

AUDITING

1. Introducing to Auditing

1.1 Basic: Financial statements, users of financial information, definition of auditing, objective of auditing – primary and secondary, expression of opinion, detection of frauds and errors.

1.2 Errors: Definition, reason and circumstances types of errors – commission, omission, principle and compensating; types of frauds, risk of frauds and error in audit, auditor duties and responsibilities in respect of frauds.

Integrity, objectivity and independence, skill and computers, confidentiality, work performed by others, documentation, panning, audit evidence, auditing system and internal control, audit conclusions and reporting.

Meaning, advantages and disadvantages of balance sheet audit, interim audit, continuous audit, annual audit etc.

Advantages of independent audit, qualities of auditors, auditing v/s accounting, auditing v/s investigations true and fair view. `

Meaning, objectives, factors to be considered, sources of obtaining information, discussions with clients, overall audit plan.

Meaning, factors, advantages and disadvantages methods of work, instruction before commencing work, overall audit approach.

Meaning, importance, factors determining forms and contents, main functions, contents of permanent audit file, temporary audit file, ownership, custody, access of other parties to audit working papers, auditors lien on working papers and on clients book.

Meaning, structure, contents, general information current information, importance etc.

Test checking v/s routine checking, test check meaning, features, factors to be considered, advantages and disadvantages etc.

Meaning and purpose, review of internal control, advantages, auditors duties, limitations of internal control, internal control samples for sales and debtors, purchase and creditors, wages and salaries.

Meaning basic principles, objectives, evaluation of internal audit by statutory auditor, usefulness of internal audit, internal audit v/s external audit internal checks v/s internal audit.

Cash sales, sales on approval, sales returns, recovery of bad debts written off, rental receipts, interest and dividend received, royalties received etc.

Purchases, purchase return, wages and salaries, rent, insurance premium, telephone expenses, postage and courier, petty cash expenses, advertisement, interest expenses, traveling salesman commission etc.

Debtors / Book debts, stock-auditors general duties, patterns dies and loose tools, spare parts, empties and containers, quoted investment and unquoted investment, trade marks/ copyrights,, patents, plant and machinery, land and building, furniture and fixtures etc.

O/s expenses, B/P, secured loans, unsecured loans, contingent liabilities etc.

INTRODUCTION TO AUDITING

*Defination:

1. Auditing to Spicer and Pegler:

Auditing Is an examination of books of accounts, registers,, vouchers of the business concern to enable the auditor to satisfy himself or not whether the balance sheet is properly drawn up so as to give a true fair view of the state of affairs of the business.

2. According to L.R. Dicksee

Accordinging is an examination of accounting record undertaken with a view o establish whether they correctly and completely reflect the transactions. The auditor also expenses his opinion whether the statement of accounts so examined show a true fair picture.

3. According to A.W. Hanson

An audit is an examination of such records to established their reliabilities and the reliability pf statement drawn from them.

4. According to Auditing and Assurance standard 1 (AAS 1) issued by ICI

Auditing is the independent examination of financial information of as entity whether profit oriented or not and irrespective of it's size and legal form, where such an examination is conducted with a view to express as opinion thereon.

* Objective of auditing:

There are 3 main objective of auditing given below:

A. Primary objective Reporting (Expression of opinion true and fair view):- the primary objective of auditing is to report whether financial statement (P/L and B/s) are properly drawn up to show a true and fair view of the state if affairs. For this purpose the auditor has to check the books of accounts, documents, vouchers, registers etc. This examination helps the auditor to form as opinion about the correctness and reliability of financial statements. He has t report whether the accounts audited by him give a true and fair view or not. If he is not satisfied with the accounts, he has to report the same in his audit report.

B. Secondary/ Incidental object (Detection and prevention of accounting arrears and frauds:- while examining the books of Accounts and other records the auditor will keep in mind the possibility of errors and frauds. They affect the correctness of the financial statement.

C. Specific object (Tax audit, cost audit etc):- Audit doesn't imply financial audit alone. It may include such arrears like review of operations, performance, past records etc. Accordingly there be specific objective of each type of audit. E.g. In cost audit an attempt is made to control the cost. In operational audit the existing operations of the organization is evaluated.

Errors:

Mistakes committed without any intention or unintentional mistakes is termed as errors. Errors usually arise out of innocence or carelessness on the part of those persons who are responsible for preparation of accounts. The auditors is required to be careful while detecting errors. The type of errors are as follows:

1. Errors of principles: There are those errors which owner from not following the accounting principles correctly. They arise when entries are not passed according to general accepted accounting principles. E.g. over or under valuation of stock over or under charging of depreciation, recording of capital expenditure as revenue expenditure etc. Such errors will not affect trial balance but will affect the P/L A/c. They are defected if as auditor out checking of book of original entries with invoices, vouchers etc.

2. Clerical and Technical errors: These are the human errors arising in the course recording the transactions in the books of accounts. They are as follows:

a. Errors of omission: This is as error of omission of recording the transactions in the books. It arises when if transaction is not been recorded wither wholly or partially. When the transaction is not recorded at all it is said to be a complete omission. It doesn't affect the agreement of trial balance and thus the errors will be more difficulty to detect. E.g. A purchase transaction not recorded at all.

When only one aspect of a transaction is recorded, it is a partial omission which affects the trial balance. Such errors are comparatively easier to detect. E.g. Sales is entered in sales register but not posted in ledger A/c.

b. Errors of commission: This is an error of recording transaction wrongly in the books. There are errors in posting, casting, carry forwarding or taking out balances etc. When such mistakes are committed in the original entry book, trial balance will agree/ tally. Posting errors may be of wrong A/c, wrong amount or wrong side. E.g. amount received from "X" credited to "Y" s A/c,

traveling expenses actually received Rs. 312 wrongly entered as Rs. 123. Thus errors will not affect the trial balance.

Casting errors which are committed while taking the total, errors in carry forward, and errors in taking out the balances affect the trial balance. Errors of commission are detected at the time of vouching and while doing scrutiny of ledger A/c

c. Errors of duplication: It arises when the entry is recorded twice in original entry book. Therefore posting are also done twice. Such errors do not affect the agreement of trial balance while examining the books of original entry with the invoices, vouchers etc. and an scrutiny of ledger A/c such errors can be detected.

d. Errors of compensating: Sometimes the effect of one error is compensated by another error. E.g. If Ram A/c is to be debited by Rs. 200 but actually debited for Rs. 20, while Shyam A/c which was to be debited for Rs. 20 was actually debited with Rs. 200. Such errors are difficult to detect as trial balance tallies/ agrees. The excess debit or credit in one account may be compensated by one or more credit or debit figures resulting out of similar types of errors. To detect such errors, posting and costing are to be checked very carefully.

*** Frauds :**

Frauds means intentional mistake or making wrong entry intentionally to deceive (cheat) others. It is a deliberate mistake committed in the accounts with a view to get personal gain. In accounting frauds means

1. Misappropriation of cash
2. Misappropriation of goods
3. Manipulation of accounts (window dressing)

1. Misappropriation of cash (Embezzlement of cash):- Where the owner of the business has no direct control over the receipts and payments of cash, the cases of misappropriation are more. In such as case a cashier or such other person can misappropriate cash. This can take at the time of receiving cash or payment of cash.

A. Receipt side of cash book:

1. No recording of cash receipts and pocketing it.
2. Omission of recording cash sales.
3. Short recording of cash sales.
4. No recording of cash actually received from debtors and write off the debts as bad debts.
5. No recording the transaction of receipt of casual or exceptional measures. E.g. sale of scrap, sale of old newspapers, receipt of donation etc.
6. Misappropriating the cash receiving on discounting of B/R and showing them as bills outstanding.
7. By undercasting receipt side total of the cash book.
8. By adopting the method of teaming an lading lapping process/ short banking.
 - It is a kind of fraud where cash is misappropriated for temporary period of time. Under this method cash received from one debtor is misappropriated and the deficiency in his A/c is made good when another payment is received from second debtor.

When cash is received from one debtor it is not recorded in cash book and is misappropriated. Later on when cash received from second debtors the A/c of first debtor is credited. Again when cash is received from third debtor then his A/c is not credited but second debtor's A/c is credited and cash A/c is debited. This process is carried out around the year or till the fraud is detected. Such type of fraud is called as teaming of lading or short balancing or lapping process.

Auditors duties in respect of teaming and lading.

The payment received must be compared with the bill. If the short amount is received an enquiry should be made.

The dates of the receipts and the dates of the entries should be verified. They should be on the same date.

The bank statement should be checked to see whether the amount has been actually received and deposited into the bank.

The auditor should see the correspondence wherever necessary.

He should see whether there is a regular practice of sending statements to all the customers to get the balances confirmed in their accounts.

The auditor should see the old unused receipt books are kept in safe custody and should be allowed to use them.

The auditor has to check whether the amount in the receipt and the corresponding amount in the counterfoil is safe.

The amounts received in cash and cheques should be deposited into the bank immediately.

The cashier should not have access to customers ledger.

The auditor should verify the amount of discount allowed and see that the correct amount is entered in the cash book.

He should verify entries of bad debts written off in detail.

Confirmation of balances by customers should be verified by the auditors.

B. Payments side of cash book:

1. By recoding fictitious or bogus payments.
2. Recording more payments than actual payments.
3. Showing the same payments twice.
4. Recording personal expenses as business expenses.
5. Not recording discounts and allowances given by the creditor.
6. Overcasting the payments side total of cash book and wages sheets, etc.

Misappropriation of goods:

Goods may be misappropriated out of goods received goods dispatched and stock in hand as follows:

Goods received may be misappropriated by not recording received goods.

Goods may be misappropriated out of the dispatches by recording dummy or excess sales.

Goods may be actually stolen out of the stock in hand lying in the warehouse.

Fraudulent manipulation of A/c (False Fiction of A/c's or window dressing)

The fraud through manipulation of A/c's is also known as window dressing because accounts are maintained to show a wrong picture of the profit or loss of the business. In accounting window dressing means the skill of presenting the accounts in a way that creates a goods impression. In window dressing the accounts are made in such a way as to show a much better condition than the actual condition. The profits and the net worth are overstated in the final account. Such fraud is committed with certain objective and is relatively difficult to detect.

Objects of window dressing:

1. To show more profits and to give more remuneration to the managerial personnel.
2. To attract more loans, credit etc. from banks and other financial institutions.
3. To attract more application for issue of shares.
4. To attract favorable terms/ credit for creditor, money lenders and financial institutions.
5. To have over valuation of goodwill at the time of admission of a new partner.

Auditors duties regarding window dressing:

1. Disclosing duties reports
2. Verifying income
3. Verify assets and liabilities
4. Verify provisions (see whether the provision in any liability is lower than the required amount)
5. Verify closing stock
6. Disclose change in the method of accounting.

* Location and Detection of Fraud:

The auditor should perform the following duties in detection of frauds:

1. Examine all the aspects of finances
2. Vouch all the receipts from the counter foils.
3. Check the wages and salary register
4. Verifying the method of valuation of stock.
5. Check up stock register, goods inward and outward register, delivery challans etc.
6. Calculate various ratios in order to detect frauds manipulation of account.
7. Exercise reasonable skill and care while performing the duty.
8. Make surprise visit to check the accounts.

*** Secret Reserve:**

Reserve means the part of profits result for future use. Secret reserves are those reserves which are not shown in the balance sheet. According to Erickhler “ Secret reserve is the amount by which the net worth has been deliberately understated – a hidden reserve such a condition exists where the assets are under valued or liabilities are over valued. When secret reserves are credited financial position of the company seems to be worst than actual. It is exactly opposite of the term window dressing.

Secret reserves are created for the following reasons:

1. To mislead its competitors by hiding it’s real profit or real earnings.
2. Sometimes the business concern may earn extraordinary or abnormal profits which may not earn in future. Such profits may be transferred to secret reserves to set off losses of for maintaining the dividend in lean years in future.
3. Secret reserve may be created with an ulterior motive. The owners may intend to withdraw the excess funds for personal use.
4. In banking companies secret reserve is legally allowed to be created because banks are not allowed to disclose their provision for bad and doubtful debts.

*** Auditor duties with regard to secret reserves:**

1. the auditor has report whether the accounts give a true and fair view in the case of balance sheet and P/L A/c. So it is his duty to report any secret reserve.
2. He should study the A/A of the company to verify the provisions of reserve.
3. He should verify whether all the income has been brought in the books of A/c’s correctly.
4. He should verify all the assets and liabilities and check the valuation of each assets. He should see no contingent liability is shown as an actual liability.
5. He should examine whether the provision of any liability is in excess of required amount considered reasonable and necessary in the opinion of directors. The excess provision if any should be treated and disclosed as reserve.
6. He should verify the value of closing stock and see that there is no cheque in the method of valuation.
7. He should see whether there is any change in the method of accounting. E.g. method of charging depreciation. If there is any such change the information and its effect on the profit should be disclosed.
8. He should verify none of the assets fixed as well as correct including closing stock has been omitted to be entered in the books.
9. He should see that bad debts written off are disclosed in the A/c’s. If any part of the secret reserve is used to meet bad and doubtful debts it must be disclosed in the balance sheet.

*** Auditing Principles:**

1. Principle of Independence
2. Principle of objectivity
3. Principle of full disclosure
4. Principle of confidentiality
5. Principle of Materiality
6. Skill and Competence

7. Work performed by others
8. Work papers
9. Audit Evidence or Proof
10. Planning
11. Evaluation of accounting and internal control
12. Opinion and Report

*** Distinguish between :**

Auditing	Accounting
1. Meaning	
Auditing is the critical examination of transactions	Accounting is recording of all the day to transaction
Records in the books of accounts.	In the books of accounts.
2. Nature of work	
It is concerned with the establishing of reliability	It is concerned with the finalization of final
Of financial statements	Accounts.
3. Objective	
To certify the correctness of financial statements	To final out profit or loss and prepare financial
	Statements.
4. Commencement	
Auditing starts when accounting ends.	Accounting starts when book keeping ends.
5. Scope	
It depends up on agreements or provisions of law	It involves various statements i.e. maintenance
	Of books of account
6. Qualification	
Auditor is an independent professional person.	Accountant is an employee require former
	Qualification
7. Status / Position	
Auditor is an independent professional person.	Accountant is an employee of the organizations
8. Errors and Frauds	
Auditor has to detect error and frauds	Accountant may commit errors and frauds in
	Maintenance of record
9. Responsibility	
Auditor is appointed by owners or shareholders and	Accountant is employed an responsible to management
Repose to them	
10. Reporting	
Auditor has to submit his report in the prescribed	An accountant doesn't submit any report .
Form	

* Auditing principle

Principle of confidentiality

The auditor should keep the information obtained during audit, confidential. He should not disclose such information to any third party. He should, it is said, keep his eyes and ears open but his mouth shut.

Skill and Competence :The auditor should have adequate training, experience and competence in auditing. He should have a professional qualification (i.e. be a (A) and practical experience. He should be aware of recent development in the field of auditing such as statements of ICAI, changes in company law, decision of court etc.

Work performed by others:

1. The auditor should carefully direct, supervise and review the work of his assistants.
2. He should satisfy himself that work done by an internal auditor is reliable.
3. He should satisfy that work done by another auditor (e.g. a branch auditor) is reliable.
4. He should satisfy himself that work done by a joint auditor is reliable.
5. He should satisfy himself that work done by an expert (lower, valuer etc.) is reliable.

Working papers: The auditor should maintain working papers of important matters to prove that audit was conducted with due care according to the basic principles.

Audit Evidence or Proof: The report of the auditor should be based on evidence obtained in the course of audit. The evidence may be obtained through vouching of transactions, verification of assets and liabilities ratio analysis etc.

Planning: the auditor should plan his audit work. He should prepare as audit programme to complete the audit efficiently and in time.

Evaluation of accounting and internal control: The auditor should ensure that the accounting is adequate. He should see that all the transactions have been properly recorded. He should study and evaluate the internal controls.

Opinion and Report: The auditor should arrive at his opinion on the accounts on the basis of the audit evidence and submit his report. The opinion may be unqualified or qualified or adverse. The audit report should clearly express his opinion. The control and form of audit report should be required by law (e.g. companies Act.)

Principle of independence: It is not only a standard but a basic veracity of auditing. The objective of auditing cannot be achieved unless the principle of independence is respects. Auditor should be honest and sincere in his audit work. He be fair and objective For this, he should be independent.

Principle of Objectivity: Auditing should be conducted objectivity. The auditor should be free from bias and emotions while conducting audit. It demands verifications of transactions and the use of reasonable skill.

Principle of full disclosure: It implies that the client should provide to the auditor all the possible evidence records and explanations. The auditor should make full disclosure of his findings.

Principle of Materiality: According to the principle, the auditor should pay more attention to the items which are more significant. Whether the items are materials or not should be decided according to situations.

*** Distinguish between:**

Auditing	Investigation
1. Meaning	
Auditing is an examination of books accounts to report whether they are true and fair	Investigation is an examination of accounts for specific purpose
2. Object	
To ascertain whether P/L A/c and Balance sheet show a true and fair view of the business concern.	To know the essential facts about a matter under enquiry with some special purpose.
3. Period	
It usually covers one accounting year	It may cover more than one accounting year.
4. conducted	
Auditing is conducted for proprietors only.	Investigation is carried out on behalf of any party interested in the matter.

