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PAPER – 6 : AUDITING AND ASSURANCE

Question No.1 is compulsory.

*Attempt any **five** questions from the remaining six questions.*

Question 1

(a) *Discuss with reference to SAs :*

- (i) *The auditor shall communicate all significant findings with those charged with Governance. (5 Marks)*
- (ii) *Factors effecting form, contents and extent of audit. (5 Marks)*

(b) *Discuss the following :*

- (i) *Is surprised checks desirable in audit, if so give important recommendations. (5 Marks)*
- (ii) *Inquiry is one of the audit procedure to obtain audit evidence. (5 Marks)*

Answer

- (a) (i) As per SA-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) As per SA-230 on "Audit Documentation", the form, content and extent of audit documentation depend on the following factors :
- 1. The size and complexity of the entity.
 - 2. The nature of the audit procedures to be performed.

3. The identified risks of material misstatement.
 4. The significance of the audit evidence obtained.
 5. The nature and extent of exceptions identified.
 6. 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.
 7. The audit methodology and tools used.
- (b) (i) The need for and frequency of surprise checks is obviously a matter to be decided having regard to the circumstances of each audit. It would depend upon the extent to which the auditor considers the internal control system as adequate, the nature of the clients' transaction, the locations from which he operates and the relative importance of items like cash, investments, stores etc. However, wherever feasible a surprise check should be made at least once in the course of an audit.

The following are the important recommendations:

- (1) Surprise checks should be considered as a desirable part of each audit.
 - (2) The areas over which surprise checks should be employed would depend upon the circumstances of each audit but should normally include:
 - (a) Verification of cash and investments.
 - (b) Test-verification of stores and stocks and the records relating thereto.
 - (c) Verification of books of prime entry and statutory registers normally required to be examined for the purposes of audit.
 - (3) The frequency of surprise checks may be determined by the auditor in the circumstances of each audit but should normally be at least once in the course of an audit.
 - (4) The results of the surprise checks should be communicated to the management if they reveal any weakness in the system of internal control or any fraud or error or deficiency in the maintenance of records.
 - (5) The auditor should satisfy himself that adequate action is taken by the management on the matters communicated by him.
 - (6) It is not necessary in all cases for the results of the surprise checks to be included in the auditors' report on the accounts. They should, however, be included if in the opinion of the auditor they are material and affect a true and fair view of the accounts on which he is reporting.
- (ii) Inquiry consists of seeking information of knowledgeable persons, both financial and non- financial, within the entity or outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures. Inquiries may range from

formal written inquiries to informal oral inquiries. Evaluating responses to inquiries is an integral part of the inquiry process.

Responses to inquiries may provide the auditor with information not previously possessed or with corroborative audit evidence. Alternatively, responses might provide information that differs significantly from other information that the auditor has obtained, for example, information regarding the possibility of management override of controls. In some cases, responses to inquiries provide a basis for the auditor to modify or perform additional audit procedures.

Although corroboration of evidence obtained through inquiry is often of particular importance, in the case of inquiries about management intent, the information available to support management's intent may be limited. In these cases, understanding management's past history of carrying out its stated intentions, management's stated reasons for choosing a particular course of action, and management's ability to pursue a specific course of action may provide relevant information to corroborate the evidence obtained through inquiry. In respect of some matters, the auditor may consider it necessary to obtain written representations from management and, where appropriate, those charged with governance to confirm responses to oral inquiries.

Question 2

Comment on any **eight** of the following:

(8 x 2 = 16 Marks)

- (i) PQR Ltd. Include underwriting commission and stamp duty as preliminary expenses.
- (ii) AGM is not held in time, auditor automatically vacates his office.
- (iii) Selling and distribution cost included in the cost of inventories.
- (iv) Internal check is part of internal control system.
- (v) Company can provide lower rate of depreciation than prescribed by Schedule XIV of the Companies Act; 1956.
- (vi) Compliance procedures are tests designed to obtain audit evidence as to completeness, accuracy and validity of data produced by accounting system.
- (vii) ABC Ltd. having turnover of ₹ 100 crores during financial year 2011-12, need not get its branch audited whose turnover is ₹ 1.5 crores during the same year.
- (viii) Computer software which is the integral part of the related hardware can be treated as intangible assets or fixed assets?
- (ix) CARO, 2004 does not apply to a foreign company.
- (x) Define shortly arm's length transaction.

