1. (a) **Appointment of the First Auditor in the Case of Government Company:** Section 139(6) of the Companies Act, 2013 lays down that the first auditor or auditors of a company, other than a Government Company, shall be appointed by the Board of directors within 30 days from the date of registration of the company. However, in the case of a Government Company, the appointment of first auditor is governed by the provisions of Section 139(7) of the Companies Act, 2013 which states that the first auditor shall be appointed by the Comptroller and Auditor General of India within 60 days from the date of registration of the company.

Hence, in the case of ABC Ltd., being a government company, the first auditors shall be appointed by the Comptroller and Auditor General of India.

Thus, the appointment of first auditors made by the Board of Directors of Health and Wealth Ltd., is null and void.

(b) **Verification of Payment of Dividends:** The procedure for the verification of payment of dividends is stated below-

(i) Examine the company’s Memorandum and Articles of Association to ascertain the dividend rights of different classes of shares.

(ii) Confirm that the profits appropriated for payment of dividend are distributable having regard to the provisions contained in Section 123 of the Companies Act, 2013. If the company proposes to pay the dividend out of past profit in reserves, see that either this is in accordance with the rules framed by the Central Government in this behalf.

(iii) Inspect the Shareholders’ Minute Book to verify the amount of dividend declared and confirm that the amount recommended by the directors.

(iv) If a separate bank account was opened for payment of dividends, check the transfer of the total amount of dividends payable from the Dividends Accounts.

(v) Check the particulars of members as are entered in the Dividend Register or Dividend List by reference to the Register of Members, test check the calculation of the gross amount of dividend payable to each shareholder on the basis of the number of the shares held and the amount of CDT, if applicable. Verify the casts and crosscast of the different columns.

(vi) Check the amount of dividend paid with the dividend warrants surrendered.
Reconcile the amount of dividend warrants outstanding with the balance in the Dividend Bank Account.

(vii) Examine the dividend warrants in respect of previous years, presented during the year for payment and verify that by their payment, any provision contained in the Articles in the matter of period of time during which amount of unclaimed dividend can be paid had not been contravened.

(viii) It is compulsory for a company to transfer the total amount of dividend which remains unpaid or unclaimed, within thirty days of the declaration of the dividend to a special bank account entitled “Unpaid Dividend Account”. Such an account is to be opened only in a scheduled bank. The transfer must be made within 7 days from the date of expiry of thirty days.

(ix) In case any money transferred to the unpaid dividend amount of a company remain unpaid or unclaimed for a period of 7 years from the date of such transfer shall be transferred to Investor Education and Protection Fund.

(x) Ensure the compliance, in case dividend is paid in case of inadequate profits.

(c) Identification of Significant Risks: SA 315 “Identifying and Assessing the Risk of Material Misstatement through understanding the Entity and its Environment” defines ‘significant risk’ as an identified and assessed risk of material misstatement that, in the auditor’s judgment, requires special audit consideration.

As part of the risk assessment, the auditor shall determine whether any of the risks identified are, in the auditor’s judgment, a significant risk. In exercising this judgment, the auditor shall exclude the effects of identified controls related to the risk.

In exercising judgment as to which risks are significant risks, the auditor shall consider at least the following-

(i) Whether the risk is a risk of fraud;

(ii) Whether the risk is related to recent significant economic, accounting or other developments like changes in regulatory environment etc. and therefore requires specific attention;

(iii) The complexity of transactions;

(iv) Whether the risk involves significant transactions with related parties;

(v) The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; and

(vi) Whether the risk involves significant transactions that are outside the normal course of business for the entity or that otherwise appear to be unusual.

