

Intermediate Course: Group – II**(Mock Test Paper – Series : 2)****DATE: 25.10.2024****MAXIMUM MARKS: 100****TIMING: 3¼ Hours****PAPER 5 : AUDITING AND ETHICS****DIVISION – A (MULTIPLE CHOICE QUESTIONS)****Case Scenario 1 carries 10 Marks****Case Scenario 2 carries 08 Marks****Case Scenario 3 carries 06 Marks****General MCQs (3 MCQs x 2 Marks Each = 06 Marks)****Total 30 Marks****Ans. 1 to Ans. 5:****Case Scenario**

1. Ans. (b)
2. Ans. (a)
3. Ans. (d)
4. Ans. (b)
5. Ans. (d)

MCQ [5 MCQ of 2 Marks Each : Total 10 Marks]**Ans. 6 to Ans. 9:****Case Scenario**

6. Ans. (c)
7. Ans. (a)
8. Ans. (b)
9. Ans. (c)

MCQ [4 MCQ of 2 Marks Each : Total 8 Marks]**Ans. 10 to Ans. 12:****Case Scenario**

10. Ans. (c)
11. Ans. (a)
12. Ans. (b)

MCQ [3 MCQ of 2 Marks Each : Total 6 Marks]

13. Ans. (c)
14. Ans. (d)
15. Ans. (d)

MCQ [3 MCQ of 2 Marks Each : Total 6 Marks]**DIVISION B-DESCRIPTIVE QUESTIONS****QUESTION NO. 1 IS COMPULSORY.****ATTEMPT ANY FOUR QUESTIONS THE REMAINING FIVE QUESTIONS****Answer 1:**

- (a) The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions. Judging the significance of a matter requires an objective analysis of the facts and circumstances. Examples of significant matters include:

MITTAL COMMERCE CLASSES

- Matters that give rise to significant risks.
- Results of audit procedures indicating (a) that the financial statements could be materially misstated, or (b) a need to revise the auditor's previous assessment of the risks of material misstatement and the auditor's responses to those risks.
- Circumstances that cause the auditor significant difficulty in applying necessary audit procedures.
- Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter paragraph in the auditor's report.

{1 M Each}

Answer:

(b) When performing risk assessment procedures as required by SA 315, the auditor shall consider whether events or conditions exist that may cast significant doubt on the entity's ability to continue as a going concern.

In so doing, the auditor shall determine whether management has already performed a preliminary assessment of the entity's ability to continue as a going concern, and:

- (i) If such an assessment has been performed, the auditor shall discuss the assessment with management and determine whether management has identified events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern and, if so, management's plans to address them; or
- (ii) If such an assessment has not yet been performed, the auditor shall discuss with management the basis for the intended use of the going concern basis of accounting, and inquire of management whether events or conditions exist that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.

{1^{1/2} M}

{1^{1/2} M}

Answer:

(c) Computation of Drawing Power:

Computation of Drawing Power for CC A/c of S Ltd.

Particulars of current assets		Amount (Rs.)	DP Amt (Rs.)
(A) Stocks:			
Stocks at realizable value		50,000	
Less: Unpaid stocks:			
- Sundry creditors	15,000	15,000	
Paid for stocks		35,000	
Margin @ 20%		7,000	28,000
(B) Debtors:			
Total Debtors		45,000	
Less: Ineligible debtors		5,000	
Eligible debtors		40,000	
Margin @ 50%		20,000	20,000
Total Drawing Power			48,000

{1^{1/2} M}

{1^{1/2} M}

{1 M}

The sanctioned limit given in the Question is Rs. 45000 whereas drawing power as per the above working is Rs. 48,000. So, drawing power would be restricted to sanctioned limit i.e., Rs. 45,000.

Answer:

(d) Integrity of principal owners has to be considered before accepting an audit engagement in accordance with SA 220. In this regard, SA 220 states requirements on lines of SQC 1. SQC 1 clearly states that in cases where there are indications that the client might be involved in money laundering or other criminal activities, appointment should not be accepted. {1 M}

With regard to the integrity of a client, matters that the firm considers include, for example:

- The identity and business reputation of the client's principal owners, key management, related parties and those charged with its governance.
- The nature of the client's operations, including its business practices.
- Information concerning the attitude of the client's principal owners, key management and those charged with its governance towards such matters as aggressive interpretation of accounting standards and the internal control environment.
- Whether the client is aggressively concerned with maintaining the firm's fees as low as possible.
- Indications of an inappropriate limitation in the scope of work.
- Indications that the client might be involved in money laundering or other criminal activities.
- The reasons for the proposed appointment of the firm and non-reappointment of the previous firm.