Answer

- (i) The expenditure incidental to the creation and floating of a company includes stamp duties, registration fees, legal costs, accountant's fees, cost of printing, etc. Underwriting commission and brokerage paid for shares and debentures should not be included under the head preliminary expenses. Therefore, PQR Ltd should include stamp duty as preliminary expense but exclude underwriting commission.
- (ii) Section 224(1) provides that an auditor is appointed for a particular period, i.e., from conclusion of one annual general meeting until conclusion of the next annual general meeting. In case the annual general meeting is not held within the period prescribed, the auditor will continue in office till the annual general meeting is actually held and concluded. Therefore, auditor shall continue to hold office till the conclusion of the annual general meeting. Auditor's office is not vacated automatically if AGM is not held in time.
- (iii) As per AS-2 on Valuation of Inventories, in determining the cost of inventories, it is appropriate to exclude selling and distribution costs and recognise them as expenses in the period in which they are incurred. Therefore, it is not appropriate to include selling and distribution cost in the cost of inventories.
- (iv) Internal check has been defined as "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". Internal check is a part of the overall internal control system and operates as a built-in device as far as the staff organisation and job allocation aspects of the control system are concerned.
- (v) It is permissible for the entity to charge depreciation on its assets at rate different from schedule XIV rates provided those rates are higher than the schedule rates based on technical estimation or otherwise allowed under Section 205 of the Act. The rates as contained in Schedule XIV are minimum rates and therefore a company cannot provide lower rate of depreciation than prescribed by Schedule XIV of the Companies Act, 1956.
- (vi) Compliance procedures are tests designed to obtain reasonable assurance that those internal controls on which audit reliance is to be placed are in effect. Here auditor is concerned with assertions that the control exists and is operating effectively.
- (vii) As per rules to section 228 (4) of the companies (Branch Audit exemption) Rules 1961, where the aggregate value of goods sold by a branch office does not exceed ₹ 2 lakhs or 2% of the average of the total turnover of the company, whichever is higher, the branch shall be exempted from audit. Hence the branch in question is not required to be audited.
- (viii) As per AS-26 on Intangible Assets, computer software for a computer controlled machine tool that cannot operate without that specific software is an integral part of the related

hardware and it is treated as a fixed asset. Therefore, computer software which is the integral part of the related hardware should be treated as fixed asset.

- (ix) CARO, 2003 applies to all companies including foreign companies except Banking, Insurance, Sec. 25 Companies and Private Ltd. Companies subject to certain conditions.
- (x) Arm's length transaction - A transaction conducted on such terms and conditions as between a willing buyer and a willing seller who are unrelated and are acting independently of each other and pursuing their own best interests.

Question 3

- (a) *What is continuous audit and what are the precautions which should be taken to avoid the disadvantages of continuous audit ?* (8 Marks)
- (b) *Explain the basic principles governing audit.* (8 Marks)

Answer

- (a) *Continuous audit* : A continuous audit is one in which the auditor's staff is engaged continuously in checking the accounts of the client the whole year round or when for this purpose the staff attends at intervals, fixed or otherwise, during the currency of the financial period.

The disadvantages of a continuous audit can be avoided if the following precautions are taken:

- (1) During the course of each visit, work should be completed upto a definite stage so as to avoid loose ends.
- (2) At the end of each visit, important balances should be noted down and the same should be compared at the time of the next visit.
- (3) The visits should be at irregular intervals of time so that the client's staff may not in advance know the exact date when the audit would be resumed and thus may be able to prepare themselves in advance for the same.
- (4) The nominal accounts should be checked only at the time of final closing.
- (5) The client's staff should be instructed not to alter or correct audited figures. The auditor should also device a special form of ticks for being placed against figures which have been altered and neither its purpose nor significance should be disclosed to the client's staff.

