2

Audit Strategy, Planning and Programming

Question 1

Describe how you would identify the inherent risk at the account balance and class of transaction level in the planning process of the audit of a large multi-locational company.

(4 Marks, November, 2014)

Answer

Evaluating Inherent Risk: To assess inherent risk, the auditor would use professional judgment to evaluate numerous factors, having regard to his experience of the entity from previous audit engagements of the entity, any controls established by management to compensate for a high level of inherent risk, and his knowledge of any significant changes which might have taken place since his last assessment.

Inherent audit risk at the level of Account Balance and Class of Transactions is:

(i) Quality of the accounting system.

(ii) Financial statements are likely to be susceptible to misstatement, for example, accounts which required adjustment in the prior period or which involve a high degree of estimation.

(iii) The complexity of underlying transactions and other events which might require using the work of an expert.

(iv) The degree of judgement involved in determining account balances.

(v) Susceptibility of assets to loss or misappropriation, for example, assets which are highly desirable and movable such as cash.

(vi) The completion of unusual and complex transactions, particularly at or near period end.

(vii) Transactions not subjected to ordinary processing.

Question 2

XY Ltd. is a manufacturing company, provided following details of wastages of raw materials in percentage, for various months. You have been asked to enquire into causes of abnormal wastage of raw materials.

Draw out an audit plan.

Wastage percentage are

July 2010	*1.5%*	
Aug 2010	*1.7%*	
Sep 2010	*1.4%*	
Oct 2010	*4.1%.*	*(8 Marks, November, 2011)*

Answer

Audit Plan to Locate the Abnormal Wastage of Raw Material: To locate the reasons for the abnormal wastage, the auditor should first of all assess the general requirements as under-

(i) Procure a list of raw materials, showing the names and detailed characteristics of each raw material.

(ii) Obtain the standard consumption figures, and ascertain the basis according to which normal wastage figures have been worked out. Examine the break-up of a normal wastage into that in process, storage and handling stages. Also obtain control reports, if any, in respect of manufacturing costs with reference to predetermined standards.

(iii) Examine the various records maintained for recording separately the various lots purchased and identification of each lot with actual material consumption and for ascertaining actual wastage figures therein.

(iv) Obtain reports of Preventive Maintenance Programme of machinery to ensure that the quality of goods manufacture is not of sub-standard nature or leads to high scrappage work.

(v) Assess whether personnel employed are properly trained and working efficiently.

(vi) See whether quality control techniques have been consistent or have undergone any change.

(vii) Examine inventory plans and procedures in report of transportation storage efficiency, deterioration, pilferage and whether the same are audited regularly.

(viii) Examine whether the basis adopted for calculating wastage for September is the same as was adopted for the other three months.

(ix) Obtain a statement showing break up of wastage figures in storage, handling and process for the four months under reference and compare the results of the analysis for each of the four months.

In addition, some specific reasons for abnormal wastage in process may be considered by the auditor are as under:

(i) Examine laboratory reports and inspection reports to find out if raw materials purchased were of a poor quality or were of sub-standard quality. This will be most useful if it is possible to identify the wastage out of each lot that has been purchased.

(ii) Machine breakdown, power failure, etc. may also result into loss of materials in process. Check the machine utilisation statements.

(iii) A high rate of rejections in the finished lots may also be responsible for abnormal wastage; therefore, examine the inspectors' reports in respect of inspection carried out on the completion of each stage of work or process.

(iv) It is possible that the wastage may have occurred because the particular lot out of which issues were made was lying in the store for a long time, leading to deterioration in quality or because of a change in the weather which may have led to the deterioration. Compare the wastage figures.

(v) Abnormal wastage in storage and handling may arise due to the following reasons:

(1) Write offs on account of reconciliation of physical and book stocks: In case of periodical physical stock taking, such write offs will be reflected only in the month such reconciliation takes place.

(2) Accidental, theft or fire losses in storage: The auditor should examine the possibility of these for the purpose.

(vi) Examine whether any new production line was taken up during the month in respect of which standard input-output ratio is yet to be set-up.

Question 3

A & Co. was appointed as auditor of Great Airways Ltd. As the audit partner what factors shall be considered in the development of overall audit plan? (8 Marks, May, 2011)

Answer

Development of an Overall Plan: Overall plan is basically intended to provide direction for audit work programming and includes the determination of timing, manpower development and co-ordination of work with the client, other auditors and other experts. The auditor should consider the following matters in developing his overall plan for the expected scope and conduct of the audit-

(i) Terms of his engagement and any statutory responsibilities.