{1 M
Each for
Any 2
Points}

In the instant case, there have been raids of NIA on suspected links with terror outfits which is a criminal activity. Further, raids by Enforcement Directorate also point towards money laundering. Therefore, proposed offer should not be accepted.

Answer 2:

(a) (i) The type of credit facilities referred to in above situation given by banks to meet working capital requirements of business which are repayable on demand are known as "cash credit facilities/overdraft" facilities. The amount of ₹1.85 crores outstanding as on 31st March, 2023 reflects borrowings of the company and it would be classified as "short-term borrowings" as loans repayable on demand from banks under current liabilities in balance sheet of the company. Borrowings shall further be sub-classified as secured. {1 M}

(ii) Specific disclosure requirements of short-term borrowings under Schedule III to Companies Act, 2013 in given situation are as under: -

- Nature of security i.e. primary security of current assets and collateral security of residential house belonging to a director shall be specified.
- As loans have been guaranteed by directors, the aggregate amount of such loans shall be disclosed.

{1 M}

To be disclosed as Additional Regulatory Information

Since the Company has borrowings from bank on the basis of security of current assets, it shall also disclose the following:-

- (a) whether quarterly returns or statements of current assets filed by the Company with banks or financial institutions are in agreement with the books of accounts.
- (b) if not, summary of reconciliation and reasons of material discrepancies, if any to be adequately disclosed.

{2 M}

Answer:

(b) Audit procedures performed by an auditor in order to ascertain that raw material and consumables are valued appropriately in accordance with generally accepted accounting policies and practices are as under:

1. Ascertain what elements of cost are included e.g. carriage inward, non-refundable duties etc.
2. If standard costs are used, enquire into basis of standards; how these are compared with actual costs and how variances are analyzed and accounted for/ treated in accounting records.
3. Test check cost prices used with purchase invoices received in the month(s) prior to counting.
4. Follow up valuation of all damaged or obsolete inventories noted during observance of physical counting with a view to establishing a realistic net realizable value.

{1 M
Each}

Answer:

(c) Audit Procedures that CA Q will follow to verify the existence, completeness, and valuation of provisions made are given hereunder:

Existence

1. Obtain a list of all provisions and compare them with balances in the ledger.
2. Inspect the underlying agreements like agreements with customers to assess warranty commitments, any legal and other claims on the entity i.e. litigations.

{1/2 M
Each}

Valuation

3. Wherever required, obtain the expert's report, calculation and underlying working for the provision amount. For example - for warranty involving complex calculations, some entities get that valued through an actuary. In such a case, the auditor may request the management to share the actuarial valuation report and in case of any matter under legal dispute, the auditor should request for assessment made by a legal expert in relation to likelihood of a liability devolving on the entity i.e. whether probable or possible or remote as defined above. The auditor should then verify the underlying assumptions used by the expert with the data shared by the management.

{1 M}

Completeness

4. Obtain the underlying working and the basis for each of the provisions made from the management and verify whether the same is complete and accurate.
5. The auditor shall obtain a written representation from the management that it has made all the provisions which were required to be made as per the recognized accounting principles.

{1/2 M
Each}

Answer:

(d) Audit testing done through this approach is more scientific than testing based entirely on the auditor's own judgment because it involves use of mathematical laws of probability in determining the appropriate sample size in varying circumstances. Statistical sampling has reasonably wide application where a population to be tested consists of a large number of similar items and more in the case of transactions involving compliance testing, trade receivables' confirmation, payroll checking, vouching of invoices and petty cash vouchers.

The advantages of statistical sampling may be summarized as follows -

- (1) The amount of testing (sample size) does not increase in proportion to the increase in the size of the area (universe) tested.
- (2) The sample selection is more objective and thereby more defensible.
- (3) The method provides a means of estimating the minimum sample size associated with a specified risk and precision.