(b) Basic Principles Governing an Audit

The basic principles which govern the auditor's professional responsibilities and which should be complied with wherever an audit is carried are described below:

- (i) ***Integrity, objectivity and independence:*** The auditor should be straight forward, honest and sincere in his approach to his professional work. He should maintain an impartial attitude and both be and appear to be free of any interest which might be

regarded, whatever is actual effect, as being incompatible with integrity and objectivity.

- (ii) **Confidentiality:** The auditor should respect the confidentiality of information acquired in the course of his work and should not disclose any such information to a third party without specific authority or unless there is a legal or professional duty to disclose.
- (iii) **Skills and Competence:** The audit should be performed and the report prepared with due professional care by persons who have adequate training, experience and competence in auditing. The auditor requires specialised skills and competence along with a continuing awareness of developments including pronouncements of the ICAI on accounting and auditing matters, and relevant regulations and statutory requirements.
- (iv) **Work performed by others:** When the auditor delegates work to assistants or uses work performed by other auditors and experts, he continues to be responsible for forming and expressing his opinion on the financial information. However, he will be entitled to rely on work performed by others, provided he exercises adequate skill and care and is not aware of any reason to believe that he should not have so relied.
- (v) **Documentation:** The auditor should document matters which are important in providing evidence 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 an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client's business.
- (vii) **Audit evidence:** The auditor should obtain sufficient appropriate audit evidence through the performance of compliance and substantive procedures to enable him to draw reasonable conclusions therefrom on which to base his opinion on the financial information.
- (viii) **Accounting system and Internal Control:** The auditor should gain an understanding of the accounting system and related controls and should study and evaluate the operation of those internal controls upon which he wishes to rely in determining the nature, timing and extent of other audit procedures.
- (ix) **Audit Conclusions and Reporting:** The auditor should review and assess the conclusions drawn from the audit evidence obtained and from his knowledge of business of the entity as the basis for the expression of his opinion on the financial information.

The audit report should contain a clear written opinion on the financial information and should comply the legal requirements. When a qualified opinion, adverse opinion 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 therefore.

Question 4

- (a) *To prepare an audit plan in CIS environment an auditor should gather information. Mention any four such important information which he has to collect. (4 Marks)*
- (b) *How will you vouch/verify the followings?*
- (i) *Purchase with invoice*
 - (ii) *Patterns, dies, loose tools etc.*
 - (iii) *Work-in-Progress* (3 x 4 = 12 Marks)

Answer

- (a) The auditor should gather information about the CIS environment that is relevant to the audit plan, including information as to:
1. How the CIS function is organized and the extent of concentration or distribution of computer processing throughout the entity.
 2. The computer hardware and software used by the entity.
 3. Each significant application processed by the computer, the nature of the processing (e.g. batch, on-line), and data retention policies.
 4. Planned implementation of new applications or revisions to existing applications.
 5. When considering his overall plan the auditor should consider matters, such as:
 - (i). Determining the degree of reliance, if any, he expects to be able to place on the CIS controls in his overall evaluation of internal control.
 - (ii). Planning how, where and when the CIS function will be reviewed including scheduling the works of CIS experts, as applicable.
 - (iii) Planning auditing procedures using computer-assisted audit techniques.
- (b) (i) **Purchase with invoice:** While vouching entries for purchases with the invoices, the following points should be specially observed:
- (a) that the date of invoice falls within the accounting period;
 - (b) that the invoice is made out in the name of the client;
 - (c) that the supplier's account has been credited with the full amount of the invoice and that the deduction in the amount of the invoice, if any, has been made on a proper basis;
 - (d) that the goods purchased are those that are regularly dealt in by the concern or required for the process of manufacture carried on by it and that the price payable has been correctly arrived at;

