

NATURE OF AUDITING

Question 1

State with reasons (in short) whether the following statement is true or false.

As per SA 200 A, one of the objectives of the audit is to detect fraud.

(2 Marks) (May 2007)

Answer

False: As per SA 200A, objective of an audit is to express an opinion on financial statements to help the users of the financial statements to determine the true and fair view.

Question 2

State with reasons (in short) whether the following statement is true or false.

Procedural error arises as a result of transactions having been recorded in a fundamentally incorrect manner.

(2 Marks) (May 2008)

Answer

False: Procedural error arises when there is error in implementation of the procedure. If transaction has been recorded in a fundamentally incorrect manner it will result in error of principle.

Question 3

What is the importance of having the accounts audited by an independent auditor?

(5 Marks) (May 2008)

Answer

Advantages of having the accounts audited by an independent auditor are:-

- (i) It safeguards the financial interest of persons not associated with the management like partners or shareholders.
- (ii) It acts as a moral check on the employees from committing fraud.
- (iii) It is helpful in settling tax liability, negotiations for loans and for determining purchase consideration for sale/merger.
- (iv) It is also helpful in settling trade or labour disputes for higher wages/bonus.

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- (v) It helps in detection and minimizing wastages and losses.
- (vi) It ensures maintenance of adequate books and records, statutory register etc.

Question 4

State with reason (in short) whether the following statement is true or false.

“Auditor is not an Insurer”.

(2 Marks) (Nov 2008)

Answer

True: While examining the evidences relating to business organization or the state of the affairs of the company, the auditor's duty is limited only to the verification of the evidence that is made available to him in ordinary course of audit or that which he would call upon to examine on a doubt having arisen that there is something wrong. Hence auditor is not an insurer.

Question 5

What are the basic principles which govern the Auditor's professional responsibilities while doing Audit?

(5 Marks) (Nov 2008))

Answer

SA 200 “**Basic Principles Governing an Audit**” explains the basic principles which govern auditor's professional responsibilities and the auditor is expected to follow them.

1. Confidentiality: the auditor should maintain complete secrecy of his client's business and information. He should disclose the information to others with the permission of his client and as per his legal or professional duty.
2. Work performed by others: the auditor can delegate work to his assistants or others but he cannot escape from his responsibilities. As per SA-610, SA 620, SA 600 and SA 299, the auditor may take the help of others but ultimately he will be held responsible.
3. Audit Evidence: While doing audit, the auditor should obtain sufficient information, written or oral, called audit evidence. Audit evidence is necessary to draw conclusions on financial statements.
4. Documentation: the auditor should maintain sufficient working papers for each audit assignment. These working papers help him to establish that he has worked with due care and diligence.
5. Accounting system and internal control: The internal control system and accounting system enables the auditor to reach the conclusions that all the accounting information has been duly recorded.
6. Audit conclusion and reporting: It is the duty of the auditor to make conclusions that the financial statements have been prepared by using the generally accepted accounting principles and comply with relevant statutory requirements and regulations.

Question 6

Discuss the basic principles governing an audit.

(10 Marks) (Nov 2009)

Answer

Basic principles governing an audit

SA 200 "Basic Principles Governing an Audit", describes the basic principles which govern the auditor's professional responsibilities and which should be complied with wherever an audit is carried. They are described below:

- (i) *Integrity, objectivity and independence*: An auditor should be honest, sincere, impartial and free from bias. He should be a man of high integrity and objectivity.
- (ii) *Confidentiality*: The auditor should respect confidentiality of information acquired during the course of his work and should not disclose the information without the prior permission of the client, unless there is a legal duty to disclose.
- (iii) *Skill and competence*: The auditor must acquire adequate training and experience. He should be competent, skillful and keep himself abreast of the latest developments including pronouncements of ICAI on accounting and auditing matters.
- (iv) *Work performed by others*: If the auditor delegates some work to others and uses work performed by others including that of an expert, he continues to be responsible for forming and expressing his opinion on the financial information.
- (v) *Documentation*: The auditor should document matters which are important in providing evidence to ensure that the audit was carried out in accordance with the basic principles.
- (vi) *Planning*: The auditor should plan his work to enable him to conduct the audit in an effective, efficient and timely manner. He should acquire knowledge of client's accounting system, the extent of reliance that could be placed on internal control and coordinate the work to be performed.
- (vii) *Audit evidence*: The auditor should obtain sufficient appropriate evidences through the performance of compliance and other substantive procedures to enable him to draw reasonable conclusions to form an opinion on the financial information.
- (viii) *Accounting System and Internal Control*: The management is responsible for maintaining an adequate accounting system incorporating various internal controls appropriate to the size and nature of business. He auditor should assure himself that the accounting system is adequate and all the information which should be recorded has been recorded. Internal control system contributes to such assurance.
- (ix) *Audit conclusions and reporting*: On the basis of the audit evidence, he should review and assess the audit conclusions. He should ascertain:
 - (a) As whether accounting policies have been consistently applied;
 - (b) whether financial information complies with regulations and statutory requirements; and

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- (c) there is adequate disclosure of material matters relevant to the presentation of financial information subject to statutory requirements.

The auditor's report should contain a clear written opinion on the financial information. A clean audit report indicates the auditor's satisfaction in all respects and when a qualified, adverse or a disclaimer of opinion is to be given or reservation of opinion on any matter is to be made, the audit report should state the reasons thereof.