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PAPER –2: AUDITING AND ASSURANCE

Question No.1 is compulsory.

Attempt any five questions from the remaining six questions.

Question 1

Discuss on the following:

- (a) *Standards collectively known as the Engagements Standards issued by AASB under the authority of the council of ICAI.* (5 Marks)
- (b) *Payment of interest to the shareholders on capital raised by issue of shares to meet the cost of construction of building which cannot be made profitable for a long period.* (5 Marks)
- (c) *Distinguish between Reserves and Provisions.* (5 Marks)
- (d) *In Joint Audit, "each Joint Auditor is responsible only for the work allocated to him".* (5 Marks)

Answer

(a) Engagement Standards

The following standards issued by the Auditing and Assurance Standards Board under the authority of the Council are collectively known as the Engagement Standards.

- (i) Standards on Auditing (SAs), to be applied in the audit of historical financial information.
- (ii) Standards on Review Engagements (SREs), to be applied in the review of historical financial information.
- (iii) Standards on Assurance Engagements (SAEs), to be applied in assurance engagements, dealing with subject matters other than historical financial information.
- (iv) Standards on Related Services (SRSs), to be applied to engagements involving application of agreed-upon procedures to information, compilation engagements, and other related services engagements, as may be specified by the ICAI.

(b) Payment of Interest out of Capital during Construction

Under the provisions of section 208, a company which has raised money by issue of shares to meet the cost of construction of any work or building or provision of any plant which cannot be made profitable for a long time, can pay interest on paid-up capital for a period and subject to conditions specified in sub-sections (2) to (7) of section 208. Accordingly, the payment of interest should be verified as follows:—

- (i) Ascertain that the payment is authorised by the Articles or by a special resolution.

- (ii) Verify that the previous sanction of the Central Government for making such payment has been obtained.
- (iii) Confirm that the interest has been paid only for such period as has been authorised by the Central Government and does not extend beyond the half-year next following during which the construction was completed or the plant was provided.
- (iv) Verify that the rate of interest shall, in no case exceed such rate as the Central Government may, by notification in official Gazette direct.
- (v) Check that the amount of interest paid has been added to the cost of assets created out of the capital.

The interest paid being a part of the capital expenditure incurred in bringing into the assets existence should be added thereto. Until so added, it must be shown as a separate item in the Balance Sheet under the head 'Miscellaneous Expenditure'.

(c) Reserves and Provision

- (i) Reserve is an appropriation of profit whereas provision is a charge against Profit.
- (ii) Reserves are not intended to meet any liability, contingency or diminution in the value of assets. Provisions are made to provide for depreciation, renewal or a known liability or a disputed claim.
- (iii) Reserves cannot be created unless there is a profit except revaluation reserve and capital subsidy. Provisions must be created whether or not there is profit.
- (iv) Reserves are generally optional except in certain situations – Capital Redemption reserve, Debenture Redemption Reserve, Declaration of dividend higher than 10% etc. Provisions are not optional and have to be made as per generally accepted accounting principles.
- (v) Reserves are shown on the liability side. Provisions for depreciation and provision for doubtful debts are shown as deduction from respective assets. Provision for liability is shown on the liability side.

(d) Responsibility of Joint Auditor

The principles governing to responsibilities of joint auditor are prescribed in SA 299, "Responsibility of Joint Auditor". As per SA 299, if joint auditors are appointed, they should divide the audit work among themselves by mutual discussion. The division of work would usually be in terms of audit of identifiable units or specified areas. Such division of work should be adequately documented and preferably communicated to the entity.

It is the responsibility of each joint auditor to determine the nature, timing and extent of audit procedures to be applied in relation to the area of work allocated to him. The issue such as appropriateness of using test checks, sampling or other audit techniques should be decided by each joint auditor individually in relation to his work. Thus, the responsibility will not be

shared by the other auditor. Therefore, it is the separate and specific responsibility of each joint auditor to study and evaluate the prevailing system of internal control relating to the work allocated to him.