{1 M
Each for
Any 3
Points}

- (4) It provides a means for deriving a "calculated risk" and corresponding precision (sampling error) *i.e.* the probable difference in result due to the use of a sample in lieu of examining all the records in the group (universe), using the same audit procedures.
- (5) It may provide a better description of a large mass of data than a complete examination of all the data, since non-sampling errors such as processing and clerical mistakes are not as large.

Answer 3:

(a) Standards on Auditing (SAs) apply in "audit of historical financial information" whereas Standards on Review Engagements (SREs) apply in "review of historical financial information". Standards on auditing apply in "audit" of historical financial information which is a reasonable assurance engagement whereas Standards on Review Engagements apply in "review" of historical financial information which is a limited assurance engagement only. {1 M}

"Historical financial information means" information expressed in financial terms in relation to a particular entity, derived primarily from that entity's accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

"Audit" and "review" are two different terms. Audit is a reasonable assurance engagement, and its objective is reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement. However, "review" is a limited assurance engagement, and its objective is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement. {1 M}

Standards on Auditing have been issued on wide spectrum of issues in the field of auditing including (but not limited to) overall objectives of independent auditor, audit documentation, planning an audit of financial statements, identifying and assessing risk of material misstatement, audit evidence, audit sampling, going concern and forming an opinion and reporting on financial statements. {1 M}

Some examples of Standards on Auditing are:

- (i) SA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing
- (ii) SA 230 Audit Documentation
- (iii) SA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment {1/2 M
- (iv) SA 500 Audit Evidence Each for
- (v) Revised SA 700 Forming an Opinion and Reporting on Financial Statements Any 2

Examples of Standards on Review engagements are:

- (i) SRE 2400 (Revised) Engagements to Review Historical Financial Statements
- (ii) SRE 2410 Review of Interim Financial Information Performed by the Independent Auditor of the Entity Points}

Answer:

(b) The control environment includes:

- (i) the governance and management functions and
- (ii) the attitudes, awareness, and actions of those charged with governance and management. {1/2 M
- (iii) The control environment sets the tone of an organization, influencing the control consciousness of its people. Each for

Elements of the Control Environment: Elements of the control environment that may be relevant when obtaining an understanding of the control environment include the following:

- (a) Communication and enforcement of integrity and ethical values – These are essential elements that influence the effectiveness of the design, administration and monitoring of controls.
- (b) Commitment to competence – Matters such as management’s consideration of the competence levels for particular jobs and how those levels translate into requisite skills and knowledge.
- (c) Participation by those charged with governance – Attributes of those charged with governance such as:
 - ◆ Their independence from management.
 - ◆ Their experience and stature.
 - ◆ The extent of their involvement and the information they receive, and the scrutiny of activities.
 - ◆ The appropriateness of their actions, including the degree to which difficult questions are raised and pursued with management, and their interaction with internal and external auditors.
- (d) Management’s philosophy and operating style – Characteristics such as management’s:
 - ◆ Approach to taking and managing business risks.
 - ◆ Attitudes and actions toward financial reporting.
 - ◆ Attitudes toward information processing and accounting functions and personnel.
- (e) Organisational structure – The framework within which an entity’s activities for achieving its objectives are planned, executed, controlled, and reviewed.
- (f) Assignment of authority and responsibility - Matters such as how authority and responsibility for operating activities are assigned and how reporting relationships and authorisation hierarchies are established.
- (g) Human resource policies and practices – Policies and practices that relate to, for example, recruitment, orientation, training, evaluation, counseling, promotion, compensation, and remedial actions.

{1 M
 Each for
 Any 3
 Points}

Answer:

(c) Written representation about management’s responsibilities involves confirmation of fulfillment of management’s responsibilities in following areas: -

(I) **Preparation of the financial statements**
 The auditor shall request management to provide a written representation that it has fulfilled its responsibility for the preparation of the financial statements in accordance with the applicable financial reporting framework, including, where relevant, their fair presentation, as set out in the terms of the audit engagement.

{1^{1/2} M}

Due to its responsibility for the preparation and presentation of the financial statements and its responsibilities for the conduct of the entity’s business, management would be expected to have sufficient knowledge of the process followed by the entity in preparing and presenting the financial statements and the assertions therein on which to base the written representations.

