

1. State with reasons (in short) whether the following statements are true or false.

[10 x 2 = 20]

(Answer any **ten**) :

- (i) While auditing the accounts of a company, it is obligatory that the auditor must adopt sampling technique.
- (ii) Interim dividend is not a part of dividend.
- (iii) A casual vacancy caused by resignation of the auditor can be filled by the Board of Directors.
- (iv) The auditor, in the interest of the users, while explaining the nature of his reservation, can describe the work of the expert with his name in the audit report without obtaining prior consent of the expert.
- (v) The auditee firm has no right to compel the auditor to provide copies of the working papers.
- (vi) Comptroller and Auditor General of India can be removed by the Prime Minister of India on the recommendation of his Council of Ministers.
- (vii) Provisions of Companies (Auditor's Report) order 2003 as amended upto date, apply to clubs, chambers of commerce, research institutes etc. which have been established under Section 25 of the Companies Act, 1956.
- (viii) Mr. X, a Chartered Accountant, is an employee of M/s M & N Co., a firm of Chartered Accountants of India. The firm is the Auditors of ABC & Co. Ltd. After auditing the accounts of the Company the Auditor firm allowed Mr. X, their employee, to sign the audit report; which he did.
- (ix) The Auditor disagreed with the management with regard to the acceptability of the Accounting Policies and the inadequacy of disclosures in the financial statements and issued a disclaimer.
- (x) Analytical procedures are unable to help the Auditor in determining the nature, timing and extent of other audit procedures at the planning stage.
- (xi) A Company which has been unable to negotiate borrowings from its bankers claims that it will be able to continue as a 'going concern'.
- (xii) The overall objective of audit changes in Computer Information System (CIS) environment.

Ans. (1) (i) False. Although Sampling is one of the tool that allows the auditor to draw inference from tests of a subset of a clients transactions, as it would not be cost beneficial or practical for the auditor to examine all the transactions of an entity during the period of audit.

As per SA 530 the auditor should design and select an audit sample, perform audit procedures thereon and evaluate results so as to provide sufficient and appropriate audit evidence.

But whether to apply sampling technique or not, depends upon the discretion of the auditor. If he wants to do 100% checking, nobody can restrict him to do that. Therefore it is not obligatory that he must apply sampling techniques.

Ans. 1 (ii) False. As per sec 205 of Companies Act, 1956 dividend includes interim dividend also.

Sec 205 says that the BOD may declare interim dividend and the amount of dividend **including interim dividend** shall be deposited in a separate bank account within 5 days from the date of declaration of such dividend. The above amount so deposited shall be used for payment of dividend. Therefore it is clear that dividend includes interim dividend also.

Ans. 1. (iii) False. BOD may fill up the casual vacancy except casual vacancy caused by the resignation of the auditor. U/s 224(6), the company at a general meeting shall do the appointment of an auditor to fill up a casual vacancy out of resignation.

Ans. 1 (iv) False. As per **SA 620**, when expressing an unqualified report, auditor should not refer to work of expert in his report. If he wish to give qualified report as a result of work of expert, it may benefit the readers of report if he describe the work of expert in explaining nature of his reservation. Where, in doing so, auditor consider it appropriate to disclose the identity of expert, **he should obtain prior consent of expert** for such disclosure if consent has not already been obtained.

Ans. 1. (v) True.

OWNERSHIP : AAS-3 states that working papers are the property of auditor. The auditor can give copies of or extract from his working paper to the client. But this is totally at his discretion. The same was decided in the case of **Chantry Martin and Co. Vs. Martin**. The auditee firm has no right to compel the auditor to provide copies of the working papers.

Ans. 1 (vi) False.

Removal – The C & AG shall not be removed from office except on the ground of proven misbehavior or incapacity. He can be removed from office only when each Parliament House decides to do so by a majority of not less than 2/3rd of the members of House present and voting.

