PAPER – 6 : AUDITING AND ASSURANCE

*Question No.**1** is compulsory.*

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

Question 1

State with reasons (in short) whether the following statements are correct or incorrect (Answer any seven)

(a) *An audit note book is usually a bound book in which temporary records of the auditor are available during the course of audit.*

(b) *If auditor purchased goods on credit from the company and company allowed auditor a period of credit, this does not disqualify him to be an auditor.*

(c) *A perceived opportunity to commit fraud may exist when an individual believes internal control can be overridden.*

(d) *Control environment can prevent, detect and correct a material misstatement.*

(e) *An unexplained decrease in GP Ratio may result due to fictitious sales.*

(f) *In case of disclosure of accounting policies, in which situations an auditor will qualify his audit report?*

(g) *Entering into contracts with persons who are directors of the company or related to or associated with the directors can be sanctioned by shareholders at General Meeting,*

(h) *When the auditor has determined that an assessed risk of material misstatement at the assertion level is a significant risk, the auditor shall perform analytical procedure.*

(7 x 2 =14 Marks)

Answer

(a) **Incorrect:** An audit note book is usually a bound book in which a large variety of matters observed during the course of audit are recorded. It is thus a part of the permanent record of the auditor available for reference later on, if required.

(b) **Incorrect:** Where an auditor purchases goods or services from a company audited by him on credit he is definitely indebted to the company and if at any point of time, the amount outstanding exceeds rupees five lakh he is disqualified for appointment as an auditor of the company and has to vacate his office. It will not make any difference if the company allows him the period of credit as it allows to other customers in the normal business. He, in fact, in such a case also has become indebted to the company and consequently has to vacate his office.

(c) **Correct:** A perceived opportunity to commit fraud may exist when an individual believes internal control can be overridden, for example, because the individual is in a position of trust or has knowledge of specific deficiencies in internal control.

Individuals may be able to rationalize committing a fraudulent act. Some individuals possess an attitude, character or set of ethical values that allow them knowingly and intentionally to commit a dishonest act. However, even otherwise honest individuals can commit fraud in an environment that imposes sufficient pressure on them.

(d) **Incorrect:** The control environment in itself does not prevent, or detect and correct, a material misstatement. It may, however, influence the auditor's evaluation of the effectiveness of other controls (for example, the monitoring of controls and the operation of specific control activities) and thereby, the auditor's assessment of the risks of material misstatement.

(e) **Incorrect:** A fictitious sale will increase the GP Ratio, instead of decreasing it. GP ratio normally comes down if there are unrecorded sales or reversal of fictitious sale entries recorded in the previous year or fictitious purchase or decrease in closing stock.

(f) **As per AS-1 –** Disclosure of Accounting Policies, in the case of a company, auditors should quality their audit reports in case –

(i) accounting policies required to be disclosed under Schedule III of the Companies Act, 2013 have not been disclosed, or

(ii) accounts have not been prepared on accrual basis, or

(iii) the fundamental accounting assumption of going concern has not been followed and this fact has not been disclosed in the financial statements, or

(iv) proper disclosures regarding changes in the accounting policies have not been made.

Where a company has been given a specific exemption regarding any of the matters stated above but the fact of such exemption has not been adequately disclosed in the accounts, the member should mention the fact of exemption in his audit report without necessarily making it a subject matter of audit qualification.

In view of the above, the auditor will have to consider different circumstances whether the audit report has to be qualified or only disclosures have to be given.

(g) **Incorrect:** Entering into contracts with persons who are directors of the company or related to or associated with the directors as are specified in Section 188 of the Act is included in number of other functions which are also carried out by the Board. Whereas some of the matters which only the shareholders can sanction at a general meeting like Appointment and fixation of remuneration of auditors in the annual general meeting - Section 139 and 142, declaration of dividends etc.

(h) **Incorrect:** When the auditor has determined that an assessed risk of material misstatement at the assertion level is a significant risk, the auditor shall perform substantive procedures that are specifically responsive to that risk. When the approach to a significant risk consists only of substantive procedures, those procedures shall include tests of details.

Question 2

(a) What are the matters which should be considered while developing an overall audit plan for the expected scope and conduct of audit? ***(4 Marks)***

(b) Define the concept of the term Benchmarking with relevant SA. What are the factors that may affect the identification of an appropriate benchmark? ***(4 Marks)***

(c) Mr. A is an auditor of a company. During the performance of audit, he found that an offence involving fraud has been committed against the company by an officer of the company. What procedure should be followed by Mr. A to report the matter to the Central Government? ***(3 Marks)***

(d) Explain the matters which should be included for factors relevant to the auditors' judgement about whether a control is relevant to the audit. ***(3 Marks)***

Answer

(a) Development of an Overall Plan: The auditor should consider the following matters in developing his overall plan for the expected scope and conduct of the audit-

(i) The terms of his engagement and any statutory responsibilities.