(d) Auditor’s Responsibilities in Respect of Corresponding Figures: As per SA 710 “Comparative Information—Corresponding Figures and Comparative Financial

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Statements”, in respect of corresponding figures, the auditor shall determine whether the financial statements include the comparative information required by the applicable financial reporting framework and whether such information is appropriately classified. For this purpose, the auditor shall evaluate whether-

(i) The comparative information agrees with the amounts and other disclosures presented in the prior period; and

(ii) The accounting policies reflected in the comparative information are consistent with those applied in the current period or, if there have been changes in accounting policies, whether those changes have been properly accounted for and adequately presented and disclosed.

If the auditor becomes aware of a possible material misstatement in the comparative information while performing the current period audit, the auditor shall perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence to determine whether a material misstatement exists. If the auditor had audited the prior period’s financial statements, the auditor shall also follow the relevant requirements of SA 560 “Subsequent Events”.

As required by SA 580, “Written Representations”, the auditor shall request written representations for all periods referred to in the auditor’s opinion. The auditor shall also obtain a specific written representation regarding any prior period item that is separately disclosed in the current year’s Statement of Profit and Loss.

2. (i) **Incorrect**: Sufficiency is the measure of the quantity of audit evidence. On the other hand, appropriateness is the measure of the quality of audit evidence.

(ii) **Incorrect**: As per section 141(3) of the Companies Act, 2013, a person shall not be eligible for appointment as an auditor of a company whose relative is a Director or is in the employment of the Company as a director or key Managerial Personnel.

(iii) **Incorrect**: The auditor shall express an unmodified opinion when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

(iv) **Incorrect**: As per Section 143(1) of the Companies Act, 2013, every auditor of a company shall have a right of access at all times to the books of account and vouchers of the company kept not only at the registered office of the company but also at any other place too.

(v) **Incorrect**: Narrative Record is a complete and exhaustive description of the system as found in operation by the auditor. On the other hand, a Check List is a series of instructions and/or questions which a member of the auditing staff must follow and/or answer.

(vi) **Incorrect**: Standards on Review Engagements (SREs) - to be applied in the review of historical financial information.
(vii) **Incorrect:** Internal evidence is the evidence that originates within the client’s organisation. Since purchase invoice originates outside the client’s organisation, therefore, it is an example of external evidence.

(viii) **Incorrect.** In terms of the general principles of law, any person having the lawful possession of somebody else’s property, on which he has worked, may retain the property for non-payment of his dues on account of the work done on the property.

On this premise, auditor can exercise lien on books and documents placed at his possession by the client for non-payment of fees for work done on the books and documents.

(ix) **Incorrect:** According to Section 142 of the Companies Act, 2013, the remuneration of subsequent auditors of a company shall be fixed in its general meeting or in such manner as may be determined therein.

(x) **Incorrect:** Teeming and Lading is one of the techniques of suppressing cash receipts and not of inflating cash payments. Money received from one customer is misappropriated and the account is adjusted with the subsequent receipt from another customer and so on.

3. (a) **Personal Expenses of Directors:**

   (i) Check the articles of association, service contract, minutes of general meeting, etc., to check the authorisation for such payment.

   (ii) Enquire to ensure that personal expenses are not camouflaged in any other revenue items as contemplated under section 143(1) of the Companies Act, 2013.

   (iii) Ascertain compliance with disclosure according to requirements of Schedule III to the Companies Act, 2013.

   (iv) Check documentary evidences to examine the payments reimbursed.

(b) **Preliminary Expenses:** It is the expenditure incurred incidental to the creation, formation and floating of a company. It consists of stamp duties, registration fees, legal costs, consultants fees, expenses of printing of memorandum and articles, etc. The following should be checked-

   (i) Check Board’s minutes book containing the resolution approving the expenses claimed by promoters as having been spent in formation of the company.

   (ii) Examine supporting papers and vouchers, contracts, agreements, etc. to support the promoters’ claims. Also check bills and receipts issued by the printer of the memorandum and articles of association, share certificates, etc.

   (iii) Check receipt for the registration fee paid for registration of the company.