5. Scope	
It is restricted to P/L A/c and Balance Sheet	It is wider in scope It may be carried out beyond Balance Sheet
6. Compulsion	
Auditing is legally compulsory for audit companies	Investigation is voluntary required under certain circumstances.
7. time	
It may be conducted at the end of the year.	It may be conducted at any time in case of suspicion about any transactions.
8. Appointment	
Owners or shareholders appoint the auditor	Even third parties can appoint investigators
9. Qualifications	
Auditor of a company must be practicing CA	Investigator doesn't require any professional qualification.
10. Re-work	
Re-audit is not generally undertaken	Re-investigation may be undertaken.
11. Report	
Form of report is prescribed. The audit report is presented to the shareholders	Form of report is not prescribed. It is not presented to the client

* **Advantages/ Necessity of auditing:** Auditing has the following advantages:-

1. It enables the auditor to comment on whether the true and fair view of the business position is shown by the company's Balance Sheet.
2. Audit helps in detecting and preventing errors and frauds.
3. Information is readily available because accounts are maintained regularly. This helps the management to study financial results.
4. It facilitates obtaining loans from banks as the audited statements are relied upon.
5. It builds up reputation of the business.
6. It enables the management to decide correct valuation of assets for the purpose of purchase and sales of business.
7. It makes the official staff alert. They keep the accounts up to date.
8. The company can get good advice from auditor in respect of taxation and other legal matters
9. Auditor can give concrete suggestions regarding improvement of business.
10. Audited accounts could be more useful for valuing the business and goodwill while admitting a partner or on requirement of a partner.
11. Auditor acts as a representative of shareholders and trustees. This helps to protect the interest of various investors.
12. For finding out the cost of production and other related data, audited accounts could be more reliable.
13. It helps to exercise moral check on directors and management to act honestly.
14. For the purpose of various licenses the govt. department requires audited statements
15. Stock exchange relies on the audited accounts for the purpose of listing of shares
16. Audited accounts are helpful in settlement of insurance claim. Insurance companies rely on audited accounts.
17. Taxation authorities can rely on audited accounts. Net profit as per audited statement is the basis of determination of taxable income. In this way auditing is advantageous to the businessmen, investors, banks and govt. etc.

* **Concept of true and fair view:**

As per Sec 227 (2) of the company's Act 1956 the auditor has to report whether the P/L a/c and Balance Sheet give true and fair view. The concept of true and fair view implies that the financial

statement should be true. They should disclose the truth about the organization. They should not contain any false information. At the same time the statement should be fair. They should disclose all that is required as per the provision of law. The following general guidelines may be laid down in this regard.

1. Adherence to accounting principles: The books of account must be kept according to normally accepted principles such as concept, of entity, double entry system, accrual method etc.
 2. No window dressing: There should not be any window dressing i.e. overstatement of profits. There should not be any secret reserve created. i.e. under statement of profit The account should reflect actual position of the business concern. In order to show true and fair view auditor should ensure that

1. Final accounts agree with the books of account
2. the assets and liabilities are not undervalued or overvalued.
3. The provision for depreciation is paper.
- 4 the stocks are properly valued and there is a consistency in the method of its valuation
- 5 Proper provision is made for bad and doubtful for bad and doubtful debt
6. Capital expenditure is not treated as revenue expenditure and vice versa
7. Capital receipts are not treated as receipts and vice versa
8. No material asset and liabilities are omitted
9. All contingent liabilities are disclosed in the balance sheet
10. The financial statement disclose information as required by schedule (6) of the company Act
11. Expected or anticipated gains are not credited to P/L

A/c

12. The exceptional or non recurring transactions are disclosed separately in the A/c

3. Disclosure if material facts: The books of accounts must disclose all material facts regarding revenue, expenses, assets and liabilities such facts help in taking business decision. There should be neither separation of vital facts nor mis-statement.

4. Legal requirement: The final accounts must be in the format prescribed under schedule 6 of the company's Act 1956 special companies such as banks, insurance electricity supply companies etc. have to prepare accounts as prescribed under special law.

5. Guidelines of ICAI: The accounts must be in accordance with various guidelines prescribed by ICAI. These guide are contained in the statements, standards and guidance note issued by the institute from time to time.

*** Qualities of an auditor:** In order to be a successful, as auditor must have the following qualities:

1. He must be a chartered accountant (A)
2. He should have expert knowledge of accounting techniques and principles, recent developments in accounting and auditing, various legislation governing the company and knowledge of industrial management, finance and administration etc.
3. He must be honest.
4. He should keep the information confidential which obtain during the course of audit.
5. An auditor must be independent and impartial.
6. He must be accurate and systematic.
7. He must have alert mind and common sense.
8. He must be cautious and vigilant.

*** Users of financial statements:** The balances of different accounts are arranged in as effective meaningful order called P/L A/c and Balance Sheet, cash flow statement etc. This financial

statements are required to be prepared in accordance with the provisions of companies Act 1956 accounting standards principles and practices and guidance note issued by ICAI. These requirements are known as financial reporting framework.

1. Owner: The owners of the business concern supply the capital for business activities. Hence, they need to know the income earned by the business concern.
2. Executive / Managers (Management): Financial statements provide accounting Information to the management to enable to decide on all important issues. The common issues are efficient utilization of capital, maintaining the profitability through cost control, payment of dividend etc.
3. Bankers/ Money lenders: Bankers/ Money lenders give loans to the business. Hence, they need to know whether loan and interest will be paid in time by the business concern. They are interested in knowing the borrows ability to repay the loans along with interest.
4. Employees: Labours/ Employees contributed to earning of the company. They are engaged in covering the raw materials into final product which produce wealth. They are also interested in the wages and salaries, bonus incentives, good working conditions etc.
5. Creditors: Creditors supply goods to the company on credit. They need to know whether their o/s bill will be paid by the business concern in time or not.
6. Shareholders and Prospective investors: Shareholders and prospective investors have permanent interest in the life and operation the company. Their desires of knowing about their companies year to year financial strength profitability, solvency position etc.

*** Accounting concept relevant to auditing:**

a) Materiality concept (AAS 13):

Auditing and Assurance standard – 14 (issued by the ICAI) deals with the concept of materiality and its relationship with the audit work. While conducting audit, the auditor should consider the concept of materiality. The assessment of materiality depends on the professional judgement. Material matters are those matters which, either individually or in the aggregate, are relatively important for true and fair presentation of financial information in accordance with recognized accounting policies and practices.

1. Considerations: the concept of Materiality is influenced by size, nature, relative importance of the matter for true and fair presentation of financial information.
2. Legal requirement: Materiality is many times influenced by law (Schedule VI of the Co's Act 1956) which requires compulsory disclosure of all the items which are material, or non-recurring or which exceed fixed percentage or the previous year's figures and so on.
3. Professional Requirements: As per AS 5 extra-ordinary items, incomes and expenses of ordinary items, prior period, items should be disclosed separately to show its effect on current profit. Any change in accounting policies which has material effect should also be disclosed separately in the financial statements.
4. Going Concern Concept (AAS 16): Auditing and Assurance Standard – 16 (issued by the ICAI) deals with the concept of Going concern. It is one of the fundamental Accounting Assumption. It is assumed that the enterprise has neither the intention nor the necessity of liquidation or of curtailing the scale of the operations. It refers to the intention and ability of the entity in near foreseeable future i.e. the next one year. Specific disclosure of the same is not required unless the assumption is not followed in the financial statements.

*** Auditor's Duty:**

1. The auditor should obtain sufficient audit evidence for deciding whether the entity is going concern.
2. He should review the events occurred after the Balance Sheet date having an effect on the Going Concern assumption e.g. earthquake, fire etc.
3. He should review the agreement relating to long term debts including debentures and see whether there is any breach of conditions.

4. He should analysis the latest interim financial statement cash flow statement, operating budget and profit forecast.
5. He should review the minutes of Board of Director shareholders and other committees.
6. The auditor should obtain legal opinion regarding the pending cases.
7. He should review the management’s future plans studying the plans to liquidate the assets, restricting the debts and further borrowing the money, cost reduction programmes, increase the ownership of equity etc.
8. He should obtain representation (management Certificate) in written form in respect of above matters.

* **Appropriateness:** When planning, performing audit procedures and evaluating the results the auditors should consider the appropriateness of the going concern consumption underlying the preparation of the financial statement. He should consider the risk that the concern consumption may not longer be appropriate. Some potential indicates of going concern problem .(as entity is not a going concern can be listed as under-

Indicates of absence of Going Concern: Following factors indicate that as entity Is not a going concern.

- a. Financial indicates like Negative net worth, working capital, cash flow positions, adverse key financial ratios, continuous operating losses, inability to pay the creditors and compromise with them etc.
- b. Operating indicates like loss of major market, major suppliers / customer, loss of key management personal without replacement etc.
- c. Other indicates like changes in Govt. policies, pending legal proceedings, non-compliances of statutory rules and regulation etc.

* **Auditor’s Report:** After considering management plan and other evidence the auditor will issue his report as under depending up on the appropriateness of going concern accounting concept.

1. Where the going concern assumption is appropriate auditor should issue unqualified report.
2. Where there were doubts regarding the going Concern assumption but the same were cleared due to management explanation the auditor should give an unqualified report provided adequate disclosure is made in Notes on Account stating –
 - (a) The conditions which affected the going concern.
 - (b) The steps taken by the management

The auditor should invite the attention of shareholders to these notes.

3. Where there were doubts regarding the going concern assumption and management explanation is not adequate auditor should issue qualified report stating reasons.
4. If the entity is not a going concern, the auditor should express as adverse opinion.

* **Classification of Audit:**

R. Robert Coomber has classified the audit on the following basis:

1. Classification on the basis Of authority	2. Based on scope	3. Based on time	4.
1) Statutory audit Balance sheet	1) complete audit	Continuous audit	
2) Non-statutory	2) Partial audit	Final audit	audit
3) Internal audit audit		Interim audit	Tax
		Concurrent audit	audit in depth

A. Classification on the basis of Authority:

1. Statutory audit: Statutory audit is conduced only by a qualified auditor i.e. CA and is compulsory under the provision of law. Appointment of auditor, remuneration, removal, duties

and rights etc are governed as per the provisions of the respective law applicable to the organization. Statutory audits are compulsory in the following cases:

- i. Companies registered under the companies Act 1956.
- ii. Banking companies governed by the Banking companies Act 1949.
- iii. Insurance companies governed by the respective Insurance Act.
- iv. Co-operative society under co-operative societies Act
- v. Public and charitable trust registered under concerned acts.
- vi. Local authorities government undertaking and dept.
- vii. all business org. having annual sales over Rs. 40 lakhs.

2. Non-statutory audit: It is a voluntary /optional/ not compulsory audit. There is no specific law for governing the conduct of such audit. Terms and conditions of audit are determined as per the agreement made between the auditor and the proprietor. For e.g. audit of individuals (Sole proprietor/ trader etc), firm, private trust etc.

3. Internal audit: An audit is said to be internal when the auditor is appointed by the proprietor / management of the company. In many cases the internal auditor is the regular of the company. An internal auditor is appointed to examine the books of accounts to review the present working and make valuable suggestions to improve it. All terms and conditions of audit work are determined by the agreement. The auditor submit his report to the management. The internal auditor is not completely independent. The scope of his duty can be controlled by the management. The objectives of interval audit varies from business to business. They area as follows:

- i. to verify the accuracy of the record
- ii. To ensure that the transactions have a proper authority
- iii. To facilitate detection and prevention of errors and frauds.
- iv. To ensure that purchase and sale of assets is authorized.
- v. to improve the system of internal check.
- vi. To make investigation for management.
- vii. To review the entire system of working and make it more effective.

B. Classification on the basis of scope:

1. Complete audit: Complete is one in which the auditor is required to check each every transaction recorded in the books of accounts. He has to examine each and every document, correspondence relating to transaction, voucher etc. This audit is not possible for large sized organization.

2. Partial audit: Partial audit is the audit in which the auditor its not required to examine all the books of accounts. Only some important transaction are scrutinized. This audit is not convenient when the audit is legally required. It cannot be followed in the case of statutory audit but may be followed in the case of non-statutory audit.

C. Classification based on time:

1. continuous audit: When the audit is carried out during the accounting period with some interval, it is called as continuous audit. According to R.C. Williams 'Continuous audit is one where the auditor or his staff is consistently engaged in checking the accounts during the whole period at regular or irregular intervals. This audit involves detailed examination of books of accounts. The auditor or his staff checks each and every transactions at regular or irregular intervals during the financial year. At the end of the financial year the auditor checks the P/L A/c and Balance Sheet. It is also called as 'each and every item audit continuous audit is applicable in the following business

- i. Where the volume of transaction is very large and complex.
- ii. where the system of internal check and internal control are not satisfactory.
- iii. Where the management requires monthly or quaterly audited statement of accounts.
- iv. When interim dividend is to be declared.

* Advantages of continuous audit:

1. Errors and frauds can be discovered easily and quickly as the auditor checks the account at regular interval and in detail.
2. the auditor remains more in touch with the business. He is in the position to know the technical details of the business, Hence he can make valuable suggestion to his client.
3. The final audited can be prepared and presented quickly after the close of the year.
4. As the auditor visits the client at regular intervals the official staff will be very regular in keeping the accounts up-to-date. They will see that there is no inaccuracy.
5. If the auditor pays surprise visit, it will have a considerable moral check on the client staff.
6. the auditor having more time can check the accounts in detail and his work will be more efficient
7. when company wants to declare an interim dividends the continuous audit will help in preparation of the interim accounts.

* **Disadvantages of continuous audit:**

1. Figures in the books of A/c which have already been checked by the auditor at his previous visit may be altered by a dishonest clerk.
2. It is an expensive system of audit.
3. The client staff may depend on the audit staff.
4. Extensive note taking may be necessary in order to avoid any alteration in the figures after the audit.

Final /completed/ Periodical / Annual audit: Final audit is one which starts after the completion of accounting year when the books of A/c are balanced and trading and P/L A/c and balance Sheet are prepared. Final audit is carried out continuously until it is completed. In case of final audit the auditor gets hold of all the books of A/c's and vouchers for the accounting period. The auditor visits his client only once the year and goes checking the A/c's until the audit work for the whole period is completed.

* **Advantages of Final audit:**

1. It is less expensive
2. No disturbance of routine work.
3. Proper planning of audit work is facilitated
4. Preparation of time-table for audit for the audit staff is made easy.
5. It is appropriate for smaller business concerns.
6. There are no changes of alternation of figures.

* **Disadvantages of final:**

1. Final audit is not convenient for large sized business organization.
2. It is difficult to detect frauds committed with proper planning.
3. It takes more time to complete the audit work and hence presentation of a/c's is delayed.
4. There is less moral force on the client staff because auditor visits his client only once a year.
5. It becomes difficult for the auditor to arrange the audit when many clients have the same financial year.

Interim Audit: Interim audit is one which is conducted between two annual, completed or final audit to final out the interim profit and know the financial position to declare an interim. It is a kind of audit which is conducted between two periodical or balance sheet auditors.

* **Advantages of Interim audit**

1. Interim audit is good where the publication of interim figures is necessary.
2. the final audit can be complete very soon if there has been an interim audit.
3. Errors frauds can be more quickly found and detected during the course of audit.
4. There is a moral check on the client staff as the a/c's are checked say after 3 or 6 months.
5. Interim audit is useful to find out interim profits which enable the company to declare an interim dividend.
6. It enables to keep up-to-date a/c's

*** Disadvantages of interim audit:**

1. Interim audit means additional work.
2. Figures may be altered in the books of A/c's have already been audited
3. It Is expensive
4. It will mean that the audit staff will have prepare detailed notes they complete interim audit.

Concurrent audit: Concurrent audit is an audit or verification of transactions or activities of an organization concurrently as the transactions / activity takes place. It is not a free audit. It helps to verify the authenticity of the transactions within the shortest possible time, after the same takes place It is similar to internal audit. If there are complex sities of economic activities, there must be system of someone other than the person involves in the operations, verifying the authenticity of the transactions on a regular basis so that any deviation can be noticed in the shortest possible time and remedial action can be taken.

This audit is accepted by public as well as private sector banks in recent years. The RBI has issued certain guidelines for the conduct of such audit. These guidelines are mandatory and all banks are required to cover 50% of total deposits and 50% of total advanced under this audit. The main object of concurrent audit is to ensure adherence to prescribed systems and procedures and timely detection of irregularities. Any bank officer or external auditor can be appointed as concurrent auditor. He has to report service irregularities to the head office.

*** Scope of concurrent audit:** The scope of concurrent audit includes the following:

1. Ensuring appropriate accounting of cash receipts and payments.
2. Checking daily cash transactions with special reference to abnormal receipts and payments
3. Verifying the purpose and sale of investment and it's authorization.
4. Verifying that advances are in accordance with the guidelines of central office (Head Office) and RBI.
5. Verification of stock declaration statement and timely reconciliation and confirmation of A/c's.