Hence, in respect of audit work divided among the joint auditors, each joint auditor is responsible only for the work allocated to him, whether or not he has prepared a separate report on the work performed by him. However, all the joint auditors are jointly and severally responsible in respect of the audit work which is not divided among the joint auditors and is carried out by all of them, in respect of decisions taken by all the joint auditors concerning the nature, timing or extent of the audit procedures to be performed by any of the joint auditors, in respect of matters which are brought to the notice of the joint auditors by any one of them and on which there is an agreement among the joint auditors, for examining that the financial statements of the entity comply with the disclosure requirements of the relevant statute and for ensuring that the audit report complies with the requirements of the relevant statute.

Question 2

- (a) *What are the general considerations in framing a system of internal check?* (8 Marks)
(b) *Discuss the audit procedure for verification of payment of dividends.* (8 Marks)

Answer

(a) General Considerations in Framing a System of Internal Check

Internal check has been defined by the Institute of Chartered Accountants of England and Wales as the "checks on day-to-day transactions which operate continuously as part of the routine system whereby the work of one person is proved independently or is complementary to the work of another, the object being the prevention or early detection of errors or fraud".

The General Considerations in Framing a System of Internal Check are as follows:

- (i) No single person should have an independent control over any important aspect of the business. All dealings and acts of every employee should, in the ordinary course, come under the review of another.
- (ii) The duties of members of the staff should be changed from time to time without any previous notice so that the same officer or subordinate does not, without a break, perform the same function for a considerable length of time.
- (iii) Every member of the staff should be encouraged to go on leave at least once in a year. Experience has shown that frauds successfully concealed by employees are often unearthed when they are on leave.
- (iv) Persons having physical custody of assets must not be permitted to have access to the books of account.

- (v) There should exist an accounting control in respect of each important class of assets. In addition, these should be periodically inspected so as to establish their physical condition.
 - (vi) To prevent loss or misappropriation of cash, mechanical devices such as the automatic cash register should be employed.
 - (vii) A majority of business concerns now-a-days work according to some kind of budgetary control. It enables them to review from time to time the progress of their trading activities. Such business houses should have a separate staff for the collection of statistical figures which later on should be checked with the corresponding figures from the financial books. If wide discrepancies are observed, these should be reconciled.
 - (viii) For stock-taking, at the close of the year, trading activities should, if possible, be suspended. The task of stock-taking and evaluation should be done by staff belonging to several sections of the organisation. It may prove dangerous to depend exclusively on the stock section staff for these tasks since they may be tempted to under or over-state the stock.
 - (ix) The financial and administrative powers should be distributed very judiciously among different officers and the manner in which these are actually exercised should be reviewed periodically.
 - (x) Procedures should be laid down for periodical verification and testing of different sections of accounting records to ensure that they are accurate.
 - (xi) Accounting procedures should be reviewed periodically, for, even well-designed and carefully installed procedures, in course of time, cease to be effective.
 - (xii) The system of Budgetary Control should be introduced. It would enable business concerns to review from time to time the progress of their trading activities.
- (b) Verification of Dividends

The procedure for the verification of payment of dividends is stated below:

- (i) Examine the company's Memorandum and Articles of Association to ascertain the dividend rights of different classes of shares.
- (ii) Confirm that the profits appropriated for payment of dividend are distributable having regard to the provisions contained in Section 205 and that the transfer to reserves is according to rules framed by the Central Government in this respect [vide Section 205(2A)]. It may be noted that now there exists a requirement to transfer profits to reserves upon 10 per cent of the profits of that year. However, if the rate of dividend does not exceed 10 per cent no such transfer is necessary. If the company proposes to pay the dividend out of past profits, see that either this is in accordance with the rules framed by the Central Government in this behalf or the consent of the Government has been obtained. [vide Section 205A(3)].

