing client. Explain. RTP M18 (N&O)
A. Refer above answer
3. CA Raj, an engagement partner wants to take decision, regarding acceptance and continuance of an audit engagement. Which informations, he should obtain before accepting an engagement? MAY 19 (3M)
A. Refer above answer

Q.No.14. What if there is a Limitation on scope of audit prior to engagement acceptance? (B) (NEW SM)

AS PER SA 210- AGREEING ON TERMS OF AUDIT ENGAGEMENT: Prior to the acceptance of the audit engagement, if there is a limitation imposed by management on the rights and duties of the auditor (Scope), then the auditor shall not accept such audit engagement.

Because with impose of limitations, the auditor cannot obtain sufficient appropriate evidence and hence cannot obtain reasonable assurance results in expression of disclaimer of opinion.

SIMILAR QUESTION:

1. The auditor shall not accept the audit engagement if there is a limitation prior to audit acceptance. Comment.
A. Refer above answer

Q.No.15. Write a short note: Pre-conditions for an audit as per SA 210. (A) (NEW SM)

The auditor shall obtain a confirmation from the management that they accept and acknowledge their responsibilities relating to financial statements. This acknowledgement will be obtained through engagement letter in accordance with SA 210. It is also known as PREMISE to audit.

THE FOLLOWING ARE PRE CONDITIONS TO BE CONFIRMED BEFORE STARTING THE AUDIT:

Obtain an agreement from the management that they are accepting their responsibility for the following activities:

- 1) Preparation of the financial statements in accordance with the applicable financial reporting framework.
- 2) Designing and implementing necessary internal control to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
- 3) To provide the auditor with:
 - a) Access to all information such as records, documentation and other matters;
 - b) Additional information that the auditor may request from management for the purpose of the audit; and
 - c) Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

SIMILAR QUESTIONS:

- 1) **State in brief, the management's responsibilities relating to the audit of financial statements.**
 - A. Refer above answer
- 2) "Premise" to the audit as per SA 200?
 - A. Refer above answer
- 3) 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-M19
 - A. Write above answer.

Q.No.16. Write about Letter of engagement and its contents?

(C) (NEW SM)

PURPOSE OF ENGAGEMENT LETTER:

- 1) Engagement letter is a document issued by the auditor to the client, to reduce the chances of misunderstanding regarding scope, objective, rights and duties of the auditor and of management.
- 2) In case of Non statutory audit, the issue of engagement letter is highly recommendatory as there is no governing law regarding rights and duties of an auditor.

THE FOLLOWING ARE THE CONTENTS OF AN AUDIT ENGAGEMENT LETTER:

- | | |
|---|--|
| 1) Title; | 6) Reference to Applicable financial reporting framework; |
| 2) Addressee; | 7) Signature of auditor; |
| 3) The objective and scope of the audit; | 8) Signature of the client confirming the acceptance of terms; |
| 4) The responsibilities of the auditor; | 9) Date and place; |
| 5) The responsibilities of management; (i.e., Preconditions to audit) | |

SIMILAR QUESTIONS:

1. **What is the purpose of a Letter of Engagement? What are the important contents of a Letter of Engagement? M17 - 6M**
 - A. Refer above answer
2. **It is important both for the auditor and client that each party should be clear about the nature of the engagement. It must be reduced to writing and should exactly specify the scope of the work. Explain? MTP M18 (N)**
 - A. Refer above answer

Q.No.17. "P" an auditor decides not to send a new audit engagement letter to G Ltd every year. Whether he is right in his approach? State the circumstances where sending new engagement letter, would be appropriate in recurring audits. (A)(NEW SM)

- 1) **INITIAL AUDIT ENGAGEMENT:** The auditor must issue an engagement letter in case of newly accepted appointment for an audit.
- 2) **RECURRING AUDIT:**
 - a) If auditor of previous year(s) has also been appointed as auditor for current year, then the current year engagement is known as "**Recurring audit**".
 - b) In recurring audits, the auditor shall decide whether there is need to re-issue the engagement letter based on circumstances and depending on professional judgment of auditor.
 - c) Circumstances where engagement letter is issued even in case of recurring audits:
 - i) Any indication that the entity misunderstands the objective and scope of the audit.
 - ii) A change in legal or regulatory requirements.
 - iii) A change in the Applicable financial reporting framework.
 - iv) A change in audit reporting requirement.
 - v) A recent change of Top management.
 - vi) A significant change in nature or size of the entity's business.

