

PAPER – 6 : AUDITING AND ASSURANCE

Question No.1 is compulsory.

Attempt any five questions from the remaining six questions.

Question 1

Comment on the following:

- (a) *"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. (5 Marks)*
- (b) *Vouching of payment of taxes. (5 Marks)*
- (c) *Removal of auditor before expiry of term. (5 Marks)*
- (d) *What procedure an auditor should adopt to test the authenticity of cash at bank. (5 Marks)*

Answer

- (a) **Issue of Audit Engagement Letter in Recurring Audits:** On recurring audits, the auditor shall assess whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms of the audit engagement.

The auditor may decide not to send a new audit engagement letter or other written agreement each period. However, in the following situations it is appropriate to revise the terms of the audit engagement or to remind the entity of existing terms:

- (i) Any indication that the entity misunderstands the objective and scope of the audit.
 - (ii) Any revised or special terms of the audit engagement.
 - (iii) A recent change of senior management.
 - (iv) A significant change in ownership.
 - (v) A significant change in nature or size of the entity's business.
 - (vi) A change in legal or regulatory requirements.
 - (vii) A change in the financial reporting framework adopted in the preparation of the financial statements.
 - (viii) A change in other reporting requirements.
- (b) **Vouching of Payment of Taxes:**
 - (i) Obtain the computation of income prepared by the auditee and verify whether it is as per the Income-tax Act, 1961 and Rules made there under.
 - (ii) Review adjustments, expenses disallowed, special rebates etc. with particular reference to the last available completed assessment.

- (iii) Examine relevant records and documents pertaining to payment of advance tax, self assessment tax and other demands.
 - (iv) Payment on account of income-tax and other taxes consequent upon a regular assessment should be verified by reference to the copy of the assessment order, assessment form, notice of demand and the receipted challan.
 - (v) Payments or advance payments of income-tax should also be verified with the notice of demand and the receipted challan acknowledging the amount paid.
 - (vi) The interest allowed on advance payments of income-tax should be included as income and penal interest charged for non-payment should be debited to the interest account.
 - (vii) Ensure that the requirements of AS 22 on 'Accounting for Taxes on Income' have been appropriately followed for the period under audit.
- (c) **Removal of Auditor before Expiry of Term:** As per section 224 of the Companies Act, 1956, an auditor may be removed from office before the expiry of his term, by the company in a general meeting, obtaining the prior approval of the Central Government in that behalf except that such approval is not required for the removal of the first auditor appointed by the Directors under the proviso to sub-section (5) of section 224 of the Companies Act, 1956.

This is a very stringent provision to ensure that any auditor who is inconvenient to the management cannot be removed so easily. Such provision goes a long way to ensure independence of auditor. Thus, first auditor, appointed by the Board of Directors may be removed by merely passing an ordinary resolution. However, a nomination notice from a member of the company of at least 14 days is required for the appointment of any other person in his place.

- (d) **Verification of Cash at Bank:** While testing the authenticity of cash at bank, the following areas may be considered by the auditor:
- (i) Apart from comparing the entries in the cash book with those in the Pass Book the auditor should obtain a certificate from the bank confirming the balance at the close of the year as shown in the Pass Book.
 - (ii) Examine the bank reconciliation statement prepared as on the last day of the year and see whether (a) cheques issued by the entity but not presented for payment, and (b) cheques deposited for collection by the entity but not credited in the bank account have been duly debited/credited in the subsequent period.
 - (iii) Pay special attention to those items in the reconciliation statements which are outstanding for an unduly long period. The auditor should ascertain the reasons for such outstanding items from the management. He should also examine whether any such items require an adjustment write-off.

- (iv) Examine relevant certificates in respect of fixed deposits or any type of deposits with banks duly supported by bank advices.
- (v) The auditor should examine the possibility, that even though the balance in an apparently inoperative account may have remained stagnant, transactions may have taken place in that account during the year.
- (vi) In relation to balances/deposits with specific charge on them, or those held under the requirements of any law, the auditor should examine that suitable disclosures are made in the financial statements.
- (vii) Remittances shown as being in transit should be examined with reference to their credit in the bank in the subsequent period. Where the auditor finds that such remittances have not been credited in the subsequent period, he should ascertain the reasons for the same. He should also examine whether the entity has reversed the relevant entries in appropriate cases.
- (viii) The auditor should examine that suitable adjustments are made in respect of cheques which have become stale as at the close of the year.
- (ix) Where material amounts are held in bank accounts which are blocked, e.g. in foreign banks with exchange control restrictions or any banks which are under moratorium or liquidation, the auditor should examine whether the relevant facts have been suitably disclosed in the financial statements. He should also examine whether suitable adjustments on this account have been made in the financial statements in appropriate cases.
- (x) Where the auditor finds that the number of bank accounts maintained by the entity is disproportionately large in relation to its size, the auditor should exercise greater care in satisfying himself about the genuineness of banking transactions and balances.