- (iii) Inspect the shareholders' Minute Book to verify the amount of dividend declared and confirm that the amount recommended by the directors.
- (iv) If a separate bank account was opened for payment of dividends, check the transfer of the total amount of dividends payable from the Dividends Accounts.
- (v) Check the particulars of members as are entered in the Dividend Register or Dividend List by reference to the Register of Members. Test check the calculation of the gross amount of dividend payable to each shareholder on the basis of the number of the shares held. Verify the casts and cross cast of the different columns.
- (vi) Check the amount of dividend paid with the dividend warrants surrendered. Reconcile the amount of dividend warrants outstanding with the balance in the Dividend Bank Account.
- (vii) Examine the dividend warrants in respect of previous years presented during the year for payment and verify that by their payment any provision contained in the Articles in the matter of period of time during which amount of unclaimed dividend can be paid had not been contravened.
- (viii) According to section 205A, as it is compulsory for a company to transfer the total amount of dividend which remains unpaid or unclaimed, within thirty days of the declaration of the dividend to a special bank account entitled "Unpaid Dividend Account of Company Limited/Company (Pvt.) Limited". Such an account is to be opened only in a scheduled bank. The transfer must be made within 7 days from the date of expiry of thirty days.

The expression "dividend which remains unpaid" means any dividend the warrant in respect thereof has not been encashed or which has otherwise not been paid or claimed.
- (ix) In case any money transferred to the unpaid dividend amount of a company remain unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred to Investor Education and Protection Fund established under section 205C of the Act.

Question 3

- (a) *How will you verify/ vouch the retirement gratuity to employees?* (6 Marks)
- (b) *Discuss appointment of Auditor by special resolution.* (6 Marks)
- (c) *State the matters which only the shareholders can sanction at a General Meeting.* (4 Marks)

Answer

- (a) **Vouching / Verification of Retirement Gratuity to Employees**
 - (i) Examine the basis on which the gratuity payable to employees is worked out. The liability for gratuity may either be worked out on actuarial rules or agreement or on the presumption that all employees retire on the balance sheet date.

- (ii) Verify computation of liability of gratuity on the aggregate basis.
- (iii) Check the amount of gratuity paid to employees who retired during the year with reference to number of years of service rendered by them.
- (iv) See that the annual premium has been charged to Profit and Loss account in case the concern has taken a policy from LIC.
- (v) Ensure that the basis of computing gratuity is valid.
- (vi) Ensure that the accounting treatment is in accordance with AS 15, "Accounting for Retirement Benefits in the Financial Statements".

(b) Appointment of Auditor by Special Resolution

Section 224A of the Act provides for appointment or re-appointment of auditors in certain cases only by special resolution. It should be remembered that normally an auditor can be appointed by an ordinary resolution. However, in terms of section 224A, a company in which not less than 25% of the subscribed capital is held by : (i) a public financial institution or a government company or the Central Government, or any State Government, or (ii) any financial or other institution established by any Provincial or State Act in which a State Government, holds not less than 51% of the subscribed share capital, (iii) a nationalised bank or an insurance company carrying on general insurance business; or (iv) any combination of the above categories, shall appoint or re-appoint an auditor in the annual general meeting only by passing a special resolution.

In case the aforesaid company omits or fails to pass a special resolution in the annual general meeting for appointing auditors, it shall be deemed that no auditor or auditors had been appointed and thereupon the Central Government's power to appoint the auditor pursuant to section 224(3) will become operative.

In determining whether the appointment calls for a special resolution or not, the measuring yard stick is the proportion of the subscribed capital held by the various categories mentioned above. If any of them singly or several of them jointly hold 25% of the subscribed capital of the company as on the day of the closing of the register of members before the annual general meeting, the company will be covered by provisions of section 224A and consequently, the appointment of auditor can only be made by passing a special resolution. Government has clarified that for the purposes of section 224A the composition of shareholding shall be of the day of annual general meeting. This will virtually be same in relation to the position available on the day of the closing of the register of members stated above. It should be noted that subscribed capital includes preference share capital also.

