

Suggested Answers and Marking Scheme

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

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 | (b) The auditor should request confirmation from third party as to the quantities and condition of the inventory held with them or perform inspection or other audit procedures as appropriate. | 2 |
| Q.2 | (d) (i), (ii) and (iii) | 2 |
| Q.3 | (c) The approach followed by team is not proper as audit documentation is being prepared at the time of finalization of audit report. | 2 |
| Q.4 | (b) Recalculation | 2 |

Part B (Descriptive Questions)

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

- Q.1 (a) Purpose of Applying Analytical Procedure:**
- Analytical procedures use comparisons and relationships to assess whether account balances or other data appear reasonable. The auditor of Grape Ltd. would achieve the following by carrying out the comparison stated in the question:
- (i) If balances included in the Statement of Profit and Loss of an entity are compared with those contained in the Statement of Profit and Loss with that of the previous period, it would be possible to find out the reasons for increase or decrease in the amount of profits of those years.
 - (ii) By setting up certain expenses' ratios on the basis of balances included in the Statement of Profit and Loss, for the year under audit, comparing them with the same ratios for the previous year, it is possible to ascertain the extent of increase or decrease in various items of expenditure in relation to sales and that of trading profit in relation to sales.
 - (iii) If differences are found to be material, the auditor would ascertain the reasons thereof and assess whether the accounts have been manipulated to inflate or suppress profits.
 - (iv) It may help identify the existence of unusual transactions or events, and amounts, ratios, and trends that might indicate matters that have audit implications.

Marking Scheme – 1 Mark for 1 Correct Point (Four Points)

- (b) In documenting the nature, timing and extent of audit procedures performed, the auditor shall record:
- (1) The identifying characteristics of the specific items or matters tested.
 - (2) Who performed the audit work and the date such work was completed; and
 - (3) Who reviewed the audit work performed and the date and extent of such review.

Marking Scheme – 1 Mark for 1 Correct Point (Any Two Points)

The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:

- (a) The nature, timing and extent of the audit procedures performed.
- (b) The results of the audit procedures performed, and the audit evidence obtained; and
- (c) Significant matters arising during the audit and the conclusions reached thereon and significant professional judgements made in reaching those conclusions.

Marking Scheme – 1 Mark for 1 Correct Point (Any Two Points)

Thus, all above matters shall be recorded to meet requirements of SA 230. Documenting nature, time and extent of audit procedures performed alone does not meet the requirements of SA 230. Therefore, CA Piku's views are not valid. **(1 Mark)**

Q.2 Using direct assistance of internal auditor:

As per SA 610 "Using the Work of Internal Auditor" statutory auditor can take direct assistance of internal auditor subject to following conditions:

1. The external auditor is not prohibited by law or regulation from obtaining direct assistance from internal auditors.
2. There are no significant threats to the objectivity of the internal auditor.
3. The internal auditor is sufficient competent to perform the proposed work.

Marking Scheme – 1 Mark for 1 Correct Point (Any Two Points)

Precautions to be taken while using direct assistance:

1. External auditor shall not use internal auditors to provide direct assistance to perform procedures that:
 - (a) Involve making significant judgments in the audit;
 - (b) Relate to higher assessed risks of material misstatement where the judgment required in performing the relevant audit procedures or evaluating the audit evidence gathered is more than limited.
 - (c) Relate to work with which the internal auditors have been involved and which has already been, or will be, reported to management or those charged with governance by the internal audit function; or
 - (d) Relate to decisions the external auditor makes in accordance with this SA regarding the internal audit function and the use of its work or direct assistance. **(1 Mark)**
2. Prior to using internal auditors to provide direct assistance for purposes of the audit, the external auditor shall:
 - (a) Obtain written agreement from an authorized representative of the entity that the internal auditors will be allowed to follow the external auditor's instructions, and that the entity will not intervene in the work the internal auditor performs for the external auditor; and

- (b) Obtain written agreement from the internal auditors that they will keep confidential specific matters as instructed by the external auditor and inform the external auditor of any threat to their objectivity. **(1 Mark)**
3. The external auditor shall direct, supervise and review the work performed by internal auditors on the engagement in accordance with SA 220. **(1 Mark)**

Q.3 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.

Marking Scheme – 1 Mark for 1 Correct Point (Any Five Points)

Q.4 Inspection of Records or documents to obtain information about related party relationship and transactions:

During the audit, the auditor should maintain alertness for related party information while reviewing records and documents. He may inspect the following records or documents that may provide information about related party relationships and transactions, for example:

- (1) Entity income tax returns.
- (2) Information supplied by the entity to regulatory authorities.
- (3) Shareholder registers to identify the entity's principal shareholders.
- (4) Statements of conflicts of interest from management and those charged with governance.
- (5) Records of the entity's investments and those of its pension plans.
- (6) Contracts and agreements with key management or those charged with governance.
- (7) Significant contracts and agreements not in the entity's ordinary course of business.
- (8) Specific invoices and correspondence from the entity's professional advisors.
- (9) Life insurance policies acquired by the entity.
- (10) Significant contracts re-negotiated by the entity during the period.
- (11) Internal auditors' reports.
- (12) Documents associated with the entity's filings with a securities regulator e.g, prospectus.

Marking Scheme – 1 Mark for 1 Correct Point (Any Five Points)