(ii) Nature and timing of reports or other communications.

(iii) Applicable Legal or Statutory requirements.

(iv) Accounting policies adopted by the clients and changes, if any, in those policies.

(v) The effects of new accounting and auditing pronouncement on the audit.

(vi) Identification of significant audit areas.

(vii) Setting of materiality levels for the audit purpose.

(viii) Conditions requiring special attention such as the possibility of material error or fraud or involvement of parties in whom directors or persons who are substantial owners of the entity are interested and with whom transactions are likely.

(ix) Degree of reliance to be placed on the accounting system and internal control.

(x) Possible rotation of emphasis on specific audit areas.

(xi) Nature and extent of audit evidence to be obtained.

(xii) Work of the internal auditors and the extent of reliance on their work, if any in the audit.

(xiii) Involvement of other auditors in the audit of subsidiaries or branches of the client and involvement of experts.

(xiv) Allocation of works to be undertaken between joint auditors and the procedures for its control and review.

(xv) Establishing and coordinating staffing requirements.

Question 4

What are the points to be considered while evaluating the "Knowledge of the Business" in the conduct of an audit? (8 Marks, June, 2009)

Answer

Evaluating the Knowledge of the Business: The broad matters to be considered while obtaining knowledge of business for a new audit assignment are set out in SA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment. These are-

(i) Relevant industry, regulatory, economic and other external factors including the applicable financial reporting framework.

(ii) The nature of the entity, including:

  (a) its operations;

  (b) its ownership and governance structures;

  (c) the types of investments that the entity is making and plans to make, including investments in special-purpose entities; and

  (d) the way that the entity is structured and how it is financed; to enable the auditor to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements.

(iii) The entity's selection and application of accounting policies.

(iv) The entity's objectives and strategies, and those related business risks that may result in risks of material misstatement.

(v) The measurement and review of the entity's financial performance.

In addition to the importance of knowledge of the client's business in establishing the overall audit plan, such knowledge helps the auditor to identify areas of special audit consideration, to evaluate the reasonableness both of accounting estimates and management representations, and to make judgement regarding the appropriateness of accounting policies and disclosures.

Question 5

You have been appointed as the auditor of a Multiplex Cinema House. Draw an audit programme in respect of its Revenue and Expenditure. (8 Marks, November, 2009)

Answer

Audit Programme of Multiplex

(i) Peruse the Memorandum of Association and Articles of Association of the entity.

(ii) Ensure the object clause permits the entity to engage in this type of business.

(iii) In the case of income from sale of tickets:

  (a) Verify the control system as to how it is ensured that the collections on sale of tickets of various shows are properly accounted.

  (b) Verify the system of relating to online booking of various shows and the system of realization of money.

  (c) Check that there is overall system of reconciliation of collections with the number of seats available for different shows on a day.

(iv) Verify the internal control system and its effectiveness relating to the income from cafe shops, pubs etc., located within the multiplex.

(v) Verify the system of control exercised relating to the income receivable from advertisements exhibited within the premises and inside the hall such as hoarding, banners, slides, short films etc.

(vi) Verify the system of collection from the parking areas in respect of the vehicles parked by the customers.

(vii) In the case of payment to the distributors verify the system of payment which may be either through out right payment or percentage of collection or a combination of both. Ensure at the time of settlement any payment of advance made to the distributor is also adjusted against the amount due.

(viii) Verify the system of payment of salaries and other benefits to the employees and ensure that statutory requirements are complied with.

(ix) Verify the payments effected in respect of the maintenance of the building and ensure the same is in order.

Question 6

M/s PQR & Company, Chartered Accountants have been appointed Statutory Auditors of a listed Company for the year ended 31st March, 2008. Draft an appropriate engagement letter to be sent to the Board of Directors for the same. (12 Marks, November, 2007)

Answer

Draft of an Engagement Letter:

To, the Board of Directors of _____

(Address)

Dear Sir,

We refer to the letter dated _____ informing us about our appointment as the auditors of the Company. You have requested that we audit the financial statements of the Company as

defined in Section 2(40) of the Companies Act, 2013 ('2013 Act'), for the financial year(s) beginning April 1, 20XX and ending March 31, 20YY. The financial statements of the Company include, where applicable, consolidated financial statements of the Company and of all its subsidiaries, associate companies and joint ventures. We are pleased to confirm our acceptance and our understanding of this audit engagement by means of this letter.