Other types of audit:

Balance Sheet audit /Limited audit:

Balance Sheet audit is an Americans term which means verification and valuation of Assets and Liabilities appearing in balance sheet. This audit is also recorded as limited audit. In this audit balance sheet a/c's are verified and the items in P/L A/c which are directly related to assets are checked e.g. Depreciation, repairs, bad debts etc. Balance Sheet audit involves an in depth examination of various items in the P/L A/c and Balance Sheet. The original entries and vouchers are examined only to the extent necessary. Balance Sheet auditor are not conducted in all cases but they are conduced in case of very large organization banks etc. in the different circumstances. The Balance Sheet audit is suitable under the following circumstances:

- i. Where the volume of transactions is very large.
- ii. Where the internal check and internal control system is very effective.
- iii. Where the business concern has its own internal department. The statutory auditor therefore need not duplicate this work.
- iv. Where mechanized system of accounting is in operation. The A/c's staff is highly qualified, the management is professional and the A/c's are computerized.

*** Procedure to conduct balance sheet audit:**

1. The auditor should examine the minute book of the concern, specially those items which have a bearing on accounts.
2. He should examine and compare the P/L A/c with that of previous year to see whether there is any material difference between two.
3. He should compare the increase or decrease in the expenditure between two periods with the turnover, adjustments regarding allowances, sales tax etc.
4. He should investigate into the case of any variation in gross profit and pay attention to the valuation of closing stock.
5. He should see the change in the rate of depreciation charged during the current year.
6. He should investigate into the items of non-recurring in nature i.e. profit or loss on sale of assets.
7. He should pay attention to any substantial change in the fixed assets regarding it's valuation.
8. Any variation in the current assets, pre payments and the accruals should be enquired into.
9. He should verify the assets held and liabilities owing
10. The auditor should see that the system of internal control is effective and qualified staff is appointed He should see that adequate provision is made for all the liabilities.
11. He should see whether the presentation of financial statements is done properly as per the provision of law.

The auditor should check the statement of sources and application of funds.

Tax audit

It is the audit done for accessing the correctness of calculation of taxable income/ profit. It is done to ensure compliance with the provision of Income Tax Act 1961. This act has made tax audit compulsory for specific persons U/s 44 AB.

Audit in depth: According to Taylor and Perry 'Auditing in depth is the examination of system applied within a business concern following the tracing of certain transaction from their origin their conclusion, investigating at each stage the records created and their appropriate authorization' Audit in depth doesn't mean 100% checking. It is a detailed examination of selected transactions from the beginning to the end. Under this audit all records and documents pertaining to the transaction are checked in detail. The basic purpose of this audit is to see whether the system of internal check or internal control is effective. Auditing in depth is applicable in the case of large sized companies. It is not suitable to small sized companies as they do not have internal check system. This audit enables the auditor to suggest to the management better procedure for recording the transactions to avoid frauds for e.g. the item purchases will be examined as follows:

- i. Requisition from the stores departmental to the purchase departmental for the purchase of material.
- ii. Invitation for quotation / secret price tenders from various suppliers.
- iii. Selection of suppliers
- iv. Copy of order placed.
- v. Copy of the chalan for the materials received
- vi. Entry in goods inward register
- vii. Material received report from stores department
- viii. Entry of the receipt in stock register
- ix. Original invoice received from the suppliers.
- x. Entry in the purchase register.
- xi. Evidence for cheque issued to suppliers.
- xii. Receipts for payment made to the suppliers
- xiii. Relevant posting in supplied A/c etc.

Internal Auditor	Statutory Auditor
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1. Compulsory / Voluntary	
Internal audit is voluntary	Statutory External audit is compulsory under law i.e. companies Act.
2. Appointment	
Internal auditor is appointed by management itself.	Statutory auditor is appointed by the shareholders of the company
3. Status / position	
Internal auditor is the employee of the concern	Statutory auditor is an independent outside expert
4. Objective	
Internal audit aims to review the internal control system of the concern	It aims to report to shareholders whether the accounts are true and fair.
5. Period	
Internal audit is continuous	Statutory audit is normally periodical or annual
6. Qualifications	
No qualifications are prescribed by law for an internal auditor	Qualifications are prescribed by law.
6. Responsible and Report to	
Internal auditor is responsible and report to management	Statutory auditor is responsible and reports to shareholders
7. Scope of duties	
Management decides the scope of duties of internal auditor is includes non accounting matters.	Duties of statutory auditors are laid down by law i.e. companies Act 1956 and its scope ltd. to according matter
8. Removal	
Internal auditor can be removed by management on its own	Statutory auditor can be removed by shareholders only if approved by the central Government

* Difference between:-

Audit of Partnership firm		Audit of limited company	
1. Statutory Requirement			
Audit of Partnership firm is not required compulsorily under any act. However it obligatory under the can be done voluntarily		Audit of limited company is compulsory and obligatory under the companies Act 1956	
2. Appointment			
Though the audit is compulsory not required partners can appoint auditor voluntarily		Shareholders of the company appoint the auditors.	
3. qualification			
Partnership act doesn't provide for any qualification However it can be prescribed in partnership deed.		Auditor of a company must be practicing CA	
4. Scope of audit			
Scope of Audit depends on the arrangement between the auditor and the partners		Scope of Audit is defined under the companies Act 1956	
5. Rights, duties, Power and Responsibilities			
Rights, duties etc are defined by the agreement between the auditor and the partners as per the letter of appointment. They		Rights, duties etc are prescribed under the companies Act 1956 and cannot be varied (changed)	

are contractual and can vary from firm to firm and also from year to year	
5. Report	
The form of report is not prescribed However the auditor should report to the partners.	The form of report is prescribed under companies Act 1956. The auditors should report to the shareholders.

***Pre-commencement Considerations:**

Audit is the examination of each and every item of P/L A/c and Balance Sheet with the help of accounting entries and various record so that an auditor can form an opinion about the state of affairs. The auditor should give important instruction to his audit staff and his client. Before commencing the audit work he should take the following steps.

1. The auditor should decide the type of audit: i.e. statutory, voluntary, continuous, final etc. The audit must be conducted as per the provisions of company's act 1956 if it is statutory audit.
2. Hr should review the various agreement in order to decide the future course of action.
3. In the case of company he has to see that his appointment is in order. He should inform to the company registrar.
4. He must known who has appointed him and to whom the report should be made. He should ascertain from whom fees are to be recovered.
5. He must ascertain the scope of his duties and responsibilities from the relevant law and agreement
6. the auditor should ascertain the period for which audit is to be conducted. Normally the period is one year but it may be less or more than one year in specific purpose.
7. He should check whether he can use the client staff as per the agreement for conducting the audit work.
8. the auditor must be certain about the place of work. He should arrange with the client for supply of working conditions necessary for audit work.
9. He should known the nature of business e.g. law applicable, accounting problems, closed branches, typical points regarding accounts and audit, accounting system, scope of audit etc.
10. The auditor should collect and study various documents. E.g. letter of appointment, organizations chart, list of directors, partners and officers, list of books of accounts etc.
11. He should study the last year's financial statement and auditors report to get good idea.
12. The auditor should known the basic accounting postulates which helps to conduct audit properly.
13. He should investigate the internal checking and internal control system.
14. He should prepare audit programme so that the audit can be completed according to generally accepted auditing standard.
15. The auditor should distribute work among senior and junior assistant so that audit work can be completed in time.
16. He should give instruction to the client such as balancing of ledger accounts, posting, preparation of trial balance, final statement and bank reconciliation statement etc.

*** Audit procedures (Post commencement considerations):**

Audit procedures means the step taken by the auditor to obtain evidences. According to AAS – 5 audit procedure can be broadly classified into compliance procedures and substantive procedure

A. Compliance Procedures: These are the steps taken to obtain evidence regarding control. The auditor has to see that the internal control exists, their effective and actually in operation. He checks and examines a few selected transactions in detail to see that the internal control is effective.

B. Substantive Procedures: These are the steps taken by the auditor to obtain the evidence regarding the transactions during the year and the assets and liability at the end of the year. These procedures are designed to obtain evidence as to the completeness accuracy and validity of the

data produced by the accounting system. In this regard the following procedures are used by the auditor during an audit.

1. Checking of opening balances
2. Vouching
3. Posting Checking
4. Casting checking
5. Ledgers scrutiny
6. Tracing of ledger balances to trial balance
7. Verification of assets and liabilities
8. Grouping disclosure and presentation in final A/c

Audit Programme:

An audit programme is a detail plan of applying the audit procedures in the given circumstances for the purpose of conducting an audit.

Meaning/ Definition:

1. According to Prof. Meigs: An audit programme is the detail plan of audit work to be performed, specifying the procedures to be followed in the verification of each item in the financial statement and giving the estimated time required.
2. According to Stettler: an audit programme is an outline of all procedure to be followed in order to arrive at an opinion concerning clients financial statement. Audit programme is prepared by the chief auditor before the commencement of an audit. It is also called as the blue print of audit work. It is detailed time table of audit work which specifies which audit work is to be done by whom and how and in what time. It allocates duties and responsibilities to audit staff. It contains instruction, hints and serve as a guidance for the audit staff. In short, audit programme is a plan according to which the audit work will be distributed and delegated among various junior and senior members of the staff according to their qualifications and experience.

* **Contents of an audit programme:** contents of audit programme depends on the nature of the business. An audit programme contains the following information.

1. Name and object of the client / undertaking/ company
2. Accounting year.
3. Date of commencement of audit and duration of audit
4. system of accounting, internal check and internal control
5. Previous years accounts with the report of the auditors.
6. Allocation and distribution of work among audit staff.
7. Outline of various books of accounts to be examined.
8. Types and no. of transactions to be selected.
9. Vouching of sales book, purchase book, cash book, journal etc.
10. Ledgers scrutiny (reading of ledger)
11. bank Reconciliation statement
12. Persons in charge of audit work
13. Date wise schedule of work to be carried for e.g. review of transactions, checking of evidences, preparation of audit reports etc.

* **Advantages of audit programme:**

1. It provides clear cut instruction to the audit staff
2. Auditor can find out the extent of work done and work to be done.
3. It becomes easy to select the assistance for carrying out the audit work and simplifies the allocation of work.
4. Responsibility of each member can be fixed.
5. It facilitates systematic auditing.
6. the chief auditor can control the audit work effectively.
7. audit programme of one year will help and guide while preparing audit programme of subsequent years.

8. It serves as an evidence in the court of law in the case of any change of neglation against the auditor.
9. It helps the auditor to draft the report properly
10. Efficiency of the audit assistant increases as they know their duties clearly.
11. It sawes time because routine is determined in advance.
12. Responsibility for any mistake or neglation on the part of the clerk can be clearly laid down.
13. due to systematic working they may get more clients.

*** Disadvantages of audit programme:**

1. The audit work becomes mechanical which in initiative of the audit staff. It affects the efficiencies of staff.
2. Work becomes rigid.
3. Audit programme is not required for small concern as the number of transaction are very less.
4. The programme may not cover all aspect of the organization.
5. Inefficient audit assistance may take shelter behind the programme.
6. audit staff has to work according to programme only
7. He has no opportunity to show his judgement and intelligence.
8. It can not be applied uniformly to all the units.
9. audit programme cannot reveal quality of evidence. It shows only the quantity of work.

***Development of an audit Programme:**

The auditor should consider the following factors while developing (preparing) audit programme:

- 1) Client's business /activities: the nature of activities of the client should be considered while designing the audit programme. The focus of audit is on different matters depending up on the type of company and type of audit to be conduced. For Exam, the audit of a manufacturing company is different from the audit of bank or co-operative credit society.
- 2) Internal control: The effectiveness of internal control system should be considered by the auditor. If the internal control system is strong, the auditor may go for test checking. Where the internal control system is weak or not existing, the auditor can decide to do detailed examination.
- 3) Cost benefits: the auditor should consider the cost of performing the procedure and the benefits likely to accrue. He should select the audit procedure which is less costly.
- 4) Terms of engagement: the auditor should keep in mind the terms of his engagement. For Exam. If is only a partial audit where the auditor is asked to verify only cash transactions his audit programme should cover audit of only cash receipts and cash payments.
- 5) Nature of evidence: audit programme contains procedures and techniques to collect evidence. The auditor should determine the evidence reasonably available and identify the best evidence. For Exam, in case of purchase of motor vehicle, the purchase bill is not sufficient evidence but entry in R.C. book issued by R.T.O and in insurance policy can be considered as the best evidence that the vehicle is owned by the client.
- 6) Possibility of errors and frauds: the auditor must take into account all possibilities of errors and frauds. If there is a possibility of errors and frauds, there should be 100% checking. For exam. Full checking of extra-ordinary transactions.
- 7) Co-ordination: the audit programme should be drawn in such a manner that the procedures are coordinated.
- 8) Involvement of other auditors and experts: If there are joint auditors, branch auditor internal auditor or other experts then the auditor should consider to what extent he can rely on them.
- 9) Assistants available: The auditor should keep in mind the number of assistants available and their level of competence. He should routine checking work to junior and ledger scrutiny to senior assistants.
- 10) Time available: the auditor should consider the time during which he has to complete the audit and submit the audit report. Accordingly he should plan his audit work by allocating time for every work. In short, the audit programmer should be time bound.

11) Verification of assets and liabilities: Auditing programme should consider those steps and procedures which are useful accomplishment of the verification of assets and liabilities.

Overall audit Approach

While conducting audit auditor's overall approach should be to achieve the object of audit i.e. to satisfy himself that the financial statement (balance sheet and profit & loss A/c) reflects a true and fair view of the state of affairs of the company. His overall audit approach should be to ensure that

- 1) All the assets and liabilities are properly verified. They are properly classified grouped and shown in the balance sheet as the legal requirements and their valuation is also proper.
- 2) Expenses and incomes for the year are properly classified and disclosed. The concept of matching the cost with revenue is properly followed and revenue is recognized as per the provision of law and the accounting standards.
- 3) Statutory provision, rules, regulations and guidelines issued by the ICAI are complied with by the final accounts.
- 4) All the methods are consistently followed and if there is change in the method, the effect of such is properly disclosed in the books of accounts.
- 5) There is no materials omission / misstatement in the financial statement.
- 6) Financial statement audited by the auditor are free from any errors or frauds.

*Audit Working papers:

audit working papers are those papers which are prepared during the course of the audit. They are the written records kept by the auditor as regard evidences accumulated during the course of audit. According to ICI audit working papers mean a record of

- A the audit plan
- B The audit procedures performed
- C the conclusions drawn from evidence obtained

These papers contain information about imp facts and explanation of working notes in connection with the accounts under audit. Normal information contained in the working papers as follows.

1. Trial balance
2. Schedule of fixed assets and depreciation
3. Schedule of investments, fixed deposits, Debtors, Creditors, Advances etc.
4. Bank Reconciliation
5. Correspondence between auditor and the outsider
6. Details regarding valuation of stock
7. Statement of closing stock and it's valuation
8. Extracts from minutes book and important agreement
9. audit programme
10. Verification of Cash etc.

* Characteristic of good working papers

1. Good Design and good layout of working papers will bring uniformity and consistency
2. Proper and relevant details should be maintained volumes of file should not be increased unnecessarily.
3. there must be clarity of thoughts and expressions in all details.
4. Working papers must be agreed
5. Complete information of necessary details should be maintained.
6. Unless the details are legibly and neatly maintained they will not be useful

The working papers belong to the auditor because the are independent contractors and not the agent of the client.

* Filing of working papers:

Working papers are valuable documents for the client as well as for the auditor. Hence they should be filed systematically and preserved in proper manner working papers may be divided between correct and permanent files as follows:-

1. Current Audit file (Temporary audit File)

Current contains working papers of the year under audit. It should include the following details

Letter of appointment:

Documents obtained from client i.e list of authorized

Audit plan and audit programme

Details of audit test performed i.e. vouching, verification etc.

Queries raised during the course of audit and official comments on the queries

Extracts of review and supervision of work of the assistance.

Confirmation letters from banks, money lenders other parties

Certificate from management regarding valuation of closing stock, current assets and verification of fixed assets etc.

Trial balance schedule final accounts

Bank Reconciliation Statement

Statement showing calculation of tax bonus and gratuity etc.

2. Permanent audit File:

Permanent audit file contains papers of continuing importance affecting the company and the audit. This file provides background info. About the company. It should include the following details.

Memorandum and Articles of Association of the company, a copy of partnership deed and trust deed.

A brief note on internal control system, description of accounting policies and systems.

A list of books of accounts.

A statement of basis of stock valuation or method of stock valuation, WIP and depreciation.

Copies of audited accounts of earlier years and the communication with the previous auditor

Clients letter containing specific instructions regarding the audit work.

Details of holding and subsidiary com

Notes on discussion with the clients in respect of – nature of business, management and org. org.

Chart, applicable laws, rules and regulations, financial and accounting problems.

Analysis of ratio, trends in earlier years

A list of directors with their details regarding their association with the company's as directors.

Audit Notebook:

The term audit working papers and audit notebooks are similar. At time however the term audit notebook is used to indicate only the current audit file containing points pertaining to the current audit notebooks is a systematic record of the day to day work performed by the audit staff on any particulars queries of various accounting records.

*** Audit notebook contains the following the following information**

A General information

1. Name of the client and the audit
2. List of books of accounts in use
3. List of statutory registers important agreements etc.
4. System of accounts and internal checks
5. Important officers, their duties and responsibilities
6. Technical details necessary for audits, mistakes and errors noticed during the course of audit.
7. Date of commencement and completion of audit
8. Bank Reconciliation statement
9. Irregularity observed
10. Points to be included in audit report
11. Any item which require discussion with the senior officers etc.