Question 2

- (a) *Explain the objectives of internal audit.* (8 Marks)
- (b) *How an auditor can audit allotment of debentures?* (8 Marks)

Answer

- (a) **Objectives of Internal Audit:** Internal Audit is an independent management function, which involves a continuous and critical appraisal of the functioning of an entity with a view to suggest improvements thereto and add value to and strengthen the overall governance mechanism of the entity, including the entity's risk management and internal control system.

The objective of internal audit can be stated as follows:

- (i) To verify the accuracy and authenticity of the financial accounting and statistical records presented by the management.

- (ii) To ascertain that the standard accounting practices, as have been decided to be followed by the organisation, are being adhered to.
 - (iii) To establish that there is a proper authority for every acquisition, retirement and disposal of assets.
 - (iv) To confirm that liabilities have been incurred only for the legitimate activities of the organisation.
 - (v) To analyse and improve the system of internal check in particular to see (1) that it is working ; (2) that it is sound ; and (3) that it is economical.
 - (vi) To facilitate the prevention and detection of frauds.
 - (vii) To examine the protection afforded to assets and the uses to which they are put.
 - (viii) To make special investigations for management.
 - (ix) To provide a channel whereby new ideas can be brought to the attention of management.
 - (x) To review the operation of the overall internal control system and to bring material departures and non-compliances to the notice of the appropriate level of management; the review also generally aims at locating unnecessary and weak controls for making the entire control system effective and economical.
- (b) **Allotment of Debentures:** Following are the steps to be taken by an auditor while doing the audit of allotment of debentures :
- (i) Verify that the Prospectus or the Statement in lieu of Prospectus had been duly filed with the Registrar before the date of allotment.
 - (ii) Check the applications for debentures with the Application and Allotment Book to verify that the name, address of the applicants and the number of debentures applied for are correctly recorded.
 - (iii) Verify the allotment of debentures by reference to the Directors' Minute Book.
 - (iv) Vouch the amounts collected as are entered in the Cash Book with the counterfoils of receipts issued to the applicants; also trace the amounts into the Application and Allotment Book.
 - (v) Check postings of allotments of debentures and the amounts received in respect thereof from the Application and Allotment Book, into the Debentures Register.
 - (vi) Verify the entries on the counterfoils of debentures issued with the Debentures Register.
 - (vii) Extract balances in the Debentures Register in respect of amounts paid by the debenture holders and agree their total with the balance in the Debentures Account in the General Ledger.

- (viii) Examine a copy of the Debenture Trust Deed and note the conditions including creation of Debenture Redemption Reserve contained therein as to issue and repayment.
- (ix) If the debentures are covered by a mortgage or charge, it should be verified that the charge has been correctly recorded in the Register of Mortgages and Charges and that it has also been registered with the Registrar of Companies. Further, that the charge is clearly disclosed in the Balance Sheet.
- (x) Compliance with SEBI Guidelines should also be seen.
- (xi) Where debentures have been issued as fully paid up to vendors as a part of the purchase consideration, the contract in this regard should be referred to.

Question 3

- (a) *Explain the process of external confirmation. Give some examples where external confirmation can be used as audit evidence.* (8 Marks)
- (b) *What are the duties of an auditor in case of reduction of capital?* (8 Marks)

Answer

- (a) **External Confirmation:** According to SA 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:

- (1) Bank balances and other information from bankers.
- (2) Accounts receivable balances.
- (3) Stocks held by third parties.
- (4) Property title deeds held by third parties.

