

PAPER – 3 : ADVANCED AUDITING AND PROFESSIONAL ETHICS

Question No. 1 is compulsory

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

Question 1

Answer the following:

- (a) As per CARO 2016, the auditor is required to report “whether the company is required to be registered under Section 45-IA of the Reserve Bank of India Act, 1934 and if so, whether the registration has been obtained”. Mention the audit procedures and reporting for the same. **(5 Marks)**
- (b) Before commencing an audit of consolidated financial statements, the auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. What are the important aspects that an auditor should consider in audit plan? **(5 Marks)**
- (c) P, a Chartered Accountant availed a loan against his securities held as investments from a nationalized bank. He issued 2 cheques towards repayment of the said loan. Both the cheques were returned unpaid by the bank with the remark “Refer to Drawer”. Comment with reference to the Chartered Accountants Act, 1949 as amended by the Chartered Accountants (Amendment) Act, 2006 and Schedules thereto. **(4 Marks)**

Answer

- (a) **Compliance with CARO 2016:** As per Paragraph 3(xvi) of CARO 2016, the auditor is required to report that “Whether the company is required to be registered under section 45-IA of the Reserve Bank of India Act, 1934 and if so, whether the registration has been obtained.” The auditor is required to examine whether the company is engaged in the business which attract the requirements of the registration. The registration is required where the financing activity is a principal business of the company.

Audit Procedures and Reporting:

- (1) The auditor should examine the transactions of the company with relation to the activities covered under the RBI Act and directions related to the Non-Banking Financial Companies.
- (2) The financial statements should be examined to ascertain whether company's financial assets constitute more than 50 per cent of the total assets and income from financial assets constitute more than 50 per cent of the gross income.
- (3) Whether the company has net owned funds as required for the registration as NBFC.
- (4) Whether the company has obtained the registration as NBFC, if not, the reasons should be sought from the management and documented.
- (5) The auditor should report incorporating the following:-
 - (i) Whether the registration is required under section 45-IA of the RBI Act, 1934.

- (ii) If so, whether it has obtained the registration.
- (iii) If the registration not obtained, reasons thereof.

(b) Auditing the Consolidation: Before commencing an audit of consolidated financial statements, the auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. The auditor should make plans, among other things, for the following:

- (i) Understanding of the group structure and group-wide controls including assessment of Information Technology (IT) system and related general and applications IT related controls (manual and automated) for consolidation process;
- (ii) Understanding of accounting policies of the parent and its components as well as of the consolidation process including the process of translation of financial statements of foreign components;
- (iii) Determining and programming the nature, timing, and extent of the audit procedures to be performed based on the assessment of the risk of material misstatement in the consolidation process;
- (iv) Determining the extent of use of other auditor's work in the audit; and
- (v) Coordinating the work to be performed.

A parent which presents consolidated financial statements is required to consolidate all its components in the consolidated financial statements other than those for which exceptions have been provided in the relevant accounting standards under the applicable financial reporting framework.

The auditor should obtain a listing of all the components included in the consolidated financial statements and review the information provided by the management of the parent identifying the components. The auditor should verify that all the components have been included in the consolidated financial statements unless these components meet criterion for exclusion.

(c) Bringing Disrepute to the Profession: A Chartered Accountant is expected to maintain the highest standard of integrity even in his personal affairs and any deviation from these standards, even in his non-professional work would expose him to disciplinary action.

A member is liable to disciplinary action under Section 21 of the Chartered Accountants Act, if he is found guilty of any professional or "Other Misconduct".

As per Clause (2) of Part IV of the First Schedule to the Chartered Accountants Act, 1949, a member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he in the opinion of the Council, brings disrepute to the profession or the Institute as a result of his action whether or not related to his professional work.

The question whether a particular act or omission constitutes "other misconduct" should be based on fact and circumstances of each case.

Under Negotiable Instruments Act 1881, where any cheque drawn by a person for the discharge of any liability is returned by the bank unpaid, either for insufficiency of funds or the cheque amount exceeds the arrangements made by the drawer of the cheque, the drawer of such cheque shall be deemed to have committed an offence.

In the given case the cheque was dishonoured with the remark "refer to drawer". However, such dishonour need not necessarily be only due to insufficiency of funds.

If it is proved that the cheques were dishonoured due to insufficiency of funds, the CA P would be held guilty of "other misconduct".