(c) Matters to be sanctioned only by the Shareholders

Some of the matters which only the shareholders can sanction at a general meeting

- (i) Appointment and fixation of remuneration of auditors in the annual general meeting - section 224 of the Companies Act, 1956.

- (ii) Declaration of dividends - Regulation 85, Table A.
- (iii) Appointment of relatives of directors etc. to an office or place of profit in the company under section 314 of the Companies Act, 1956.
- (iv) Sale, lease or a disposal of the whole of the company's undertaking or a substantial part of it and donations above a certain limits [Section 293(1)].
- (v) Rectification of name or adoption of new name where it resembles the name of an existing company with the previous approval of the Central Government.
- (vi) Issue of shares at a discount.
- (vii) Alteration of share capital.
- (viii) Re-issue of redeemed debentures.
- (ix) Adoption of statutory report.
- (x) Passing of annual accounts and balance sheet, alongwith reports of Board of directors and auditors.
- (xi) Appointment of first directors who are liable to retire by rotation.
- (xii) Increase or reduction in the number of directors within the limit fixed by the Articles.
- (xiii) Appointment of managing/whole-time director.
- (xiv) Removal of a director and appointment of a director in his place.
- (xv) Approval of appointment of sole selling agents.
- (xvi) Winding up a company voluntarily in certain events.
- (xvii) Appointment and fixation of remuneration of liquidators in members voluntary winding up.
- (xviii) Nomination of a liquidator in creditors voluntary winding up.

Question 4

- (a) *Explain "Going Concern" assumption with reference to SA. State some financial events or conditions that may cast doubt about going concern assumption.* (8 Marks)
- (b) *You are the auditor and examining the book debts of a company. Give some indications which leads to doubt about recovery as uncollectable debts from debtors and advances.* (8 Marks)

Answer

- (a) **Going Concern Assumption**

SA 570, "Going Concern" deals with the auditor's responsibility in the audit of financial statements with respect to management's use of the going concern assumption in the preparation and presentation of the financial statements.

Under the going concern assumption, an entity is viewed as continuing in business for the foreseeable future. General purpose financial statements are prepared on a going concern basis, unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so. Special purpose financial statements may or may not be prepared in accordance with a financial reporting framework for which the going concern basis is relevant. When the use of the going concern assumption is appropriate, assets and liabilities are recorded on the basis that the entity will be able to realise its assets and discharge its liabilities in the normal course of business.

Financial Events or Conditions That May Cast Doubt about Going Concern Assumption

The following are examples of events or conditions that, individually or collectively, may cast significant doubt about the going concern assumption.

- Net liability or net current liability position.
- Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment; or excessive reliance on short-term borrowings to finance long-term assets.
- Indications of withdrawal of financial support by creditors.
- Negative operating cash flows indicated by historical or prospective financial statements.
- Adverse key financial ratios.
- Substantial operating losses or significant deterioration in the value of assets used to generate cash flows.
- Arrears or discontinuance of dividends.
- Inability to pay creditors on due dates.
- Inability to comply with the terms of loan agreements.
- Change from credit to cash-on-delivery transactions with suppliers.
- Inability to obtain financing for essential new product development or other essential investments.

(b) Indications of Doubtful and Uncollectible Debts

The term 'book debts' suggests particularly amounts recoverable from customers, but in practice it is applied to a wide range of claims which a business may carry as an asset in its books. Advances or loans cannot, however, be included under this head.

The following are some of the indications of doubtful and uncollectible debts, loans and advances:

- (i) The terms of credit have been repeatedly ignored.

- (ii) There is stagnation or lack of healthy turnover in the account.
- (iii) Payments are being received but the balance is continuously increasing.
- (iv) Payments though being received regularly, are quite small in relation to the total outstanding balance.
- (v) An old bill has been partly paid (or not paid), while later bills have been fully settled.
- (vi) The cheques received from the debtors have been repeatedly dishonoured.
- (vii) The debt is under litigation, arbitration, or dispute.
- (viii) The auditor becomes aware of unwillingness or inability of the debtor to pay the dues, e.g., a debtor has either become insolvent, or has closed down his business, or is not traceable.
- (ix) Amounts due from employees, which have not been repaid on termination of employment.
- (x) Collection is barred by statute of limitation.

