

WT 1 (Ch. 1 – Nature, Objective and Scope of Audit)

Instructions: Part A comprises of MCQ.

Part B Comprises of descriptive questions.

Part – A (Multiple Choice Questions)

- Q.1 (a) (2 Marks)
Q.2 (a) (2 Marks)
Q.3 (c) (1 Mark)
Q.4 (a) (1 Mark)

Part B (Descriptive Questions)

Q.1 (a) Statement is Incorrect.

- An audit is not an official investigation into alleged wrongdoing.
- Accordingly, the auditor is not given specific legal powers, such as the power of search, which may be necessary for such an investigation. **(2 Marks)**

(b) Statement is Incorrect.

“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. **(2 Marks)**

Q.2 (a) Three Party relationship of assurance engagement:

An assurance engagement involves three parties – a practitioner, a responsible party, and intended users.

- (1) **Practitioner:** Person who provides the assurance. Practitioner is broader than auditor. Audit is related to historical information whereas practitioner may provide assurance not necessarily related to historical financial information. **(1 Mark)**
- (2) **Responsible party:** Party responsible for preparation of subject matter. **(1 Mark)**
- (3) **Intended users:** Persons for whom an assurance report is prepared. These persons may use the report in making decisions. **(1 Mark)**

(b) **Elements to be included in Scope of Audit:**

An Audit of Financial Statements include within its scope the following:

- (1) **Coverage of all aspects of entity:** Audit of F.S. should be organized adequately to cover all aspects of the entity relevant to the F.S. **(1 Mark)**
- (2) **Reliability and sufficiency of financial information:** Auditor should be reasonably satisfied that information contained in accounting records and other source data (like bills, vouchers, documents etc.) is reliable and provide sufficient basis for preparation of F.S. **(1 Mark)**
- (3) **Proper disclosure of financial information:** Auditor should decide whether relevant information is properly disclosed in F.S in compliance with applicable statutory requirements. For this purpose, auditor is required to study and assess accounting systems and internal controls. **(1 Mark)**

Q.3 (a) **Objectives of Auditor:**

As per SA-200 “Overall Objectives of the Independent Auditor”, in conducting an audit of financial statements, the overall objectives of the auditor are:

- (i) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and
- (ii) To report on the financial statements, and communicate as required by the SAs, in accordance with the auditor’s findings. **(2 Marks)**

In the given case of SR Ltd., CA N expressed his opinion on the financial statements of SR Ltd. without obtaining reasonable assurance about whether the financial statements as a whole are free from material misstatement or not.

Therefore, it can be concluded that CA N did not comply with the objective of audit as stated in SA 200.

(1 Mark)

(b) **Types of Assurance Standards:**

- (a) **Standards on Auditing (SAs):** to be applied in the audit of historical financial information. **(1 Mark)**
- (b) **Standards on Review Engagements (SREs):** to be applied in the review of historical financial information. **(1 Mark)**
- (c) **Standards on Assurance Engagements (SAEs):** to be applied in assurance engagements, engagements dealing with subject matter other than historical financial information. **(1 Mark)**

Q.4 (a) **Duties in relation to Engagement and Quality Control Standards:**

- It is the duty of professional accountants to see that Standards are followed in engagements undertaken by them.
- However, a situation may arise when a specific procedure as required in Standards would be ineffective in a particular engagement. In such a case, professional accountant is required to ensure the following:
 - (a) Document how alternative procedures performed to achieve the purpose of required procedure;
 - (b) Reason for departure has also to be documented;
 - (c) Report should draw attention to such departures. **(3 Marks)**

Conclusion: CA P Babu is required to document how alternative procedures performed achieve the purpose of required procedure. Reason for departure has to be documented. His report should draw attention to such departure.

(b) **Practical and legal limitations on the auditor's ability to obtain audit evidence:**

There are practical and legal limitations on the auditor's ability to obtain audit evidence. For example:

- (1) Auditor does not test all transactions and balances. He forms his opinion only by testing samples. It is an example of practical limitation on auditor's ability to obtain audit evidence. **(1 Mark)**
- (2) Management may not provide complete information as requested by auditor. There is no way by which auditor can force management to provide complete information as requested. In case he is not provided with required information, he can only report. It is an example of legal limitation on auditor's ability to obtain audit evidence. **(1 Mark)**

The management may consist of dishonest and unscrupulous people and may be, itself, involved in fraud. It may be engaged in concealing fraud by designing sophisticated and carefully organized schemes which may be hard to detect by the auditor. It may produce fabricated documents before auditor to lead him to believe that audit evidence is valid. However, in reality, such documents could be fake or non-genuine.

(0.5 Mark)

It is quite possible that entity may have entered into some transactions with related parties. Such transactions may be only paper transactions and may not have actually occurred. The auditor may not be aware of such related party relationships or audit procedures may not be able to detect probable wrong doings in such transactions.

(0.5 Mark)



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