(II) **Information provided and completeness of transactions**
 The auditor shall request management to provide a written representation that: -

- (i) It has provided the auditor with all relevant information and access as agreed in the terms of the audit engagement and
- (ii) All transactions have been recorded and are reflected in the financial statements.

{1^{1/2} M}

Answer:

(d) Many related party transactions are in the normal course of business. In such circumstances, they may carry no higher risk of material misstatement of the financial statements than similar transactions with unrelated parties. However, the nature of related party relationships and transactions may, in some circumstances, give rise to higher risks of material misstatement of the financial statements than transactions with unrelated parties.

Example

- ◆ Related parties may operate through an extensive and complex range of relationships and structures, with a corresponding increase in the complexity of related party transactions.
- ◆ Information systems may be ineffective at identifying or summarising transactions and outstanding balances between an entity and its related parties.
- ◆ Related party transactions may not be conducted under normal market terms and conditions; for example, some related party transactions may be conducted with no exchange of consideration.

{1 M
Each}

Answer 4:

(a) For the purpose of audit programme construction, CA X should keep in mind the following points:

- (1) Stay within the scope and limitation of the assignment.
- (2) Prepare a written audit programme setting forth the procedures that are needed to implement the audit plan.
- (3) Determine the evidence reasonably available and identify the best evidence for deriving the necessary satisfaction.
- (4) Apply only those steps and procedures which are useful in accomplishing the verification purpose in the specific situation.
- (5) Include the audit objectives for each area and sufficient details which serve as a set of instructions for the assistants involved in audit and help in controlling the proper execution of the work.
- (6) Consider all possibilities of error.
- (7) Co-ordinate the procedures to be applied to related items.

{1 M
Each for
Any 4
Points}

Answer:

(b) Meaning and benefits of understanding Internal Control:

Meaning of Internal Control: As per SA-315, "Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and its Environment", the internal control may be defined as "the process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, safeguarding of assets, and compliance with applicable laws and regulations. The term "controls" refers to any aspects of one or more of the components of internal control."

{1 M}

Benefits of Understanding of Internal Control: An understanding of internal control assists the auditor in:

- i. identifying types of potential misstatements;
- ii. identifying factors that affect the risks of material misstatement, and
- iii. designing the nature, timing, and extent of further audit procedures.

{1 M
Each}

Answer:

(c) The important points to be examined in the lease agreement are:

- (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.

{1 M
Each for
Any 3
Points}

Answer:

(d) Given below are some of the points that an auditor should consider to obtain an understanding of the company’s automated environment:

- ◆ Information systems being used (one or more application systems and what they are).
- ◆ Their purpose (financial and non-financial).
- ◆ Location of IT systems - local vs global.
- ◆ Architecture (desktop based, client-server, web application, cloud based).
- ◆ Version (functions and risks could vary in different versions of same application).
- ◆ Interfaces within systems (in case multiple systems exist).
- ◆ In-house vs Packaged.
- ◆ Outsourced activities (IT maintenance and support).
- ◆ Key persons (CIO, CISO, Administrators).

{1/2 M
Each for
Any 6
Points}

Answer 5:

(a) Reliability of Audit Evidence: As per SA 500 on “Audit Evidence”, the reliability of information to be used as audit evidence, and therefore of the audit evidence itself, is influenced by its source and its nature, and the circumstances under which it is obtained, including the controls over its preparation and maintenance where relevant. Therefore, generalisations about the reliability of various kinds of audit evidence are subject to important exceptions. Even when information to be used as audit evidence is obtained from sources external to the entity, circumstances may exist that could affect its reliability. For example, information obtained from an independent external source may not be reliable if the source is not knowledgeable, or a management’s expert may lack objectivity. While recognising that exceptions may exist, the following generalisations about the reliability of audit evidence may be useful:

- (i) The reliability of audit evidence is increased when it is obtained from independent sources outside the entity.
- (ii) The reliability of audit evidence that is generated internally is increased when the related controls, including those over its preparation and maintenance, imposed by the entity are effective.
- (iii) Audit evidence obtained directly by the auditor (for example, observation of the application of a control) is more reliable than audit evidence obtained indirectly or by inference (for example, inquiry about the application of a control).
- (iv) Audit evidence in documentary form, whether paper, electronic, or other medium, is more reliable than evidence obtained orally (for example, a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed).