(ii) The nature and timing of reports or other communication.

(iii) The applicable legal or statutory requirements.

(iv) The accounting policies adopted by the client and changes in those policies.

(v) The effect of new accounting or auditing pronouncements on the audit.

(vi) The identification of significant audit areas.

(vii) The setting of materiality levels for audit purposes.

(viii) Conditions requiring special attention, such as the possibility of material error or fraud or the involvement of parties in whom directors or persons who are substantial owners of the entity are interested and with whom transactions are likely.

(ix) The degree of reliance he expects to be able to place on accounting system and internal control.

(x) Possible rotation of emphasis on specific audit areas.

(xi) The nature and extent of audit evidence to be obtained.

(xii) The work of internal auditors and the extent of their involvement, if any, in the audit.

(xiii) The involvement of other auditors in the audit of subsidiaries or branches of the client.

(xiv) The involvement of experts.

(xv) The allocation of work to be undertaken between joint auditors and the procedures for its control and review.

(xvi) Establishing and coordinating staffing requirements.

The auditor should document his overall plan. The form and extent of the documentation will vary depending on the size and complexity of the audit. A time budget, in which hours are budgeted for the various audit areas or procedures, can be an effective planning tool.

(b) **Concept of Benchmarking & factors affecting identification of benchmark:** As per SA 320, "Materiality in Planning and Performing an Audit ", determining materiality involves the exercise of professional judgment. A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole.

Factors that may affect the identification of an appropriate benchmark include the

following:

(a) The elements of the financial statements (for example, assets, liabilities, equity, revenue, expenses);

(b) Whether there are items on which the attention of the users of the particular entity's financial statements tends to be focused (for example, for the purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets);

(c) The nature of the entity, where the entity is at in its life cycle, and the industry and economic environment in which the entity operates;

(d) The entity's ownership structure and the way it is financed (for example, if an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings); and

(e) The relative volatility of the benchmark.

(c) **Reporting of frauds to Central Government for frauds committed by employee of the company: Reporting to the Central Government-** As per **section 143(12)** of the Companies Act, 2013 read with **Rule 13** of the Companies (Audit and Auditors) Rules, 2014, if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of ₹1 crore or above, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as prescribed.

Here, the auditor of the company is required to report the fraudulent activity to the Board or Audit Committee (as the case may be) within 2 days of his knowledge of fraud. Further, the company is also required to disclose the same in Board's Report. It may be noted that the auditor need not to report the Central Government in case the amount of fraud involved is less than ₹1 crore.

The manner of reporting the matter to the Central Government is as follows:

(a) the auditor shall report the matter to the Board or the Audit Committee, as the case may be, immediately but not later than 2 days of his knowledge of the fraud, seeking their reply or observations within 45 days;

(b) on receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government within 15 days from the date of receipt of such reply or observations;

(c) in case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of 45 days, he shall forward his report to the Central Government along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he has not received any reply or observations;

(d) the report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed Post followed by an e-mail in confirmation of the same;

(e) the report shall be on the letter-head of the auditor containing postal address, e-mail address and contact telephone number or mobile number and be signed by the auditor with his seal and shall indicate his Membership Number; and

(f) the report shall be in the form of a statement as specified in Form ADT-4.

(d) Controls Relevant to the Audit: Factors relevant to the auditor's judgment about whether a control, individually or in combination with others, is relevant to the audit may include such matters as the following:

(i) Materiality.

(ii) The significance of the related risk.

(iii) The size of the entity.

(iv) The nature of the entity's business, including its organisation and ownership characteristics.

(v) The diversity and complexity of the entity's operations.

(vi) Applicable legal and regulatory requirements.

(vii) The circumstances and the applicable component of internal control.

(viii) The nature and complexity of the systems that are part of the entity's internal control, including the use of service organisations.

(ix) Whether, and how, a specific control, individually or in combination with others, prevents, or detects and corrects, material misstatement.