SIMILAR QUESTIONS:

1. Indicate the factors which make it appropriate for an auditor to send a new engagement letter for a recurring audit. RTP N18, N14 - 5M, N11 - 5M,
- A. Write about Purpose of engagement letter and above answer.
2. "It is not mandatory to send a new engagement letter in recurring audit, but sometimes it becomes mandatory to send new letter". Explain those situations where new engagement letter is to be sent. OLD PM
- A. Refer above answer

Q.No.18. Write a short note on: Change in terms of engagement as per SA 210? (A) (NEW SM)

- 1) **REASONS FOR REQUEST MADE BY CLIENTS:** A request from the client to change the terms of engagement may result from:
 - a) Change in circumstances.
 - b) Misunderstanding of terms originally agreed.
 - c) With a view to restrict the scope of engagement or to alter terms and conditions.
- 2) **"ACCEPTANCE OF CHANGE" IN TERMS OF ENGAGEMENT BY AUDITOR:**
 - a) If there is a reasonable justification, the auditor can accept the changes to terms of engagement.
 - b) Further the auditor and management shall agree and record the new terms of the engagement in a new engagement letter.
- 3) **"NON-ACCEPTANCE" OF CHANGE IN TERMS OF ENGAGEMENT BY AUDITOR:** The auditor shall not agree for changes in the terms of the audit engagement where there is no reasonable justification for doing so.
- 4) **WITHDRAWAL FROM ENGAGEMENT:** If the auditor is unable to agree to a change of the terms of engagement and is not permitted by management to continue the original audit engagement, the auditor shall withdraw from the audit engagement.

SIMILAR QUESTIONS:

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." Discuss. RTP M18 (N), MTP M17
- A. Refer above answer

2. X, a Chartered Accountant was engaged by PQR & Co. Ltd. for auditing their accounts. He sent his letter of engagement to the Board of Directors, which was accepted by the Company. In the course of audit of the company, the auditor was unable to obtain appropriate sufficient audit evidence regarding receivables. The client requested for a change in the terms of engagement. OLD PM
- A. Refer above answer

19. Mention a few points which assists the auditor in establishing leadership responsibility for quality of audits as per SA 220. (A) (RTP Nov 2020, NEW SM)

As per SA 220 "Quality Control for an Audit of Financial Statements", the engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned.

The actions of the engagement partner and appropriate messages to the other members of the engagement team, in taking responsibility for the overall quality on each audit engagement, emphasise:

1) THE IMPORTANCE TO AUDIT QUALITY OF:

- a) Performing work that complies with professional standards and regulatory and legal requirements;
 - b) Complying with the firm's quality control policies and procedures as applicable;
 - c) Issuing auditor's reports that are appropriate in the circumstances; and
 - d) The engagement team's ability to raise concerns without fear of reprisals; and
- 2) The fact that quality is essential in performing audit engagements.

SIMILAR QUESTIONS:

- 1) As per SA 220 "Quality Control for an Audit of Financial Statements", the engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned. Explain clearly stating the meaning of engagement partner and also the actions of the engagement partner and appropriate messages to the other members of the engagement team, in taking responsibility for the overall quality on each audit engagement. RTP NOV 2020
- A. Refer above answer
- 2) The engagement partner shall take the responsibility for the overall quality on each audit engagement to which that partner is assigned. Discuss with reference to SA 220 "Quality Control for an audit of financial statements". NOV 2019 (3M)
- A. Refer above answer

SECTION 2: QUESTIONS FOR ACADEMIC INTEREST – FOR STUDENTS SELF STUDY

Q.No.1. Write about Independence of auditor?

(C) (NEW SM)

1) CONCEPT OF INDEPENDENCE:

- a) Independence implies that the judgement of a person is not subordinate to the wishes or direction of another person who might have engaged him.
 - b) It is not possible to define "independence" precisely.
 - c) Independence is a condition of mind as well as personal character.
 - d) There are two perspectives of independence of auditors:
 - i) **Independence of mind:** The state of mind that takes an opinion without being affected by influences of others, allowing such person to act with integrity, objectivity and professional scepticism.
 - ii) **Independence in appearance:** A person who is a third party to the client (Not related to management and not holding any financial or operating interest) would reasonably be accepted as an auditor. As only a third party will safeguard integrity, objectivity or professional scepticism.
- 2) **SAFEGUARDS TO INDEPENDENCE:** The Chartered Accountant has a responsibility to remain independent by taking into account the context in which they practice, the threats to independence and the safeguards available to eliminate the threats.

THE FOLLOWING ARE THE GUIDING PRINCIPLES IN THIS REGARD:

- a) For the public to have confidence in the quality of audit, it is essential that auditors should always be and appears to be independent of the entities that they are auditing.
- b) In the case of audit, the key fundamental principles are integrity, objectivity and professional scepticism, which necessarily require the auditor to be independent.
- c) Before taking on any work, an auditor must consider whether it involves threats to his independence.
- d) When such threats exist, the auditor should either withdraw from the task or take certain precautions to eliminate them.
- e) If the auditor is unable to fully implement credible and adequate safeguards, then he must not accept the work.

SIMILAR QUESTIONS:

- 1) Independence of Mind and Independence in appearance are interlinked perspectives of independence of auditors. Explain. QP-M19(N)-3M
- A. Write Point – A.
- 2) Chartered Accountant has a responsibility to remain independent by taking into account the context in which they practice, the threats to independence and the safeguards available to eliminate the threats. Explain the guiding principles in this regard.. MTP MAY 20(N) -4M
- A. Write Point – B.