   (iv) Verify rates of stamp required to be affixed on the memorandum and articles of association.
(v) Examine the compliance of AS 26 with regard to treatment of such preliminary expenses in the books of account.

(vi) Check that no expenses other than those what constitutes preliminary expenses are booked under this head, e.g. underwriting commission and brokerage paid.

(c) Advances to the Suppliers:

(i) Obtain schedule of debit balances in trade payables’ account and pay particular attention to the age of the balances. Also scrutinise the bought ledger.

(ii) Enquiry should be made for long unadjusted outstandings and check as to whether any of them would require provisioning.

(iii) Examine that the advances have not been shown as deposits in balance sheet as per Section 143(1) of the Companies Act, 2013.

(iv) Confirmation of balances should be obtained and reconciliation be done in case of any discrepancies.

(d) Endowment Policies:

(i) Ascertain the specific purpose for which the endowment policy is taken, e.g., Sinking Fund policies for redemption of debentures, redemption of leases or policies taken for other similar purposes, etc.

(ii) Verify the terms and conditions of policies and ensure that all such conditions are in force and being followed.

(iii) Check that premium has been deposited in time and the policy is in force.

(iv) Examine that proper disclosures have been made in the financial statements in respect of items for which the policy has been taken.

4. (a) Areas Where Surprise Checks can Significantly Improve the Effectiveness of an Audit: Surprise checks constitute an important part of normal audit procedure. An element of surprise both with regard to the time of checking and selection of items, significantly improves the effectiveness of an audit. Normally, areas over which surprise check can be employed are-

(i) Verification of cash and investments.

(ii) Inventory.

(iii) Internal control and internal checks.

(iv) Books of prime entries and statutory registers.

(b) Duties of C&AG: The Comptroller & Auditor General’s (Duties, Powers and Conditions of Service) Act, 1971 lays down duties of the C&AG as under-

(i) **Compile and submit Accounts of Union and States** - The C&AG shall be responsible for compiling the accounts of the Union and of each State from the
initial and subsidiary accounts rendered to the audit and accounts offices under his control by treasuries, offices or departments responsible for the keeping of such account.

(ii) **General Provisions Relating to Audit** - It shall be the duty of the C&AG –

(a) to audit and report on all expenditure from the Consolidated Fund of India and of each State and of each Union Territory having a Legislative Assembly and to ascertain whether the moneys shown in the accounts as having been disbursed were legally available for and applicable to the service or purpose to which they have been applied or charged and whether the expenditure conforms to the authority which governs it;

(b) to audit and report all transactions of the Union and of the States relating to Contingency Funds and Public Accounts;

(c) to audit and report on all trading, manufacturing profit and loss accounts and balance-sheets and other subsidiary accounts kept in any department of the Union or of a State.

(iii) **Audit of Receipts and Expenditure** - Where any body or authority is substantially financed by grants or loans from the Consolidated Fund of India or of any State or of any Union Territory having a Legislative Assembly, the Comptroller and Auditor General shall, subject to the provisions of any law for the time being in force applicable to the body or authority, as the case may be, audit all receipts and expenditure of that body or authority and to report on the receipts and expenditure audited by him.

(iv) **Audit of Grants or Loans** - Where any grant or loan is given for any specific purpose from the Consolidated Fund of India or of any State or of any Union Territory having a Legislative Assembly to any authority or body, not being a foreign State or international organisation, the Comptroller and Auditor General shall scrutinise the procedures by which the sanctioning authority satisfies itself as to the fulfillment of the conditions subject to which such grants or loans were given and shall for this purpose have right of access, after giving reasonable previous notice, to the books and accounts of that authority or body.

(v) **Audit of Receipts of Union or States** - It shall be the duty of the Comptroller and Auditor General to audit all receipts which are payable into the Consolidated Fund of India and of each State and of each Union Territory having a Legislative Assembly and to satisfy himself that the rules and procedures in that behalf are designed to secure an effective check on the assessment, collection and proper allocation of revenue and are being duly observed and to make this purpose such examination of the accounts as he thinks fit and report thereon.

