

## WT 3 (Ch. 4 – Audit Evidence and Ch. 6 – Audit Documentation)

**Instructions: Part A comprises of MCQ.**

**Part B Comprises of descriptive questions.**

**Part – A (Multiple Choice Questions)**

- Q.1 (c) (1 Mark)  
 Q.2 (d) (1 Mark)  
 Q.3 (d) (1 Mark)  
 Q.4 (b) (1 Mark)  
 Q.5 (d) (1 Mark)  
 Q.6 (b) (1 Mark)  
 Q.7 (c) (1 Mark)

**Part B (Descriptive Questions)**

**Q.1 (a) Statement is incorrect.**

The audit procedure used by the auditor of XYZ Ltd. is known as "Inspection".

Whereas Observation consists of looking at a process or procedure being performed by others.

**(2 Marks)**

**(b) Statement is incorrect.**

- External Evidence is one that originates outside client's organization.
- Sales invoice is internal evidence as it originates within the entity.

**(2 Marks)**

**(c) Statement is incorrect.**

As per requirements of SQC 1 and SA 230, audit engagement documentations should be kept for a minimum of 7 years from the date of audit report.

**(2 Marks)**

**Q.2 (a) Objective and nature of audit documentation**

Audit Documentation refers to the record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached.

**The objective of the auditor is to prepare documentation that provides:**

- A sufficient and appropriate record of the basis for the auditor's report; and
- Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.

**(2 Marks)**

**Nature of Audit Documentation**

Audit documentation provides:

- (a) evidence of the auditor's basis for a conclusion about the achievement of the overall objectives of the auditor; and
- (b) evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements. **(2 Marks)**

**(b) Definition of various terms:**

SA 505 "External Confirmations" defines the various terms as follows:

- (i) **Positive confirmation request:** A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information. **(1 Mark)**
- (ii) **Negative confirmation request:** A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request. **(1 Mark)**

**Q.3 (a) Using work of Management Expert:**

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:

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

Auditor should consider the above before using the work of the management's expert.

**(b) Nature of Related Party Relationships & Transactions:**

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. For example:

- (a) 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.

- (b) Information systems may be ineffective at identifying or summarising transactions and outstanding balances between an entity and its related parties.
- (c) 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.

**3 Marks (1 Mark for each correct Point)**

**Q.4 (a) Circumstances when work of the internal audit function cannot be used:**

External auditor shall not use work of internal audit function if he determines that:

- (a) The function's organizational status and relevant policies and procedures do not adequately support the objectivity of internal auditors; **(1 Mark)**
- (b) The function lacks sufficient competence; or **(1 Mark)**
- (c) The function does not apply a systematic and disciplined approach. **(1 Mark)**

**(b) Precautions to be taken while applying test check techniques are**

- (1) Thorough study of accounting system should be done before adopting sampling.
- (2) Proper study of internal control systems.
- (3) Areas which are not suitable for sampling should be carefully considered. For example: compliance with statutory provisions, transactions of unusual nature etc.
- (4) Proper planning for Sampling methods to be used and explaining the staff.
- (5) Transactions and balances have to be properly classified (stratified).
- (6) Sample size should be appropriately determined.
- (7) Sample should be chosen in unbiased way.
- (8) Errors located in the sample should be analysed properly.

**3 Marks (1 Mark for each correct Point – Any three Point)**