- (e) that the cost of purchases has been debited to an appropriate nominal account or accounts;
 - (f) that the invoice is signed by the accountant to show that he has verified it as well as the store-keeper to indicate that the delivery of goods have been taken by him. If the invoice relates to the purchase of a technical store or a chemical, the price whereof is dependent on its quality, a copy of the report of a technical person showing that the article purchased is of the specification for which the order has been placed; and
 - (g) that the manager or some other official, competent to sanction payment, has authorised its payment.
- (ii) Patterns, Dies, Loose Tools, etc.: Several entities have large investments in such assets which have a relatively short useful life and low unit cost. Evidently, it is a difficult matter, under the circumstances, to prepare a separate account for each such asset although a careful control over such property is necessary.

On these considerations, some entities charge off small tools and other similar items to Production Account as and when they are purchased and do not place any value on the unused stock on the Balance Sheet. Nevertheless, a record of issues and receipts of tools to workmen is kept, as a check on the same being pilfered and a memorandum stock account of dies and patterns is also maintained. In other concerns, the cost of tools, dies, etc. purchased is debited to appropriate assets account, and an inventory of the unused items at the end of the year is prepared and valued; the sum total of opening balance and purchase reduced by the value of closing stock, as disclosed by the inventory, is charged off to Production Account in respect of such assets. On the other hand, some concerns carry such assets at their book values at the end of the first year and charge off the cost of all the purchases in the subsequent year to the Production Account on the plea that they represent cost of replacement.

The most satisfactory method, however, is that of preparing an inventory of serviceable articles, at the close of each year, and revaluing the assets on this basis, the various articles included in the inventory being valued at cost. It should be seen that the inventory does not include any worn out or defective articles the life of which has already run out.

- (iii) **Work-in-Progress:** The audit procedures regarding work-in-progress are similar to those used for raw materials and finished goods. However, the auditor has to carefully assess the stage of completion of the work-in-progress for assessing the appropriateness of its valuation. For this purpose, the auditor may examine the production/costing records (i.e., cost sheets), hold discussions with the personnel concerned, and obtain expert opinion, where necessary. The auditor may advise his client that where possible the work-in-progress should be reduced to the minimum

before the closing date. Cost sheets of work-in-progress should be verified as follows:

- (i) Ascertain that the cost sheets are duly attested by the works engineer and works manager.
- (ii) Test the correctness of the cost as disclosed by the cost records by verification of quantities and cost of materials, wages and other charges included in the cost sheets by reference to the records maintained in respect thereof.
- (iii) Compare the unit cost or job cost as shown by the cost sheet with the standard cost or the estimated cost expected.
- (iv) Ensure that the allocation of overhead expenses had been made on a rational basis.

Compare the cost sheet in detail with that of the previous year. If they vary materially, investigate the cause thereof.

- (v) Ensure that the Work-in-Progress as at Balance Sheet date has been appropriately disclosed in Balance Sheet as per the requirements of Part I of Revised Schedule VI (applicable w.e.f. 1.4.2011) to the Companies Act, 1956

Question 5

- (a) State the circumstances which could lead to any of the following in an Auditors Report:
 - (i) A modification of opinion
 - (ii) Disclaimer of opinion
 - (iii) Adverse opinion
 - (iv) Qualified opinion (4 x 2 = 8 Marks)
- (b) What are the cases in which special audit may be called by Central Government? (4 Marks)
- (c) Anandbhai & Co. Ltd. issued shares to the equity shareholders in the proportion of one bonus share for every three existing shares. As an auditor of the Company how would you verify this issue? (4 Marks)

Answer

- (a) (i) The auditor shall modify the opinion in the auditor's report when:
 - (a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or
 - (b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

- (ii) The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

The auditor shall disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.