Ans. 1 (vii) False : A company licenced to operate u/s 25 of the Companies Act, 1956 is specially exempted from the application of provisions of Companies (Auditor's Report) order 2003.

Ans. 1 (viii) False.

U/s 229, only a person appointed as the auditor of the company or where a firm is so appointed, a partner in the firm practicing in India, may sign the auditor's report or sign or authenticate any other document of the company required by law to be signed or authenticated by the auditor.

Mr. Rajendra, a fellow member of the ICAI, and a manager of a practicing firm Srivastava & Co., being a manager and not a partner of the firm, cannot sign of behalf of the firm.

u/s 233 the effect of such an act, if done willfully is a fine which may extent up to Rs.10,000.

Ans. 1 (ix) Disclaimer of opinion : As per AAS – 5, the auditor must collect sufficient & appropriate audit evidence, on the basis of which he drawn his conclusion to form an opinion, on the financial statements. But, if the auditor fails to obtain sufficient information to form an overall opinion on the matter contained in the financial statements, he issues a disclaimer of opinion.

Ans. 1 (x) False.

Compliance procedure are test designed to obtain reasonable assurance that those internal control on which audit reliance is to be placed are in effect. Obtaining audit evidence through compliance procedure is intended to reasonably assure the auditor that

- a. The internal control exist (existence).
- b. Effectiveness (that internal control is operating effectively)
- c. that internal control has so operated throughout the period of intended reliance (continuity).

Substantive procedure are designed to obtain audit evidence as to the completeness, accuracy and validity of data produced by the accounting system. They are of two types :

- i. Tests of details of transaction and balances.
- ii. Analysis of significant ratios and trends including the resulting enquiry of unusual fluctuation and unusual items.

Conclusion : Analytical procedures are substantive procedures and unable to help the auditor in determining the nature, timing & extent of other audit procedures at the planning stage.

Ans. 1 (xi) Partly True Partly False. Going Concern means that enterprise has intention for continuing the operation for foreseeable future. Foreseeable means coming one or two years. In other words, there is no intention of discontinuance of business, necessity of liquidation of organization and discontinuance of major operations of the business.

In this case the Company is unable to negotiate borrowings from its bankers, if the Company is able to arrange the finance from other sources like its parent company or unsecured loan then we can say that the company is a Going concern otherwise there may be the necessity of liquidation, in that case it will not be a Going concern.

Ans. 1 (xii) False. The principal objective of an audit of financial statements, prepared within a framework of recognised accounting policies and practices and relevant statutory requirements, if any, is to ensure that the financial statement reflect a true and fair view.

The scope of an audit of financial statements is determined by the auditor having regard to the terms of the engagement, the requirements of relevant legislation and the pronouncements of the institute. This would involve assessment of reliability and sufficiency of the information contained in the accounting records and other source data by study and evaluation of accounting system and internal controls in operation.

The overall objective and scope of an audit does not change in an CIS environment but the use of a computer changes the processing and storage of financial information and may affect the organisation and procedures employed by the entity to achieve adequate internal control.

Thus, it is clear from the above that overall objective and scope of audit does not change irrespective of fact that whether the accounting information is generated manually or through computer.

2. Comment on the following situations :

[8]

- (a) XYZ Ltd. Co. gave a donation of Rs. 50,000 each to a Charitable Society running a school and a trust set up for the service of Blinds during financial year ending on 31st March, 2009. The average net profits of the company for the last three years were 15 lakhs.

Ans. 2 (a) As per sec 293 of companies act, the BOD of a public company can make charitable contribution upto Rs.50000 or 5% of average net profit of preceeding there financial years, whichever is more, in every financial year. The Board can make charitable contribution in excess of its limits only if so authorized by members. Here profit is to be calculated in accordance with the provisions of sec 349 and 350 of the Act.