Question 2

Answer the following:

- (a) *The provisions of Sec. 269SS of Income Tax Act, 1961 are not applicable to some organisations. Mention those organisations. (5 Marks)*
- (b) *A, a practicing Chartered Accountant, is appointed to conduct peer review of another practicing unit. Which areas A should review in the assessment of independence of the practicing unit? (5 Marks)*
- (c) *M/s PQR, a firm of Chartered Accountants responded to a tender from a State Government for computerization of land revenue records. For this purpose, the firm also paid ₹ 50,000 as earnest deposit as part of the terms of the tender. Comment with reference to the Chartered Accountants Act, 1949, Code of Ethics and Schedules to the Act. (4 Marks)*

Answer

- (a) As per the proviso to section 269SS, the provisions of section 269SS shall not apply to any loan or deposit taken or accepted from, or any loan or deposit taken or accepted by-
 - (i) Government;
 - (ii) any banking company, post office savings bank or co-operative bank;
 - (iii) any corporation established by a Central, State or Provincial Act;
 - (iv) any Government company as defined in section 2(45) of the Companies Act, 2013; Section 617 of the Companies Act, 1956 has been replaced with section 2(45) in the Companies Act, 2013 with effect from 1.4.2014.
 - (v) such other institution, association or body or class of institutions, associations or bodies which the Central Government may, for reasons to be recorded in writing, notify in this behalf in the Official Gazette.

The auditor should maintain the prescribed information in his working papers for the purpose of reporting against this clause in the format provided in the e-filing utility. These particulars need not be given in case of a Government Company, a banking company or a corporation established by a Central, State or Provincial Act.

- (b) **Review in the Assessment of Independence of the Practicing Unit** – The reviewer should carry out the compliance review of the five general controls, i.e., independence, maintenance of professional skills and standards, outside consultation, staff supervision and development and office administration and evaluate the degree of reliance to be placed upon them. The degree of reliance will, ultimately, affect the attestation service engagements to be reviewed.

A, a practicing Chartered Accountant should review following controls in respect of assessment of independence of the practicing unit:

- (i) Does the practice unit have a policy to ensure independence, objectivity and integrity, on the part of partners and staff? Who is responsible for this policy?
 - (ii) Does the practice unit communicate these policies and the expected standards of professional behaviour to all staff?
 - (iii) Does the practice unit monitor compliance with policies and procedures relating to independence?
 - (iv) Does the practice unit periodically review the practice unit's association with clients to ensure objectivity and independence?
- (c) **Responding to Tenders:** Clause (6) of Part I of the First Schedule to the Chartered Accountants Act, 1949 lays down guidelines for responding to tenders, etc. As per the guidelines if a matter relates to any services other than audit, members can respond to any tender. Further, in respect of a non-exclusive area, members are permitted to pay reasonable amount towards earnest money/security deposits.

In the instance case, since computerization of land revenue records does not fall within exclusive areas for chartered accountants, M/s PQR can respond to tender as well as deposit ₹ 50,000 as earnest deposit and shall not have committed any professional misconduct.

Question 3

- (a) *Comment on the disclosure compliances from the following information in respect of the financial statements of PP Ltd. which have to be drawn up in compliance with Ind AS, under Division II of Schedule III to the Companies Act, 2013.*
- (i) *Insurance claims receivable is classified as Non-current Trade Receivables.*
 - (ii) *Foreign exchange differences relating to foreign currency borrowings to the extent not capitalized in accordance with Ind AS 23 is disclosed under other expenses.*
 - (iii) *Interest on shortfall in payment of advance income-tax is clubbed with the current tax disclosed on the face of the statement to profit and loss account.*
 - (iv) *Share based payment to employees in accordance with Ind AS 102 are disclosed under finance cost.*

- (v) *Expenditure on CSR activities has been disclosed in the notes to the cash flow statement.* **(5 Marks)**
- (b) *PDJ Ltd. has engaged an actuary to ascertain actuarial valuation of defined benefit obligations viz. Gratuity and Leave Encashment liabilities. As an auditor of PDJ Ltd. you would like to use the report of the actuary as audit evidence. How would you evaluate the work of the actuary?* **(5 Marks)**
- (c) *Mr. KK is a contractor dealing in food catering, flower decorating and light decorating activities. He has received contract in respect of food catering and flower decorating from one NGO for holding Annual Talent evening event to celebrate completion of 25 years of their establishment. For the said event Mr. KK has received in cash ₹ 1,85,000 for food catering and ₹ 1,25,000 for flower decoration. As a tax auditor how would you deal and report on the above?* **(4 Marks)**