Question 3

(a) State the requirements as stated in Schedule III to the Companies Act, 2013, related to disclosure of expenses in case of companies. ***(4 Marks)***

(b) Mention the indicators of doubtful and uncollectible debts, loans and advances which create doubts while examining the book debts. ***(4 Marks)***

(c) As an auditor we are aware that except for any physical losses that the goods may suffer during the manufacturing process or due to some extra-ordinary factors, e.g., fire or pilferage; there should be no difference in the quantities of opening inventory and the quantities purchased being equal to the quantities of goods sold and those held in inventory at the close of the year, however, there has not been any loss or leakage of goods in the process of trading.

What are the factors that the auditor should keep in mind which may give rise to discrepancy in the inventory? ***(3 Marks)***

(d) Differentiate between provision and Reserve. ***(3 Marks)***

Answer

(a) Requirements as stated in Schedule III to the Companies Act, 2013, related to disclosure of expenses in case of Companies are:

(i) A Company shall disclose aggregate of the following expenses separately on the face of the Statement of Profit and Loss-Item IV. Expenses:

(a) Cost of Materials Consumed

(b) Purchases of Stock-in-trade

(c) Changes in Inventories of Finished Goods, Work-in-progress and Stock-in-trade

(d) Employee Benefits Expense

(e) Finance Costs

(f) Depreciation and amortization expense

(g) Other Expenses

(ii) A Company shall disclose separately by way of notes on the face of the Statement of Profit and Loss additional information regarding aggregate expenses as under:-

(a) Consumption of stores and spare parts;

(b) Power and fuel;

(c) Rent;

(d) Repairs to buildings;

(e) Repairs to machinery;

(f) Insurance;

(g) Rates and taxes, excluding, taxes on income;

(h) Miscellaneous expenses.

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

(1) The terms of credit have been repeatedly ignored.

(2) There is stagnation, or lack of healthy turnover, in the account.

(3) Payments are being received but the balance is continuously increasing.

(4) Payments, though being received regularly are quite small in relation to the total outstanding balance.

(5) An old bill has been partly paid (or not paid), while later bills have been fully settled.

(6) The cheques received from the trade receivables have been repeatedly dishonoured.

(7) The debt is under litigation, arbitration, or dispute.

(8) The auditor becomes aware of unwillingness or inability of the trade receivable to pay the dues, e.g., a trade receivable has either become insolvent, or has closed down his business, or is not traceable.

(9) Amounts due from employees, which have not been repaid on termination of employment.

(10) Collection is barred by statute of limitation.

(c) Factors giving rise to discrepancy in the Inventory:

Except for any physical losses that the goods may suffer during the manufacturing process or due to some extra-ordinary factors, *e.g.,* fire or pilferage, there should be no difference in the quantities of opening inventory and the quantities purchased being equal to the quantities of goods sold and those held in inventory at the close of the year. It is the duty of the auditor to verify that there has not been any loss or leakage of goods in the process of trading. He should, therefore, reconcile the closing inventory with the opening inventory on taking into account the quantities of goods purchased and sold. If there is a discrepancy, he must locate the cause thereof.

Some of the factors which give rise to discrepancy in the inventory are stated below:

(i) Inclusion in the closing inventory of goods that should have been returned to suppliers and non-inclusion of goods returned by account receivables.

(ii) Inclusion in the closing inventory of goods received for sale on approval or on a consignment basis and, conversely, non-inclusion in the closing inventory of goods sent out for sale on approval or on consignment basis.

(iii) Failure to adjust the quantities of inventories lost by fire or given away as samples.

(iv) Failure to adjust any sales, the proceeds whereof have been misappropriated, or purchases, the bills in respect of which had not been received from the suppliers.

(v) Failure to include goods purchased that were in transit at the close of the year and to exclude goods which had been sold but not delivered.

(vi) Non-adjustment of the losses in weight of material in the process.

(d) Reserves and Provisions:

(i) Reserve is an appropriation of profit whereas provision is a charge against Profit.

(ii) Reserves are not intended to meet any liability, contingency or diminution in the value of assets. Provisions are made to provide for depreciation, renewal or a known liability or a disputed claim.

(iii) Reserves cannot be created unless there is a profit except revaluation reserve and capital subsidy. Provisions must be created whether or not there is profit.

(iv) Reserves are generally optional except in certain situations – Capital Redemption reserve, Debenture Redemption Reserve, etc. Provisions are not optional and have to be made as per generally accepted accounting principles.

(v) Reserves are shown on the liability side. Provisions for depreciation and provision for doubtful debts are shown as deduction from respective assets. Provision for liability is shown on the liability side.