In this question 5% of net profit of preceeding three financial years is Rs.75,000 (15,00,000/- x 5%). The Board has given donation in excess of the limits prescribed in sec 293 (1) (e). It Board intends to make contribution in excess of limits aforesaid, it required prior approval of members by an ordinary resolution. If so authorized by the general meeting the board can make contribution to the extent so specified in the resolution.

- 2. (b)** Mr. X, a shareholders of the company pointed out that : **[6]**
- (i) The goodwill in the Balance Sheet of the company has appeared on same figure during the past three years.
 - (ii) Premium received on issue of shares prior to the date of balance sheet has been transferred to Profit and Loss account for arriving at the figure of commission payable to the managing director.

Ans. 2 (b) (i) Accounting Standard 26 "Intangible Assets" states that the **depreciable amount** of an intangible asset should be allocated on a systematic basis over the best estimates of its **useful life**. Amortization should start when the asset is available for use.

Useful Life : The Accounting Standard suggests **10 years** as useful life until and unless there is clear evidence that useful life is longer than **10 years**.

Amortisation Method : If the pattern of benefit and cost can be determined reliably, then the enterprises should amortize the intangible as per the pattern. However, if no pattern of benefit consumed can be determined reliably, then **Straightline method** should be followed.

Conclusion : The Company should provide for amortization in the value of Goodwill as per AS 26. In this case the company has not followed the provisions of As 26, the auditor should qualify his report.

Ans. 2 (b) (ii) As per **Sec 349(3)** for calculating Net Profit for the purpose of calculation of Managerial Remuneration, Premium on shares or debentures issued or sold by the company should not be taken into P&L account. It is a capital receipt and should not be credited to P&L Account. Managerial remuneration includes commission also. Hence transferring the share premium to P&L account by the company is not correct.

2. (c) A, B & C Company Ltd. removed its first Auditor before the expiry of his term without obtaining approval of the Central Government.

Ans. 2 (c) Sec 224(5)(a) of the Companies Act, 1956 provides that first auditor appointed by the BOD can be removed by the company at a general meeting before the expiry of his term by the company in general meeting. The other auditors of the company can be removed at the general meeting but prior approval of Central Govt. is required. This provision ensures that the auditor may not be removed if he is inconvenient to management.

Analysis & Inference: Here in this question, it is not clear that who have appointed the first auditor. If he has been appointed by BOD, then CG approval is not necessary for his removal. But if he has been appointed at General Meeting, then CG approval is necessary.

3. Discuss the basic principles governing an audit. **[10]**

Ans. 3. Following are basic principles which govern auditor's professional responsibility and which should be complied with whenever an audit is carried out :

1. Integrity, objectivity and independence : Integrity refers to honesty and sincerity of auditor; Objectivity means his impartial and unbiased attitude; Independence means he should be free from any such interest which may affect his integrity and objectivity.

He should be fair and must not allow prejudice to overcome his objectivity. He must maintain an impartial attitude.

In the words of **Lord Justice Lindley**: (in the famous case of '**London & General Bank**')

"An auditor must be honest i.e. he must not certify what he does not believe to be true and must make reasonable care and skill before he believes that what he certifies is true. "

2. Confidentiality: The auditor should maintain the confidentiality of the client's information. It is well said that an auditor keeps his ears and eyes open, but his mouth shut. He should disclose the information only when:—

- He has obtained permission of his client.
- There is legal or professional duty to do so.

3. Skills and Competence: Audit work should be performed with due care and skill. Auditor should have specialized skills and competence which are acquired through general education, technical knowledge and practical training. He should also be aware of continuing developments, pronouncements of ICAI and other statutory requirements.

4. Work performed by others: The auditor can delegate work to assistants or can use work performed by others, auditors or experts. But, he will continue to be responsible for expressing an opinion of financial statements.

The auditor should obtain reasonable assurance that work performed by other auditors or experts is adequate for his purpose. ICAI has issued AAS-7, AAS-9, AAS-10, AAS-12, and AAS-17 in regard to this issue.