Question 5

- (a) *Mention the eight important points which an auditor will consider while conducting the audit of educational institutions.* (8 Marks)
- (b) *Explain the meaning of term "Subsequent Events" as used in the SA560. Should all types of subsequent events be considered by the auditor in his attest functions?* (8 Marks)

Answer

(a) Audit of Educational Institutions

The important points which an auditor should consider while conducting the audit of education institutions are as follows:

- (i) Examine the Trust Deed or Regulations, in the case of school or college and note all the provisions affecting accounts. In the case of a university, refer to the Act of Legislature and the Regulation framed thereunder.
- (ii) Read through the minutes of the meetings of the Managing Committee or Governing Body, noting resolutions affecting accounts to see that these have been duly complied with, specially the decisions as regards the operation of bank accounts and sanctioning of expenditure.
- (iii) Check names entered in the Students Fee Register for each month or term, with the respective Class Registers, showing names of students on rolls and test amount of fees charged; and verify that there operates a system of internal check which ensures that demands against the students are properly raised.

- (iv) Check fees received by comparing counterfoils of receipts granted with entries in the Cash Book and tracing the collections in the Fee Register to confirm that the revenue from this source has been duly accounted for.
- (v) Total up the various columns of the Fees Register for each month or term to ascertain that fees paid in advance have been carried forward and that the arrears that are irrecoverable have been written off under the sanction of an appropriate authority.
- (vi) Check admission fees with admission slips signed by the head of the institution and confirm that the amount has been credited to a Capital Fund, unless the Managing Committee has taken a decision to the contrary.
- (vii) See that free studentship and concessions have been granted by a person authorised to do so, having regard to the Rules prescribed by the Managing Committee.
- (viii) Confirm that fines for late payment or absence, etc. have been either collected or remitted under proper authority.
- (ix) Confirm that hostel dues were recovered before student's accounts were closed and their deposits of caution money refunded.
- (x) Verify rental income from landed property with the rent rolls, etc.
- (xi) Vouch income from endowments and legacies, as well as interest and dividends from investment; also inspect the securities in respect of investments held.
- (xii) Verify any Government or local authority grant with the relevant paper of grant. If any expense has been disallowed for purposes of grant, ascertain the reasons and compliance thereof.
- (xiii) Report any old heavy arrears on account of fees, dormitory rents, etc. to the Managing Committee.
- (xiv) Confirm that caution money and other deposits paid by students on admission, have been shown as liability in the balance sheet not transferred to revenue, unless they are not refundable.
- (xv) See that the investments representing endowment funds for prizes are kept separate and any income in excess of the prizes has been accumulated and invested along with the corpus.
- (xvi) Verify that the Provident Fund money of the staff has been invested in appropriate securities.
- (xvii) Vouch donations, if any with the list published with the annual report. If some donations were meant for any specific purpose, see that the money was utilised for the purpose.

- (xviii) Vouch all capital expenditure in the usual way and verify the same with the sanction for the Committee as contained in the minute book.
- (xix) Vouch, in the usual manner, all establishment expenses and enquire into any unduly heavy expenditure under any head. If there was any annual budget prepared, see that any excess under any head over the amount budget was duly sanctioned by the Managing Committee. If not, bring it to the Committee's notice in your report.
- (xx) See that increase in the salaries of the staff have been sanctioned and minuted by the Committee.
- (xxi) Ascertain that the system ordering inspection on receipt and issue of provisions, foodstuffs, clothing and other equipment is efficient and all bills are duly authorised and passed before payment.
- (xxii) Verify the inventories of furniture, stationery, clothing, provision and all equipment etc. These should be checked by reference to Stock Register or corresponding inventories of the previous year and values applied to various items should be test checked.
- (xxiii) Confirm that the refund of taxes deducted from the income from investment (interest on securities etc.) has been claimed and recovered since the institutions are generally exempted from the payment of income-tax.
- (xxiv) Finally, verify the annual statements of account and, while doing so see that separate statements of account have been prepared as regards Poor Boys Fund, Games Fund, Hostel and Provident Fund of staff, etc.