Answer**(a) Division II of Schedule III of the Companies Act, 2013:**

- (i) Insurance claims receivable should be classified as **"other financial assets"** and **each such item should be disclosed nature-wise**. Thus, disclosure of insurance claims receivable by the company under Non-current Trade Receivable is **not in compliance** with Division II of Schedule III of the Companies Act, 2013.
- (ii) Foreign exchange differences relating to foreign currency borrowings to the extent not capitalized in accordance with Ind AS 23 can be presented under the head **finance costs**. Thus, disclosure of foreign exchange difference relating to foreign currency borrowing to the extent not capitalised under other expenses is **not in compliance** with Division II of Schedule III of the Companies Act, 2013.
- (iii) Any interest on shortfall in payment of advance income-tax is in the nature of finance cost and hence should not be clubbed with the Current tax. The same should be **classified as Interest expense under finance costs**. However, such amount should be **separately disclosed**. Thus, disclosure of interest of shortfall by the company is **not in compliance** with Division II of Schedule III of the Companies Act, 2013.
- (iv) Share based payment to employees in accordance with Ind AS 102 should be disclosed under the head **Employee Benefits Expense**. Therefore, disclosure of share based payment to employees under Finance Cost is **not in compliance** with Division II of Schedule III of the Companies Act, 2013.

Expenditure incurred on corporate social responsibility activities it is recommended that all expenditure on CSR activities, that qualify to be recognised as expense should **be recognised as a separate line item as 'CSR expenditure'** in the statement of profit and loss. Further, the relevant note should **disclose the break-up of various heads** of expenses included in the line item 'CSR expenditure'. Thus, disclosure of expenditure on CSR Activities in notes to the cash flow statement is **not in compliance** with Division II of Schedule III of the Companies Act, 2013.

(b) Evaluating the Work of Management's Expert: As per SA 500 "Audit Evidence", when information to be used as audit evidence has been prepared using the work of a management's expert, the auditor shall, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes-

- (1) Evaluate the competence, capabilities and objectivity of that expert;
- (2) Obtain an understanding of the work of that expert; and
- (3) Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion.

The auditor may obtain information regarding the competence, capabilities and objectivity of a management's expert from a variety of sources, such as personal experience with previous work of that expert; discussions with that expert; discussions with others who are familiar with that expert's work; knowledge of that expert's qualifications; published papers or books written by that expert.

Aspects of the management's expert's field relevant to the auditor's understanding may include what assumptions and methods are used by the management's expert, and whether they are generally accepted within that expert's field and appropriate for financial reporting purposes.

The auditor may also consider the following while evaluating the appropriateness of the management's expert's work as audit evidence for the relevant assertion:

- (i) The relevance and reasonableness of that expert's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial statements;
 - (ii) If that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods; and
 - (iii) If that expert's work involves significant use of source data, the relevance, completeness, and accuracy of that source data.
- (c)** Section 269ST provides that no person shall receive sum of ₹ 2 lakh or more a) in aggregate from a person in a day; or b) in respect of a single transaction; or c) in respect of transactions relating to one event or occasion from a person otherwise than by an account payee cheque or an account payee demand draft or by use of electronic clearing system through a bank account.

Further, the tax auditor has the responsibility to verify the compliance with the provisions of 269T of the Income Tax Act.

Furthermore, the tax auditor is required to report under Clause 31 (ba) particulars of each receipt in an amount exceeding the limit specified in section 269ST, in aggregate from a person in a day or in respect of a single transaction or in respect of transactions relating

to one event or occasion from a person, during the previous year, where such receipt is otherwise than by a cheque or bank draft or use of electronic clearing system through a bank account:-

(i)	Name, address and Permanent Account Number (if available with the assessee) of the payer;
(ii)	Nature of transaction;
(iii)	Amount of receipt (in ₹);
(iv)	Date of receipt;

In the present case, Mr. KK, contractor dealing in food catering, flower decorating and light decorating activities, received in cash ₹ 1,85,000 for food catering and ₹ 1,25,000 for flower decoration from one NGO for holding one event, by way of cash which is exceeding prescribed amount of ₹ 2,00,000. Thus, tax auditor is required to report the same in compliance with Clause 31 (ba) of Form 3CD.