(vi) **Audit of Accounts of Stores and Inventory** - The Comptroller and Auditor General shall have authority to audit and report on the accounts of stores and
inventory kept in any office or department of the Union or of a State.

(vii) **Audit of Government Companies and Corporations** - The duties and powers of the Comptroller and Auditor General in relation to the audit of the accounts of government companies shall be performed and exercised by him in accordance with the provisions of the Companies Act, 2013. The comptroller and Auditor-General of India shall appoint the auditor under sub-section (5) or sub-section (7) of section 139 (i.e. appointment of First Auditor or Subsequent Auditor) and direct such auditor the manner in which the accounts of the Government company are required to be audited and thereupon the auditor so appointed shall submit a copy of the audit report to the Comptroller and Auditor-General of India which, among other things, include the directions, if any, issued by the Comptroller and Auditor-General of India, the action taken thereon and its impact on the accounts and financial statement of the company.

(c) **Circumstances where Retiring Auditor Cannot be Reappointed:** In the following circumstances, the retiring auditor cannot be reappointed-

(i) A specific resolution has not been passed to reappoint the retiring auditor.

(ii) The auditor proposed to be reappointed does not possess the qualification prescribed under section 141 of the Companies Act, 2013.

(iii) The proposed auditor suffers from the disqualifications under section 141(3), 141(4) and 144 of the Companies Act, 2013.

(iv) He has given to the company notice in writing of his unwillingness to be reappointed.

(v) A resolution has been passed in AGM appointing somebody else or providing expressly that the retiring auditor shall not be reappointed.

(vi) A written certificate has not been obtained from the proposed auditor to the effect that the appointment or reappointment, if made, will be in accordance within the limits specified under section 141(3)(g) of the Companies Act, 2013.

5. (a) **Risk of Material Misstatement at the Assertion Level:** According to SA 315 "Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and its Environment", risks of material misstatement at the assertion level for classes of transactions, account balances, and disclosures need to be considered because such consideration directly assists in determining the nature, timing, and extent of further audit procedures at the assertion level necessary to obtain sufficient appropriate audit evidence. In identifying and assessing risks of material misstatement at the assertion level, the auditor may conclude that the identified risks relate more pervasively to the financial statements as a whole and potentially affect many assertions.
(b) Audit Procedures to Obtain Audit Evidence: According to SA 500 “Audit Evidence”, the auditor may obtain evidence by one or more of the following audit procedures:

**Inspection:** Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production. An example of inspection used as a test of controls is inspection of records for evidence of authorisation.

Some documents represent direct audit evidence of the existence of an asset, for example, a document constituting a financial instrument such as a inventory or bond. Inspection of such documents may not necessarily provide audit evidence about ownership or value. In addition, inspecting an executed contract may provide audit evidence relevant to the entity’s application of accounting policies, such as revenue recognition.

Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity’s rights and obligations or the valuation of the assets. Inspection of individual inventory items may accompany the observation of inventory counting.

**Observation:** Observation consists of looking at a process or procedure being performed by others, for example, the auditor’s observation of inventory counting by the entity’s personnel, or of the performance of control activities. Observation provides audit evidence about the performance of a process or procedure, but is limited to the point in time at which the observation takes place, and by the fact that the act of being observed may affect how the process or procedure is performed.

**External Confirmation:** An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium. External confirmation procedures frequently are relevant when addressing assertions associated with certain account balances and their elements. However, external confirmations need not be restricted to account balances only. For example, the auditor may request confirmation of the terms of agreements or transactions an entity has with third parties; the confirmation request may be designed to ask if any modifications have been made to the agreement and, if so, what the relevant details are. External confirmation procedures also are used to obtain audit evidence about the absence of certain conditions, for example, the absence of a “side agreement” that may influence revenue recognition.