5. Documentation: Documentation is an important aspect of any audit. An auditor should maintain sufficient working papers for each audit assignment. Such documentation is very important in providing evidence that the audit was carried out in accordance with the basic principles.

6. Planning: The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of business of client. Plans should be revised as necessary during the course of audit.

AAS-8 issued by ICAI deals with aspects of planning.

7. Audit Evidence: The information which may be oral or written, obtained for the purpose of the audit is known as audit evidence. Auditor should obtain sufficient and appropriate evidence to enable him to draw conclusions so as to make an opinion on financial statements. Audit evidence can be obtained with the help of following:

- Compliance procedures
- Substantive procedures:—
 - ◆ Tests of details
 - ◆ Analytical procedures

8. Accounting system and Internal control: Management is responsible for maintaining an auditable and adequate accounting system incorporating various internal controls to the extent appropriate to the size and nature of the business. The internal controls contribute to audit assurance that the accounting system is adequate and that all the accounting information has been duly recorded.

AAS-6 has established standards for obtaining an understanding of accounting and internal control system.

9. Audit conclusions and reporting: Auditor should review and assess the conclusions drawn from the audit evidence obtained. He should assess whether the financial information complies with recognized accounting principles. He should also assess the disclosure requirements. The review and assessment involves forming an overall conclusion as to whether:

- 1) The financial statements have been prepared using the generally accepted accounting principles.
- 2) The financial statements comply with relevant statutory requirements and regulations.
- 3) There is adequate disclosure of all material matters relevant to proper presentation of financial information.

The audit report should contain a clear and written expression of opinion on financial information. AAS-28 describes the elements and types of audit reports.

4. (a) Explain concept of materiality and factors which act as guiding factors to this concept.

[6]

Ans. 4 (a) MATERIALITY (AAS 13) : According to AS-1, 'Material items are those items, the knowledge of which might influence decisions of the user of the financial statements.'

According to AAS-13, 'Information is material if its misstatements i.e. omission or erroneous statement, could influence the economic decisions of users taken on the basis of financial information.'

(1) Auditor should consider materiality and its relationship with **AUDIT RISK** when conducting an Audit. The assessment of what is material is a matter of professional judgement. Information is material if it can influence the decision of user of financial statement. Materiality depends upon size and nature of item.

(2) The concept of materiality recognises that some items, either individually or in the aggregate are relatively important for true and fair presentation of financial statement in conformity with recognised accounting policies and practices.

(3) Materiality is judged by auditor at both overall financial statement level and at individual balance-wise and class of transaction.

- i) At the Financial Statement Level – Eg. integrity of management, management experience, knowledge and changes during the period, (Management may effect the preparation of financial statement of the entity) unusual pressures on management, the nature's of the entity's business.
- ii) At the Account balance and class of transaction level – Eg. complexity of any transaction which require expert judgment, presence of any prior period items, judgment involve in determining account balances, year end adjustments in accounts.

(4) Materiality is also influenced by legal and regulatory requirements, non compliance of which may have significant bearing on financial statement.

(5) Auditor should establish both qualitative and quantitative criteria for setting up materiality level. Example of qualitative criteria is misstatement of accounting policy.

(6) The auditor should consider possibility of misstatement of relatively small amount, that cumulatively may have material effect on financial statement. For example :-

Misstatement if error is repeated each month or each period.

(7) Materiality should be considered by auditor when (a) determining nature timing and extent of audit procedure and (b) evaluating effect of misstatement.

(8) When planning an audit, the auditor consider what would make the financial statement materially mis-stated. This help auditor to consider as to what item to examine and whether to use sampling or analytical procedure. This help auditor to select such audit procedure that can be expected to support the audit opinion at an low degree of audit risk.

(9) If aggregate of un-corrected mis-statement, that the auditor has identified, is MATERIAL, he may request mgt to adjust the financial statement. For example, disclosure of inadequate or undisclosed information or adjustment in Qty/Amount.