- (iii) The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.
- (iv) The auditor shall express a qualified opinion when:
- (a) The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or
 - (b) The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.
- (b) Section 233 A empowers the Central Government, in certain cases, to call for a 'special audit'. Such an audit may be required where the Central Government has reasons to believe:
- (i) that the affairs of the company are not being managed on sound business principles or according to prudent commercial practices; or
 - (ii) that the company is being managed in a manner likely to cause serious injury or damage to the interests of the trade, industry or business to which it pertains; or
 - (iii) that the financial position of the company is such as might endanger its solvency.
- (c) **Verification of Issue of Bonus Shares:** Primarily, it should be ascertained whether the Articles permit capitalisation of profits; also whether the company had a sufficient number of unissued shares for allotment as bonus shares. In addition, the following steps should be taken:
- (i) Inspect the Minute book of Shareholders for the resolution authorising declaration of the Bonus and Director's Minute for the resolution appropriating profits for being applied in payment of shares to be allotted to shareholders as bonus shares;

- (ii) Trace the allotment of shares as per particulars contained in the Allotment Book or sheets into the Register of Members; and
- (iii) Confirm that all statutory requirements relevant to the issue of shares have been complied with, viz., the filing of the particulars of the bonus shares allotted with the Registrar together with a copy of the resolution pursuant to which allotment has been made.
- (iv) Confirm that the issue of fully paid up bonus shares in pursuance of sub-section (3) of Section 205 has been kept in abeyance in respect of shares where any instrument of transfer of such shares has been delivered to the company for registration and the transfer of such shares has not been registered by the company as required by the provisions of section 206A of the Companies (Amendment) Act, 1988.
- (v) Ensure that SEBI Guidelines relating to issue of bonus shares have been complied with.

Question 6

- (a) *Mention important points which auditors will consider while conducting audit of accounts of a partnership firm.* (8 Marks)
- (b) *What are the points on which an auditor should concentrate while planning audit of an N.G.O. ?* (8 Marks)

Answer

- (a) Important points which auditors will consider while conducting audit of accounts of a partnership firm are:
 - (i) Confirming that the letter of appointment, signed by a partner, duly authorised, clearly states the nature and scope of audit contemplated by the partners, specially the limitation, if any, under which the auditor shall have to function.
 - (ii) Studying the minute book, if any, maintained to record the policy decision taken by partners specially the minutes relating to authorisation of extraordinary and capital expenditure, raising of loans; purchase of assets extraordinary contracts entered into and other such matters as are not of a routine nature.
 - (iii) Verifying that the business in which the partnership is engaged is authorised by the partnership agreement; or by any extension or modification thereof agreed to subsequently.
 - (iv) Examining whether books of account appear to be reasonable and are considered adequate in relation to the nature of the business of the partnership.
 - (v) Verifying generally that the interest of no partner has suffered prejudicially by an activity engaged in by the partnership which, it was not authorised to do under the partnership deed or by any violation of a provision in the partnership agreements.

- (vi) Confirming that a provision for the firm's tax payable by the partnership has been made in the accounts before arriving at the amount of profit divisible among the partners.
- (vii) Verifying that the profits and losses have been divided among the partners in their agreed profit-sharing ratio.
- (b) While planning the audit of an N.G.O, the auditor should concentrate on the following:
 - (i) Knowledge of the NGO's work, its mission and vision, areas of operations and environment in which it operates.
 - (ii) Updating knowledge of relevant statutes especially with regard to recent amendments, circulars, judicial decisions viz. Foreign Contribution (Regulation) Act 1976, Societies Registration Act, 1860, Income Tax Act 1961 etc. and the Rules related to the statutes.
 - (iii) Reviewing the legal form of the Organisation and its Memorandum of Association, Articles of Association, Rules and Regulations.
 - (iv) Reviewing the NGO's Organisation chart, Financial and Administrative Manuals, Project and Programme Guidelines, Funding Agencies Requirements and formats, budgetary policies if any.
 - (v) Examination of minutes of the Board/Managing Committee/Governing Body/Management and Committees thereof to ascertain the impact of any decisions on the financial records.
 - (vi) Study the accounting system, procedures, internal controls and internal checks existing for the NGO and verify their applicability.
 - (vii) Setting of materiality levels for audit purposes.
 - (viii) The nature and timing of reports or other communications.
 - (ix) The involvement of experts and their reports.
 - (x) Review the previous year's Audit Report.