Question 4

- (a) As an auditor, how will you report under CARO in each of the following situation?
- Since more than seven months, payment of electricity bills to company established under statute is outstanding.
 - The company had imported goods 5 years back and were placed in bonded warehouse till the end of financial year under Audit. The company has not paid import duty as goods have not been removed from such warehouse. The company has also not paid rent and interest expenditure payable on the amount of custom duty.
 - The company has received income tax assessment order along with demand notice from Assessing officer. The company has not paid dues payable as the same is not acceptable to the company. The company has neither preferred appeal against the order nor an application for rectification of mistake has been made. The company has just merely represented to the Assessing Officer.
 - The company in view of voluminous pay-roll data consistently follows the method of making lump sum deposit of estimated amount of ESI collections and adjust the excess or deficit against next following months' deposit and the difference of the said amount always remains insignificant. **(5 Marks)**
- (b) Clause 5F of form GSTR 9C under GST law requires disclosure of trade discounts which have been given effect to in the audited financial statements but which are not permissible as part of deductions from the value of supply under GST Laws.

As a GST auditor, which control checks you will perform for validation of the amounts reported under this head? **(5 Marks)**

- (c) While conducting audit of VED Ltd., you as an auditor are not only prevented in completing certain audit procedures but also are not able to obtain audit evidence even by performing alternative procedures. How you will deal with this situation? **(4 Marks)**

OR

- (c) What are the circumstances in which auditors are required to qualify their reports of companies for matters related to AS-I 'Disclosure of Accounting Policies'? **(4 Marks)**

Answer

- (a) **Clause (vii) (a) of Para 3 of CARO, 2016** requires the auditor to state in his report whether the company is **regular in depositing undisputed statutory dues** including provident fund, employees' state insurance, income-tax, sales-tax, Goods and Services Tax (with effect from July 1, 2017), service tax, duty of customs, duty of excise, value added tax, cess and any other statutory dues to the appropriate authorities and if not, the **extent of the arrears of outstanding statutory dues as on the last day of the financial year concerned for a period of more than six months** from the date they became payable, shall be indicated;

It is important to mention that any sum, which is to be regularly paid to an appropriate authority under a **statute (whether Central, State or Local or Foreign) applicable to the company, should be considered as a "statutory due"** for the purpose of this clause. In other words, obligation to pay a statutory due is created or arises out of a statute, **rather than being based on an independent contractual or legal relationship.**

- (i) Any sum payable to an electricity company as electricity **bill would not constitute a statutory due** despite the fact that such a company has been established under a statute. This is so because the **due has arisen on account of contract of supply of goods or services** between the parties. Thus, **reporting under CARO is not required** for electricity dues.
- (ii) In the given situation, payment of import duty where the goods had been imported five years back and were placed in the bonded warehouse and even till the end of the financial year under audit, the goods have not been removed from such warehouse. It may be noted that when the imported goods are lodged in a bonded warehouse, **the payment of import duty is to be made when the goods are removed from the bonded warehouse.** However, till the time the importer opts to remove the goods from the warehouse, **the importer is required to incur the rent and interest expenditure on the amount of customs duty payable.** Since the payment of the custom duty is not due in the current case, the question of regularity does not arise in respect of custom duty. However, it may be noted that the **interest and rent that are required to be incurred** under section 61 of the Customs Act, 1962 **would come under other statutory dues and the auditor would have to examine and comment upon the regularity of the company in depositing such interest and rent.**

- (iii) In the given situation, the company has received income tax assessment order along with demand notice from Assessing Officer and company has not paid such demand and is also not in agreement for the same. Further, the company has just merely represented before the Assessing Officer. The auditor is required to check whether **time limit for filing the appeal is expired / application for rectification of mistake or not**. In case time limit, for filing the appeal or application for rectification of mistake, **has expired disputed amount will become undisputed statutory due (as mere representation to the concerned Department shall not be treated as a dispute)**.

Further, the auditor is also required to ascertain whether such dues are outstanding for a period of **more than six months** from the date they became payable. Accordingly, after ensuring the above, **if the statutory dues are outstanding for more than six months the auditor is required to report the same under clause (vii)(a) of CARO, 2016**.

However, in case the statutory dues are not outstanding for a period of more than six months from the date they became payable the auditor is not required to report the same under CARO.