If mgt refuses to adjust the financial statement and result of extended audit procedure enable auditor to reach at opinion that the misstatement is material, he should consider issuing a QUALIFIED or NEGATIVE OPINION.

4 (b) Describe a set of instructions, which an auditor has to give to his client before 4 the start of actual audit. [4]

Ans. 4 (b) Audit Engagement Letters : The auditor should send an engagement letter (set of instructions) , preferably before the commencement of the engagement, to help avoid any misunderstanding.

Following are the **set of instructions**, which an audit has to give to his client before the start of actual audit :

- a. Objective of Audit of financial statements.
- b. Management's responsibility for the financial statements.
- c. Management's responsibility for selection and consistent application of accounting policies and accounting standards.
- d. Management's responsibility for preparing the financial statements on a going concern basis.
- e. Management's responsibility for making judgements and estimates that are reasonable and prudent.
- f. Management's responsibility for the maintenance of adequate records and internal controls.
- g. The scope of audit, including reference to applicable legislation, regulations, etc.
- h. The fact that having regard to test nature of an audit, persuasive rather than conclusive nature of audit evidence together with inherent limitations of internal control system, there is an unavoidable risk that some fraud and error may remain undetected.
- i. Unrestricted access to whatever records, documentation and other information requested in connection with audit.

5. (a) What are the six important points that will attract your attention in the case of audit of a Hotel ? [5]

Ans. 5 (a) AUDIT OF A HOTEL : The following matters deserve the auditor's attention in the audit of a Hotel:

S. No.	Aspects	Auditor's Duties

1.	Internal Control Room Sales	(i) Verify the Room Sales, Collection from the guest register. (ii) Sometimes, daily occupancy reports and exit reports are prepared. In such case test check a few reports with the guest register and with the individual guest's bill to ensure proper billing. (iii) See whether standard room rates have been charged in different guests bills. In case there are variation, get the satisfactory explanation and sanction for the same.
2.	Internal Control- Restaurant, Billing and Sales.	All Sales points in a hotel make both cash and credit sales. The auditor must see the internal control system as regards. (i) Procedure for billing customers for room services and sundry services. (ii) Procedure for issue of provisions and commodities. (iii) Safe custody of edibles wines, linen etc. He should :- • Perform the compliance test to ensure the internal control system operates effectively. • Reconcile the total sales reported with the total of the bills issued by the sale point. • Check the numerical control system to ensure that all bills are included in the total. • Verify a few restaurant bills by reference to KOT's (Kitchen Order Tickets) or basic records. • Trace the cash elements of sales in the cash book and the credit sales in total and detail to the guests bills.
3.	Internal Control- Stocks.	(i) Examine the documentation procedure in respect of stock since hotel stock are readily (a) portable & (b) saleable, (ii) Perform compliance tests to ensure that all such documentation is accurately processed. (iii) Ensure that movements of provision & goods in or out of the stores take place only after proper authorisation and recording, (iv) Supervise the physical stock taking and test checking pricing calculations. (v) Verify the basis of valuation adopted for stocks.
4.	Casual Labour	Generally the hotels employ casual labour to a very large extent. Hence the auditor should: (i) Examine the wage payment registers and attendance records to see whether any manipulation has been made. (ii) Verify whether adequate records, as needed by law, wherever applicable, have been maintained.
5.	Fixed Assets	(i) Obtain a schedule of fixed assets and verify whether adequate depreciation has been provided at the prescribed rates. (ii) Verify whether the capitalisation and depreciation policies have been followed properly or not. (iii) Conduct physical inspection of fixed assets and get management certificates for periodic inspections. (iv) Examine the method of recording the assets.
6.	Statutory Compliance	(i) Note the provisions, rules and regulations of various law governing the operation of hotels. (ii) Verify whether the condition of licence for running the hotel have been complied with. (iii) Check whether all the foreign exchange transactions have been properly entered into any appropriately reported.