{1 M
Each for
Any 4
Points}

- (v) Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies or facsimiles, or documents that have been filmed, digitized or otherwise transformed into electronic form, the reliability of which may depend on the controls over their preparation and maintenance.

Answer:

(b) Verification of inventories in the nature of food and beverages: The inventories in any hotel are both readily portable and saleable particularly the food and beverage inventories. It is therefore extremely important that all movements and transfers of such inventories should be properly documented to enable control to be exercised over each individual stores' areas and sales point. The auditor should carry out tests to ensure that all such documentation is accurately processed. Therefore, following points may be noted in this regard:

- (i) All movement and transfer of inventories must be properly documented.
- (ii) Areas where inventories are kept must be kept locked and the key retained by the departmental manager.
- (iii) The key should be released only to trusted personnel and unauthorized persons should not be permitted in the stores area.
- (iv) Many hotels use specialized professional valuers to count and value the inventories on a continuous basis throughout the year.
- (v) The auditor should ensure that all inventories are valued at the year end and that he should himself be present at the year-end physical verification, to the extent practicable, having regard to materiality consideration and nature and location of inventories.

{1 M
Each for
Any 4
Points}

Answer:

(c) The auditor's report, pursuant to CARO 2020, in respect of physical verification of inventory and in respect of sanctioned working capital, shall include the statements as follows:

- (a) Whether physical verification of inventory has been conducted at reasonable intervals by the management and whether in the opinion of the auditor, the coverage and procedure of such verification by the management is appropriate: whether any discrepancies of 10% or more in the aggregate for each class of inventory were noticed and if so whether such discrepancies have been properly dealt within the books of account.
- (b) whether during any point of time of the year, the company has been sanctioned working capital limits in excess of five crore rupees, in aggregate, from banks or financial institutions on the basis of security of current assets; whether the quarterly returns or statements filed by the company with such banks or financial institutions are in agreement with the books of account of the Company, if not, give details.

{1^{1/2} M}

{1^{1/2} M}

Answer:

(d) The Assistant Engaged – Be Encouraged to Keep an Open Mind:
To start with, an auditor having regard to the nature, size and composition of the business and the dependability of the internal control and the given scope of work, should frame a programme which should aim at providing for a minimum essential work which may be termed as a standard programme.

{1 M}

As experience is gained by actually carrying out the work, the programme may be altered to take care of situations which were left out originally, but are found relevant for the particular concern. Similarly, if any work originally provided for proves beyond doubt to be unnecessary or irrelevant, it may be dropped.

{1 M}

The assistant engaged in the job should be encouraged to keep an open mind beyond the programme given to him. He should be instructed to note and report significant matters coming to his notice, to his seniors or to the partners or proprietor of the firm engaged for doing the audit. {1 M}

In the given case, the attitude of assistants of TP & Co. is not justified. They should keep an open mind and go beyond the programme to take care of newer areas of the business of KSR Ltd. into which the Company has diversified.

Answer 6:

(a) Responsibilities of Management for the Financial Statements: The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements."

SA 200 explains the premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit in accordance with SAs is conducted. Management and, where appropriate, those charged with governance accept responsibility for the preparation of the financial statements. {1 M}

Management also accepts responsibility for such internal control as it determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. {1 M}

The description of management's responsibilities in the auditor's report includes reference to both responsibilities as it helps to explain to users the premise on which an audit is conducted.