B Current information:

1. Audit queries not clear immediately e.g. missing receipts vouchers etc.
2. Mistake or irregularities observed. For e.g. failure to comply with the requirements of company act or provisions of M/A or A/A failure to provide adequate dep
3. Unsatisfactory book keeping
4. Special points requiring consideration at the time of verification of final a/c
5. Important matters for future reference etc.

*** Important of audit notebook:**

Audit notebook forms an important part of the documentation for the auditor. The following points indicate the usefulness of audit notebooks

1. Evidence value: It has no evidence value in case a suit file is against the auditor for negligence. Such

Notebook will be documentary evidence in favour of the auditor.

2. Subsequent audit value: The clear, complete and concise audit notebook can be useful guide to the clerk to audit the accounts of the same company, next year.

3. Planning value: It is useful document in planning the next audit of the company. It is also useful in preparing the next audit programme as it shows the weakness.

4. Protection value: The audit notebook is a comprehensive record of work done and the audit observation. Hence it is extremely valuable to the auditors as a document of defence when a charge is brought against him.

5. Control value: It has also controlled value as it will show the extent and coverage of work done when the assistance are shifted or when there is temporary stoppage of work.

6. audit process value: the audit notebook provides new in the manner extend and timing of audit checking

7. Report finalization value: Audit notebook Is the primary basic document in preparing the audit report on true and fair view of the financial statement.

Auditing Techniques & Internal Introduction

Audit Techniques:

These are the techniques by which an auditor obtain evidence about the transactions record in the books of accounts. Audit techniques stand for the methods for carrying out the audit procedures. For collection and accumulation of audit evidence. Certain methods and means are available known as audit techniques. Important techniques of auditing as given by SAPS (Standard Auditing Practices) are given as follows:

1. Inspection: It consists of examination of records, documents and tangible assets. The auditor to examine large number of documents in the course of audit because most of the transactions are supported by documents. They are examined with reference to authenticity appropriateness, authorisation and proper recording which imply genuineness and proper approval of the transaction. From the view point of reliability documentary evidence is classified into 4 categories.

- a. Evidence originating from and held by the concern
- b. Evidence originating from and held by the 3rd party
- c. Evidence originating from 3rd party and held by the concern.
- d. Evidence originating from the entity and held by the 3rd party.

2. Observation: It implies witnessing a process or procedure which is performed by others. For e.g. the auditor may observe stock taking done by the staff.

3. Enquiry and confirmation: The auditor may make enquiry by asking oral question to the concerned persons. He may prepare questions and send it to the right person with the request to

complete the same and send by to the creditors. Confirmation consist of response to as enquiry For e.g. the organization may get confirmation from debtors and creditors.

4. Computation: It refers to checking the arithmetical accuracy of the transactions recorded in the books of A/c's. The auditor may follow the same procedures as followed by the accountant to verify arithmetical accuracy.

5. Analytical review: It implies studying important ratios and trends and investigation into the unusual fluctuation. The auditor can scan various unusual transactions and examine them thearily. He can co-relate various figures in order to established financial soundness in auditing of financial statement.

* Principles of Audit	Techniques of audit
1. principle of audit is defined as a fundamental truth a primary or basic law, a settled rule of action.	For accumulation and collection of audit evidence, certain methods and means are available known as audit techniques.
2. Audit principles guide an auditor as to how to conduct an audit and give an audit report.	Audit techniques means methods used to obtain audit evidence.
3. Principles of audit are necessary for a	Techniques of audit Is for obtaining the transaction recorded in the books of A/c
4. Principles are of fundamental nature, and do not change frequently	Techniques may change depending on circumstances for e.g. techniques for verification of cash is different from verification of debtors.

* **Internal check:** Internal check is one of the mode of executing internal control. Internal check is the method of organizing the accounts system of the business concern in such a way that the work of one person is automatically checked by another.

* **Meaning /Defination:**

1. According to Prof. L.R. Dicksee: Internal check is such as arrangement of bookkeeping routine that errors and frauds are likely to be discovered and prevented by the very operation of the bookkeeping itself.

2. According to De Paul : Internal check means practically a continuous internal audit carried on by the staff itself by means of which the work of each individuals is independently checked by the other members of the staff..

* **Object of Internal Check:**

1. To eliminate the acts of errors and frauds.
2. To fix up responsibility of each person.
3. To prevent misappropriation of goods and cash.
4. To detect errors and frauds immediately
5. To exercise moral in fluence on the staff
6. To expedite the work of employees.
7. To simplify the work of auditor.
8. To increase the efficiency of employees.

* **Auditor duties in respect of internal check:** the auditor may depend on test check if there is a good system of internal check in the organization. He should apply a few test checks. He select the representative transactions. During the course of examination, if he across any mistake, he should go into the details of it.

SAP 6 has made the following recommendation in this regard:

1. Responsibility of management: Basically, the management is responsible for establishment and operation of internal check system
2. Reliability: He should verify the reliability of the internal check system.
3. Evaluation: The auditor should evaluate the system to ensure that the system prevents errors and frauds. It ensures that all the transactions are properly recorded. For proper evaluation the auditor should take the following steps.
 - a. Undertaking the system: The auditor should get full knowledge of the system by having discussions with managers and by studying the managers.
 - b. Test application: He should verify whether internal checks were applied in practice. He can verify some transactions in debt.
 - c. Evaluating the system: He should judge on the basis of above test whether he can rely on the internal check and if so to what extent.
4. Reporting: Under the company Act (MAOCARO 19880), the auditor has to report on the following internal checks
 - a. whether the service company has a reasonable system of recording receipts, issues and consumption of materials and allocation of materials consumed to the relative jobs.
 - b. Whether a service company has a reasonable system of allocating man hours utilized to the relative jobs
 - c. Whether there is a reasonable system of authorisation of proper levels on issue of stores (materials) and allocation of stores and labours to jobs.

*** Test checking:** Auditor basic is to judge the quality of the final accounts. He has to judge whether the accounts are true and fair. For this purpose, he has to obtain audit evidence. He can obtain maximum audit evidence by vouching of all transactions and by verifying all assets and liabilities. However such 100% checking is neither possible nor necessary. He can select only few sample transactions and assets for vouching and verifications. Such test checks enables an auditor to judge whether the remaining entries are correct or not and can form an opinion about the entries class of transactions and balances.

***Meaning / Defination:**

1. According to Prof Meigs: Test checking means to select and examine a representative sample from a large number of similar items.
2. According to international Auditing guideline 90 on audit sampling.
Test checking or audit sampling means checking less than 100% of the items within an accounts, balance or class of transaction. It enables the auditor to obtain and evaluate evidence and form an opinion about such balances or transactions as a whole.
3. According to ICAI: ICAI states that if forming an opinion an auditor may obtain audit evidences on a selective basis. When items are selected and checked on the basic of personal judgment of the auditor it is called test checking, and when they are selected by applying statistical technique of sampling, random selection etc it is called statistical sampling.

Test checking is not a complete or full checking

*** Need /Importance of Test Checking:**

1. Full checking impossible: when the number of transactions Is large the auditor cannot check all the transactions 100% I is physically impossible to check all the transaction For e.g. Payments made by the bank during the accounting year.
2. Full checking unnecessarily: In most cases routine and mechanical. Test checking allows an auditor to concentrate important arrears of audit.

*** Advantages of Test checking:**

1. The volume of work is reduced and the time is considerably saved.
2. The scope and areas of test checking can be greatly extended.

3. Sometimes audit cannot be completed in time due to shortage of time. Under such circumstances the work can be completed if test checking is applied.
4. Test checking can be quite effective and can serve as the purpose if it is done properly and carefully.
5. There is a moral check on the client staff.

*** Disadvantages/ Limitations of test checking:**

1. an auditor doesn't audit completely. Some of the errors and frauds may remain undetected.
2. Client staff becomes careless because they know that their work will not be checked in detail by the auditor.

*** Precaution to be taken while applying test checking:**

1. Care should be taken to see that all types entries are selected for checking.
2. No book of account should be left out fully unchecked.
3. Entries of every description should be checked
4. Selection of entries should be done on random basis.
5. Periods and entries selected for test check should be different at each audit and they should not be known to the clients in advance.
6. As far as possible a large number of entries of the first month and last month should be checked
7. Test check should not be applied for cash transaction. All the cash transactions should be checked.
8. Items of exceptional and recurring in nature should be checked fully.
9. The auditor should change the method of test checking
10. The methods should be kept secret

*** Consideration in introduction of internal check:** The following aspects must be considered while introducing effective system of internal check internal on various transactions

1. No independent control: Independent control of any aspect of a transaction shall not be entrusted to any one person alone
2. Automatic check/ control: duties working of each employee should be so arranged that the work of one is automatically checked by another person.
3. Reshuffling of duties: there need to be frequent reshuffling of duties without disturbing the efficiencies
4. No work for a long period: No person should be entrusted with the particular work for a long period. The duties of the employees should be changed from time to time. This is a must in case of employee's handling cash, stock etc to prevent misuse and frauds.
5. No access to books: All employees should not have access to books of accounts.
6. Physical verification: Accounts should be physically verified and periodically intervals.
7. Budgetary control: Budgetary control estimates may be prepared carefully and the actual may be compared with the same to ascertain the deviation and the reasons.
8. Physical stock taking: The valuation and Physical stock taking work shall be interested to the employees from different department
9. Review of accounting procedures: Accounting procedures should be reviewed periodically and evaluate their effectiveness and adequacy.
10. Mechanical devices: Mechanical devices where possible should be used e.g. automatic cash register will help to prevent misappropriation of cash.
11. Clear Definition of duties: duties of each member should be defined clearly
12. Proper record keeping: All the books, vouchers and documents should be classified, filed linked together so as to facilitate easy reference.
13. Simplicity: the clerical labour involved should be reduced to a minimum. The should be simple and effective.

14. Annual leave: Every member should be encouraged to go on leave at least once a year. Frauds to light during such leave period.
15. Accounting policies: A transaction should be recorded on the basis of accounting policies followed by the managers.
16. Complete and accurate: All the records should be always complete and accurate.
17. Authority levels: There must be clear cut authority levels for

* **Routine checking:** Routine checking always involves following 4 function

1. checking totals, sub-totals, costing, carry forwards brought forwards in the books of prime entry
2. Checking of posting from prime entry book into ledger
3. Checking of totals and balancing of ledger accounts
4. Checking of balances of ledgers in to trial balance

* **Advantages of routine checking:**

1. It will bring out the clerical errors of common nature.
2. Arithmetical accuracy of book of accounts is verified.
3. Routine checking can help in tallying the trial balance as arithmetical accuracy is verified.
4. Routine checking can be entrusted to junior staff. The time of senior staff is not wasted on it.

* **Disadvantages/ Limitations of routine checking:**

1. Routine checking becomes mechanical process.
2. Staff engaged in such routine may get bored because of continuous activities.
3. High levels of frauds and irregularities may not come to light.
4. Compensating errors and errors of principles may not come to light.

* **Internal Control:** where internal control is good, the recording of fictitious transactions would be less. Chances of frauds in accounts or in documents would also be minimum. On the other hand where is no system of internal control or such system is not adequate, the chances of errors and frauds are more. Under such circumstances the auditor will have to do the audit more in details. He will try to verify more evidences and supporting data.

* **Meaning/ Definition:**

1. According to ICI (SAP 6): "Internal control is the plan of organization and all the methods and procedures adopted by the management of a concern to ensure the orderly and efficient conduct of it's business"
2. According to American Institute of certified Public Accountants: "Internal control is the of organization and all the co-ordinate methods and measures adopted within a business to safeguard its assets check the accuracy and reliability of its atcing data, promote operational efficiency and encourage addivous to prescribed managerial policies"

* **Objectives of internal control:**

1. Aroid inefficiency in business
2. To prevent frauds
3. Transactions are executed in accordance with managements general or specific authorisation
4. to increase accuracy and reliability in all the aspects of the business.
5. to measures the effectiveness of business policies
6. All transactions are promptly recorded in the correct amount in the appropriate account and correct accounting periods.
7. to safeguard the asset of the organization by avoiding wastages.
8. to evaluate performance of the employees
9. the recorded assets are compared with the existing assets at reasonable intervals and appropriate action is taken with regard to any differences.

*** Auditors duties in respect of internal control:** The management of the organization is responsible for installation of internal control system for the various purposes. An auditor is entitled to rely on the system implemented by the management. The auditors duties in relation to internal control are as follows – SAP 6 has made the following recommendation in this regard.

1. Basically the management is responsible for establishing and operating the internal control system.
2. An auditor should study and evaluate the system to ascertain how much he can rely up on it.
3. an auditor needs to evaluate the system for establishing reliability of internal control so that he can show that all transactions are authorized, a/cing policies of management are actually followed, the books of A/c's are complete accurate and free from errors and frauds etc.
4. Study of internal control helps the auditor to decide what to check, when to check, how to check and how much to check. If IC are reliable he can use
5. He should collect information about the test check financial powers of the various departmental head.
6. He should study the mechanical devices in use.
7. He should see the limits of inspection over financial and other matter.
8. He should bring to the notice of the management the shortcomings in the system and suggest measures for improvement.
9. He should review the present system of internal control by applying a few test.

*** Difference between:**

Internal Check	Internal audit	Internal Control
1. Meaning		
It is an arrangement of duties in such a way that work of one employee is checked by work of another	It is a review of operations & records by a special staff	It is a plan of the org. to safeguard its assets, check accuracy
2. Objective		
To prevent errors and frauds	To review the operations and records of the organizations.	To promote operational efficiency
3. Relationship		
It is a part of internal control	It is a part of internal control	It includes internal check and internal audit
4. Implementation of checks		
It is automatic and continuous	It is done by internal auditor	It includes implementation of internal check and internal audit
5. Nature of checks		
It is objectives	It is subjective	It includes internal check and internal audit
6. Scope for suggestions		
There is no scope for suggestions	There is a scope for suggestions	It includes both internal check and internal audit

*** Internal audit:**

Meaning/ Definition:

1. According to Prof. Meigs: Internal Auditing is a continuous critical review of financial and other operating activities by the staff of auditors functioning as full time salaried employees

2. According to AAS – 7 issued by: Internal Audit is a separate component of internal control established to determine whether other internal controls are well designed and properly operated.

Thus internal Audit is

- a. Normally done by the employees of the concern
- b. A part of the internal control system
- c. A critical review of other internal controls (i.e. accounting controls and operational controls)
- d. A kind of continuous audit

* **Objectives of internal audit:** the scope and objective of internal audit are as follows:

1. to verify the accuracy, reliability and authenticity of the accounting records, statistical records and the system established by the management.

To ascertain that the standard accounting policies and practices established by the management are being followed properly and effectively

2. To confirm that the acquisition used and disposal of assets are according to the pre-determined procedures and system.

3. To confirm that the liabilities are incurred only for the legitimate activities of the company

4. Analyses the improve existing procedures and the system of internal check and see that eh system are effective economical and strictly followed.

6. to facilitate detection and prevention of errors and frauds.

7. to carry our special investigation for the management.

8. to undertake physical examination and verification of assets of the organization. To review the operation of the overall internal control system and to bring to the notice of the management the material departures and non-compliance and make meaningful suggestions for better internal control.

* **Usefulness of internal audit:**

1. Useful for management: Internal audit is useful for the management to ensure that:

- a. Accounting and alive records have been properly maintained
- b. The assets of the concern have been properly safeguarded and
- c. the policies and procedures laid down by the management have been complied with

Now a days internal audit is viewed assessential management tool for the efficient running of the business. The scope of internal audit has expanded which included management audit, operational audit, efficiently audit, performance audit, social audit etc. while financial audits are concerned with financial aspects of transactions other audits deal with non-financial aspects such as managerial, operational, efficiency, performance etc. Internal audit helps in early detection and prevention of errors and frauds. As a tool of management such internal audit is expected report on the “quality of management”.

2. useful for statutory auditor: Internal auditor report is useful for the statutory auditor. Much of the work of the internal auditor may be useful to the external auditor in determining the nature, timing and extent of his procedures statutory auditor evaluates internal audit systems and decides how much he can rely on the audit done by the internal auditor.

* **Audit sampling:**

AUDITING (OBJECTIVES)

CHP 1

Q.1 MULTIPLE CHOICE QUESTIONS:

1. Financial statements need to be prepared in accordance with **All the above**.
 - (a) Relevant statutory requirements
 - (b) Accounting standards issued by the Institute of Chartered Accountants of India.
 - (c) Guidance Notes issued by the Institute of Chartered Accountants of India
 - (d) All the above.

2. Objective of an audit of financial is to enable the auditor to express an opinion **Whether the financial statements are prepared in accordance with an identified financial reporting framework**
 - (a) Whether the financial statements are prepared in accordance with the system of double entry book-keeping

3. If the financial statements are prepared as per the financial reporting framework the auditor gives an opinion that the financial statements. **Give “a true and fair view”**
 - (a) Are true and correct
 - (b) Are correct and fair
 - (c) Give a true and fair view
 - (d) Are reliable

4. The term “General Purpose financial Statements” never includes – **Statement by Chairman**.
 - (a) A cash flow statement
 - (b) Statements and explanatory notes which form part there of
 - (c) Statement by Chairman
 - (d) Supplementary schedules and information based on such statements.