5. (b) State the informations to be disclosed in the financial statements according to the requirements of A.S.—6. [5]

Ans. 5 (b) Disclosure requirement in the Financial Statements according to the requirement of AS 6 -

- Total cost of each class of assets – historical cost or revalued cost.
- Total depreciation for the period of each class of assets,
- Accumulated depreciation of each class of assets,

- (d) Depreciation method.
- (e) A change in the method of depreciation is treated as a change in accounting policy and is disclosed separately.
- (f) Effect of the revaluation of the fixed assets on the amount of depreciation.

6. (a) State clearly provisions of the Companies Act, 1956 with regard to issue of shares at a discount. [5]

Ans. 6 (a) DISCOUNT ON ISSUE OF SHARES (Sec 79) : When shares are issued at a price, less than its nominal value, they are said to be issued at a discount. Section 79 states that shares may be issued at a discount, if all the following conditions are satisfied, namely-

- i) The shares must be of the class already issued ;
- ii) At least one year must have elapsed since the company became entitled to commence business ;
- iii) The issue must be authorised by resolution of general meeting, which must specify maximum rate of discount ;
- iv) The resolution must be confirmed by CG ;
- v) The rate of discount must not exceed 10%. But CG may allow higher rate as per special circumstances of case.
- vi) The shares must be issued within two months, from the date of sanction by CG . CG may extend time of two months.
- vii) Every prospectus must state the detail of discount allowed on issue of shares or extent to which it has not been written off on date of prospectus.

If default is made, company and every officer in default shall be liable to penalty up to Rs. 500/-.

Consequence of Issue of Shares at irregular discount :

- a. Every director is responsible to return the amount of discount to company, if illegal discount is given.
- b. Every person, who has applied for issue, can apply to court to remove his name, from Register of Member.
- c. If a person had knowledge of irregularity, then if he is allotted any shares at discount, that person has to pay amount of discount to company.

6. (b) As an auditor comment on the following situation : [5]
MNR Co. Ltd. did not provide for depreciation during the financial year 2007-08 due to inadequacy of profits. The company declared dividend during the financial year 2008-09 without providing for the previous year's depreciation.

Ans. 6 (b) Conditions to pay Dividend (Sec 205) - No Dividend can be paid unless

- (a) Present as well as arrear of depreciation have been provided for out of profits of company.
- (b) Where the company has incurred any loss in any financial year, an amount equal to amount of loss or depreciation for that year, whichever is less, has been provided for out of profits of company.
- (c) Transfer to reserve is made as per rules.
- (d) Irredeemable pref. shares have been redeemed as per Section 80A.

In the present case, the company declared dividend during the financial year 2008-2009 without providing for the previous year's (2007-2008) depreciation. The payment of dividend by the company is not as per Sec 205 of Companies Act, 1956. Therefore the dividend payment is invalid in the present case.

7. (a) Comment on the following situation : [5 x 2=10]
XYZ Co. Ltd. reappointed A and B as their joint auditors in the Annual General Meeting. The AGM authorised the Board of fillup the vacancy at their own in the event of both or either of auditors declined to accept the assignment. The Board passed a resolution to appoint C if any of the auditors declined to accept the assignment.

B declined to accept the assignment and Board of Directors appointed C in place of B as per its resolution.

Note : How would you vouch/verify the following. (Answer any one) :

Ans. 7 (a) Ans: No, appointment of Mr. C is invalid.

Casual vacancy arises after valid appointment. Normal law of contract also apply to appointment of Auditor. Resolution passed at AGM to appoint an auditor is an offer from company. Intimation by auditor to ROC accepting this appointment is the acceptance. After acceptance valid appointments takes place. In this case Mr. B never accepted appointment. Hence there is no question of casual vacancy.

Sec 224 states that Board of Director can fill up casual vacancy, As Mr. B has not accepted appointment, hence his appointment was Void ab Initio. There is no question of casual vacancy. Hence BOD is not authorised to make appointment. If company want to appoint Mr. C as auditor, he can be appointed by Regional Director.