Q.No.21. Write short notes on relationship of auditing with other disciplines. (C) (NEW SM)

1) AUDITING AND ECONOMICS:

- a) As, it is well known, accounting is concerned with the accumulation and presentation of data relating to economic activity.
- b) The auditors are more concerned with Micro economics rather than with the Macro economics.
- c) The knowledge of Macroeconomics should include the nature of economic force that affect the firm, relationship of price and the role of Government and Government regulations.
- d) Auditor is expected to be familiar with the overall economic environment in which his client is operating.

2) AUDITING AND BEHAVIORAL SCIENCE:

- a) The discipline of behavioral science is closely linked with the subject of auditing.
- b) While it may be said that an auditor deals basically with the figures contained in the financial statements but he shall be required to interact with a lot of people in the organization.
- c) As against the financial auditor, the internal auditor is expected to deal with human beings rather than financial figures.
- d) One of the basic elements in designing the internal control system is personnel. However, if a sound internal control structure is designed, it cannot work until and unless the people who are working in the organization are competent and honest.
- e) The knowledge of human behavior is indeed very essential for an auditor so as to effectively discharge his duties.

3) AUDITING AND STATISTICS & MATHEMATICS:

With the passage of time, test check procedures in auditing have become part of generally accepted auditing procedures.

- a) With the emergence of test check procedure, discipline of statistics has come quite close to auditing as the auditor is also expected to have the knowledge of statistical sampling so as to arrive at meaningful conclusions.
- b) The knowledge of mathematics is also required on the part of auditor particularly at the time of verification of inventories.

4) AUDITING AND DATA PROCESSING:

- a) Today, organisations are witnessing revolution in the field of data processing of accounts.
- b) Many organisations are carrying out their financial accounting activities with the help of computers which can document, record, collate, allocate and value accounting data and information in very large quantity at very high speed.
- c) Dependence on the accuracy of the programmed instructions given today, the computer is able to carry out each of these activities with complete accuracy.
- d) With such a phenomenal growth in the field of computer sciences, the auditor should have good knowledge of the components, general capability of the system and the related terms. In fact, EDP auditing in itself is developing as a discipline in itself.

5) AUDITING AND FINANCIAL MANAGEMENT:

- a) The auditor is expected to have knowledge about various financial techniques such as working capital management, funds flow, ratio analysis, capital budgeting etc.
- b) The knowledge of various institutions and Government activities that influence the operations of the financial market are also required to be understood by an auditor.

6) AUDITING AND PRODUCTION:

- a) While carrying out the audit activity, the auditor is required to evaluate transactions from the accounting aspect in relation to the process through which it has passed through as accounting for by-products; joint products may also require to be done.
- b) The auditor shall also require understanding the cost system in operation in the factory and assessing whether the same is adequate for the particular company.
- c) The understanding of the terminology of the production shall enable an auditor to communicate with production employees in connection with his work.

7) AUDITING AND ACCOUNTING:

- a) It has been pointed out earlier that both accounting and auditing are closely related with each other as auditing reviews the financial statements which are nothing but a result of the overall accounting process.
- b) It naturally calls on the part of the auditor to have a thorough and sound knowledge of generally accepted principles of accounting before he can review the financial statements.

8) AUDITING AND LAW:

- a) The relationship between auditing and law is very close one. Auditing involves examination of various transactions from the view point of law, whether or not these have been properly entered into.
- b) It necessitates that an auditor should have a good knowledge of business laws affecting the entity.
- c) He should be familiar with the law of contracts, negotiable instruments, etc. The knowledge of taxation laws is also inevitable as entity is required to prepare their financial statements taking into account various provisions affected by various tax laws.
- d) In analysing the impact of various transactions particularly from the accounting aspect, an auditor ought to have a good knowledge about the direct as well as indirect tax laws.

SIMILAR QUESTIONS:

- 1) The relationship between auditing and law is very close one. Discuss. RTP - N18(N)
A. Refer Point – H in above answer
- 2) Both accounting and auditing are closely related with each other. Explain. RTP – N20(N)
B. Refer Point – G in above answer

Q.No.2. Explain the purpose of monitoring compliance with quality control policies and procedures (B) (NEW SM)

The purpose of monitoring compliance with quality control policies and procedures is to provide an evaluation of:

- 1) Adherence to professional standards and regulatory and legal requirements;
- 2) Whether the quality control system has been appropriately designed and effectively implemented; and
- 3) Whether the firm's quality control policies and procedures have been appropriately applied, so that reports that are issued by the firm or engagement partners are appropriate in the circumstances.

Follow-up by appropriate firm personnel so that necessary modifications are promptly made to the quality control policies and procedures.

SIMILAR QUESTION:

- 1) 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. Such policies and procedures should include an on-going consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements.

Explain the purpose of monitoring compliance with quality control policies and procedures.

RTP – N 20(N)

- A Refer above answer

THE END

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