

Suggested Answers and Marking Scheme

MTP 2 (Ch. 2 – Audit Strategy, Planning & Programme and Ch. 3 – Risk Assessment and IC)

Marks: 27

Time: 50 Minutes

Instructions: Part A comprises of MCQ.

Part B Comprises of descriptive questions.

Part – A (Multiple Choice Questions)

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| Q.1 | (1) | The understanding of company's risk management policy is required by auditor. It may help the auditor in identifying risks of material misstatement that management failed to identify. | 2 |
| Q.2 | (d) | Seeking confirmation letters from bankers regarding outstanding balances | 2 |
| Q.3 | (a) | Procedures planned to identify significant audit risks pertaining to inventory valuation forms part of overall audit plan. | 2 |
| Q.4 | (b) | Materiality has to be decided by auditor prior to identification and assessment of risks of material misstatements. | 2 |

Part B (Descriptive Questions)

Q. No. 1 is Compulsory. Attempt ANY TWO from the rest.

- Q.1 (a) Factors affecting identification of appropriate benchmark as per SA 320:**
- Determining materiality involves the exercise of professional judgment. A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole. Factors that may affect the identification of an appropriate benchmark include the following:
- (1) Elements of the financial statements (for example, assets, liabilities, equity, revenue, expenses);
 - (2) Whether there are items on which the attention of the users of the particular entity's financial statements tends to be focused (for example, for the purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets);
 - (3) The nature of the entity, where the entity is at in its life cycle, and the industry and economic environment in which the entity operates;
 - (4) The entity's ownership structure and the way it is financed (for example, if an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings); and
 - (5) The relative volatility of the benchmark.

4 Marks – One Mark for One Point (Any Four)

(b) Cases by which auditor can ascertain the reporting objectives of the engagement:

As per SA 300 “Planning an Audit of Financial Statements” the auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. In establishing the overall audit strategy, the auditor shall, among other ascertain the reporting objectives of the engagement to plan the timing of the audit.

Various cases through which auditor can ascertain the reporting objectives of the engagement are:

- (1) Entity’s timetable for reporting, such as at interim and final stages.
- (2) Organization of meetings with management and TCWG to discuss the NTE of the audit work.
- (3) Discussion with management regarding expected type and timing of reports to be issued.
- (4) Discussion with management regarding the expected communications on the status of audit work throughout the engagement.
- (5) Expected nature and timing of communications among ET members, including the nature and timing of team meetings and timing of the review of work performed.

5 Marks – One Mark for One Point

Q.2 For the purpose of programme construction, the following points should be kept in mind:

- (i) Stay within the scope and limitation of the assignment.
- (ii) Prepare a written audit programme setting forth the procedures that are needed to implement the audit plan.
- (iii) Determine the evidence reasonably available and identify the best evidence for deriving the necessary satisfaction.
- (iv) Apply only those steps and procedures which are useful in accomplishing the verification purpose in the specific situation.
- (v) 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.
- (vi) Consider all possibilities of error.
- (vii) Co-ordinate the procedures to be applied to related items.

5 Marks – One Mark for One Point (Any Five)

Q.3 Access Security in Automated Environment:

The objective of Access Security is to ensure that access to programs and data is authenticated and authorized to meet financial reporting objectives. **(1 Mark)**

Activities:

- (i) Security Organization & Management
- (ii) Security Policies & Procedures
- (iii) Application Security
- (iv) Data Security
- (v) Operating System Security
- (vi) Network Security
- (vii) Physical Security

(2 Marks – 0.5 Mark for one Point – Any Four)

Program Change in Automated Environment:

The objective of program change controls is to ensure that modified systems continue to meet financial reporting objectives. **(1 Mark)**

It includes activities such as change in management process, recording, managing and tracking change requests, making and testing changes etc. **(1 Mark)**

Q.4 Elements of Control Environment:

Control environment includes:

- the governance and management functions and
- the attitudes, awareness, and actions of those charged with governance and management concerning the entity's internal control and its importance in the entity.

The control environment sets the tone of an organization, influencing the control consciousness of its people.

2 Marks

Control environment includes the following elements:

- (1) Communication and enforcement of integrity and ethical values:** These are essential elements that influence effectiveness of design, administration & monitoring of controls.
- (2) 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.
- (3) Participation by TCWG:** It includes attributes of TCWG such as their independence from management, their experience, extent of their involvement and the information they receive, and the scrutiny of activities.
- (4) Management's philosophy and operating style:** It comprises of management characteristics such as:
 - Approach to taking and managing business risks.
 - Attitudes and actions toward financial reporting.
 - Attitudes toward information processing and accounting functions and personnel.
- (5) Organisational structure:** Framework within which an entity's activities for achieving its objectives are planned, executed, controlled, and reviewed.
- (6) 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.
- (7) Human resource policies and practices:** Policies & practices that relate to, e.g., recruitment, orientation, training, evaluation, counselling, promotion, compensation, and remedial actions.

3 Marks – One Mark for One Point (Any Three)