- (5) Investments purchased but delivery not taken.
 - (6) Loans from lenders.
 - (7) Accounts payable balances.
 - (8) Long outstanding share application money.
 - (9) Terms of Agreement or transaction with the third parties
- (b) Reduction of Capital: The duties of the auditor in this regard are following :
- (i) Verify that the meeting of the shareholders was properly convened and the proposal of reduction of share capital was passed by Special Resolution and also that the proposal was circularised in advance among the members.
 - (ii) Verify that the reduction of share capital is authorised by the Articles of Association and the procedure prescribed by the Article has been followed.
 - (iii) Examine the order of the Tribunal confirming the reduction of share capital and see that a copy of the order and the minutes have been registered and filed with the Registrar of Companies.
 - (iv) Inspect Registrar's Certificate as regards reduction of capital.
 - (v) Vouch the journal entries recorded to reduce the capital and to write down the assets by reference to the resolution of shareholders and other documentary evidence; also seeing that the requirements of Schedule VI, Part I, have been complied with.
 - (vi) Confirm that revaluation of assets have been properly disclosed in Balance Sheet.
 - (vii) Verify the adjustment made in the member's accounts in the Register of Members and confirm that either the paid up amount shown on the old share certificates have been altered or new certificates have been issued in lieu of the old, and the old ones have been cancelled.
 - (viii) Confirm that the words "and reduced", if required by the order of the Tribunal, have been added to the name of the company in the Balance Sheet.
 - (ix) Verify that the Memorandum of Association of the company has been suitably altered.

Question 4

- (a) *What are CAATS? Why are CAAT required in computerized information system (CIS) environment?* (8 Marks)
- (b) *What is Companies (Auditor's Report) Order 2003? Explain the companies which are not covered by the CARO order.* (8 Marks)

Answer

- (a) **Computer Aided Audit Techniques (CAATs):** The use of computers may result in the design of systems that provide less visible evidence than those using manual procedures. Computer Aided Audit Techniques (CAATs) are such techniques applied through the computer which are used in the verifying the data being processed by it.

System characteristics resulting from the Computerised Information System (CIS) Environment that demand the use of Computer Aided Audit Techniques (CAAT) are:

- (i) ***Absence of input documents:*** Data may be entered directly into the computer systems without supporting documents. In on-line transaction systems, written evidence of individual data entry authorization, e.g., credit limit approval may not be available.
- (ii) ***Lack of visible transaction trail:*** Certain data may be maintained on computer files only. In a manual system, it is normally possible to follow a transaction through the system by examining source documents, books of account, records, files and reports. In CIS environment, however, the transaction trail may be partly in machine-readable form, and it may exist only for a limited period of time.
- (iii) ***Lack of visible output:*** In a manual system, it is normally possible to examine visually the results of processing. In CIS environment, the results of processing may not be printed or only a summary data may be printed. Thus, lack of visible output may result in the need to access data retained on machine readable files.
- (iv) ***Ease of Access to data and computer programmes:*** Data and computer programmes may be altered at the computer or through the use of computer equipment at remote locations. Therefore, in the absence of appropriate controls, there is an increased potential for unauthorized access to, and allocation of, data and programmes by persons inside or outside the entity.
- (v) ***Audit effectiveness:*** The effectiveness and efficiency of auditing procedures will be improved through the use of CAAT in obtaining and evaluating audit evidence, for example –
 - (1) Some transactions may be tested more effectively for a similar level of cost by using the computer.
 - (2) In applying analytical review procedures, transactions or balance details of unusual items may be reviewed and reports got printed more efficiently by using the computer.
- (vi) ***Savings in time:*** The auditor can save time by reviewing the CIS controls using CAAT than through other audit procedures.
- (vii) ***Effective test checking and examination in depth:*** CAAT permits effective examination in depth of selected transactions since the auditor constructs the lost audit trail.

- (b) CARO, 2003: CARO is an additional reporting requirement Order which was issued by the Central Government in consultation with the Institute of Chartered Accountants of India under section 227 (4A) of the Companies Act, 1956. This Order is legally known as Companies Auditor's Report Order, 2003 and it makes obligatory for the statutory Auditor to make a specific statement on certain additional points contained in as 21 Clauses/Paragraph in their audit report.