Mr. A can act as auditor until Mr. C is so appointed.

7. (b) Leasehold property.

Or

Goods sent out on Sale or Return Basis.

Ans. 7 (b) LEASE HOLD PROPERTY -

- i. Lease Deed - conditions satisfied.
- ii. Premium paid - see receipt. Look that lease is in force which may be known by premium.
- iii. Premium - If paid to acquire lease, then write it off over useful life of lease. If recoverable after completion of lease then show it as current asset.
- iv. Expenses - If any expenses are incurred, look whether they are recoverable from Lessor (who has given lease). If no, then write off over life of lease. If yes, then show as current assets.
- v. Sub-lease : If sub-lease given then look for tenancy agreement. Also premium received.
- vi. Mortgage : If lease hold property mortgage, then lease deed would be with third party, get his confirmation.
- vii. Physical verification of lease hold property if possible.
- viii. Fixed Assets register - Entry.
- ix. Write off all expenses and lease amount over life of lease.
- x. The cost of lease hold land should be verified by reference to the letter from legal advisor and other relevant documents.

Or

Ans. 7 (b) : Goods sent out on sale or return basis.

Sl. No.	Documents to be vouched	Aspects to be verified
1.	Sale or Return Day book	(i) Examine the sale or return day book for the manner of accounting, (ii) Check actual movement of goods from Despatch register/Goods outward register. (iii) Note the period of approval in the case of different goods/customers, (iv) Verify whether goods returned have been properly reversed in the day book.
2.	Order book or Confirmation book	Examine this register to verify sale confirmed by customers & goods held by customers at their end as sale or return stock.
3.	Sales register	Ensure that sales have been recognised whenever:- (i) approval is received from the party, (ii) goods are appropriated by the party, (iii) period of approval has expired and goods have not been returned.
4.	Stock registers & statements	(i) Ensure that closing stock includes good lying with customers and period of approval has not expired, (ii) Ensure that goods validly returned by customers are duly accounted in stock.

7. (c) Bank overdraft.

Ans. 7 (c) Answer : Bank overdraft

Sl. No.	Document to be vouched	Aspects to be verified
1.	Reconciliation from Pass Book	Reconcile the balances of overdraft A/c with that of the Bank Pass Book. Also confirm the balance stated at last by obtaining a certificate from Bank showing the accounts balances at the year-end.
2.	Securities Certificate and Records of	Obtain a securities certificate from the bank that shows the particulars of securities deposited with the bank as security for overdraft or charge created on an asset (s) of the business.

	Registrar	Also ensure that these facts have been appropriately disclosed and duly registered with the Registrar of the companies and written down in the Register of charges.
3.	Purpose and Authority of overdrawn	Determine the purpose for raising overdraft and the mode of utilising it and also that it has not caused any damage to the concern. Also check the authority under which the overdraft has been raised. In a company, only the Board of Director can raise overdraft from banks.
4.	Compliance of Section 293	In a company, ensure that the provisions of Section 293 of Companies Act, 1956 regarding the maximum amount of overdraft that a company can raise have been complied with.

8. (a) X, a Chartered Accountant was engaged by PQR & Co. Ltd. for auditing their accounts. He sent his letter of engagement to the Board of Directors, which was accepted by the Company. In the course of audit of the company, the auditor was unable to obtain appropriate sufficient audit evidence regarding receivables. The client requested for a change in the terms of engagement.

Offer your comments in this regard.

[5 x 2 = 10]

Note : Write short notes on the following. **(Answer any one) :**

Ans. 8 (a) RIGHTS OF AUDITOR : The rights of auditors cannot be limited or abridged in any way. Any resolution limiting the powers of the auditor or any such provision in Articles of Association will be void. The client cannot change the terms of engagement because the rights are given to the auditor in the Companies Act, 1956.

