1.State with reasons (in short) whether the following statements are correct or incorrect: (a) The primary objective of an audit is to detect fraud and errors in Financial Statements. (b) An Auditor's external expert is not subjected to quality control policies and procedures of an audit firm.

(a) Incorrect: Detection of fraud and errors in the financial statements is not the primary objective of audit. The primary objective of an audit is to obtain reasonable assurance about whether the financial statements are free from material misstatements thereby enabling the auditor to express an opinion on the financial statements.

(b) Correct: As per Standard “Using the Work of an Auditor’s Expert”, an auditor’s external expert is not a member of the engagement team and is not, therefore, subject to quality control policies and procedures of the audit firm.

2.State with reason (in short) whether the following statements are correct or incorrect. (a) Branch auditor of a company should give photocopies of his working papers on demand by Company Auditor. (b) Events occurring after the balance sheet date must be disclosed in the financial statements.

Incorrect: As per Standard 230 on “Audit Documentation”, audit documentation is the property of the auditor. He may at his discretion, make portions of, or extracts from, audit documentation available to clients, provided such disclosure does not undermine the validity of the work performed, or, in the case of assurance engagements, the independence of the auditor or of his personnel.

Main auditor does not have right of access to the working papers of the branch auditor. In the case of a company, the main auditor has to consider the report of the branch auditor and has a right to seek clarification and to visit the branch but cannot ask for the copy of working papers and therefore, the branch auditor is under no compulsion to give photocopies of his working papers to the principal auditor of the Company.

(b) Incorrect: As per “Contingencies and Events Occurring After the Balance Sheet Date”, events occurring after the balance sheet date which do not affect the figures stated in the financial statements would not normally require disclosure in the financial statements although they may be of such significance that they may require a disclosure in the report of the approving authority to enable users of financial statements to make proper evaluations and decisions

3.Discuss with reference to Auditing standard: (i) The auditor shall communicate all significant findings with those charged with Governance.

(ii) Factors affecting form, contents and extent of audit documentation.

(i) Communication of Findings with ‘Those Charged with Governance’: As per Standard 260 “Communication with Those Charged with Governance”, the auditor shall communicate the following significant findings from the audit, with those charged with governance- (a) The auditor’s views about significant qualitative aspects of the entity’s accounting practices, including accounting policies, accounting estimates and financial statement disclosures. When applicable, the auditor shall explain to those charged with governance why the auditor considers a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be most appropriate to the particular circumstances of the entity; (b) Significant difficulties, if any, encountered during the audit; (c) Unless all of those charged with governance are involved in managing the entity: (i) Significant matters, if any, arising from the audit that were discussed, or subject to correspondence with management; and (ii) Written representations the auditor is requesting; and (d) Other matters, if any, arising from the audit that, in the auditor’s professional judgment, are significant to the oversight of the financial reporting process.

(ii) Factors affecting Form, Contents and Extent of Audit Documentation: As per Standard 230 on “Audit Documentation”, the form, content and extent of audit documentation depend on the following factors- (a) The size and complexity of the entity. (b) The nature of the audit procedures to be performed. (c) The identified risks of material misstatement. (d) The significance of the audit evidence obtained. (e) The nature and extent of exceptions identified. (f) The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained. (g) The audit methodology and tools used.

4.Explain the process of external confirmation. Give some examples where external confirmation can be used as audit evidence.

External Confirmation: According to Standard 505 on “ External Confirmation, it is the process of obtaining and evaluating through a direct communication from a third party in response to a request for information about a particular item affecting assertions made by the management in the financial statements. When using external confirmation procedures, the auditor shall maintain control over external control requests, including- (i) Determining the information to be confirmed or requested; (ii) Selecting the appropriate confirming party; (iii) 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 (iv) Sending the requests, including follow-up requests when applicable, to the confirming party. (v) Selecting the items for which confirmations are needed. Examples of situations where external confirmations may be used include the following: (i) Bank balances and other information from bankers. (ii) Accounts receivable balances. (iii) Inventories held by third parties. (iv) Property title deeds held by third parties. (v) Investments purchased but delivery not taken. (vi) Loans from lenders. (vii) Accounts payable balances. (viii) Long outstanding share application money. (ix) Terms of Agreement or transaction with the third parties

5.(a) "The auditor is faced with sampling risk in both tests of control and substantive procedures." Comment on this statement with reference to Standard 530 on "Audit Sampling".

(b) What are the factors that determine the extent of reliance that the auditor places on results of analytical procedures? Explain with reference to Standard 520 on "Analytical procedures

(a) Sampling Risk: As per Standard 530 “Audit Sampling”, audit sampling enables the auditor to obtain and evaluate audit evidence about some characteristic of the items selected in order to form or assist in forming a conclusion concerning the population from which the sample is drawn. Audit sampling can be applied using either non-statistical or statistical sampling approaches. When designing a sample, the auditor determines tolerable misstatement in order to address the risk that the aggregate of individually immaterial misstatements may cause the financial statements to be materially misstated and provide a margin for possible undetected misstatements. The risk that the auditor’s conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. Sampling risk can lead to two types of erroneous conclusions: (i) In the case of a test of controls, that controls are more effective than they actually are, or in the case of a substantive procedure i.e. test of details, that a material misstatement does not exist when in fact it does. The auditor is primarily concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion. (ii) In the case of a test of controls, that controls are less effective than they actually are, or in the case of a substantive procedure i.e. test of details, that a material misstatement exists when in fact it does not. This type of erroneous conclusion affects audit efficiency as it would usually lead to additional work to establish that initial conclusions were incorrect.

