

WT 4 (Ch. 3 – Risk Assessment and Internal Control)

Marks: 25

Time: 45 Minutes

Instructions: Part A comprises of MCQ.

Part B Comprises of descriptive questions.

Part – A (Multiple Choice Questions)

- Q.1** To evaluate the Internal Control of Kingsway Limited, a team member of the auditors used a method according to which, number of questions relating to internal control of the company were required to be answered by the employees of the company. After obtaining the answers there was a discussion relating to those answers between team member of the auditor and employees of the company for a clear picture. 2
- State the method of evaluation of internal control as discussed above.
- (a) Narrative record
 - (b) Check List
 - (c) Internal Control questionnaire
 - (d) Flow chart
- Q.2** The term Internal Financial Controls (IFC) basically refers to the policies and procedures put in place by companies for ensuring: 2
- (i) Reliability of financial reporting
 - (ii) Compliance with applicable laws and regulations
 - (iii) Safeguarding of assets.
 - (iv) Effectiveness and efficiency of operations
 - (v) Prevention and detection of frauds
- Which statement is correct?
- (a) (i), (ii) and (iv)
 - (b) (i), (iii) (v) and (ii)
 - (c) (i), (ii), (iii) and (iv)
 - (d) (i), (ii),(iii),(iv) and (v)
- Q.3** Financial statements of a company have been put up for audit before the auditor. On going through financial statements, he wants to verify some major bills debited in “Machinery repair” account. The purpose of it is to ensure that bills are entered correctly and their classification is proper. As regards verification of bills debited in “Machinery repair” account, identify what he intends to perform? 1
- (a) Tests of Controls

- (b) Tests of transactions
- (c) Tests of balances
- (d) Risk assessment procedures

Q.4 The Objective of establishing Security Policies and Procedures is to _____ 1

- (a) To ensure that production systems are processed to meet financial reporting objectives.
- (b) To ensure that modified systems continue to meet financial reporting objectives
- (c) To ensure that access to programs and data is authenticated and authorized to meet financial reporting objectives.
- (d) To ensure that systems are developed, configured and implemented to meet financial reporting objectives.

Q.5 Risk of material misstatement may be defined as the risk that the financial statements are materially misstated _____ 1

- (a) after audit.
- (b) during audit.
- (c) prior to audit.
- (d) All of the above.



Part B (Descriptive Questions)

Q. No. 1 is Compulsory. Attempt Any two from the rest.

Q.1 State with reasons (in short) whether the following statements are correct or incorrect: 4

- (a) With reference to General IT control, the objective of Data Center and Network Operations is to ensure that systems are developed, configured and implemented to meet financial reporting objectives.
- (b) Control environment can prevent, detect and correct a material misstatement.

Q.2 (i) Identify the component of risks of material misstatement involved as an auditor of the company in following cases: 2

- (a) Wear & Tear Private Limited is a “start-up” engaged in providing holistic solutions to problem of paddy stubble burning mainly catering to needs of farmers of North western India. Due to importance given by governments to this issue, companies have entered in the market in past few years. Many of these companies have not been successful and have gone bust.

- (b) A company has devised a control that its inventory of perishable goods is stored in appropriate conditions in a controlled environment to prevent any damages to inventory. Responsibility is fixed on two persons to monitor environment using sensors and to report on deviations.
- (ii) Risk of material misstatement refers to the risk that the financial statements are materially misstated prior to audit. Discuss the levels at which this risk exists. 2
- (iii) Understanding the entity and its automated environment involves understanding how IT department is organised, IT activities, the IT dependencies, relevant risks and controls. Explain stating the points that an auditor should consider to obtain an understanding of the company’s automated environment. 3
- Q.3 (a) The auditor obtains an understanding of the information system, including the related business processes, relevant to financial reporting to gain insight of this important component of internal control. What are the specific areas in respect of which auditor gains such understanding? 4
- (b) An auditor has to exercise professional judgement in determining materiality. Explain the factors that may affect the identification of an appropriate benchmark in determining materiality for the financial statements as whole. 3
- Q.4 (a) While it is true that companies can benefit immensely from the use of data analysis in terms of increased profitability, better customer service, etc., analyse various functions that can be performed even by the auditor also using Data Analytics tools and techniques in the audit process to obtain good results. 4
- (b) Significant risks often relate to significant non- routine transactions or judgmental matters. Nonroutine transactions are transactions that are unusual, due to either size or nature, and that therefore occur infrequently. Judgmental matters may include the development of accounting estimates for which there is significant measurement uncertainty. In context of significant risk, explain the factors to be considered by the auditor in exercising judgment as to which risks are significant risks. 3



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