5. Which of the following errors is an error of omission? **The total of the sales journal has not been posted to the Sales Account**
 - (a) Sale of Rs. 500 was written in the purchase journal
 - (b) Wages paid to Mohan have been debited to his account.

- (c) The total of the sales journal has not posted to the Sales Account
(d) None of these.
6. Which of the following errors is an error of principle? **Purchase of Rs. 2,000 has been entered in the sales journal**
(a) Rs. 600 received from Ganpat has been debited to his account
(b) Purchase of Rs. 2,000 has been entered in the sales journal
(c) Repairs to building have been debited to Building Account.
(d) None of these.
7. Errors of recording to not allow **None of these.**
(a) Correct totaling of the Balance Sheet
(b) Correct totaling of the Trial Balance
(c) The Trial Balance to agree
(d) None of these.
8. Which of the following errors will affect the Trial Balance? **The total of purchases journal is Rs. 2,000 short**
(a) Repairs to building have been debited to builders
(b) The total of purchases journal is Rs. 2,000 short
(c) Freight paid on new machinery has been debited to the Freight Account
(d) None of these.
9. Which of the following errors will not affect the Trial Balance? **Writing an amount in the wrong And account but no the correct side.**
(a) Wrong balancing of an account
(b) Writing an amount in the wrong account but on the correct side
(c) Wrong totaling of an account
(d) None of these
10. The total of Sales Book was not posted to the ledger. This is **>there were all in their own**
(a) Error of Omission (b) Error of Commission
(c) Error of Principle (d) None of the above
11. Sales Book was overcast by Rs. 500. This is **Error of Commission.**
(a) Error of Omission (b) Error of Commission
(c) Error of Principle (d) None of the above
12. The total of a folio in the Sales Book Rs. 1,000 was carried forward as Rs. 100. This is **Error of Commission.**
(a) Error of Omission (b) Error of Commission
(c) Error of Principle (d) None of the above
13. Sales to Ram Rs. 143 posted to his account as Rs. 134. This is **Error of Commission.**
(a) Error of Omission (b) Error of Commission
(c) Error of Principle (d) None of the above
14. Sales to Meena Rs. 143 posted to Meenu as Rs. 143. This is **Error of Commission.**
(a) Error of Omission (b) Error of Commission

- (c) Error of Principle (d) None of the above
15. Goods of the value of Rs. 376 were returned by Ram and were taken into stock on the same date but no entry was made in the books. This is **Error of Omission.**
 (a) Error of Omission (b) Error of Commission
 (c) Error of Principle (d) None of the above
16. A credit sale wrongly passed through the purchases book. This is **Error of Commission.**
 (a) Error of Omission (b) Error of Commission
 (c) Error of Principle (d) None of the above
17. Repairs of newly purchased second-hand machinery debited to Repairs Expenses Account. This is **Error of Principle.**
 (a) Error of Omission (b) Error of Commission
 (c) Error of Principle (d) None of the above
18. Repairs to Machinery had been charged to Machinery A/c. This is **Error of Principles.**
 (a) Error of Omission (b) Error of Commission
 (c) Error of Principle (d) None of the above
19. Cartage paid for newly purchased machinery, postage to Cartage Account. This is **Error of Principle**
 (a) Error of omission (b) Error of Commission
 (c) Error of Principle (d) None of the above
20. Goods taken away by the Proprietor for personal use not recorded anywhere. This is **me in**
 (a) Error of Omission (b) Error of Commission
 (c) Error of Principle (d) None of the above
21. Which of the following errors will affect the trial balance. Total of purchase Journal is short by Rs.
And then
 (a) Repairs to building wrongly debited to Building A/c
 (b) Total of purchase Journal is short by Rs. 1000
 (c) Freight paid on purchase of new machinery debited to freight account.
 (d) None of the above.
22. If a purchase return of Rs. 84 has been wrongly posted to the debit of the sales return account, but had been correctly entered in the suppliers account, the total of the trial balance would show **the new the debit side to be Rs. 168 more than credit side.**
 (a) The credit side to be Rs. 84 more than debit side.
 (b) The debit side to be Rs. 84 more than credit side.
 (c) The credit side to be 168 more than debit side.
 (d) The debit side to be Rs. 168 more than credit side.
23. A purchase of Rs. 1,870 by cheque has been wrongly posted in the cash book as Rs. 1,780. This has the effect of **Increasing the bank balance by Rs. 90.**
 (a) Increasing the bank balance by Rs. 90.
 (b) Decreasing the bank balance by Rs. 90.
 (c) Increasing the bank balance by Rs. 180.

(d) Decreasing the bank balance by Rs. 180.

24. And in After preparing the trial balance the accountant finds that the total of the credit side is short by Rs. 1,500. This difference will be **Credited to suspense account.**

- (a) Credited to suspense account.
- (b) Debited to suspense account
- (c) Adjusted to any of the debit balance a/c
- (d) Adjusted to any of the credit balance a/c.

25. The accountant of the firm M/s ABC is unable to tally the following trial balance.

No. Account heads	Debit (Rs.)	Credit (Rs.)
1 Sales	---	12,500
2 Purchases	10,000	----
3 Miscellaneous expenses	---	2,500
Total	10,000	15,000

The above difference in trial balance is due to **wrong placing of miscellaneous expenses account**

- (a) Wrong placing of sales account
- (b) Incorrect totaling
- (c) Wrong placing of miscellaneous expenses account
- (d) Wrong placing of all accounts.

26. **Management** is basically responsible for prevention and detection of errors and frauds,

- (a) Auditor
- (b) Accountant
- (c) Management
- (d) Cashier.

27. Which of the following is not true about opinion on financial statements? **He is responsible for detection and prevention of frauds and errors in financial statement.**

- (a) The auditor should expenses on opinion on financial statements.
- (b) His opinion is no guarantee to future viability of business
- (c) He is responsible for detection and prevention of frauds and errors in financial statements
- (d) He should examine whether recognized accounting principles have been consistently followed.

28. Which of the following statements is not true? **Internal control system prevents employee frauds and management fraud**

- (a) Management frauds is more difficult to detect than employee frauds.
- (b) Internal control system prevents employee frauds and management frauds.
- (c) The management is basically responsible for detection and prevention of errors and frauds
- (d) All statements are correct.

29. As per AAS-4 if auditor detects an error then **The auditor auditor should ensure financial statement are adjusted for adjustment detected errors**

- (a) He should submit his recon nations.
- (b) He should communicate it to the shareholder.
- (c) The account should ensure financial statement are adjusted for detected terror.
- (d) All of the able.

30. Which of the following is not a limitation at of audit as per AAS 4? **An cannot rely up on experts**

- (a) An auditor cannot rely up on experts.
- (b) Auditor cannot check all transition.
- (c) Audit evidence is not conclusive.
- (d) Auditor cannot discover all frauds

31. How money principles listed in AAS 1 which govern auditor's professional obligation?

Nine

- (a) The working capital is high
- (b) The case sales are high
- (c) The auditor's is in the hands of a single person.

32. The risk of fraud increases when **Management is in the hands of a single person.**

- (a) The working capital is high
- (b) The cash sales are high
- (c) The auditors remain the same
- (d) Management is in the hands of a single person.

33. Which of the following factors likely to be identified as a frauds factor by the auditor?

The company is planning is planning offer of shares to shares to raise additional capital for expansion

- (b) the company is planning an initial public offer of shares deposited but not credited.
- (b) The Bank reconciliation statement including cheque deposited but not credited.
- (c) Lawyers are not changed frequently
- (d) There is under- payment for service.

34. Professional skepticism requires that the auditor assume that management is **Neither honest nor dishonest.**

- (a) Reasonable honest
- (b) Neither honest nor dishonest
- (c) Not necessarily honest
- (d) Dishonest unless proved otherwise.

35. Audit of banks is an example of – **All of the above.**

- (a) Statutory audit
- (b) Balance Sheet audit
- (c) Concurrent audit
- (d) All of the above.

36. Balance Sheet audit includes verification of – **all of the above.**

- (a) Assets.
- (b) Liabilities
- (c) Income and expenses accounts where appropriate
- (d) All of the above.

37. Which of the folio wing statements is not true about continuous audit? **It is needed when the organization has a good internal control system.**

- (a) It is conducted at regular interval
- (b) It may be carried out on daily basis
- (c) It is needed when the organization has a good interval control system
- (d) It is expensive.

38. Balance sheet audit does not include **Routine Checks.**

- (a) Verification of assets and liabilities.
- (b) Vouching of income and expenses accounts related to assets and liabilities.
- (c) Examination of adjusting and closing entries

(d) Routine checks.

39. Which of the following statements is not correct about materiality? **Auditor should consider materiality when drafting the audit report**

- (a) Material provides a quantitative cut-off point
- (b) Material is a matter of professional judgement
- (c) AAS-13 deals with materiality
- (d) Auditor should consider materiality when drafting the audit report

40. State which of the following statements is false – **The detection of errors and frauds is the primary audit objective.**

- (a) The detection of errors and frauds is no longer an audit objective.
- (b) An audit does not guarantee that the accounts are free from frauds and errors
- (c) The auditor is not primarily responsible for all the frauds in the accounts audited by him
- (d) The detection of errors and frauds is the primary audit objective.

41. Audit under statute means: **An audit where duties, rights etc. if the auditor are laid down by law**

- (a) An audit ordered by the Government
- (b) An audit where duties, rights etc. of the auditor are laid down by law
- (c) an audit ordered by the Court
- (d) An audit under legal contract

42. In case of audit of partnership or sole proprietorship: **The auditor's duties are defined purely by the contract between him and the client.**

- (a) The auditor's duties are defined purely by the contract between him and the client.
- (b) The auditor need not be as careful as in case of companies.
- (c) The audit must be as extensive as in case of companies
- (d) The auditor can decide his own duties.

Q.2. FILL IN THE BLANKS

1. "Error" means a **bona fide** (bona fide/ mala fide) mistake in financial information.
2. "Frauds" means a **Mala Fide** (bona fide/ mala fide) mistake in financial information.
3. **Continuous** Audit means an audit at regular intervals through the accounting year.
4. **Final or Periodic** Audit means an audit taken up after the end of the accounting year.
5. An audit of accounts prepared for the period of six months from 1st April to 30th September, would be called **Interim** audit.
6. **Concurrent** audit is an audit of transaction as soon as a transaction takes place.
7. Auditing and Assurance Standard **13** issued by the ICAI deals with the concept of materiality.
8. Information is material if its **Misstatement** could influence the economic decision of users.
9. Material matters are those matters which, either individually or in the aggregate, are **relatively** (relatively/ absolutely) important for true fair presentation of financial information in accordance with recognized accounting policies and practices.
10. AAS **16** deals with Going Concern concept.
11. Negative net worth **is** (is/ is not) an indicator that the concern is not a Going Concern.
12. Inability to pay the creditors is an indicator that the concern **is not** (is/ is not) a Going Concern.
13. The total of Sales Book was not posted to the ledger. This **will** (will/ will not) affect the trial balance.

14. Sales Book was overcast by Rs. 500. This **will** (will/ will not) affect the trial balance.
15. The total of a folio in the Sales Book Rs. 1,000 was carried forward as Rs. 100. This **will** (will/ will not) affect the trial balance.
16. Sales to Ram Rs. 143 posted to his account as Rs. 134. This **will** (will/ will not) affect the trial balance.
17. Sales to Meena Rs. 143 posted to Meenu as Rs. 143. This **will not** (will/ will not) affect the trial balance.
18. Goods of the value of Rs. 376 were returned by Ram and were taken into stock on the same date but no entry was made in the books. This **will not** (will/ will not) affect the trial balance.
19. A credit sale was wrongly passed through the purchase book. This **will not** (will/ will not) affect the trial balance.
20. Repairs of newly purchased second-hand machinery were debited to Repairs Expenses Accountant. This **will not** (will/ will not) affect the Trial balance.
21. Repairs to Machinery had been charged to Machinery A/c. This **will not** (will/ will not) affect the trial balance.
22. Cartage paid for newly purchased machinery was posted to Cartage Account. This **will** (will/ will not) affect the trial balance.
23. Goods taken away by the Proprietor for personal use were not recorded anywhere. This **will not** (will/ will not) affect the trial balance.
24. Recording a transaction in a wrong book of original entry with wrong amount **will not** (will/ will not) affect the trial balance.
25. Recording a transactions in a correct book of original entry but not posted in the ledger. This **will** (will/ will not) affect the trial balance.
26. Wrong carrying forward of a balance to next page **will** (will/ will not) affect the trial balance.
27. Writing an amount in the wrong account but not correct side **will not** (will not/ will) affect the trial balance.
28. Wrong balancing of an account **will** (will/ will not) affect the trial balance.
29. Wrong totaling of an account **will** (will/ will not) affect the trial balance.
30. Treating a Capital Item as a revenue item **will not** (will/ will not) affect the trial balance.
31. Audit of Co-operative Societies is **Statutory** (voluntary/ statutory) audit.
32. In **continuous** (Continuous / Periodic) Audit the Final Accounts can be prepared immediately after the year end.
33. **Continuous** (Continuous/ Final) Audit is known as Audit in Installments.
34. Public Limited Companies listed on the stock exchange have to declare their quarterly results. It is preferable to declare such result on the basis of **interim** (interim/ in-depth) audit.
35. Balance Sheet audit is done if the Internal Control System is very **strong** (strong / weak).
36. **Periodical** (Periodical audit/ Continuous audit) audit is less expensive and suitable for a small business.

Q.3 MATCH THE FOLLOWING COLUMNS:

Column A	Column B
1. Making less provision for bad debts	a) Voluntary Audit
2. Treating an items of income as capital receipt	b) window Dressing
3. Tax audit	c) Kingston Cotton Mills Case
4. Internal Audit	d) 11
5. Basic Principles listed in AAS -1	e) Statutory Audit

6. "An auditor must be honest that is he must not certify what he does not believe to e true	f) 9
7. "An auditor is not bound to be a defective".	g) Secret Reserve
	h) London and General Bank Case

Ans: 1 – (b); 2 – (g); 3 – (e); 4 – (a); 5 – (f); 6 – (h); 7 – (c).

Column A	Column B
1. International mistake	a) Error of Principle
2. Personal Transaction of owner recorded in business books.	b) One sided Error
3. Cheque recorded in cash column of cash book	c) Under – casting
4. Total of sales Book taken as Rs. 1,000 instead of Rs. 10,000	d) Two Sided Errors
5. Errors of partial omission; Error of posting and Casting Errors	e) Frauds
	f) Suspense A/c.
	g) error of Commission in Subsidiary Book
	h) Over- casting

Ans: 1 – (e); 2 – (a); 3 – (g); 4 – (c); 5 – (b).

Q.4 STATE WHETHER TRUE OR FALSE.

- The term "General Purpose Financial Statement" includes a cash flow statement (wherever applicable). **True**
- The term "General Purpose Financial Statements" includes statements and explanatory notes which form part thereof. **True**.
- The term "General Purpose Financial Statements" does not includes supplementary schedules and information based on such statements. **False**
- The term " General Purpose Financial Statements" does not include Directors Report. **True**
- According to AAS – 1. Auditing is the independent examination of financial information of any profit oriented entity. **False**
- It is not the objective of the audit to give an opinion on the future prospects of business. **True**
- It is the objective of the audit to give opinion on the efficiently or effectiveness of the management. **False**
- A clean audit report indicates that the business will continue to be profitable in future. **False**
- An agreed Trial Balance indicates error-free books. **False**
- Any type of error causes difference in the Trial Balance. **False**
- Two-sided error do not affect the agreement of Trial Balance. **True**
- Casting error is a type of two-sided error. **False**
- Compensating error causes difference in the Trial balance. **False**
- In Book-keeping, are rectified by erasing the wrong figures and writing the correct figures instead. **False**
- Errors of omission do not allow the Trial Balance to agree. **False**
- Posting a correct amount in the wrong account on correct side does not affect the Trial Balance. **True**
- Error of recording in the books of original entry will affect the Trial Balance. **False**

18. Correct recording in the Journal Proper but not posted in the ledger at all will not affect the Trial Balance. **True**.
19. Correct recording in the Cash Book but not posted in the ledger will affect the Trial Balance. **True**.
20. Errors of principle will affect the Trial Balance. **False**
21. If the amount is posted in the wrong account or it is written on the wrong side of an account, it is called an error of commission. **True**
22. The Trial Balance ensures the arithmetical accuracy of the book. **True**
23. Wrong casting of subsidiary books does not affect the Trial Balance. **False**
24. Rectification of error will not necessarily balance a Trial Balance. **True**
25. A tallied trial balance will not reveal compensating errors. **True**.
26. In window dressing, the net worth is understated in the final account. **False**
27. Secret reserve arise when the profits are understated in the final account. **True**
28. A secret reserve is legally allowed to be created by banks. **True**
29. Balance Sheet Audit does not involve an examination of the various items in the Profit and Loss Account. **False**
30. Audit evidence is not conclusive in nature. **True**
31. An auditor cannot be expect4d to discover deeply laid frauds. **True**
32. An auditor cannot take the help of experts such as valuers etc. **False**
33. Auditing of accounts is compulsory in a partnership firm. **False**
34. Auditing of accounts is undertaken to defect frauds in the books of accounts. **False**
35. Audited of accounts are free from errors and frauds . **False**
36. Audit of accounts is optional in case of a private limited company. **False**
37. The auditor must not disclose any information acquired by him in the course of his work without the written permission of the Institute of C. A. of India. **False**
38. The phrase used to express the auditor's opinion is " give a true and correct view". **False**
39. Unless an auditor is able to discover all frauds and errors, he has not performed its main function. **False**
40. there is little difference between auditing and accounting as both deal with financial statements. **False**
41. The auditor compares entries in the books of account with the vouchers; and if the two agree, his work is done. **False**
42. Safeguarding the company's property is the function of management; hence the auditor is not concerned with verification of assets and liabilities. **False**
43. Auditor is not concerned with the compliance with the accounting principles. **False**
44. Accounts become incorrect when the principle of double entry is not followed. **True**
45. The auditor should act like a bloodhound and not a watchdog. **False**
46. Interim audit of a company is compulsory under the Indian Companies Act, 2956. **False**
47. Continuous audit helps the company to present its audited accounts to the shareholders immediately after the close of the financial year. **True**.