(b) Extent of Reliance on Analytical Procedures: As per Standard 520 “Analytical Procedures”, the application of analytical procedures is based on the expectation that relationships among data exist and continue in the absence of known conditions to the contrary. The presence of these relationships provides audit evidence as to the completeness, accuracy and validity of the data produced by the accounting system. However, reliance on the results of analytical procedures will depend on the auditor's assessment of the risk that the analytical procedures may identify relationships as expected when, in fact, a material misstatement exists. The extent of reliance that the auditor places on the results of analytical procedures depends on the following factors: (i) Materiality of the items involved, for example, when inventory balances are material, the auditor does not rely only on analytical procedures in forming conclusions. However, the auditor may rely solely on analytical procedures for certain income and expense items when they are not individually material. (ii) Other audit procedures directed toward the same audit objectives, for example, other procedures performed by the auditor in reviewing the collectibility of accounts receivable, such as the review of subsequent cash receipts, might confirm or dispel questions raised from the application of analytical procedures to an ageing schedule of customers' accounts. (iii) Accuracy with which the expected results of analytical procedures can be predicted. For example, the auditor will ordinarily expect greater consistency in comparing gross profit margins from one period to another than in comparing discretionary expenses, such as research or advertising. (iv) Assessments of inherent and control risks, for example, if internal control over sales order processing is weak and, therefore, control risk is high, more reliance on tests of details of transactions and balances than on analytical procedures in drawing conclusions on receivables may be required. (v) The auditor will need to consider testing the controls, if any, over the preparation of information used in applying analytical procedures. When such controls are effective, the auditor will have greater confidence in the reliability of the information and, therefore, in the results of analytical procedures. The controls over nonfinancial information can often be tested in conjunction with tests of accounting related controls. For example, an entity in establishing controls over the processing of sales invoices may include controls over the recording of unit sales. In these circumstances, the auditor could test the controls over the recording of unit sales in conjunction with tests of the controls over the processing of sales invoices.

6. Write short notes on the following: (a) Reliability of external confirmations. (b) Factors governing modes of communication of auditor with those charged with governance. (c) Procedures to be performed by the auditor in expressing opinion on 'going concern' assumption.

(a) Reliability of External Confirmations: As per Standard 505 “External Confirmation”, the reliability of external confirmations depends among other factors, upon the application of appropriate procedures by the auditor in designing the external confirmation request, performing the external confirmation procedures, and evaluating the results of the external confirmation procedures. The factors that affect the reliability of confirmations include: (i) The control which the auditor exercises over confirmation request and responses; (ii) The character of respondents; and (iii) Any restrictions included in the response or imposed by the management. (b) Factors Governing Modes of Communication of Auditor with Those Charged with Governance: As per Standard 260, “Communication with Those Charged with Governance” the auditor may decide whether to communicate orally or in writing. Effective communication may involve structured presentations and written reports as well as less structured communications, including discussions. The form of communication may be affected by such factors as- (i) Whether the matter has been satisfactorily resolved. (ii) Whether management has previously communicated the matter. (iii) The size, operating structure, control environment, and legal structure of the entity. (iv) In the case of an audit of special purpose financial statements, whether the auditor also audits the entity’s general purpose financial statements. (v) Legal requirements. In some jurisdictions, a written communication with those charged with governance is required in a prescribed form by local law. (vi) The expectations of those charged with governance, including arrangements made for periodic meetings or communications with the auditor. (vii) The amount of ongoing contact and dialogue the auditor has with those charged with governance. (viii) Whether there have been significant changes in the membership of a governing body.

(c) Procedures to be performed by the Auditor in Expressing Opinion on 'Going Concern' Assumption: As per Standard 570, “Going Concern”, the following are the relevant procedures that are relevant in this connection- (i) Analyse and discuss cash flow, profit and other relevant forecasts with management. (ii) Analyse and discuss the entity's latest available interim financial statements. (iii) Review the terms of debentures and loan agreements and determine whether any of the terms have been breached. (iv) Read minutes of the meetings of shareholders, those charged with governance and relevant committees for reference to financing difficulties. (v) Inquire of the entity’s legal counsel regarding the existence of litigation and claims and the reasonableness of management’s assessments of their outcome and the estimate of their financial implications. (vi) Confirm the existence, legality and enforceability of arrangements to provide or maintain financial support with related and third parties and assess the financial ability of such parties to provide additional funds. (vii) Evaluate the entity’s plans to deal with unfilled customer orders. (viii) Perform audit procedures regarding subsequent events to identify those that either mitigate or otherwise affect the entity’s ability to continue as a going concern. (ix) Confirm the existence, terms and adequacy of borrowing facilities

7. State with reasons (in short) whether the following statements are True or False: (i) The auditor, in the interest of the users, while explaining the nature of his reservation, can describe the work of the expert with his name, in the audit report without obtaining prior consent of the expert. (ii) Analytical procedures are unable to help the Auditor in determining the nature, timing and extent of other audit procedures at the planning stage. (iii) A Company which has been unable to negotiate borrowings from its bankers claims that it will be able to continue as a 'going concern'.

(i) False: As per Standard 620, “Using the Work of an Auditor’s Expert”, if the auditor, in the interest of the users includes the name of the expert in his audit report, he can do so only after obtaining the prior permission of the auditor’s expert. (ii) True: As per Standard 520 “Analytical Procedures” states that the auditor shall design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor’s understanding of the entity. (iii) False: In the case of the company which has not been able to negotiate its borrowings with its bankers, there will be a substantial doubt in its ability to continue as a going concern without such financial support.