Question 7

Write short notes on any **four** of the following:

- (i) *Audit Planning & Materiality*
- (ii) *Impairment of Assets*
- (iii) *Internal Control Questionnaire*
- (iv) *Letter of Weakness*
- (v) *Assertion about balance at the end of the reporting period.* (4x4 = 16 Marks)

Answer

- (i) **Audit Planning and Materiality:** Materiality is an important consideration for an auditor to evaluate whether the financial statements reflect a true or fair view or not. SA 320 on "Materiality in Planning and Performing an Audit" requires that an auditor should consider materiality and its relationship with audit risk while conducting an audit. When planning the audit, the auditor considers what would make the financial information materially misstated. The auditor's preliminary assessment of materiality related to specific account balances and classes of transactions helps the auditor decide such questions as what items to examine and whether to use sampling and analytical procedures. This enables the auditor to select audit procedures that, in combination, can be expected to support the audit opinion at an acceptably low degree of audit risk. It may be noted that the auditor's assessment of materiality and audit risk may be different at the time of initially planning of the audit as against at the time of evaluating the results of audit procedures.
- (ii) **Impairment of assets:** Besides charging annual depreciation on assets by the reason of normal wear and tear, effluxion of time and obsolescence to reinstate the correct value of the assets considering the future cash flows that the assets can generate, impairment loss needs to be provided. The difference between the carrying amount of an asset and recoverable amount is termed as impairment loss. The treatment of impairment loss is similar to depreciation except the fact that it can be reinstated in future, if the recoverable amount of the asset exceeds the carrying amount.

The auditor must ensure that provisions of AS 28 "Impairment of assets" are followed.

- (iii) **Internal Control Questionnaire:** This is a comprehensive series of questions concerning internal control. This is the most widely used form for collecting information about the existence, operation and efficiency of internal control in an organisation.

An important advantage of the questionnaire approach is that oversight or omission of significant internal control review procedures is less likely to occur with this method. With a proper questionnaire, all internal control evaluation can be completed at one time or in sections. The review can more easily be made on an interim basis. The questionnaire form also provides an orderly means of disclosing control defects. It is the general practice to review the internal control system annually and record the review in detail. In the questionnaire, generally questions are so framed that a 'Yes' answer denotes satisfactory position and a 'No' answer suggests weakness. Provision is made for an explanation or further details of 'No' answers. In respect of questions not relevant to the business, 'Not Applicable' reply is given.

The questionnaire is usually issued to the client and the client is requested to get it filled by the concerned executives and employees. If on a perusal of the answers, inconsistencies or apparent incongruities are noticed, the matter is further discussed by auditor's staff with the client's employees for a clear picture. The concerned auditor then prepares a report of deficiencies and recommendations for improvement.

(iv) Letter of Weakness

- (1) The auditor does compliance procedure to ascertain that the internal control system exist in the entity, it works effectively; it work continuously in the entity during review period.
- (2) When he comes across any weakness in the control points, he issues letter of weakness.
- (3) Letter of weakness is a report issued by auditor stating the weakness in internal control mechanism. It also suggests measures by which the weakness in the system be corrected and the control system be made better protected.
- (4) Lapses in operation of internal control too are reported in the communication of weakness.
- (5) The communication of weakness is reporting to management of such weakness in design and operation of internal control as have come to notice of auditor during his auditing and it should not be taken to be a review and comment on adequacy of the control mechanism for management purpose.

(v) Assertions about account balances at the end of the reporting period:

Assertions about account balances at the period end are :

- (i) Existence—assets, liabilities, and equity interests exist.
- (ii) Rights and obligations—the entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
- (iii) Completeness—all assets, liabilities and equity interests that should have been recorded have been recorded.
- (iv) Valuation and allocation—assets, liabilities, and equity interests are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.