Our audit will be conducted with the objective of our expressing an opinion if the aforesaid financial statements give the information required by the 2013 Act in the manner so required, and give a true and fair view in conformity with the applicable accounting principles generally accepted in India, of the state of affairs of the Company as at 31st March, 20YY, and its profit/loss and its cash flows for the year ended on that date which, inter alia, includes reporting in conjunction whether the Company has an adequate internal financial controls system over financial reporting in place and the operating effectiveness of such controls. In forming our opinion on the financial statements, we will rely on the work of branch auditors appointed by the Company and our report would expressly state the fact of such reliance.

We will conduct our audit in accordance with the Standards on Auditing (SAs), issued by the Institute of Chartered Accountants of India (ICAI) and deemed to be prescribed by the Central Government in accordance with Section 143(10) of the 2013 Act. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements. An audit involves performing procedures to obtain audit evidence about the amounts and the disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal financial control relevant to the Company's preparation of the financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances.

The terms of reference for our audit of internal financial controls over financial reporting carried out in conjunction with our audit of the Company's financial statements will be as stated in the separate engagement letter for conducting such audit and should be read in conjunction with this letter.

An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made by the Management, as well as evaluating the overall presentation of the financial statements.

Because of the inherent limitations of an audit, including the possibility of collusion or improper management override of controls, there is an unavoidable risk that material misstatements due to fraud or error may occur and not be detected, even though the audit is properly planned and performed in accordance with the SAs. Also, projections of any evaluation of the internal financial controls over financial reporting to future periods are subject to the risk that the internal financial control over financial reporting may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our audit will be conducted on the basis that the Management and those charged with governance (Audit Committee / Board) acknowledge and understand that they have the responsibility:

(a) For the preparation of financial statements that give a true and fair view in accordance with the applicable Financial Reporting Standards and other generally accepted accounting principles in India. This includes:

- Compliance with the applicable provisions of the 2013 Act;
- Proper maintenance of accounts and other matters connected therewith;
- The responsibility for the preparation of the financial statements on a going concern basis;
- The preparation of the annual accounts in accordance with, the applicable accounting standards and providing proper explanation relating to any material departures from those accounting standards;
- Selection of accounting policies and applying them consistently and making judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the Company at the end of the financial year and of the profit and loss of the Company for that period;
- Taking proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of the 2013 Act for safeguarding the assets of the Company and for preventing and detecting fraud and other irregularities;
- Laying down internal financial controls to be followed by the Company and that such internal financial controls are adequate and were operating effectively; and
- Devising proper systems to ensure compliance with the provisions of all applicable laws and that such systems were adequate and operating effectively.

(b) Identifying and informing us of financial transactions or matters that may have any adverse effect on the functioning of the Company.

(c) Identifying and informing us of:

- All the pending litigations and confirming that the impact of the pending litigations on the Company's financial position has been disclosed in its financial statements;
- All material foreseeable losses, if any, on long term contracts including derivative contracts and the accrual for such losses as required under any law or accounting standards; and
- Any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the Company.

(d) Informing us of facts that may affect the financial statements, of which Management may become aware during the period from the date of our report to the date the financial statements are issued.

(e) Identifying and informing us as to whether any director is disqualified as on March 31, 20YY from being appointed as a director in terms of Section 164(2) of the 2013 Act. This should be supported by written representations received from the directors as on March 31, 20YY and taken on record by the Board of Directors.

(f) To provide us, inter alia, with:

(i) Access, at all times, to all information, including the books, accounts, vouchers and other records and documentation of the Company, whether kept at the Head Office or elsewhere, of which the Management is aware that are relevant to the preparation of the financial statements such as records, documentation and other matters. This will include books of account maintained in electronic mode;

(ii) Access, at all times, to the records of all the subsidiaries (including associate companies and joint ventures as per Explanation to Section 129(3) of the 2013 Act) of the Company in so far as it relates to the consolidation of its financial statements, as envisaged in the 2013 Act;

(iii) Access to reports, if any, relating to internal reporting on frauds (e.g., vigil mechanism reports etc.), including those submitted by cost accountant or company secretary in practice to the extent it relates to their reporting on frauds in accordance with the requirements of Section 143(12) of the 2013 Act;

(iv) Additional information that we may request from the Management for the purposes of our audit;

(v) Unrestricted access to persons within the Company from whom we deem it necessary to obtain audit evidence. This includes our entitlement to require from the officers of the Company such information and explanations as we may think necessary for the performance of our duties as the auditors of the Company; and

(vi) All the required support to discharge our duties as the statutory auditors as stipulated under the Companies Act, 2013/ ICAI standards on auditing and applicable guidance.