**Recalculation:** Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.
Reperformance: Reperformance involves the auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal control.

Analytical Procedures: Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial and non-financial data. Analytical procedures also encompass the investigation of identified fluctuations and relationships that are inconsistent with other relevant information or deviate significantly from predicted amounts.

Inquiry: Inquiry consists of seeking information of knowledgeable persons, both, financial and non-financial, within the entity or outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures. Inquiries may range from formal written inquiries to informal oral inquiries. Evaluating responses to inquiries is an integral part of the inquiry process.

Responses to inquiries may provide the auditor with information not previously possessed or with corroborative audit evidence. Alternatively, responses might provide information that differs significantly from other information that the auditor has obtained, for example, information regarding the possibility of management override of controls. In some cases, responses to inquiries provide a basis for the auditor to modify or perform additional audit procedures.

Although corroboration of evidence obtained through inquiry is often of particular importance, in the case of inquiries about management intent, the information available to support management's intent may be limited. In these cases, understanding management's past history of carrying out its stated intentions, management's stated reasons for choosing a particular course of action, and management's ability to pursue a specific course of action may provide relevant information to corroborate the evidence obtained through inquiry.

In respect of some matters, the auditor may consider it necessary to obtain written representations from management and, where appropriate, those charged with governance to confirm responses to oral inquiries.

(c) Different Design and Procedural Aspects of a Computerised Information System (CIS): The development of Computerised Information Systems (CIS) will generally result in design and procedural characteristics that are different from those found in manual systems. These different design and procedural aspects of CIS are-

(i) Consistency of Performance: Computerised Information Systems (CIS) perform functions exactly as programmed and are potentially more reliable than manual systems, provided that all transaction type and conditions that could occur are anticipated and incorporated into the system.

(ii) Programmed Control Procedures: The nature of computer processing allows the design of internal control procedures in computer programs. These
procedures can be designed to provide controls with limited visibility (e.g., protection of data against unauthorized access may be provided by passwords). Other procedures can be designed for use with manual intervention, such as review of reports printed for exception and error reporting, and reasonableness and limit checks of data.

(iii) **Single Transaction Update of Multiple or Data Base Computer Files:** A single input to the accounting system may automatically update all records associated with the transaction (e.g., shipment of goods documents may update the sales and customers’ accounts receivable files as well as the inventory file). Thus, an erroneous entry in such a system may create errors in various financial accounts.

(iv) **Systems Generated Transactions:** Certain transactions may be initiated by the Computerised Information System (CIS) itself without the need for an input document. The authorisation of such transactions may neither be supported by visible input documentation nor documented in the same way as transactions which are initiated outside the CIS (e.g., interest may be calculated and charged automatically to customers’ account balances on the basis of pre-authorized terms contained in a computer program).

(v) **Vulnerability of Data and Programme Storage Media:** Large volumes of data and the computer programs used to process such data may be stored on portable or fixed storage media, such as magnetic discs and tapes. These media are vulnerable to theft, or international or accidental destruction.

6. (a) **Special Points in Audit of a Partnership Firm:** Matters which should be specially considered in the audit of accounts of a partnership firm are as under-

(i) Confirming that the letter of appointment, signed by a partner, duly authorised, clearly states the nature and scope of audit contemplated by the partners, specially the limitation, if any, under which the auditor shall have to function.

(ii) Examine the partnership deed signed by all partners and its registration with the registrar of firms. Also ascertain from the partnership deed about capital contribution, profit sharing ratios, interest on capital contribution, powers and responsibilities of the partners, etc.

(iii) Studying the minute book, if any, maintained to record the policy decision taken by partners specially the minutes relating to authorisation of extraordinary and capital expenditure, raising of loans, purchase of assets, extraordinary contracts entered into and other such matters which are not of a routine nature.

(iv) Verifying that the business in which the partnership is engaged is authorised by the partnership agreement; or by any extension or modification thereof agreed to subsequently.