- (iv) It is possible that in a large company where there are a number of departments with separate payrolls and where payments are spread over a number of days, the collection of data regarding the provident fund/employees' state insurance collections and the company's contribution thereto may take some time. In order to ensure that deposit of the dues is made in time, the company may make lump-sum deposits of estimated amounts and adjust the excess or deficit against the following month's deposit. If this method is **consistently followed and the difference between the total dues and the lump-sum deposit is not significant, it need not be considered that dues have not been regularly deposited and no unfavorable comment is necessary. Thus, no reporting is required for the same under CARO**.
- (b) Clause 5F requires disclosure of trade discounts which have been given effect to, in the audited financial statements but which are not permissible as part of deductions from the value of supply under the GST Laws.

The following are the control checks that a person should perform for validation of the amounts reported under this head:

- (i) The valuation of trade discounts for the purposes of disclosures under this head, has to be clearly documented.
- (ii) The input tax credit reflected in GSTR-2A attributable to such trade discounts has to be maintained.
- (iii) The trade discount has to be demarcated between the supplies made in the erstwhile law and the GST regime.
- (iv) The customer agreements have to be scrutinised to determine the quantum of nonallowable discounts.

- (c) As per SA 705, "Modifications to the Opinion in the Independent Auditor's Report", if, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall request that management remove the limitation.

If management refuses to remove the limitation, the auditor shall communicate the matter to those charged with governance, unless all of those charged with governance are involved in managing the entity, and determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence.

If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall determine the implications as follows:

- (1) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive, the auditor shall qualify the opinion; or
- (2) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall:
 - (i) Withdraw from the audit, where practicable and possible under applicable law or regulation; or
 - (ii) If withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements.

If the auditor withdraws, before withdrawing, the auditor shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion.

or

- (c) While discharging their attest function, the members of the Institute may keep the following in mind with regard to mandatory Accounting Standards. As per **AS 1 - Disclosure of Accounting Policies**, in the case of a company, members should qualify their audit reports in case:
- (i) accounting policies required to be disclosed under Schedule III or any other provisions 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.

Question 5

- (a) *K Ltd. is intending to acquire M Ltd. Your firm of Chartered Accountants is appointed to conduct due diligence. While reviewing hidden liabilities list out any five areas which will be specifically examined by you in your due diligence exercise.* **(5 Marks)**
- (b) *A certificate of compliance of conditions of corporate governance has been issued by CEO of VAM Ltd. In the context of internal control, which points you as an auditor would like to ensure and examine in the said compliance certificate?* **(5 Marks)**
- (c) *Mr. P, a practicing Chartered Accountant did not reply within a reasonable time and without any cause to the letter received from the local Police Station, a public authority, soliciting his suggestions as regards some non-professional work. Comment with reference to Chartered Accountant Act, 1949.* **(4 Marks)**

Answer

- (a) In the given situation K Ltd. is intending to acquire M Ltd., in order to review hidden liabilities, firm of Chartered Accountants should pay attention to the following areas:
- ◆ The company may not show any show cause notices which have not matured into demands, as contingent liabilities. These may be material and important.
 - ◆ The company may have given "Letters of Comfort" to banks and Financial Institutions. Since these are not "guarantees", these may not be disclosed in the Balance sheet of the target company.
 - ◆ The Company may have sold some subsidiaries/businesses and may have agreed to take over and indemnify all liabilities and contingent liabilities of the same prior to the date of transfer. These may not be reflected in the books of accounts of the company.
 - ◆ Product and other liability claims; warranty liabilities; product returns/discounts; liquidated damages for late deliveries etc. and all litigation.
 - ◆ Tax liabilities under direct and indirect taxes.
 - ◆ Long pending sales tax assessments.
 - ◆ Pending final assessments of customs duty where provisional assessment only has been completed.
 - ◆ Agreement to buy back shares sold at a stated price.
 - ◆ Future lease liabilities.
 - ◆ Environmental problems/claims/third party claims.
 - ◆ Unfunded gratuity/superannuation/leave salary liabilities; incorrect gratuity valuations.
 - ◆ Huge labour claims under negotiation when the labour wage agreement has already expired.
 - ◆ Contingent liabilities not shown in books.

- (b) **Compliance Certificate as per Part B of Schedule II:** The Chief Executive Officer and the Chief Financial Officer shall certify to the Board that they accept responsibility for establishing and maintaining internal controls for financial reporting and that they have evaluated the effectiveness of the internal control systems of the listed entity pertaining to financial reporting and they have disclosed to the auditors and the Audit Committee, deficiencies in the design or operation of internal controls, if any, of which they are aware and the steps they have taken or propose to take to rectify these deficiencies.