As part of our audit process, we will request from the Management written confirmation concerning representations made to us in connection with our audit.

Our report prepared in accordance with relevant provisions of the 2013 Act would be addressed to the shareholders of the Company for adoption of the accounts at the Annual General Meeting. In respect of other services, our report would be addressed to the Board of Directors. The form and content of our report may need to be amended in the light of our audit findings.

In accordance with the requirements of Section 143(12) of the 2013 Act, if in the course of performance of our duties as auditor, we have reason to believe that an offence involving fraud is being or has been committed against the Company by officers or employees of the Company, we will be required to report to the Central Government, in accordance with the rules prescribed in this regard which, inter alia, requires us to forward our report to the Board or Audit Committee, as the case may be, seeking their reply or observations, to enable us to forward the same to the Central Government.

As stated above, given that we are required as per Section 143(12) of the Act to report on frauds, such reporting will be made in good faith and, therefore, cannot be considered as breach of maintenance of client confidentiality requirements or be subject to any suit, prosecution or other legal proceeding since it is done in pursuance of the 2013 Act or of any rules or orders made thereunder.

We also wish to invite your attention to the fact that our audit process is subject to 'peer review' / 'quality review' under the Chartered Accountants Act, 1949. The reviewer(s) may inspect, examine or take abstract of our working papers during the course of the peer review/quality review.

We may involve specialists and staff from our affiliated network firms to perform certain specific audit procedures during the course of our audit.

In terms of Standard on Auditing 720 – "The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Statements" issued by the ICAI and deemed to be prescribed by the Central Government in accordance with Section 143(10) of the 2013 Act , we request you to provide to us a Draft of the Annual Report containing the audited financial statements so as to enable us to read the same and communicate material inconsistencies, if any, with the audited financial statements, before issuing the auditor's report on the financial statements.

Our fees will be billed as the work progresses.

This letter should be read in conjunction with our letter dated _____ for the Audit of Internal Financial Controls Over Financial Reporting under the 2013 Act, in respect of which separate fees have been fixed/will be mutually agreed.

We look forward to full cooperation from your staff during our audit.

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our audit of the financial statements including our respective responsibilities.

Yours faithfully,

(Signature)

(Name of the Member)

(Designation)[1]

PQR & Company

Chartered Accountants

Date:

Place:

[1] Partner or Proprietor, as the case may be.

Copy to: Chairman, Audit Committee

Acknowledged on behalf of _____Company

Name and Designation: _____

Date: _____

Question 7

As a chartered accountants firm draft an engagement letter to the Board of Directors for the compilation of financial statements of XYZ Ltd. as at 31.3.2007. (16 Marks, May, 2007)

Answer

Engagement letter to the Board of Directors for the compilation of financial statements of XYZ Ltd. as at 31.3.2007:

To

The Board of Directors
XYZ Ltd.
……..

You have vide your letter dated ……requested that we compile the Balance Sheet of XYZ Ltd. as at 31.3.20XX and the related Profit and Loss account and the Cash Flow Statement for the year ended on that date.

We are pleased to confirm our acceptance and understanding of the engagement by means of this letter. As no audit or review engagement procedures would be carried out, no opinion on the financial statements will be expressed. Further, our engagement cannot be relied upon to disclose whether frauds or defalcations, or illegal acts exist. However, we will inform you of any such matters which might come to our attention in the course of the engagement.

As Management, you are responsible for:

(a) The accuracy and completeness of the information supplied to us, including maintenance of adequate accounting records and internal controls and selection and application of appropriate accounting policies.

(b) Preparation and presentation of the financial statements of the entity, in accordance with the applicable laws and regulations, if any.

(c) Safeguarding the assets of the entity and also establishing appropriate controls designed to prevent and detect fraud and other irregularities.

(d) Ensuring that the activities of the entity are carried on in accordance with applicable laws and regulations and that it institutes appropriate controls to prevent and detect any non-compliance.

You will confirm that events and transactions are recorded in accordance with the applicable accounting standard(s), issued by the Institute of Chartered Accountants of India and other recognized accounting principles and practices and inform us of any departures therefrom.

As part of our normal procedures, we may request you to provide written confirmations of any information or explanations given to us orally during the course of our work.