Question 4

(a) CA X was indebted to ABC (P) Limited for a sum of ₹ 6,00,000 as on April 1, 2019. However, CA X having come to know that he might be appointed as auditor of the company, he repaid ₹ 1,00,000 on August 10, 2019. Later on, he was appointed as auditor of the company for the year ended March 31, 2020 at the Annual General Meeting held on August 11, 2019. Subsequently, one of the shareholders complains that the appointment of CA X as an auditor is invalid because he incurred disqualification under Section 141 of the Companies Act, 2013. Discuss. ***(4 Marks)***

(b) While drafting report of LK Ltd., what are the matter to be included by auditor in introductory paragraph? ***(4 Marks)***

(c) "When more persuasive audit evidence is needed regarding the effectiveness of a control, it may be appropriate to increase the extent of testing of the control as well as the degree of reliance on controls."

What are the matters, the auditor may consider in determining the extent of test of controls? ***(3 Marks)*** *(d) As per Companies (Accounts) Rules, 2014 read with second proviso to section 128(1) of Companies Act, 2013, companies can keep their books of accounts and other relevant paper in electronic form. What are the responsibilities of companies at the time of filling of annual financial statement to registrar?* ***(3 Marks)***

Answer

(a) Indebtedness to the Company: According to the section 141(3)(d)(ii) of the Companies Act, 2013, a person who is indebted to the company for an amount exceeding ₹ 5,00,000 shall be disqualified to act as an auditor of such company and he should vacate his office of auditor when he incurs this disqualification subsequent to his appointment.

However, where the person has liquidated his debt before the appointment date, there is no disqualification to be construed for such appointment.

In the given case, CA. X was appointed as an auditor of ABC (P) Ltd. for the year ended 31.03.2020 at the Annual General Meeting held on 11.08.2019. He repaid ₹1,00,000 to the company on 10.8.2019 i.e., before the date of his appointment and balance of ₹ 5,00,000 as indebtedness is within prescribed limit as per section 141(3)(d)(ii)

Hence, the appointment of CA. X as an auditor is valid and the shareholder's complaint is not correct.

(b) Introductory Paragraph of Auditor's report:

The introductory paragraph in the auditor's report shall-

(i) Identify the entity whose financial statements have been audited;

(ii) State that the financial statements have been audited;

(iii) Identify the title of each statement that comprises the financial statements;

(iv) Refer to the summary of significant accounting policies and other explanatory information; and

(v) Specify the date or period covered by each financial statement comprising the financial statements.

(c) Matters to be considered in determining extent of test of control: When more persuasive audit evidence is needed regarding the effectiveness of a control, it may be appropriate to increase the extent of testing of the control as well as the degree of reliance on controls. Matters the auditor may consider in determining the extent of tests of controls include the following:

(i) The frequency of the performance of the control by the entity during the period.

(ii) The length of time during the audit period that the auditor is relying on the operating effectiveness of the control.

(iii) The expected rate of deviation from a control.

(iv) The relevance and reliability of the audit evidence to be obtained regarding the operating effectiveness of the control at the assertion level.

The extent to which audit evidence is obtained from tests of other controls related to the assertion.

(d) Filing of annual financial statement to registrar: The company is required to intimate to the Registrar on an annual basis at the time of filing of financial statement, the following-

(i) The name of the service provider;

(ii) The internet protocol address of service provider;

(iii) The location of the service provider (wherever applicable);

(iv) Where the books of account and other books and papers are maintained on cloud, such address as provided by the service provider.

Question 5

(a) What is the procedure adopted by an auditor in respect of leasing transactions entered by the leasing company? ***(4 Marks)***

(b) The effectiveness of an audit depends on reporting results to the proper authority, Explain the statement along with the role of C&AG. ***(4 Marks)***

(c) Some municipal corporation can appoint their own external auditors.

What are the objectives of audit in this case? ***(3 Marks)***

(d) Categorize the public enterprises which are required to maintain commercial accounts.

(3 Marks)

Answer

(a) Audit of leasing transactions by the leasing company: In respect of leasing transaction entered into by the leasing company, the following procedures may be adopted by the auditor:

1. The object clause of leasing company to see that the goods like capital goods, consumer durables etc. in respect of which the company can undertake such activities. Further, to ensure that whether company can undertake financing activities or not.

2. Whether there exists a procedure to ascertain the credit analysis of lessee like lessee's ability to meet the commitment under lease, past credit record, capital strength, availability of collateral security, etc.