CHAPTER 2: AUDIT PLANNING, PROCEDURES AND DOCUMENTS

Q.1 MULTIPLE CHOICE QUESTIONS:

1. The auditor should plan his work to enable him to conduct an effective audit in, manner. **An efficient and timely**.
 - (a) A professional
 - (b) A proper
 - (c) A confident
 - (d) An efficient and timely
2. `Audit Plans should be based on knowledge of the client's **Business**
 - (a) Profits
 - (b) Net worth

- (c) Business (d) Reputation
3. an audit Programme may be **Fixed or Flexible**
 (a) Statutory (b) Permanent
 (c) Fixed or Flexible (d) Standard
4. **Client and the Auditor** Paper is the link between the client's records and the auditor's report.
 (a) News (b) Working
 (c) Loose (d) Ruled
5. Working Papers are the property of the **Auditor**
 (a) client (b) Client and the auditor
 (c) auditor (d) None of the above
6. Which of the following Auditing Assurance Standard deals with Audit Planning ? **AAS 8**
 (a) AAS 7 (b) AAS 8
 (c) AAS 9 (d) AAS 3
7. Audit programme is prepared by **The auditor and his assistants**
 (a) The client (b) The client and the auditor
 (c) The auditor and his assistants (d) The chief accountant
8. Audit Working Papers record- **All the above.**
 (a) The audit plan (b) The audit procedures performed
 (c) The conclusions drawn from the evidence obtained
 (d) All the above.
9. Current Audit File relating to audit of a partnership firm will not contain **Partnership Deed**
 (a) Audit Plan (b) Audit Programme
 (c) Partnership Deed (d) Letters of confirmation
10. Which of the following is not an advantage of the preparation of working paper? **To provide a guide for advising another client on similar issue**
 (a) To provide a basis for review of audit work
 (b) To provide a basis for subsequent audits
 (c) To ensure audit work is being carried out as per programme
 (d) To provide a guide for advising another client on similar issues
11. An auditor cannot have any lien on the books of accounts of the company audited by him, **Since the books cannot be removed from the registered office of the company.**
 (a) As laid down in section 224 of the Companies Act.
 (b) As laid down by the rules of the Inst. Of C. A. of India
 (c) As laid down in AAS 3
 (d) Since the books cannot be removed from the registered office of the company.
12. Consider the stages in audit given below
 1. Ascertain type of audit
 2. Vouch receipts and payments
 3. Obtain Documents from Client

4. Prepare Audit Programme

what is the correct sequence of the above stages. **1,3,4,2**

- (a) 1,2,3,4 (b) 1,3,4,2
(c) 2,3,1,4 (d) 1,4,3,2

13. Current file and permanent file are together known as **Audit Working Partners**

- (a) Audit plan (b) Audit programme
(c) Audit procedures (d) Audit working papers

14. Consider the following documents

1. Audit notebook
2. Audit report
3. Audit programme
4. Audit plan

What is the correct sequence in which the documents are prepared? **4,3,1,2**

- (a) 1,2,3,4 (2) 3,1,4,2
(c) 2,3,1,4 (d) 4,3,1,2

Q.2 FILL IN THE BLANKS

1. AAS **8** deals with Audit Planning.
2. The auditor should plan his work to enable him to conduct an **Effective** audit in an efficient and timely manner.
3. Working Papers are the property of the **Auditor**.
4. AAS **3** deals with Audit Working Papers.
5. Audit Plans should establish the expected degree of **Reliance** to be placed on internal control.
6. Audit Plans should determine the nature, extent of the audit **Procedure** to be performed.
7. Audit Planning should be **Continuous** throughout the audit engagement.
8. Adequate audit planning helps to ensure that appropriate attention is devoted to **important** (all/ important) arrears of the audit.
9. Adequate audit planning, helps to ensure that **potential problems** (potential problems/ frauds) are promptly identified.
10. Audit Planning involves developing **an overall plan** (an overall plan/ audit techniques) for the expected scope and conduct of the audit
11. Audit Planning involves developing **an audit programme** (a flow-chart/ an audit programme) showing the nature, timing and extent of audit procedures.
12. Adequate audit planning helps to co-ordinate the work done by **other auditors and experts** (other auditors and experts/ audit assistants and accountants).
13. The auditor should document his overall plan including a **time** (time/ cost/ fees) budget.
14. Copies of audited accounts of earlier years will be filed in the **Permanent** (permanent/ Current) Audit File.
15. Trial Balance for year under audit will be filed in the **Current** (Permanent / Current) Audit File.
16. working Papers are the property of the auditors (auditor/ client).
17. audit **Plan** (Plan/ Evidence) will enable the auditor to conduct an effective audit in an efficient and timely manner.
18. Audit **procedure** mean the steps taken to obtain audit evidence.
19. Audit Procedures can be classified into **Compliance** and Procedures and **Substantive** Procedures.
20. **'Compliance'** Procedures are the steps taken to obtain regarding the internal controls.

21. The steps taken by the auditor to obtain evidence regarding the balances of the assets and liabilities as at the year end are known as **Substantive** Procedures.
22. The steps taken by the auditor to obtain evidence regarding the transactions during the year are known as **Substantive** Procedures.
23. Evidence obtain from **Compliances** procedures determines the nature, timing and extent of the Substantive procedures.
24. **Vouching** is the substantive audit procedure used in order to order evidence regarding the transactions during the accounting year.
25. **Casting** Checking is the procedure to check the total of the books, ledgers etc.
26. **Ledger Scrutiny** is the procedure to check and review the accounts of parties, assets, liabilities, income and expenses in the Debtors ledger. Creditor's and the General ledger.
27. **Verification** is the audit procedure to check the balances of various accounts as at the end of the year.
28. Audit **Techniques** means the methods used to obtain audit evidence.
29. Audit technique of **Inspection** consist of examining records, documents or tangible assets.
30. Audit technique of **Observation** consists of observing a procedure being performed by others.
31. Audit technique of **Inquiry** consist of seeking information from others.
32. Audit technique of **Confirmation** means a formal inquiry outsiders.

Q.3 MATCH THE FOLLOWING COLUMNS:

Column A	Column B
1. AAS dealing with Audit Planning	a) Memorandum and Articles of Association
2. Knowledge of client's business	b) Charges in management
3. Discussions with the client	c) AAS 8
4. AAS dealing with Working Papers	d) Expected scope and conduct of the audit
5. Permanent Audit File	e) Nature, timing and extent of audit procedures
6. Current Audit File	f) Visits to Clients Premises and Factories
7. Overall Audit Plan	g) Audit Programme
8. Audit Programme	h) AAS 3

Ans: 1 – (c); 2 – (f); 3 – (b); 4 – (h); 5 – (a); 6 – (g); 7 – (d); 8 – (e).

Q.4 STATE WHETHER THE TRUE OR FALSE

1. Audit Plans once developed should be never be revised during the course of the audit.
False
2. After the auditor discusses his overall plan with the client, the overall auditor plan and the audit programme become their joint responsibility. **False**
3. Auditor should developed a Standard Audit Programme applicable to all audits permanently. **False**.
4. An auditor cannot have any lien on the books of accounts of the company audited by him.
True
5. An Audit Programme should not be in writing as it is confidential. **False**
6. An Audit Programme serves as an evidence of a true and fair view of the state of affairs of the company. **False**
7. an Audit Programme shows the programme for preparation of the financial statements of the company. **False**

8. Audit Programme helps to fix the responsibility of each audit assistant in case of mistake or negligence. **True**
9. Distribution of duties to audit staff for checking of accounts must be in consultation with the management of the company so that they work together to complete the audit in time. **False**
10. An Audit Note Book is the property of the audit assistants and need not be shown to the auditor. **False**
11. Material errors and frauds discovered during the audit should be in the Audit Note Book. **True**.
12. A copy of the Audit Working Papers should also be given to the company for their reference. **False**
13. The purpose of Audit Working Papers is served as soon as the audit report for the year is submitted; they need not be retained for the future. **False**
14. An Auditor Programme is at best an evidence for the quantitative aspects of an audit but it cannot reveal the quality of audit or an error of judgement. **True**
15. Audit Plan should be primarily based on knowledge of Accounting Standards. **False**
16. Audit Plans are confidential and should never be discussed with the client being audited. **False**
17. AAS 8 recommends that Audit Programmes should be fixed and Auditor should not change the; audit programme once the audit commences. **False**
18. Electronic records (e-mails) obtained by auditors from client from part of working papers. **True**
19. Internal audit report is the property of the internal auditor and the statutory auditor has no right to inspect the same. **False**
20. The old auditor must hand over his working papers to the new auditor appointed in his place. **False**
21. Audit techniques mean the steps taken to obtain audit evidence. **False**
22. Audit Procedures mean the methods used to obtain audit evidence. **False**
23. Audit techniques can be classified basically into (1) Compliance techniques and (2) Substantive I techniques. **False**
24. Substantive Procedures are the steps taken to obtain evidence regarding the internal controls. **False**
25. Compliance Procedures are the steps taken by the auditor to obtain evidence regarding the: transactions during the year and the balances of the assets and liabilities as at the year end. **False**
26. Verification is the audit procedure used in order to obtain evidence regarding the transactions during the accounting year. **False**
27. Vouching is the audit procedure to check the balances of various accounts as at the end of the year. **False**
28. The audit technique of Observation consists of examining records, documents or tangible assets. **False**
29. The audit technique of Inspection consists of observing a procedure being performed by others. **False**
30. The audit technique of Inquiry consists of seeking formal confirmation from outsiders. **False**
31. The audit technique of Confirmation is a formal inquiry from insiders. **False**

CHAPTER 3: AUDIT TECHNIQUES AND INTERNAL AUDIT

Q.1 MULTIPLE CHOICE QUESTIONS:

1. "Audit Sampling" enables the auditor to **obtain and evaluate** the items selected.

- (a) Ignore (b) Obtain and evaluate
(c) Manipulate (d) None of the above
2. When designing an audit sample, the auditor should consider – **all the above.**
(a) The specific audit objectives
(b) The population from which the auditor wishes to sample.
(c) The sample size
(d) All the above
3. The risk that, although the sample result does not support the auditor assessment of control risk, the actual compliance rate would support such an assessment is known as – **Risk of Under Reliance**
(a) Risk of Over Reliance (b) Risk of Under Reliance
(c) Risk of Incorrect Rejection (d) Risk of Incorrect Acceptance
4. The risk that, although the sample result the auditor's assessment of control risk, the actual compliance rate would not support such an assessment is known as – **Risk of Over Reliance**
(a) Risk of Under Reliance (b) Risk of Incorrect Rejection
(c) Risk of Incorrect Acceptance (d) Risk of Over Reliance
5. The risk that, although the sample result support the conclusion that a recorded account balance or class of transactions is materially misstated, in fact it is not materially mis-stated is known as – **Risk of Incorrect Rejection**
(a) Risk of Incorrect Rejection (b) Risk of Over Reliance
(c) Risk of Under Reliance (d) Risk of Incorrect Acceptance
6. The risk that, although the sample result supports the conclusion that a recorded account balance or class of transactions is not materially mis-stated, in fact it is materially misstated is known as – **Risk of Incorrect Acceptance**
(a) Risk of Over Reliance (b) Risk of Under Reliance
(c) Risk of Incorrect Acceptance (d) Risk of Incorrect Rejection
7. The risk of over reliance and the risk of incorrect acceptance **Both (a) and (b)**
(a) Affect audit effectiveness
(b) May lead to an erroneous opinion on the financial statements
(c) Both (a) and (b) above
(d) None of (a) or (b) above.
8. The risk of under reliance and the risk of incorrect rejection **Both (a) and (b)**
(a) Affect audit efficiency
(b) Lead to additional work being performed by the auditor, or the entity
(c) Neither (a) nor (b) above.
(d) Both (a) and (b) above.
9. Tolerable error is the **Insignificant** error in the population that the auditor would be willing to accept, and still conclude that the result from the sample had achieved the audit objective,
(a) Minimum (b) Reasonable
(c) Maximum (d) Insignificant

10. In substantive procedures, the tolerable error is the **Maximum monetary error in an account balance that the auditor would be willing to accept.**
- (a) Maximum rate of deviation from a prescribed account that the auditor would be willing to accept
 - (b) Minimum monetary error in an account balance that the auditor would be to accept
 - (c) Minimum rate of deviation from a prescribed account balance that the auditor would be willing to accept
 - (d) Maximum monetary error in an account balance that the auditor would be willing to accept.
11. In tests of control, the tolerable error is the **Maximum rate of deviation from a prescribed control procedure that the auditor would be willing to accept**
- (a) Maximum rate of deviation from a prescribed control procedure that the auditor would be willing to ignore
 - (b) Minimum rate of deviation from a prescribed control procedure that the auditor would be willing to accept
 - (c) Maximum rate of deviation from a prescribed control procedure that the auditor would be willing to accept.
 - (d) Minimum rate of deviation from a prescribed control procedure that the auditor would be willing to ignore
12. This method of selecting sample ensures that all items in the population have an equal chance of selection. **Random Selection.**
- (a) Random Selection
 - (b) systematic selection
 - (c) Haphazard selection
 - (d) None of the above.
13. This method of sample selection involves selecting items using a constant interval between selections, the first interval having a random start, **Systematic Selection**
- (a) Random Selection
 - (b) Systematic Selection
 - (c) Haphazard selection
 - (d) None of the above
14. “Letter of Weakness” deals with weaknesses in **Internal Controls**
- (a) Statutory Audit
 - (b) Internal Controls
 - (c) Financial Position
 - (d) None of the above
15. The following is suitable for test checking. **Payments made by a bank, during audit of a bank**
- (a) Opening and closing entries
 - (b) Bank Reconciliation Statements
 - (c) Transactions on which auditor must be report under the Companies Act
 - (d) Payments made by a bank, during audit of a bank
16. AAS which deals with Audit Sampling **15**
- (a) 15
 - (b) 6
 - (c) 7
 - (d) None of the above
17. Internal auditor are appointed by **The management**
- (a) Board of Directors in a Board meeting
 - (b) Shareholders in annual general meeting
 - (c) The management
 - (d) The central government

18. What is the correct sequence of the following stages **3,2,1**

1. Statutory Audit
2. Internal Audit
3. Internal Check

- (a) 1,2,3 (b) 2,3,1
(c) 3,2,1 (d) 3,1,2

Q.2 FILL IN THE BLANKS:

1. **Test** Checking means to select and examine a representative sample from a larger number of similar items.
2. Opening and closing entries **are not** (are/ are not) suitable for test checking.
3. Bank Reconciliation Statements **are not** (are/ are not) suitable for test checking
4. **Routine** Checking is the checking of totals and calculations etc. in subsidiary books, checking of posting into the ledgers etc.
5. Vide AAS 15, Audit **Sampling** means the application of audit procedures to less than 100 % of the items within an account balance,
6. The **population** is the entire set of data from which the auditor wishes to sample in order to reach a conclusion.
7. The individual items that make up the **population** are known as sampling units.
8. **Tolerable** error is the maximum error in the population that the auditor would be willing to accept, and still conclude that the result from the sample has achieved the audit objective.
9. The **smaller** (smaller/ greater) the tolerable error, the greater the sample size will need to be.
10. The smaller the tolerable error, the **greater** (smaller/ greater) the sample size will need to be.
11. In tests of control, the **Tolerable** error is the maximum rate of deviation from a prescribed control procedure that the auditor would be willing to accept.
12. The auditor should select sample items in such a way that the sample can be expected to be **representative** of the population.
13. **Random** method of selecting sample ensures that all items in the population have an equal chance of selection.
14. **Operational** (Operational / Accounting) Controls aim to ensure that the management policies in respect of the operations and administration of the concern are implemented.
15. **Internal Audit** is a separate component of Internal Control established to determine whether other Internal Controls are well designed and properly operated.
16. The internal audit department **should not be** (should be /should not be) involved in the performance of executive actions.
17. The copy of the report of the internal auditor should be (should be/ should be not) made available to the statutory auditor.
18. The Internal Audit work **should be** (should be/ should not be) planned in consultation with the external auditor.
19. Internal Auditor is appointed by the **management** (management / shareholders)
20. Internal Auditor can be removed **by the management** (by the management / by the central government)
21. In **Internal Check** (routine check/ internal check) the work is divided in such a way that the document prepared by one person are automatically checked by other persons.
22. Division of work is an integral aspect of **internal check** (internal check / test check)
23. In **Internal check** (internal / internal check) the duties of the employees are changed from time to time.