(b) Meaning of Subsequent Events

SA 560 on "Subsequent Events", defines the term 'subsequent events' as events occurring between the date of the financial statements and the date of the auditor's report, and facts that become known to the auditor after the date of the auditor's report "subsequent events" also refer to significant events which occurred up to the date of report of the auditor of that component. Thus, subsequent events are those events which occur after the date of the balance sheet till the audit report is signed by the auditor.

Consideration of Subsequent Events by the Auditor

SA 560 requires that the auditor should consider the effect of subsequent events on the financial statements and the auditor's report. However, the exact manner of treatment would depend upon whether the event falls in the category of 'adjusting event' or 'non-adjusting event'. As per Accounting Standard (AS) 4, events occurring after the date of the balance sheet are of two types, viz., adjusting events which provide further evidence of conditions that existed at the date of the balance sheet; and, non-adjusting events are those which are indicative of conditions that arose subsequent to the date of the balance sheet.

Therefore, an auditor is required to consider all subsequent events while discharging his duties and determine whether those shall have to be adjusted or simply required to be disclosed. However, the auditor should perform work as near as practicable to the date of the auditor's report.

Question 6

- (a) Discuss CARO 2003 requirement with regard to internal audit system. What are the factors to be considered by the auditor to examine whether the internal audit system is commensurate with the size of the company and the nature of its business? (8 Marks)
- (b) What are the advantages of an independent audit? (8 Marks)

Answer

- (a) Internal Audit System and CARO, 2003:

As per Para 4(vii) of CARO, 2003, statutory auditor is required to comment on whether the auditee company has an internal audit system commensurate with its size and nature of its business.

The clause has a mandatory application in respect of listed companies. For other companies, it is applicable if either of the following conditions is satisfied:

- (1) the paid-up capital and reserves of the company are more than rupees fifty lakhs as at the commencement of the financial year; or
- (2) average annual turnover exceeds rupees five crores for a period of three consecutive financial years immediately preceding the financial year concerned.

The following are some of the factors to be considered to ensure that the internal audit system commensurate with the size of the company and the nature of its business:

- (i) Size of the internal audit department.
- (ii) The qualifications of the persons who undertake the internal audit work
- (iii) Reporting officer of the internal auditor.
- (iv) Areas covered by the internal auditor.
- (v) Technical assistance of the internal auditor.
- (vi) Reports submitted by the internal auditor or other evidence of his work: It is important that the auditor should satisfy himself that not merely does an internal audit system exist but also that it is functioning effectively. He can do so by examining the reports submitted by the internal auditor.
- (vii) Follow-up: It is not sufficient that the internal audit system should point out errors in operation or deficiencies in the internal control system. It is equally necessary that there is an adequate follow-up system to ensure that the errors pointed out are corrected and remedial action taken on the deficiencies reported upon.

(b) Advantages of an Independent Audit

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, these advantages are given below:

- (i) It safeguards the financial interest of persons who are not associated with the management of the entity, whether they are partners or shareholders.
- (ii) It acts as a moral check on the employees from committing defalcations or embezzlement.
- (iii) Audited statements of account are helpful in settling liability for taxes, negotiating loans and for determining the purchase consideration for a business.
- (iv) These are also useful for settling trade disputes for higher wages or bonus as well as claims in respect of damage suffered by property, by fire or some other calamity.
- (v) An audit can also help in the detection of wastages and losses to show the different ways by which these might be checked, especially those that occur due to the absence or inadequacy of internal checks or internal control measures.
- (vi) Audit ascertains whether the necessary books of account and allied records have been properly kept and helps the client in making good deficiencies or inadequacies in this respect.
- (vii) As an appraisal function, audit reviews the existence and operations of various controls in the organisations and reports weaknesses, inadequacies, etc., in them.
- (viii) Audited accounts are of great help in the settlement of accounts at the time of admission or death of partner.
- (ix) Government may require audited and certified statements before it gives assistance or issues a license for a particular trade.