(v) Examining whether books of account appear to be reasonable and are
considered adequate in relation to the nature of the business of the partnership.

(vi) Verifying generally that the interest of no partner has suffered prejudicially by an activity engaged in by the partnership which, it was not authorised to do under the partnership deed or by any violation of a provision in the partnership agreement.

(vii) Confirming that a provision for the firm’s tax payable by the partnership has been made in the accounts before arriving at the amount of profit divisible among the partners. Also see various requirements of legislations applicable to the partnership firm like Section 44(AB) of the Income-tax Act, 1961 have been complied with.

(viii) Verifying that the profits and losses have been divided among the partners in their agreed profit-sharing ratio.

(b) Comment on Matters Contained under Section 143(1) of the Companies Act, 2013: Section 143(1) of the Act deals with duties of an auditors requiring auditor to make an enquiry in respect of specified matters. The matters in respect of which the enquiry has to be made by the auditor include relating to loans and advances, transactions represented merely by book entries, investments sold at less than cost price, loans and advances shown as deposits, etc. Since the law requires the auditor to make an enquiry, the Institute opined that the auditor is not required to report on the matters specified in sub-section (1) unless he has any special comments to make on any of the items referred to therein. If the auditor is satisfied as a result of the enquiries, he has no further duty to report that he is so satisfied. Therefore, the auditor of XYZ Ltd. is correct in non-reporting on the matters specified in Section 143(1).

(c) Audit Procedure for Conducting the Audit of Non-Governmental Organisation:

NGOs can be defined as non-profit making organisations which raise funds from members, donors or contributors apart from receiving donation of time, energy and skills for achieving their social objectives. Non-Governmental Organisations are generally incorporated as societies under the Societies Registration, Act, 1860 or as a trust under the India Trust Act, 1882, or under any other law corresponding to these Acts enforced in any part of India. NGOs can also be incorporated as a company under section 8 of the Companies Act, 2013. While planning the audit of a Non-Governmental Organisation (NGO), the auditor may concentrate on the following:

(i) Knowledge of the NGO’s work, its mission and vision, areas of operations and environment in which it operate.

(ii) Reviewing the legal form of the organisation and its Memorandum of Association, Articles of Association, rules and Regulations.

(iii) Reviewing the NGO’s Organisation chart, Financial and Administrative Manuals, Project and Programme Guidelines, Funding Agencies Requirements and Formats, budgetary policies, if any.
(iv) Examination of minutes of the Board/Managing Committee/Governing Body/Management and Committees thereof to ascertain the impact of any decisions on the financial records.

(v) Study the accounting system, procedures, internal controls and internal checks existing for the NGO and verify their applicability.

The audit programme should include in a sequential order all assets, liabilities, income and expenditure ensuring that no material is omitted:

(i) **Corpus fund**: The contributions/grants received towards corpus are vouched with reference to the letters from the donor(s). The interest income is checked with investment Register and physical investments in hand.

(ii) **Reserves**: Vouch transfers from projects/programmes with donor’s letters and board resolutions of NGO. Also check transfers and adjustments made during the year.

(iii) **Ear-marked Funds**: Check requirements of donors’ institutions, board resolution of NGO, rules and regulations of the schemes of the ear-marked funds.

(iv) **Project/Agency Balances**: Vouch disbursements and expenditures as per agreements with donors for each of the balances.

(v) **Loans**: Vouch loans with loan agreements receipt counterfoil issued.

(vi) **Fixed Assets**: Vouch all acquisitions/sale or disposal of assets including depreciation and the authorisations for the same. Also check donor’s letters/agreements for the grants. For immovable property, check title, etc.

(vii) **Investments**: Check Investment Register and the investments physically ensuring that investments are in the name of the NGO. Verify further investments and dis-investments for approval by the appropriate authority and reference in the bank accounts for the principal amount and interest.