As per Sec 227 (1), every auditor of a company shall have a right of access at all time to the Books, accounts and vouchers of Company, whether they are kept at registered office or any where else. Books and accounts includes financial, stock and memorandum books etc. therefore the auditor shall have the right to check the records related to **receivables**.

As per decided case law **Newton V. Birmingham Small Arms. Co. Ltd.,** an auditor's statutory rights are absolute and cannot be curbed either by the articles of association of the company or by resolving at a meeting.

Conclusion : In that case Mr. X, the auditor of PQR Ltd. can either issue a Qualified opinion or Disclaimer of opinion, if the client is not ready to offer all the informations and explanations which are necessary for the purpose of his audit.

8. (b) Cut-off arrangements

Or

Audit risk at the account balance level and at the class of transactions level.

Ans. 8 (b) Cut off arrangements :- Accounting is a continuous process as the business never comes to an end. Therefore, it is essential that the transactions of one period are separated from those of the coming next period so the results of the working of each period is rightly ascertained. The arrangement that is made for such purpose is technically known as "*Cut – off arrangement.*" It essentially forms a significant part of the internal check of the organization. Since the accounts other than sale, purchase and stock are usually not affected by the business continuity and therefore, the cut-off arrangement is generally applied to these aforesaid accounts only, i.e. sales purchase and stock accounts. The auditor may satisfy himself by examining and test checking that the cut-off procedure is adequately followed and ensures that : -

1. The goods purchased, the property in which has passed to the client have been infact included in the inventories and that liability has been provided for in case of credit purchase.
2. The goods sold have been excluded from the inventories and the credit has been taken for sales, if the sales value is to be received, the concerned party has been debited.

The auditor may examine a sample of documents to evidence the movement of stock to and from the store, including the document relating to the period shortly before and after cut-off date and he may check that whether the stocks represented by those documents were included or not as appropriate during stock taking for correct and perfect presentation in the financial statements.

Or

Ans. 8 (b) Audit Risk : Identifying and assessing the risk of material misstatement

The auditor should identify and assess the risks of material misstatement at the –

- financial statement level
- relevant assertion level

Financial Statement Level – Risks of material misstatement at the financial statement level refer to risks that relate pervasively to the financial statements as a whole and potentially affect many assertions. Risks of this nature are not necessarily risks identifiable with specific assertions at the class of transactions, account balance, or disclosure level.

Assertion level – In representing that the financial statements are in accordance with the applicable financial reporting framework, management implicitly or explicitly makes assertions regarding the recognition, measurement, presentation and disclosure of the various elements of financial statements and related disclosures.

Risks of material misstatement at the assertion level for classes of transactions, account balances and disclosures need to be considered.

Assertion about the classes of transactions

- Occurrence
- Completeness
- Accuracy
- Cut-off
- Classification

Assertion about account balances

- Existence
- Rights and obligations
- Completeness
- Valuation and allocation

In nutshell, the auditor should assess the risks of material misstatement by answering the following questions –

- what can go wrong at the relevant assertion level
- whether the risks are of a magnitude that could result in a material misstatement of the financial statements

8. (c) Powers of C & A.G. in connection with the performance of his duties.

Ans. 8 (c) POWER OF CAG : Power of CAG are given in CAG (Duties, Power & Conditions of Service) Act, 1971. CAG has following four powers: -

(a) To inspect any office of account under the control of Union Government/ State Government/Union Territory including any office responsible for keeping initial and subsidiary books.

(b) To require that any accounts, books, papers and other documents which deal with any transaction under audit, to be sent to specified places.

(c) To put such questions or make such observations as he may consider necessary to the person who is incharge of the office and to say for such informations as he may require for preparation of any accounts or report which is its duty to prepare.

(d) To avoid any detailed audit of accounts and to apply test check regarding such accounts and transactions as he may consider necessary. Example, instead of 100% vouching, CAG can limit to 5% or 10% vouching also.