As per CARO, 2003, the auditor is required to report in relation to fixed assets, inventories, terms and condition of loans and advances, adequacy of internal control system, maintenance of cost records, deposition of statutory dues, default in repayment of dues FI/bank/debenture holders, Disclosure of the end use of money raised by the public issues, fraud on or by the company noticed or reported etc. Some of the reporting requirements contained in the Order go beyond the scope of financial audits and involved propriety aspects as well

Companies not Covered by the Order

Companies which are not covered under CARO 2003 are :

- (i) a banking company as per the Banking Regulation Act, 1949;
- (ii) an insurance company as per the Companies Act, 1956;
- (iii) a company licensed to operate under section 25 of the Companies Act, 1956; and
- (iv) a private limited company with a paid-up capital and reserves not more than rupees fifty lakh and which does not have outstanding loan exceeding rupees twenty five lakhs from any bank or financial institution and does not have a turnover exceeding rupees five crores at any point of time during the financial year.

Question 5

- (a) *Mention 8 special points which you as an auditor would look into while auditing the accounts of a Recreation Club with facilities for indoor games and in house eatery.*

(8 Marks)

- (b) *What are the focus points in doing propriety audits by C & AG as regards government expenditure?*

(8 Marks)

Answer

- (a) **Audit of Accounts of Recreational Club**

- (i) Examine the constitution, powers of governing body and relevant rules relating to preparation and finalisation of accounts. In case, it is constituted as a company limited by guarantee, application of provisions of the Companies Act, 1956 should also be seen.
- (ii) Vouch the receipt on account of entrance fees with member's applications, counterfoils issued to them, and minutes of the Managing Committee.

- (iii) Vouch Members' subscription with the counterfoils of receipts issued to them. Trace receipts for a selected period to the Register of members; reconcile the amount of total subscription due with the amount collected and the outstanding. Check totals of various columns of the Register of Members and tally them across. See the Register of Members to ascertain the Member's dues which are in arrear and enquire whether necessary steps have been taken for their recovery. The amount considered irrecoverable, if any should be written off.
 - (iv) Ensure that arrears of subscriptions for the previous year have been correctly brought over and arrears for the year under audit and subscription received in advance have been correctly adjusted.
 - (v) Verify the internal check as regards members being charged with the price of foodstuffs and drinks provided to them and their guests as well as with the fees chargeable for the special service rendered such as billiards, tennis, etc. Trace debits for a selected period from subsidiary registers maintained in respect of supplies and services to members to confirm that the account of every member has been debited with amounts recoverable from him.
 - (vi) Vouch purchase of sports items, furniture, crockery, etc., and trace their entries into the respective stock registers. Vouch purchases of food-stuffs, cigars, wines, etc. and test their sale price so as to confirm that the normal rates of profit have been earned on their sales. The stock of unsold provisions and stores, at the end of the year should be verified physically and its valuation checked.
 - (vii) Check the stock of furniture, sports material and other assets physically with the respective stock registers or inventories prepared at the end of the year.
 - (viii) Inspect the share scrips and bonds in respect of investments, check their current values for disclosure in final accounts, also ascertain that the arrangements for their safe custody are satisfactory, check the accrual of income there from and provision of income tax thereon. .
- (b) **Focus points for doing Propriety Audits of Government Expenditure:** The Propriety audit is to vet the expenditure in the annals of financial wisdom and uprightness. It is to check to bring out the improper, avoidable, or in fructuous expenditure even though such expenditure has been incurred in conformity with the existing rules and regulations. A transaction may satisfy all the requirements of regularity audit in so far as the various formalities regarding rules and regulations are concerned but may still be highly wasteful. It is not audit of sanction or against norms. It is a qualitative, opinion-based expression of auditor's findings as regards the efficiency, effectiveness and economy dimensions of expenditure.

In this regards, the following main points should be kept for consideration:

- (i) The expenditure should not be prima facie more than what the occasion demands. Public money should be spent by the officers, as of their own with utmost diligence and care.

- (ii) No order for sanction of expenditure should be made by an authority which results in pecuniary gains directly or indirectly.
- (iii) Public moneys should not be utilised for the benefit of a particular person or section of the community unless:
 - (1) the amount of expenditure involved is insignificant; or
 - (2) a claim for the amount could be enforced in a Court of law; or
 - (3) the expenditure is in pursuance of a recognised policy or custom; and
 - (4) the amount of allowances, such as travelling allowances, granted to meet expenditure of a particular type should be so regulated that the allowances are not, on the whole, sources of profit to the recipients.
- (iv) There should not be profiteering by the authority or anybody where the expenditure is in the nature of compensating.
- (v) Wastages are avoided in expenditure.
- (vi) The cost of administering should not eat off the benefits of the expenditure.
- (vii) The expenditure should percolate down the beneficiary without corruption.
- (viii) The expenditure should bring out optimum, enduring benefits instead of mere frittering away the public money on meeting day to day needs repeatedly.