Question 7

Write short notes on any four of the following:

- (a) *Preliminary Expenses.*
- (b) *Initial Engagements.*
- (c) *Disadvantages of the use of an audit programme.*
- (d) *Audit Techniques.*
- (e) *Simple random sampling.*

(4 x 4 = 16 Marks)

Answer**(a) Preliminary Expenses**

This term is applied to expenses incurred in connection with the formation of a limited company. They generally include the following expenses:

- (i) Legal costs in drafting the memorandum and articles of association;
- (ii) Capital duty and other fees on registration of the company;
- (iii) Cost of printing the memorandum and articles of association;
- (iv) Cost of statutory books and the companies seal, etc; and
- (v) Any other expense incurred to bring into existence the statutory books of the company.

Preliminary expenses in so far as they have not been written off to date must be shown separately in the balance sheet of the company under the heading "Miscellaneous Expenditure".

The auditor should verify these expenses with reference to supporting documents such as invoices and contracts relating to these expenses. In the case of a company, the auditor should also examine that the reimbursement of such expenses to promoters is in accordance with the disclosures made in the prospectus. Compliance with legal provisions regarding reimbursement of the promoters' expenses should be specifically examined.

(b) Initial Engagements

In conducting an initial engagement, the objective of the auditor with respect to opening balances is to obtain sufficient appropriate audit evidence about whether opening balances contain misstatements that materially affect the current period's financial statements; and appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are properly accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

Note : Alternative answer may be given on the basis of SA 210 or in relation to audit engagement letter.

(c) Disadvantages of the use of an Audit Programme

There are some disadvantages in the use of audit programmes but most of these can be removed by taking some steps which otherwise also contribute to the making of a good audit. The disadvantages are :

- (i) The work may become mechanical and particular parts of the programme may be carried out without any understanding of the object of such parts in the whole audit scheme.

- (ii) The programme often tends to become rigid and inflexible following set grooves; the business may change in its operation of conduct, but the old programme may still be carried on. Changes in staff or internal control may render precaution necessary at points different from those originally decided upon.
- (iii) Inefficient assistants may take shelter behind the programme i.e. defend deficiencies in their work on the ground that no instruction in the matter is contained therein.
- (iv) A hard and fast audit programme may kill the initiative of efficient and enterprising assistants.

(d) Audit Techniques

For collection and accumulation of audit evidence, certain methods and means are available and these are known as audit techniques. Some of the techniques commonly adopted by the auditors are the following:

- (i) Posting checking
- (ii) Casting checking
- (iii) Physical examination and count
- (iv) Confirmation
- (v) Inquiry
- (vi) Year-end scrutiny
- (vii) Re-computation
- (viii) Tracing in subsequent period
- (ix) Bank Reconciliation

The audit techniques stand for the methods employed for carrying out the procedure. For example, procedure requires an examination of the documentary evidence. This job is performed by the procedure known as vouching which would involve techniques of inspection and checking computation of documentary evidence.

(e) Simple random sampling:

Under this method each unit of the whole population e.g. purchase or sales invoice has an equal chance of being selected. The mechanics of selection of items may be by choosing numbers from table of random numbers by computers or picking up numbers randomly from a drum. It is considered that random number tables are simple and easy to use and also provide assurance that the bias does not affect the selection. This method is considered appropriate provided the population to be sampled consists of reasonably similar units and fall within a reasonable range. For example the population can be considered homogeneous, if say, debtors balances fall within the range of ₹ 5,000 to ₹ 25,000 and not in the range between ₹ 25 to ₹ 2, 50,000.