3. The lease agreement should be examined and the following points may be noted:

   (i) the description of the lessor, the lessee, the equipment and the location where the equipment is to be installed. (The stipulation that the equipment shall not be removed from the described location except for repairs. For the sake of identification, the lessor may also require plates or markings to be attached to the equipment).

(ii) the amount of tenure of lease, dates of payment, late charges, deposits or advances etc. should be noted.

(iii) whether the equipment shall be returned to the lessor on termination of the agreement and the cost shall be borne by the lessee.

(iv) whether the agreement prohibits the lessee from assigning the subletting the equipment and authorises the lessor to do so.

4. Examine the lease proposal form submitted by the lessee requesting the lessor to provide him the equipment on lease.

5. Ensure that the invoice is retained safely as the lease is a long-term contract.

6. Examine the acceptance letter obtained from the lessee indicating that the equipment has been received in order and is acceptable to the lessee.

7. See the Board resolution authorising a particular director to execute the lease agreement has been passed by the lessee.

8. See that the copies of the insurance policies have been obtained by the lessor for his records.

(b) Role of C& AG: The effectiveness of an audit depends on reporting results to the proper authority so that appropriate action may be taken to rectify the irregularities or impropriety where possible or to prevent re-occurrence. The right as also the obligation to report on the results of audit findings is inherent to the institution of the Auditor General and is usually safeguarded in the Constitution and related enactments. Article 151 of the Indian Constitution enjoins that the C&AG shall report on the accounts of the Union and of each of the States to the President or the Governor concern and the letter shall cause the report to be laid before the legislatures. The reports should not only be presented to the legislatures but thereafter also publicised adequately in order to create a proper climate of public opinion for taking remedial action where necessary, on the findings of the Auditor General. This may also constitute a more effective safeguard in the future.

In India the reporting is factual and the conclusion are left to be drawn by the reader. This is presumably to ensure total objectivity. Nothing debars C&AG from making recommendations in the audit report but traditionally this has been left to be done by the Public Accounts Committee. The overall Indian position regarding reporting standards contained in instructions issued by the C&AG on the subject. Experience and professional judgement ultimately determine what is to be included in the audit reports. The auditor has to be a thorough professional and the audit reports have to be prepared with great skill for both the presentation and contents should compel readership.

(c) Objectives of Audit – if external auditor appointed by Municipal Corporations: The external control of municipal expenditure is exercised by the state governments through the appointment of auditors to examine municipal accounts. The municipal corporations of Delhi, Mumbai and a few others have powers to appoint their own auditors for regular external audit. The important objectives of audit are:

(i) reporting on the fairness of the content and presentation of financial statements;

(ii) reporting upon the strengths and weaknesses of systems of financial control;

(iii) reporting on the adherence to legal and/or administrative requirements;

(iv) reporting upon whether value is being fully received on money spent; and

(v) detection and prevention of error, fraud and misuse of resources.

(d) Classification of Commercial Accounts maintained by Public Enterprise:

Public enterprises are required to maintain commercial accounts and are generally classified under three categories—

(i) departmental enterprises engaged in commercial and trading operations, which are subject to the same laws, financial and other regulations as other government departments and agencies.

(ii) statutory bodies, corporations, created by specific statutes mostly financed by government in the form of loans, grants, etc.; and

(iii) government companies set up under the Companies Act, 2013.

Question 6

(a) ABC Pvt. Ltd. have outstanding of ₹ 25.50 crore. One of the directors said that it becomes necessary to appoint an internal auditor for which another director not agreeing, Advise the company in this regard. ***(4 Marks)***

(b) XY & Co is the internal auditor of PQR Ltd. Explain how the statutory auditor of PQR Ltd. can evaluate whether the work of XY & Co is likely to be adequate for the purpose of audit? ***(4 Marks)***

OR

"Irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure." Discuss.

(c) What are the criteria for classification of liability as current as per Part 1, Schedule III of the Companies Act, 2013? ***(3 Marks)***

(d) The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. As an auditor, explain the points to be kept in mind while making an audit plan. ***(3 Marks)***

Answer

(a) Applicability of Provisions of Internal Audit: As per section 138 of the Companies Act, 2013, following class of companies (prescribed in Rule 13 of Companies (Accounts) Rules, 2014) shall be required to appoint an internal auditor or a firm of internal auditors, namely every private company having-

(1) turnover of two hundred crore rupees or more during the preceding financial year; or

(2) outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more at any point of time during the preceding financial year.