Question 6

- (a) *Discuss the areas in which different accounting policies may be adopted* (6 Marks)
- (b) *Discuss the types of audits required under law.* (5 Marks)
- (c) *Disclosure requirements of debtors in the financial statements.* (5 Marks)

Answer

- (a) **Areas in which Different Accounting Policies are adopted:** Accounting policies refer to the specific accounting principles and the methods of applying those principles adopted by the enterprise in the preparation and presentation of financial statements.

There is no single list of accounting policies which are applicable to all circumstances. The different circumstances in which enterprises operate in a situation of diverse and complex economic activity make alternative accounting principles and methods of applying those principles acceptable. The choice of the appropriate accounting principles and the methods of applying those principles in the specific circumstances of each enterprise require for considerable judgment by the management of the enterprise.

The following are examples of the areas as given in AS- 1, Disclosure of Accounting Policies in which different accounting policies may be adopted by different enterprises.

- (i) Method of depreciation, depletion and amortization.

- (ii) Valuation of fixed assets.
- (iii) Valuation of inventories.
- (iv) Valuation of goodwill.
- (v) Valuation of investment.
- (vi) Treatment of retirement benefits.

(The above list is not exhaustive. There may be other examples as well.)

- (b) **Audit required under Law:** Audit is not legally obligatory for all types of business organisations or institutions. On this basis audits may be of two broad categories i.e., audit required under law and voluntary audits.

The organisations which require audit under law are the following:

- (i) Companies governed by the Companies Act, 1956;
- (ii) Banking companies governed by the Banking Regulation Act, 1949;
- (iii) Electricity supply companies governed by the Electricity Supply Act, 1948;
- (iv) Co-operative societies registered under the Co-operative Societies Act, 1912;
- (v) Public and charitable trusts registered under various Religious and Endowment Acts;
- (vi) Corporations set up under an Act of Parliament or State Legislature such as the Life Insurance Corporation of India.
- (vii) Specified entities under various sections of the Income-tax Act, 1961.
- (viii) Audit required under Sales-tax and VAT by various State Government.

- (c) **Disclosure Requirements of Debtors in Financial Statements:**

1. Classification by Age

- (i) Debtors outstanding for a period exceeding 6 months and
- (ii) Other debts.

The amount of provision for doubtful debts shall be shown separately. This is called classification by Age.

2. Classification by nature:

- (i) Debts considered good and in respect of which the company is fully secured.
- (ii) Debts considered good for which the company holds no security other than the debtor's personal security and
- (iii) Debts considered doubtful or bad.

3. Classification by party:

- (i) Debts due by the Directors or other officers of the company, or any of them

severally or jointly with any other person. (The term "officer" includes any Director, Manager, or secretary but not auditor).

- (ii) Debts due by Firms or private companies respectively in which any director is a partner or a director or a member, as the case may be.
- (iii) Debts due from other companies under the same management along with names of companies concerned.

The maximum amount due, by directors or other officers of the company at any time during the year to be shown by way of a note.

- 4 **Provisions:** Provisions shown herein should not ensure the amount of the debts considered doubtful or bad-surplus provided, if any shall be shown as revenue under the head "reserves and surplus" under the heading "Reserve for Doubtful or bad debts".
5. **Excluded items:** The amounts to be shown under sundry debtors shall include the amounts due in respect of goods sold or services rendered or in respect of other contractual obligations, but shall not include the amounts which are in the nature of loans or advances.

Question 7

Write short notes on any four of the following:

- (a) *Importance of working papers.*
- (b) *Reliability of Audit Evidence.*
- (c) *Audit of sale of Investments*
- (d) *Verification of assets acquired on lease.*
- (e) *Advantages of statistical sampling in Auditing.*

(4 x 4 = 16 Marks)

Answer

- (a) **Importance of Working Papers:** Audit working papers constitute the basic records for the auditor in respect of the audit carried out by him. They constitute the link between the auditor's report and the client's record.