This section of the auditor's report shall describe management's responsibility for:

(a) Preparing the financial statements in accordance with the applicable financial reporting framework, **and for such internal control** as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; [because of the possible effects of fraud on other aspects of the audit, materiality does not apply to management's acknowledgement regarding its responsibility for the design, implementation, and maintenance of internal control (or for establishing and maintaining effective internal control over financial reporting) to prevent and detect fraud.] and {1 M}

(b) Assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern. The explanation of management's responsibility for this assessment shall include a description of when the use of the going concern basis of accounting is appropriate. {1 M}

Answer:

(b) Change in Terms of Engagement: According to SA 210 "Agreeing the Terms of Audit Engagements", an auditor who is required to change the engagement which requires lower level of assurance before the completion of engagement should consider the appropriateness of doing so. But when the terms of engagement are changed, both the auditor and the client should agree on the new terms. However, the auditor should not agree to a change in terms where there is no reasonable justification for doing so. {1 M}

If the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted by management to continue the original audit engagement, the auditor shall:

(i) Withdraw from the audit engagement where possible under applicable law or regulation; and {1 M}

- (ii) Determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators. {1 M}

In the instant case, the auditor was unable to obtain sufficient evidence regarding receivables. The client requested him for a change in the terms of the agreement to avoid qualified/adverse opinion. Hence there is no reasonable justification for change in the terms of engagement. {1/2 M}

Thus, the auditor should not agree for change in the terms of engagement letter. He may withdraw from the engagement if possible under law; and determine any obligation to report accordingly. {1/2 M}

Answer:

(c) Assertions while Obtaining Audit Evidence from Substantive Procedure: In obtaining audit evidence from substantive procedures, the auditor is concerned with the following assertions-

- (i) Existence - that an assets or liability exists at a given date.
 - (ii) Rights and obligations - that an asset is a right of the entity and a liability is an obligation at a given date.
 - (iii) Occurrence - that a transaction or event took place which pertains to the entity.
 - (iv) Completeness - that there are no unrecorded assets, liabilities or transaction.
 - (v) Valuation - that an asset or liability is recorded at an appropriate carrying value.
 - (vi) Measurement - that a transaction is recorded in the proper amount and revenue or expenses are allocated to proper period.
 - (vii) Presentation & disclosure - that an item is disclosed, classified and described in accordance with recognized accounting policies, practices and statutory requirements.
- {1/2 M
Each for
Any 6
Points}

Answer:

(d) Following elements comprise an assurance engagement: -

- 1. A three party relationship involving a practitioner, a responsible party, and intended users**
An assurance engagement involves above said three parties. A practitioner is a person who provides the assurance. The term practitioner is broader than auditor. Audit is related to historical information whereas practitioner may provide assurance not necessarily related to historical financial information. A responsible party is the party responsible for preparation of subject matter. Intended users are the persons for whom an assurance report is prepared. These persons may use the report in making decisions.
 - 2. An appropriate subject matter**
It refers to the information to be examined by the practitioner. For example, financial information contained in financial statements while conducting audit of financial statements.
 - 3. Suitable criteria**
These refer to benchmarks used to evaluate the subject matter like standards, guidance, laws, rules and regulations.
 - 4. Sufficient appropriate evidence**
The practitioner performs an assurance engagement to obtain sufficient appropriate evidence. It is on the basis of evidence that conclusions are arrived and an opinion is formed by auditor. "Sufficient" relates to quantity of evidence obtained by auditor. "Appropriate" relates to quality of evidence obtained by auditor.
- {1 M
Each for
Any 3
Points}

5. A written assurance report in appropriate form

A written report is provided containing conclusion that conveys the assurance about the subject matter. A written assurance report is the outcome of an assurance engagement.

OR

Answer:

(d) It has been suggested that actual operation of the internal control should be tested by the application of procedural tests and examination in depth. Procedural tests simply mean testing of the compliance with the procedures laid down by the management in respect of initiation, authorisation, recording and documentation of transaction at each stage through which it flows.

For example, the procedure for sales requires the following:

1. Before acceptance of any order the position of inventory of the relevant article should be known to ascertain whether the order can be executed in time.
2. An advice under the authorisation of the sales manager should be sent to the party placing the order, internal reference number, and the acceptance of the order. This advice should be prepared on a standardised form and copy thereof should be forwarded to inventory section to enable it to prepare for the execution of the order in time.
3. The credit period allowed to the party should be the normal credit period. For any special credit period a special authorisation of the sales manager would be necessary.
4. The rate at which the order has been accepted and other terms about transport, insurance, etc., should be clearly specified.
5. Before deciding upon the credit period, a reference should be made to the credit section to know the creditworthiness of the party and particularly whether the party has honoured its commitments in the past.

{1 M
Each for
Any 3
Points}

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