In the instant case, ABC Pvt. Ltd. is a private company having outstanding of ₹ 25.50 crores during the preceding financial year which is less than prescribed limit for the applicability of provisions on internal audit.

Hence, the company has no statutory obligation to appoint an Internal Auditor and mandatorily conduct internal audit. Consequently, the contention of the director of the company regarding mandatorily appointment of internal auditor is not tenable.

(b) Evaluating the Internal Audit Functions: As per SA – 610, "Using the Work of an Internal Auditor", in determining whether the work of the internal auditors is likely to be adequate for purposes of the audit, the external auditor shall evaluate:

(i) The objectivity of the internal audit function;

(ii) The technical competence of the internal auditors;

(iii) Whether the work of the internal auditors is likely to be carried out with due professional care; and

(iv) Whether there is likely to be effective communication between the internal auditors and the external auditor.

Alternative Solution:

As per SA 610, "Using the work of Internal Auditors", the external auditor shall determine whether the work of the internal audit function can be used for purposes of the audit by evaluating the following:

(i) The extent to which the internal audit function's organizational status and relevant policies and procedures support the objectivity of the internal auditors

(ii) The level of competence of the internal audit function; and

(iii) Whether the internal audit function applies a systematic and disciplined approach, including quality control.

OR

(b) Designing and Performing Substantive Procedures: Irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure.

1. This requirement reflects the facts that:

   (i) the auditor's assessment of risk is judgmental and so may not identify all risks of material misstatement; and

   (ii) there are inherent limitations to internal control, including management override.

2. Depending on the circumstances, the auditor may determine that:

   (i) Performing only substantive analytical procedures will be sufficient to reduce audit risk to an acceptably low level. For example, where the auditor's assessment of risk is supported by audit evidence from tests of controls.

   (ii) Only tests of details are appropriate.

   (iii) A combination of substantive analytical procedures and tests of details are most responsive to the assessed risks.

3. Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. SA 520, "Analytical Procedures" establishes requirements and provides guidance on the application of analytical procedures during an audit.

4. The nature of the risk and assertion is relevant to the design of tests of details. For example, tests of details related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence. On the other hand, tests of details related to the completeness assertion may involve selecting from items that are expected to be included in the relevant financial statement amount and investigating whether they are included.

5. Because the assessment of the risk of material misstatement takes account of internal control, the extent of substantive procedures may need to be increased when the results from tests of controls are unsatisfactory.

6. In designing tests of details, the extent of testing is ordinarily thought of in terms of the sample size. However, other matters are also relevant, including whether it is more effective to use other selective means of testing.

(c) Classification of Current Liability: As per Part I of Division I of Schedule III, a liability shall be classified as current when it satisfies any of the following criteria:

(a) it is expected to be settled in the company's normal operating cycle;

(b) it is held primarily for the purpose of being traded;

(c) it is due to be settled within twelve months after the reporting date; or

(d) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

All other liabilities shall be classified as non-current.

(d) Points to be kept in mind while making an audit plan: "The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client's business. Following points to be kept in mind while making an audit plan as an auditor:

(i) acquiring knowledge of the client's accounting systems, policies and internal control procedures;

(ii) establishing the expected degree of reliance to be placed on internal control;

(iii) determining and programming the nature, timing, and extent of the audit procedures to be performed; and

(iv) coordinating the work to be performed.

Plans should be further developed and revised as necessary during the course of the audit."

Alternative Solution:

Following points to be kept in mind while making an audit plan as an auditor:

(i) The terms of his engagement and any statutory responsibilities.

(ii) The nature and timing of reports or other communication.

(iii) The applicable legal or statutory requirements.

(iv) The accounting policies adopted by the client and changes in those policies.

(v) The effect of new accounting or auditing pronouncements on the audit.

(vi) The identification of significant audit areas.

(vii) The setting of materiality levels for audit purposes.

(viii) Conditions requiring special attention, such as the possibility of material error or fraud or the involvement of parties in whom directors or persons who are substantial owners of the entity are interested and with whom transactions are likely.

(ix) The degree of reliance he expects to be able to place on accounting system and internal control.

(x) Possible rotation of emphasis on specific audit areas.

(xi) The nature and extent of audit evidence to be obtained.

(xii) The work of internal auditors and the extent of their involvement, if any, in the audit.

(xiii) The involvement of other auditors in the audit of subsidiaries or branches of the client.

(xiv) The involvement of experts.

(xv) The allocation of work to be undertaken between joint auditors and the procedures for its control and review.

(xvi) Establishing and coordinating staffing requirements.