(viii) **Cash in Hand**: Physically verify the cash in hand and imprest balance, at the close of the year and whether it tallies with the books of accounts.

(ix) **Bank Balance**: Check the bank reconciliation statements and ascertain details for old outstanding and unadjusted amounts.

(x) **Inventory in Hand**: Verify inventory in hand and obtain certificate from the management for the quantities and valuation of the same.

(xi) **Programme and Project Expenses**: Verify agreement with donor/contributor (s) supporting the particular programme or project to ascertain the conditions with respect to undertaking the programme/project and accordingly, in the case of programmes/projects involving contracts, ensure that income tax is deducted, deposited and returns filed and verify the terms of the contract.
(xii) **Establishment Expenses:** Verify that provident fund, life insurance and their administrative charges are deducted, contributed and deposited within the prescribed time. Also check other office and administrative expenses such as postage, stationery, travelling, etc.

**The receipt of income of NGO may be checked on the following lines:**

(i) **Contribution and Grants for projects and programmes:** Check agreements with donors and grants letters to ensure that funds received have been accounted for. Check that all foreign contribution receipts are deposited in the foreign contribution bank account as notified under the Foreign Contribution (Regulation) Act, 1976.

(ii) **Receipts from Fund arising programmes:** Verify in detail the internal control system and ascertain who are the persons responsible for collection of funds and mode of receipt. Ensure that collections are counted and deposited in the bank daily.

(iii) **Membership Fees:** Check fees received with membership register; ensure proper classification is made between entrance and annual fees and life membership fees. Reconcile fees received with fees to be received during the year.

(iv) **Subscription:** Check with subscription register and receipts issued. Reconcile subscription received with printing and dispatch of corresponding magazine / circulars / periodicals. Check the receipts with subscription rate schedule.

(v) **Interest and Dividends:** Check the interest and dividends received and receivable with investments held during the year.

7. (a) **Fraudulent Financial Reporting:** Fraudulent financial reporting involves intentional misstatements including omissions of amounts or disclosures in financial statements to deceive financial statement users. It can be caused by the efforts of management to manage earnings in order to deceive financial statement users by influencing their perceptions as to the entity’s performance and profitability. Such earnings management may start out with small actions or inappropriate adjustment of assumptions and changes in judgments by management. Pressures and incentives may lead these actions to increase to the extent that they result in fraudulent financial reporting.

In some entities, management may be motivated to reduce earnings by a material amount to minimize tax or to inflate earnings to secure bank financing.

Fraudulent financial reporting may be accomplished by the following:

(i) Manipulation, falsification (including forgery), or alteration of accounting records or supporting documentation from which the financial statements are prepared.

(ii) Misrepresentation in or intentional omission from, the financial statements of
events, transactions or other significant information.

(iii) Intentional misapplication of accounting principles relating to amounts, classification, manner of presentation, or disclosure.

Fraudulent financial reporting often involves management override of controls that otherwise may appear to be operating effectively.

(b) Concept of Materiality: According to SA 320 "Materiality in Planning and Performing an Audit", financial reporting frameworks often discuss the concept of materiality in the context of the preparation and presentation of financial statements. Although financial reporting frameworks may discuss materiality in different terms, they generally explain that:

- Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements;

- Judgments about materiality are made in the light of surrounding circumstances, and are affected by the auditor’s perception of the financial information needs of users of the financial statements, and by the size or nature of a misstatement, or a combination of both; and

- Judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.

1. Such a discussion, if present in the applicable financial reporting framework, provides a frame of reference to the auditor in determining materiality for the audit. If the applicable financial reporting framework does not include a discussion of the concept of materiality, the characteristics referred above provides the auditor with such a frame of reference.