Q.3 MATCH THE FOLLOWING COLUMNS:

Column A	Column B
1. AAS which deals with Audit Sampling	a) Management policies in respect of the operations and administration of the concern are implemented
2. AAS which deals with study and evaluation of Internal Control	b) AAS 15
3. AAS which deals with Internal Audit	c) Letter from audit assistant for sick leave
4. Accounting Control aim to ensure that	d) Statutory Auditor
5. Operational Controls aim to ensure that	e) Internal Check
6. Letter of weakness	f) AAS 6
7. Operational Control	g) Budgetary Control
8. Report to shareholders	h) AAS 7
9. Report to management	i) Accounting Control
10. System of Allocation of Responsibility	j) The accounting policies adopted by the Management are implemented
	k) From the auditor to the management regarding internal controls
	l) Internal Auditor

Ans: 1 – (b); 2 – (f); 3 – (h); 4 – (j); 5 – (a); 6 – (k); 7 – (g); 8 – (d); 9 – (l); 10 – (e)

Q.4 STATE WHETHER TRUE OR FALSE

- In test checking, the selection of sample depends up on the personal judgement of the auditor. **True**
- Test checking emphasizes quantity rather than quality of checking. **True**
- Test checking does not reduce auditor's liability. **True**
- the higher the risk the auditor is willing to accept, the greater the sample size will need to be. **False**
- Tolerable error is the minimum error population that the auditor would be willing to accept, and still conclude that the result from the sample has achieved the audit objective. **False**
- Tolerable error is the maximum error in the population that the auditor would be willing to ignore, and still conclude that the result from the sample has achieved the audit objective. **False**
- Tolerable error is the reasonable error in the population that the auditor would be willing to accept, and still conclude that the result from the sample has achieved the audit objective. **False**
- The smaller the tolerable error, the greater the sample size will need to be. **True**
- Three methods of sampling commonly used are: (1) Random Selection (2) Simple Random Sampling and (3) Stratified Sampling. **False**
- Random Selection method of Sampling is known as Interval Sampling. **False**
- Systematic Selection may be of the following types. (i) Block Sampling (ii) Cluster Sampling. **True**
- Basically, the management is responsible for establishing and operating the Internal Control System. **True**
- The responsibility of the statutory auditor is to some extent reduced if he has relied up on the Internal Audit, **False**
- Internal auditor must be a qualified chartered accountant . **False**
- Once internal control system is implemented, there can be no fraud or error. **False**
- Internal control is part of the broader system of internal audit. **False**
- Separate staff is appointed to conduct internal checks. **False**
- Internal check is carried after the work is done. **False**

19. Internal check helps to prevent rather than errors. **True**
20. An essential feature of internal check is that an employee has an exclusive control over a specific work without any fear of external check. **False**
21. Internal Audit is done by actual administrative staff during day-today operation. **False**
22. Internal audit is carried out during the work itself. **False**
23. Internal audit helps to detect rather than prevents errors. **True**
24. Internal auditor reports to the shareholders whether the internal controls are true and fair. **False**
25. Statutory auditor reports to the management whether the internal controls are true and fair. **False**
26. Internal auditor of a Company whose Managing Director committed a fraud is liable to the shareholder for negligence. **False**
27. The rights and duties of internal auditor are laid down in the Companies Act. **False**
28. Internal Auditor must be appointed as the Chairman of the Audit Committee of a public company as per s. 292 A of the Companies Act. **False**
29. Internal auditor is responsible for establishing the system of internal controls. **False**
30. The first internal auditor must be appointed within 30 days of the incorporation of the company. **False**
31. The internal auditor of a company must be appointed in the annual general meeting every year. **False**
32. The internal auditor of a company must be appointed by passing a special resolution. **False**
33. If an internal auditor, the casual vacancy must be filled in bypassing a resolution in an extraordinary general meeting of the company. **False**
34. The internal auditor must inform the register of companies of his appointment within 30 days. **False**
35. A person who is indebted to the company for an amount exceeding Rs. 1,000 cannot be appointed as the internal auditor of the company. **False**
36. A relative of a director cannot be appointed as internal auditor of a company. **False**
37. A shareholder of a company cannot be appointed as the internal auditor of the company. **False**
38. Schedule VI to the Companies Act requires that the remuneration of internal must be auditor must be disclosed separately in the final accounts of the company. **False**
39. Internal auditor has the right to attend the annual general meeting of the company u/s 231 of the Companies Act. **False**
40. an internal auditor cannot carry out internal of more than 20 concerns belonging to the group. **False**
41. Internal auditors are appointed by the statutory auditors. **False**
42. Auditor must do a100% checking of all transaction and balances. **False**
43. Statutory audit cannot start unless internal is complete. **False**

CHAPTER 4: VOUCHING OF INCOME AND EXPENDITURE

Q.1. MULTIPLE CHOICE QUESTIONS:

1. The following points should be noted or checked by the auditor in vouching: **All the above.**
 - (a) Checking the Voucher
 - (b) Checking the Supporting Documents
 - (c) Checking the Entry in the Books
 - (d) All the above

2. Checking serial no. of vouchers during vouching helps the auditor to **Detect errors of omission**
- (a) Defect errors of principle (b) Defect errors of omission
(c) Defect compensating errors (d) None of the above.
3. Checking the head of account debited or credited during voiding helps the auditor to **Defect errors of principle**
- (a) Defect errors of principle (b) Defect errors of omission
(c) Defect compensating errors (d) None of the above
4. Checking the amount in words during vouching of cash transactions helps the auditor to **Defect misappropriation**
- (a) Defect errors of principle (b) Defect errors of commission
(c) Defect misappropriation (d) None of the above
5. Verifying the signature of the authorized official on the voucher during vouching helps the auditor to check the **Validity of the transaction**
- (a) Occurrence of the transaction (b) Validity of the transaction
(c) Amount of the transaction (d) Period of the transaction
6. Checking the serial no. of vouchers on the voucher during vouching helps the auditors to obtain evidence that **there are no unrecorded transactions**
- (a) The transactions took place
(b) There are no unrecorded in the books on the right date
(c) The transaction is recorded in the books on the right date
(d) The transaction is valid
7. Checking the date of voucher on the voucher during vouching mainly helps the auditor to obtain evidence that **the transaction related to current year.**
- (a) The transaction relates to current year.
(b) The transaction is legal
(c) All the transaction are recorded in the books
(d) Transactions take place every day
8. Verifying the signature of the person preparing the voucher helps the auditor to **Fix responsibility for errors in preparing the voucher.**
- (a) Fix responsibility for errors in making entry of the voucher
(b) Fix responsibility for preparing the voucher
(c) Ensure that the voucher is posted in the ledger.
(d) Ensure that the voucher has proper supporting documents.
9. Checking the signature of the payee during vouching of cash payments helps the auditor to **verify that the cash received is acknowledged**
- (a) Verify that the payment is properly authorized
(b) Verify that the cheque was signed by an authorized person
(c) Verify that the cash received is acknowledged
(d) Identify from whom cash was received
10. Serial no. of supporting bill from supplier attached with a voucher helps the auditor to **Defect entry of duplicate bill in the register.**
- (a) Defect entry of duplicate bill in the register.

(c) 5,4,2,1,3

(d) 1,2,3,4,5

Q.2 FILL IN THE BLANKS:

- Vouching** means comparing the entries in books of accounts with documentary evidence in support thereof.
- As soon as any transaction takes place, a **voucher** is prepared giving details of the transactions.
- Purchase bill is an example of **extent** (internal/ external) documents.
- Payroll is an example of **Internal** (internal/ external) document.
- Date of the Voucher is checked to see that the transaction pertains to the **Current** year.
- The amount in **Words** in a voucher helps prevent alteration of amount in figures
- The payee should sign on a Revenue stamp, if the payment exceeds Rs. 5,000.
- Checking the date of entry helps to prevent and defect frauds in the nature of Teeming and Lading
- The auditor of a company has to comment in his report, in case of sales to group concerns, whether the rates charged to such group concerns are Reasonable or not with regard to the prevailing market prices at the relevant time.
- The dividend received should be vouched from the following supporting documents: (i) Counterfoils of Dividend Warrants, (ii) Pay-in-slips for deposits in Bank Account.

Q.3 MATCH THE FOLLOWING COLUMNS:

Column A	Column B
1. Sales	a) Debit Note from customer
2. Goods Dispatched	b) Dividend Warrants
3. Exports	c) Signature of payee on revenue stamp
4. Sales Returns	d) Cash Memo
5. Recovery of bad debts written off	e) Sanction from Reserve Bank of India
6. Income from investment	f) Debit Note of Auditee
7. Royalty	g) Dividend from Official Receiver
8. Cash payment exceeding Rs. 5000	h) Delivery Challan
9. Purchases	i) Lease Deed
10. Purchase Return	j) Pay Rolls
11. Salary	k) Bills of lading
12. Traveling expenses in foreign currency	l) Goods Received Note

Ans: 1 – (d); 2 – (h); 3 – (k); 4 – (a); 5 – (g); 6 – (b); 7 – (i); 8 – (c); 9 – (l); 10 – (f); 11 – (j); 12 – (e)

Q.4 STATE WHETHER TRUE OR FALSE

- When goods are sent on approval, sale is to be booked only when the inspection or installation is complete and the buyer has accepted the goods. **True**
- Goods are sent on approval. If the buyers has not formally sent a letter of acceptance, the sale can be booked if the buyer has not sent back the goods within a reasonable period. **True**
- When the goods are sent to an agent on consignment basis sales should be booked when the agent actually receives the goods. **False**.
- The Sales Return should be supported by wither the Copy of Credit Note of the Audit tee or Debit Note of the customer. **True**
- If the amount of sales returns is heavy in the beginning of the year, it may indicate that fictitious sales were booked last year. **True**
- Auditor should ensure that the value of goods returned is disclosed separately in the profit and loss account. **False**

7. Auditor should ensure that the recovery of bad debts earlier written off is credited to the concerned Debtor's Account. **False**
8. A statutory auditor is not mainly concerned that prevailing market price is uniformly to all customers. **True**
9. The auditor has to comment in his report, in case of sales to group concerns, whether the rates charged to such group concerns are reasonable or not with regard to the prevailing market prices at the relevant time. **True**
10. If tax is deducted at source (TDS) from interest, auditor should see that interest is shown in the accounts net of TDS. **False**
11. Auditor should verify whether the payee has signed on a revenue stamp, if the sum exceeds Rs. 50 **False**
12. Auditor need not check the Goods Received Note in case of cash purchase. **False**
13. The purchase Return should be supported by the Copy of Debit Note of wither the auditee or the supplier. **False**
14. While checking purchase returns, auditor should see that the Serial Numbers on the Credit Notes are continuous ant tally those in the Credit Note Register. **False**
15. While checking purchase returns, auditor should check the corresponding Goods Received Note. **False**
16. While checking sales returns, auditor should check the corresponding Delivery Challan. **False**
17. Auditor should ensure that Remuneration to directors is disclosed separately and it is within the limits prescribed under the Companies Act. **True**
18. Deferred Advertisement Expenses should be disclosed under "Miscellaneous Expenditure" in the Balance Sheet. **True**

CHAPTER 5: VERIFICATION OF ASSETS AND LIABILITIES

Q.1 MULTIPLE CHOICE QUESTIONS:

1. The following points should be noted or checked by the auditor in verification of an asset **Checking existence ownership, non-omission and disclosure**
 - (a) Checking the Voucher
 - (b) Checking the transactions
 - (c) Checking the Entry in the Books
 - (d) Checking existence, ownership, non-omission and disclosure
2. While checking the cut-off procedures, the Auditor should ensure that – **Both the above**
 - (a) Sales bills are raised for all goods dispatched till the last day of the accounting year,
 - (b) No sales bills are raised unless the goods were actually dispatched and sold during the accounting year.
 - (c) Both the above
 - (d) None of the above.
3. Auditor should verify stocks which are not lying with the concern e.g. goods on consignment, **Bu obtaining and examining the confirmation from the consignee**
 - (a) Through physical verification at consignee's godown
 - (b) Through observing the physical verification carries out by the consignee
 - (c) By obtaining and examining the confirmation from the consignee
 - (d) By obtaining examining the confirmation from the consignor
4. closing stock with consignee is to be shown as the asset of **the consignor**
 - (a) The consignor
 - (b) The consignee

- (c) Both the above (d) None of the above.
5. Stock of Goods on Consignment should be valued at **Cost or Market price whichever is lower**
- (a) Invoice price
(b) Cost or market price whichever is lower
(c) Price at which goods were sent to the consignee
(d) None of the above
6. Prior Period Expenses are **Expenses of the previous year paid in current year**
- (a) Expenses of the current year paid in previous year
(b) Expenses of the previous year paid in current year
(c) Expense of the previous year paid in previous year
(d) Expenses of the current year paid in next year
7. Prior Period Expenses are **Expenses debited to the current year's profit and loss account, though relating to earlier years.**
- (a) Expenses credited to the current year's profit and loss account. Though relating to earlier years.
(b) Expenses debited to the current year's profit and loss account, though relating to next year
(c) Expenses debited to the current year's profit and loss account relating to earlier years
(d) Expenses debited to the previous year's profit and loss account, though relating to the current year.
8. If the market value of the security is less than the outstanding amount of loan taken, **Difference should be shown as unsecured loan**
- (a) Difference should be shown as loans and advances
(b) difference should be shown as current liability
(c) Difference should be shown as unsecured loan
(d) None of the above
9. A mortgage duly registered under the Transfer of Property Act is known as **Legal mortgage**
- (a) Equitable mortgage (b) Legal mortgage
(c) Hypothecation (d) Pledge
10. **Equitable mortgage** involves depositing the title deeds of the property with the lender as security,
- (a) Equitable mortgage (b) Legal mortgage
(c) Hypothecation (d) Pledge
11. Deferred credits from machinery suppliers **All of the above**
- (a) Are credits payable over more than one year
(b) Arise because of financing provided by the vendor or by a refinancing agency
(c) Involve signing bills of exchange counter guaranteed by buyer's bank
(d) All of the above
12. An auditor is verifying valuation of building which has been self-constructed by the client. Which of the following documents is least relevant to the auditor for verification purpose? **Minutes of meeting of board of Directors**
- (a) Bills of contractor

- (b) Minutes of meeting of board of directors
- (c) certificates of engineer and architect
- (d) Loan agreement

13. Equity shares of XY Ltd. by ABC Ltd. are in the custody of Stock Holding corporation of India Limited (SHCIL). The auditor may verify this investment by

Obtaining a certificate from SHCIL

- (a) Reviewing last year's working papers
- (b) Obtaining a certificate from a responsible official of the ABC Ltd.
- (c) Obtaining a certificate from SHCIL
- (d) Obtaining a certificate from XY Ltd.

14. While reconciling a client's annual physical inventory with book stock, an auditor observed that for certain items the stock in hand was more than that shown in the books. This is could be the result of the client's failure to record **Sales returns**

- (a) Purchase return
- (b) Sales return
- (c) Goods with consigner
- (d) Purchase discount

15. Goods Received Notes support entries in **Purchase book and sales return book**

- (a) Sales book and sales return book
- (b) Purchase book and sales return book
- (c) Cash book and purchase book
- (d) Sales book and purchase return book

16. Which of the following assets cannot be subjected to physical verification **Debtors**

- (a) Debtors
- (b) Land
- (c) Building
- (d) Machinery

Q.2 FILL IN THE BLANKS

1. Verification involves obtaining and examining evidence in respect of an item of **Asset** or **Liabilities**
2. **Confirmation** means obtaining written evidence from outside parties regarding existence of an asset or liability.
3. **Cut-off** procedures ensure separation of transactions of the current year from those of the next year.
4. If any debtor has become insolvent after the balance sheet date, provision **should be** (should be / should not be) made for such debts as bad debts.
5. Auditor **needs to** (needs to/ is not required to) ensure that the book stocks are adjusted for any excess or shortage found on physical verification.
6. If the stocks are undervalued the profits and assets will be **understated** (overstated/ understated)
7. Auditor should ensure that, in valuing stocks of goods sold on hire purchase, the proportionate estimated profit applicable to outstanding installments, (is / is not) added.
8. Auditor should see that Loose tools have been disclosed separately as an item of **current** (fixed /current) assets.
9. In case of right shares acquired the year, their cost should be **added to** (added to/ deducted from) the cost of the original shares.
10. In case of **Bonus** (Right / Bonus) Shares received during the year, no adjustment should be made to the cost of original shares.
11. In case of a company the amount of depreciation should be in accordance with the provisions of the Companies Act and Schedule **XIV** thereto.
12. Revaluation Reserve **is not** (is / is not) available for distribution i.e. payment of dividend.
13. Mortgage means a **Charge** on immovable property to secure a debts.