These includes retention of permanent record in the nature of a document to show the actual audit work executed, the nature of work, the extent of work and the important points, facts, dates and decisions having bearing on the audit of the accounts audited. The audit working papers are found very useful in the following aspects as:

- (i) It provides guidance to the audit staff with regard to the manner of checking the schedules.
- (ii) The auditor is able to fix responsibility on the staff member who signs each schedule checked by him.

- (iii) It acts as evidence in the court of law when a charge of negligence is brought against the auditor.
 - (iv) It acts as the process of planning for the auditor so that he can estimate the time that may be required for checking the schedules.
- (b) **Reliability of Audit Evidence:** As per SA 500 "Audit Evidence", the reliability of information to be used as audit evidence, and therefore of the audit evidence itself, is influenced by its source and its nature, and the circumstances under which it is obtained, including the controls over its preparation and maintenance where relevant. Therefore, generalisations about the reliability of various kinds of audit evidence are subject to important exceptions. Even when information to be used as audit evidence is obtained from sources external to the entity, circumstances may exist that could affect its reliability. For example, information obtained from an independent external source may not be reliable if the source is not knowledgeable, or a management's expert may lack objectivity. While recognising that exceptions may exist, the following generalisations about the reliability of audit evidence may be useful:
- (i) The reliability of audit evidence is increased when it is obtained from independent sources outside the entity.
 - (ii) The reliability of audit evidence that is generated internally is increased when the related controls, including those over its preparation and maintenance, imposed by the entity are effective.
 - (iii) Audit evidence obtained directly by the auditor (for example, observation of the application of a control) is more reliable than audit evidence obtained indirectly or by inference (for example, inquiry about the application of a control).
 - (iv) Audit evidence in documentary form, whether paper, electronic, or other medium, is more reliable than evidence obtained orally (for example, a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed).
 - (v) Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies or facsimiles, or documents that have been filmed, digitised or otherwise transformed into electronic form, the reliability of which may depend on the controls over their preparation and maintenance.
- (c) **Audit of Sale of Investments:**
- (i) See that sale of investment has been made on the proper authorisation of Board or other competent authority.
 - (ii) Ascertain the method of selling investments. It may be either through broker, directly or through a bank. See the broker's sold note.
 - (iii) See that the difference between the carrying amount and the sales proceeds, net of expenses, is recognised in the Profit & Loss Account. Ensure that when only a part

of the holding of an individual investment is sold, the carrying amount is allocated on the basis of average carrying amount of the total holding of the investments.

- (iv) See that proper disclosures as required by AS 13 are made as follows:
 - (1) Interest, dividends, rentals on investments are to be shown in P& L A/c at Gross Value and TDS as advance tax paid.
 - (2) Showing separately profit & Loss on disposal and changes in carrying amount of current and long term investments.

(d) Verification of Assets acquired on Lease:

- (i) Examine the terms and conditions of the lease deed.
- (ii) If a part of the leasehold property has been sublet, examine the tenant's agreement.
- (iii) Verify relevant document to check the cost of property.
 - (1) In case of acquisition of an asset is on operating lease, lease payment should be recognized as an expense in the statement of profit and loss account on a straight line basis over the lease term, in case of operating lease;
 - (2) In case of acquisition of an asset is on finance lease, ensure all the substantial risks and rewards to ownership are transferred, considering the indication as prescribed in AS-19, the lessee should recognize the lease as an asset and as a liability. Such recognition should be at an amount equal to the fair value of the leased assets at the inception of the lease. Ensure contingent rents are recognized as expense in the statement of profit & loss for the period in case of Finance lease.
- (iv) Ensure assets acquired under finance lease are segregated from the assets owned.
- (v) Ensure that the assets under lease have been properly disclosed as per requirement of Schedule VI

(e) Advantage of Statistical Sampling in Auditing:

- (i) The sample size does not increase in proportion to the increase in the size of population.
- (ii) The sample selection is more objective and is based on mathematical law of probability.
- (iii) This method gives a minimum sample size associated with a specified risk and precision level.
- (iv) It also provides a means for taking a calculated risk and corresponding precision i.e., the probable difference in the result due to checking of transaction on sample basis in lieu of checking the entire universe.
- (v) It may provide a better description of large mass of data than a complete examination of all the data, since non-sampling errors such as processing and clerical mistake are not large.