2. The auditor’s determination of materiality is a matter of professional judgment, and is affected by the auditor’s perception of the financial information needs of users of the financial statements. In this context, it is reasonable for the auditor to assume that users:

   (a) Have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;

   (b) Understand that financial statements are prepared, presented and audited to levels of materiality;

   (c) Recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment and the consideration of future events; and
(d) Make reasonable economic decisions on the basis of the information in the financial statements.

(3) The concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor’s report.

(c) Advantages of Statistical Sampling in Auditing: The advantages of using statistical sampling technique in auditing are-

(i) Sample size does not increase in proportion to the increase in the size of population.

(ii) Sample selection is more objective and based on law of probability.

(iii) This provides a means of estimating the minimum sample size associated with a specified risk and precision level.

(iv) It also provides a means for deriving a calculated risk and corresponding precision.

(v) It may provide a better description of a large mass of data than a complete examination of all the data, since non-sampling errors such as processing and clerical mistake are not large.

(d) Quality Control for Audit Work at Firm Level: SA 220 on Quality Control for an Audit of Financial Statements deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. Quality control systems, policies and procedures are the responsibility of the audit firm. Within the context of the firm’s system of quality control, engagement teams have a responsibility to implement quality control procedures that are applicable to the audit engagement and provide the firm with relevant information to enable the functioning of that part of the firm’s system of quality control relating to independence. The requirements are-

(i) Leadership Responsibilities for Quality on Audits: The engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned.

(ii) Relevant Ethical Requirements: Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement.

(iii) Acceptance and Continuance of Client Relationships and Audit Engagements: The engagement partner shall be satisfied that appropriate
procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed, and shall determine that conclusions reached in this regard are appropriate.

(iv) **Assignment of Engagement Teams**: The engagement partner shall be satisfied that the engagement team, and any auditor’s experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to perform the audit engagement in accordance with professional standards and regulatory and legal requirements and enable an auditor’s report that is appropriate in the circumstances to be issued.

(v) **Engagement Performance**: The engagement partner shall take responsibility for the direction, supervision and performance of the audit engagement. He shall take responsibility for reviews being performed in accordance with the firm’s review policies and procedures and shall take responsibility for the engagement team undertaking appropriate consultation on difficult or contentious matters. For audits of financial statements of listed entities, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required, the engagement partner shall determine that an engagement quality control reviewer has been appointed. Further, if differences of opinion arise within the engagement team, with those consulted or, where applicable, between the engagement partner and the engagement quality control reviewer, the engagement team shall follow the firm’s policies and procedures for dealing with and resolving differences of opinion.

(vi) **Monitoring**: The engagement partner shall consider the results of the firm’s monitoring process as evidenced in the latest information circulated by the firm and, if applicable, other network firms and whether deficiencies noted in that information may affect the audit engagement.

(e) **Audit Trail**: An audit trail refers to a situation where it is possible to relate ‘one-to-one’ basis, the original input along with the final output. The work of an auditor would be hardly affected if “Audit Trail” is maintained i.e. if it were still possible to relate, on a ‘one-to-one’ basis, the original input with the final output. A simplified representation of the documentation in a manually created audit trail.

For example, the particular credit notes may be located by the auditor at any time he may wish to examine them, even months after the balance sheet date. He also has the means, should he so wish, of directly verifying the accuracy of the totals and sub-totals that feature in the control listing, by reference to individual credit notes. He can, of course, check all detailed calculations, casts and postings in the accounting records, at any time.

In first and early second-generation computer systems, such a complete and trail was generally available, no doubt, to management’s own healthy skepticism of what the
new machine could be relied upon to achieve – an attitude obviously shared by the auditor.

It is once iterated that there is an abundance of documentation upon which the auditor can use his traditional symbols of scrutiny, in the form of colored ticks and rubber stamps. Specifically:

(i) The output itself is as complete and as detailed as in any manual system.

(ii) The trail, from beginning to end, is complete, so that all documents may be identified by located for purposes of vouching, totaling and cross-referencing.

Any form of audit checking is possible, including depth testing in either direction.