14. A mortgage duly registered under the transfer of Property Act is known as **Legal** mortgage.
15. **Equitable** Mortgage means simply depositing the title deeds of the property with the lender as a security.
16. Bills Receivable discounted before maturity, but likely to be dishonoured on presentation are considered as **Contingent** (current/ contingent) liabilities.
17. During the scrutiny of ledger, auditor should see that all entries are posted in sequence of dates i.e. **Chronological** order.
18. During the scrutiny of ledger, auditor should see that, there is a reference of the **Folio** of the original book or register.
19. **Composition** of Debtor's Balance mean all the sales bills pending as at the year end which add up the closing balance in the account.
20. If the balance in a debtor's account is a credit balance, it indicates that **Receipts** are more than sales made.
21. The credit balances in the Debtor Account are shown on the **Liabilities** (Assts /Liabilities) side of the Balance Sheet.
22. Credit balances in the Debtors Account **should not be** (should be / should not be deducted) from the gross debit balances in the Debtors Accounts.
23. In the **positive** (positive/ negative) from of confirmation, the debtor is asked to write back whether he agrees or not with the balance shown.
24. In the **negative** (negative / positive) from of confirmation, the debtor is asked to write back only if he disagrees with the balance shown.
25. The debtors confirmation should be returned to the **Auditor** (auditor/ client) and not to the client (auditor/ client)

Q.3 MATCH THE FOLLOWING COLUMNS:

Column A	Column B
1. right Shares	a) Confirmation
2. Bonus Shares	b) Add cost to the cost of original shares
3. Stocks	c) Certificate from Chartered Engineer
4. Debtors	d) Check Title Deeds deposited with lender or Solicitor
5. Value of building constructed by auditee	e) Check Mortgage Deed
6. Value of machinery fabricated by auditee	f) Add only no. of shares received to the number of original shares.
7. Future installments under hire purchase Agreement of the purchase of asset	g) Certificate from Civil Contractor
8. Loan secured by Legal Mortgage of Immovable Property	h) Treat as contingent liability
9. Loan secured by Equitable Mortgage or Immovable Property	i) Physical Verification
	j) Certificate from Architect
	k) Certificate from Factory Manager
	l) Show separately as secured loans

Ans: 1 – (b); 2 – (f); 3 – (i); 4 – (a); 5 – (j); 6 – (c); 7 – (l); 8 – (e); 9 – (d).

Q.4 STATE WHETHER TRUE OR FALSE

1. Verification involves obtaining and examining evidence in respect of an items of revenue or expenditure. **False**

2. Confirmation means obtaining written evidence from management regarding existence of an asset or liability. **False**
3. Verification involves obtaining and examining evidence in respect of an item of asset or liability at the beginning of the year. **False**
4. Verification means comparing the entries in books of accounts with documentary evidence in support thereof. **False**
5. When the auditor whether the inventory is being by the staff of the concern in the right manner, he is said to employ the audit technique of “ inspection”. **False**
6. The opening balance of the stock books for the next year should be the closing stock of the current year as per the physical inventory. **True**
7. If the stocks are overvalued the profits and assets will be overstated. **True**
8. Investments are valued at the market price as at the year end. **False**
9. Depreciation is to be provided on the investments annually. **False**
10. In case of Bonus Shares received during the year, no adjustment should be made to the cost of original shares. Only the number of share should be increased resulting in a lower average cost per share. **True**
11. Investment in subsidiary companies is valued at cost, even if the subsidiary company had incurred any losses. **True**
12. Patents should be written off over their legal period of validity or their working life, whichever is shorter. **True**
13. In case patents were developed in-house they are shown in the books at Nil value. **False**
14. Interest on loans taken to purchase machineries up to the date of completion of the project should be included in the cost of the machineries. **True**
15. Increase in value of plat and machineries due to revaluation should be debited to the Plant & Machineries Account, and credited to Profit & Loss Account. **False**
16. No depreciation can be claimed in respect of freehold land. **True**
17. A decrease in the value of freehold land on revaluation should be debited to the Profit and Loss Account, and credited to Land Account. **True**
18. A loan should be classified as secured, only to the extent of the market value of the security. **True**
19. The entry for amounts payable to suppliers of machinery under deferred payment arrangement is passed for the full amount of bills of exchange including the future discount charges. **True**
20. If an asset is purchased by a company, it is necessarily owned by the company. **False**
21. An asset which is owned by a company need not necessarily be in its possession. **True**
22. An invoice is a reliable evidence that the asset is owned by the company. **True**
23. Goods in transit are to be included in Closing Stock-in-Trade. **True**
24. Inspection means observation of an asset. **False**
25. Confirmation means obtaining documents from the client supporting the voucher. **False**
26. It is the responsibility of the auditor to carry out physical verification of fixed assets at appropriate intervals in order to ensure that they are in existence. **False**
27. In case of Bonus Shares received during the year, adjustment should be made to the cost of original shares. **False**
28. Investment in subsidiary companies is valued at cost or net realizable value whichever is lower. **False**
29. When inventory is under the custody and control of a third party, the auditor must attend the physical verification of the inventories. **False**
30. Vouching includes verification. **False**
31. Obtaining direct confirmation from debtors does not mean that the debt will be recovered. **True**

32. Direct confirmation procedures for debtors balances need not be carried out with the consent of the concern (auditee). **False**
33. The detailed procedure for obtaining debtors confirmation (from whom, when, how, in what form etc.) is to be decided by the entity (auditee). **False**
34. In the negative form of confirmation, the debtor is asked to write back whether he disagrees with the balance shown. **False**
35. In the positive form of confirmation, the debtor is asked to write back only if he agrees with the balance shown. **False**
36. The positive form of confirmation is used when many parties are likely to agree with the book balances shown. **False**
37. The negative form of confirmations used when few accounts having large balances are involved. **False**
38. The debtor confirmation should be returned to the client. **False**

CHAPTER 6: INTRODUCTION TO COMPANY AUDIT

Q.1 MULTIPLE CHOICE QUESTIONS:

1. The first auditors of a company are appointed **By the directors in the first meeting of the Board of Directors to be held within 30 days of the incorporation of the company.**
- (a) By the shareholders in their first meeting to be held within 30 days of the incorporation of the company.
- (b) By the directors within 30 days of their first meeting held after the incorporation of the company.
- (c) By the directors in the first meeting of the Board of Directors to be held within 30 days of the incorporation of the company.
- (d) Through the appointments clause in the memorandum of association
2. Every company shall, at each annual general meeting, appoint an auditor who will hold office **From the conclusion of the meeting until the conclusion of the next annual general meeting**
- (a) From the conclusion of the meeting until the beginning of the next annual general meeting
- (b) From the conclusion of the meeting until the conclusion of the next accounting year.
- (c) From the beginning of the accounting year until the end of the accounting year.
- (d) From the conclusion of the meeting until the conclusion of the next annual general meeting.
3. The auditor of a Government company is appointed by – **The Comptroller and Auditor – General of India**
- (a) The shareholders
- (b) The Board of Directors
- (c) The Comptroller and Auditor – General of India
- (d) The Central Government
4. Any auditor appointed in a casual vacancy shall hold office **Until the conclusion of the next annual general meeting.**
- (a) Until the end of the accounting period during which is appointed
- (b) Until the end of the immediately succeeding accounting period during which he is appointed
- (c) Until the conclusion of the next annual general meeting.
- (d) Till the date of termination as mentioned in the letter of appointment

5. In the case of a company in which not less than 25% of the subscribed share capital is held by any of the specified financial institutions, **The Appointment of an auditor shall be made by a special resolution**
- (a) The appointment of an auditor shall be made by an unanimous resolution
 - (b) The appointment of an auditor shall be made by special resolution
 - (c) The appointment of an auditor shall be made by such financial institution
 - (d) The appointment of an auditor shall be approval by the central government
6. Who is primarily responsible for the appointment of statutory auditor of a limited company? **Members of the company.**
- (a) Managing Director of the company
 - (b) Members of the company
 - (c) The Central Government
 - (d) All of the above
7. Which of the following sections of the Companies Act deal with qualifications of the auditor? **Section 226 (1) and section 226 (2).**
- (a) Section 226 (1) and section 226 (2)
 - (b) Section 224 (1) and section 224 (2)
 - (c) Section 226 (3) and section 226 (4)
 - (d) Section 224 (3) & Sec. 224.
8. Which of the following statement is not true?
- (a) A partnership firm can be appointed as a statutory auditor of limited company **Majority of the partners should be practicing India.**
 - (b) Appointment can be made in the name of the firm
 - (c) Majority of the partners should be practicing India
 - (d) All partners should be chartered accountants
9. As per requirements of section 226 (3) and 226 (4) a person is disqualified from being appointed as a statutory auditor if he holds **Security carrying voting rights of the company**
- (a) Debentures of the company
 - (b) Equity shares of the company
 - (c) Preference Shares of the company
 - (d) Security carrying voting rights of the company
10. The board of directors shall first auditor of a company **Within 30 days of incorporation of the company.**
- (a) Within 30 days of the first shares issue of the company.
 - (b) Within 30 days of the payment of registration fees of the company
 - (c) within 30 days of the commencement of the business of the company
 - (d) Within 30 days of incorporation of the company
11. If a casual vacancy in the office of auditor arises by his resignation it should only be filled by the company in a **General Meeting**
- (a) Board meeting
 - (b) Extraordinary general meeting
 - (c) General meeting
 - (d) Annual general meeting
12. The authority to remove the first auditor before the expiry of term is with **The shareholders in a general meeting**
- (a) The shareholders in a general meeting
 - (b) The shareholders in the first annual General meeting
 - (c) The board of director
 - (d) The Central Government

13. Which of the following statements is not correct regarding removal of first auditor before expiry of the term? **The approval of the Central Government is required for such removal**

- (a) He is removed at a general meeting
- (b) The shareholders are authorized to do so
- (c) The approval of the Central Government is required for such removal
- (d) The directors are not authorized to do so

14. The retiring auditor does not have a right to **Make defamatory statements in his written representation**

- (a) Make written representation
- (b) Get his representations circulated
- (c) Be heard at the meeting
- (d) Make defamatory statement in his written representation

15. Who out of the following cannot be appointed as a statutory auditor of the company?
Internal Auditor

- (a) Retiring auditor
- (b) Internal auditor
- (c) Tax consultant
- (d) First Auditor

16. The remuneration of an auditor of a company may be fixed by the board of directors in case of -

The first auditor

- (a) The first auditors
- (b) The auditor appointed in any casual vacancy caused by resignation
- (c) The retiring auditors who are re-appointed
- (d) The auditor appointed in place of the retiring auditors

17. The remuneration of an auditor of a company may not be fixed by the shareholders in case of the first auditors

- (a) The first auditors
- (b) The auditors appointed in any casual vacancy caused by resignation
- (c) The retiring auditors who are re-appointed
- (d) The auditor appointed in place of the retiring auditors.

18. The rights of the company auditor Cannot be limited or restricted in any way

- (a) Can be limited if a special resolution approved by 75% of the members is passed
- (b) Can be limited if there is a specific provision in the Articles of Association
- (c) Cannot be limited or restricted in any way
- (d) Depend on the term mentioned in the letter of appointment

Q.2 FILL IN THE BLANKS:

1. The first auditors of a company are appointed by the directors in the first meeting of the Board of Directors to be held within **30** days of the incorporation of the company.
2. The provision of law relating to appointment and removal of auditor ensure the independence of **Auditors** (auditors / shareholders)
3. A **certified** (certified/ government) auditor is the only non-chartered accountant who can be appointed as the auditor of a company.
4. The auditor of a Government company is appointed by the **Comptroller and Auditor – General of India.**
5. any auditor appointed in a casual vacancy shall hold office until the **conclusion** of the next annual general meeting.

6. In the case of a company in which not less than 25% of the subscribed share capital is held by any of the specified financial institutions, the appointment of an auditor shall be by a **Special** resolution.
7. A partnership firm **can be** (can be/ cannot be) appointed as a statutory auditor of limited company.
8. If a casual vacancy in the office of auditor arises by his resignation it should only be filled by the company in a **General** meeting.
9. The approval of the Central Government **is not** (is / is not) required for the removal of first auditor.
10. a person who has given any guarantee in connection with the loan of any third persons to the company for an amount exceeding one thousand rupees **is not** (is/ is not) qualified to be appointed as an auditor of that company.
11. A director or a member of the private company **is not** (is/ is not) qualified to be appointed as an auditor of that company

Q.3 MATCH THE FOLLOWING COLUMNS:

Column A	Column B
1. First Auditor	a) C & AG
2. Re-appointment of Auditor	b) Must be approved by Central Government
3. Re-appointment of Auditor when 25% share holding with specified financial institutions	c) Board of Directors
4. Failure of shareholders to re-appoint auditor	d) Special Resolution
5. Auditor of Government Company	e) Need not be approved by Central Govt.
6. Removal of first auditor appointed by Board	f) Shareholders at Annual General Meeting
7. Removal of subsequent auditor by shareholders	g) Central Government

Ans: 1 – (c); 2 – (f); 3 – (d); 4 – (g); 5 – (a); 6 – (e); 7 – (b).

Q.4 STATE WHETHER TRUE OR FALSE

1. Section 226 of Companies Act, 1956 states that any chartered accountant, whether in practice or not, can be appointed as the auditor of a company. **False**
2. Section 226 of the Companies Act, 1956 states that a firm whereof the majority of partners are Chartered Accountants practicing in India may be appointed as an auditor by its firm name. **False**
3. A body corporate whereof all the members are Chartered Accountants practicing in India may be appointed as an auditor a company. **False**
4. An officer or employee of the company who is a Chartered Accountant practicing in India may be appointed as an auditor of the company. **False**
5. A Chartered Accountant practicing in India who is a partner of an officer or employee of the company maybe appointed as an auditor of the company. **False**
6. A debtor of the company for an amount exceeding one thousand rupees cannot be appointed as the auditor of a company. **True**
7. A creditor of the company for an amount exceeding one thousand rupees cannot be appointed as the auditor of a company. **False**
8. A shareholder of the company cannot be appointed as the auditor of a company. **True**
9. A shareholders of the company holding shares of less than one thousand rupees can be appointed as the auditor of a company. **False**

10. The first auditors of a company are appointed by the directors in the first of the Board of Directors to be held within 30 days of obtaining the certificate of commencement of the company.

False

11. The first auditor of a company are appointed by the shareholders in the first meeting of the members to be held within 30 days of the date of incorporation of the company. **False**

12. The auditor of a Government company is appointed by the shareholders. **False**

13. The auditor of a Government company is appointed by the Comptroller and Auditor-General of India. **True**

14. Any casual vacancy in the post of an auditor shall be filled by the company in a general meeting. **False**

15. Where a vacancy is caused due to the death of an auditor, the vacancy may be filled by the Board of directors. **True**

16. When one of the two joint auditors resigns, the remaining auditor cannot continue to act as the auditor. **False**

17. In the case of a company in which not more than 25% of the paid-up-share capital is held by any of the specified financial institutions, the appointment of an auditor shall be made by a special resolution. **False**

18. In the case of a company in which not less than 75% of the subscribed share capital is held by any of the specified financial institutions the appointment of an auditor shall be made by a special resolution. **False**

19. The first auditor, appointed by the board of directors, can be removed by the Board of Director before the expiry of his term, without obtaining the previous approval of the shareholders. **False**

20. The first auditor, appointed by the board of directors, can be removed by the shareholders at a general meeting before the expiry of his term, only after obtaining the previous approval of the central government. **False**

21. The first auditor, appointed by the shareholders, can be removed by the Board of Directors before the expiry of his term, after obtaining the previous approval of the central government. **False**

22. Any auditor, other than the first auditor, can be removed before the expiry of his term by the company only at a general meeting, after passing a special resolution. **False**

23. An auditor can be removed only by the authority (Board Shareholders or Central Government) which appointed him. **False**

24. Every company auditor is a chartered accountant but every chartered accountant cannot be an auditor of a company. **True**

25. An auditor must retire once he attains the age of 60. **False**

26. If the auditor is inefficient, directors can change him even before his term is over. **False**

27. A partner of a firm whereof all the partners are Chartered Accountants practicing in India may be appointed as an auditor in his individual name. **False**

28. Any resolution limiting the powers of the auditor will be void. **True**

29. Every auditor of a company shall have a right of access only to those books and accounts and vouchers of the company, kept at the registered office of the company. **False**

30. Every auditor of a company shall have a right of access to only those books and accounts and vouchers of the company prepared after the date of his appointment. **False**

31. Every auditor of a company shall have a right of access to the books and accounts and vouchers of the company only after the end of the financial year. **False**

32. Once a separate branch auditor is appointed the company auditor cannot visit the branch office. **False**

33. Once a separate branch auditor is appointed the company the auditor cannot have a right of access to the books and vouchers of the company maintained at the branch office. **False**

34. The auditor shall be entitled to vote at any general meeting on any part of the business which concerns him as auditor. **False**
35. The first auditor appointed by the board of directors can be removed by the board at its subsequent meeting. **False**
36. Government companies are also considered for the ceiling on number of audits. **False**
37. Whoever appoints the auditor, the remuneration is always fixed by the shareholders. **False**
38. An auditor can be removed only after a special resolution to this effect is approved by the shareholders in a general meeting. **False**
39. The observations or comments of the auditors which have adverse effect on the functioning of the company shall be printed in the auditors report in capital letters. **False**
40. An auditors can be appointed as first auditor of a newly formed company simply because his name has been stated in the Articles of Association. **False**