In the context of internal controls, the auditor should ensure that:

- The management has instituted an internal control framework with respect to financial reporting controls. The framework should be examined in the context of the documentation created for each significant process in terms of the related risk and mitigating control;
 - He has further examined whether the assessment process followed for evaluation of controls is reasonable and there is a process by which significant deficiencies as well as steps taken to correct them is communicated to the Audit Committee and to the auditors; and
 - He should also examine whether a process exists in the listed entity whereby all significant changes in the accounting policies and in the system of internal controls are communicated to the Audit Committee and the auditors.
 - The auditor should examine the adequacy of the process followed for issuing the Compliance Certificate and should review the same in regard to matters stated above and the consideration of the same by the Audit Committee. For this purpose he should refer to the minutes of the Audit Committee meetings.
 - In situations where negative or adverse comments or exclusions/disclaimers are contained in the Compliance Certificate, the auditor should take cognizance of the same in the Audit Report and/or the certificate of compliance of conditions of corporate governance.
- (c) Section 21 of the Chartered Accountants Act, 1949 provides that a member is liable for disciplinary action if he is guilty of any professional or "Other Misconduct." Though the term "Other Misconduct" has not been defined in the said Act, this provision enables the Council to enquire into any misconduct of a member even if it does not arise out of his professional work.

This is considered necessary because a chartered accountant is expected to maintain the highest standards of integrity even in his personal affairs and any deviation from these standards even in his non-professional work, would expose him to disciplinary action. The Council has also laid down that among other things "non-replying within a reasonable time and without a good cause to the letter of the public authorities." would amount to "other misconduct".

In the given scenario, CA. P did not reply within a reasonable time and without any cause to the letter received from the local police station, a public authority regarding soliciting his suggestion as regards some non-professional work. Thus, in the instant case, CA. P would be liable for disciplinary action.

Question 6

- (a) *During the course of Audit of POP Ltd., you as an auditor while performing the audit procedures become aware of the existence of certain instances which seem to be an indication of non-compliance with Laws and regulations. List out any five such instances identified by you as an auditor, suggestive of non-compliance with Laws and regulations.*

(5 Marks)

- (b) *Under which circumstances the retiring Statutory Auditor of a company cannot be reappointed?*

(5 Marks)

- (c) *"In reviewing any System or Procedure, the management auditor must concern himself with its purpose as well as its design." Elucidate how you as a management auditor will study system and procedural functions?*

(4 Marks)

Answer

- (a) **Indications of Non-Compliance with Laws and Regulations:** As per SA 250, "Consideration of Laws and Regulations in an Audit of Financial Statements" when the auditor becomes aware of the existence of, or information about, the following matters, it may be an indication of non-compliance with laws and regulations:
- Investigations by regulatory organisations and government departments or payment of fines or penalties.
 - Payments for unspecified services or loans to consultants, related parties, employees or government employees.
 - Sales commissions or agent's fees that appear excessive in relation to those ordinarily paid by the entity or in its industry or to the services actually received.
 - Purchasing at prices significantly above or below market price.
 - Unusual payments in cash, purchases in the form of cashiers' cheques payable to bearer or transfers to numbered bank accounts.
 - Unusual payments towards legal and retainership fees.
 - Unusual transactions with companies registered in tax havens.
 - Payments for goods or services made other than to the country from which the goods or services originated.
 - Payments without proper exchange control documentation.
 - Existence of an information system which fails, whether by design or by accident, to provide an adequate audit trail or sufficient evidence.

- Unauthorised transactions or improperly recorded transactions.
 - Adverse media comment.
- (b)** A retiring auditor cannot be re-appointed at an annual general meeting, if-
- (i) he is disqualified for re-appointment.
 - (ii) he has given the company a notice in writing of his unwillingness to be re-appointed; and
 - (iii) a special resolution has been passed at that meeting appointing some other auditor or providing expressly that he shall not be re-appointed.
 - (iv) Where at any annual general meeting, other auditor is appointed or re-appointed.
- (c)** In reviewing any system or procedure, the management auditor must concern himself with its purpose as well as its design and then he must decide on its merits as the best serving the interests of the enterprise. A poor system or procedure may prevent the carrying out of the policy for which it was intended. A system may have outgrown its usefulness. The end result of a system or a procedure may be loose and may require improvement. In the study of the systems and procedural functions, the auditor should ask himself:
1. Is the function properly located in the organisation?
 2. Do the staff personnel have the necessary training and experience to perform the work?
 3. Has a definite programme been established and has been taken for its attentive accomplishment?
 4. Is productivity satisfactory?