We understand that the intended use and distribution of the information we have compiled is (specify purpose)

We look forward to full co-operation with your staff and we trust that they will make available to us whatever records, documents and other information requested in connection with our engagement.

Our fees will be billed as the work progresses.

Please sign and return the attached copy of this letter to indicate that it is in accordance with your understanding of the arrangements for our compilation of your financial statements.

XYZ & Co.
Chartered Accountants
Firm Registration No.

S/d

Question 8

Write a short note on Analytical procedures in planning an audit. *(4 Marks, May, 2007)*

Answer

Analytical Procedures in Planning an Audit: In the planning stage, analytical procedures assist the auditor in understanding the client's business and in identifying areas of potential risk by indicating aspects of and developments in the entity's business of which he was previously unaware. This information will assist the auditor in determining the nature, timing and extent of his other audit procedures.

Analytical procedures in planning the audit use both financial data and non-financial information, such as number of employees, the square feet of selling space, volume of goods produced and similar information.

Question 9

(a) What are general matters to be considered by an auditor while taking up an engagement?

(b) What are the major sources of obtaining information about the client's business?

(4 Marks each, November, 2006)

Answer

(a) General Matters to be considered while taking up a New Engagement:

General Economic factors: General level of economic activity (for example, recession, growth) -

(i) The market and competition.

(ii) Cyclical or seasonal activity.

(iii) Government policies.

The industry: Important conditions affecting the client's business -

(i) The market and competitions.

(ii) Cyclical or seasonal activity.

(iii) Changes in product technology.

(iv) Business risk.

The entity:

(i) Management and ownership- important characteristics.

(ii) Operating Management.

(iii) The entity's business – products markets, suppliers, expenses, operations.

  (1) Nature of business(es) (for example manufacturing whole seller, financial services, import/ exports).

  (2) Location of production facilities, warehouses, offices.

  (3) Employment (for example, by location, supply, wage levels, union contracts, pension commitments, Government regulation).

  (4) Products or services and markets.

(iv) Financial performance– factors concerning the entity's financial condition and profitability.

(v) Reporting environment- external influences which affect management in the preparation of the financial statements.

(vi) Legislation:

  (1) Regulatory environment and requirements.

  (2) Taxation both direct and indirect.

(b) Information about the Client's Business: The auditor can obtain information about client's business from the following sources -

(i) The client's annual Reports to shareholders;

(ii) Minutes of meetings of shareholders, board of directors and important committees;

(iii) Internal financial management report for current and previous periods, including budgets, if any;

(iv) The previous year's audit working papers, and other relevant files;

(v) Firm personnel responsible for non audit services to the client who may be able to provide information on matters that may affect the audit;

(vi) Discussions with the client;

(vii) The client's policy and procedures manual;

(viii) Relevant publications of the Institute of Chartered Accountants of India and other professional bodies, industry publication, trade Journals, magazines, newspapers or text books;

(ix) Consideration of the state of the economy and its effects on the client's business;

(x) Visits to the client's premises and plant facilities to the management.

Question 10

Designing an Audit Strategy is the backbone of the "Audit Planning" process. Discuss.

(10 Marks, May, 2006)

Answer

Audit Strategy as the Backbone of Audit Planning: Audit strategy is concerned with designing optimised audit approaches that seeks to achieve the necessary audit assurance at the lowest cost within the constraints of the information available. The formulation of audit strategy as shall be evident from the process as explained in the following paragraphs in fact shall form the basis of audit planning to achieve the audit objectives in the most efficient and effective manner. Audit strategy generally involves the following steps -

(i) Obtaining Knowledge of Business: SA 315 and SA 330 "Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and its Environment" and "The Auditor's Responses to Assessed Risks" states that in performing an audit of financial statements, the auditor should have or obtain knowledge of the business sufficient to enable the auditor to identify and understand the events, transactions and practices that, in the auditor's judgement, may have a significant effect on the financial statements or on the examination or audit report. Knowledge of the business is a frame of reference within which the auditor exercises professional judgement. Understanding the business and using this information appropriately assists the auditor in assessing risks and identifying problems, planning and performing the audit effectively and efficiently. It also ensures that the audit staff assigned to an audit engagement obtains sufficient knowledge of the business to enable them to carry out the audit work delegated to them. This would also ensure that the audit staff understands the need to be alert for additional information and the need to share that information with the auditor and the other audit staff.

(ii) Performing Analytical Procedures: The purpose of analytical procedures at the planning stage is attention-directing; corroboration is not normally necessary at this stage. The use of the analytical procedures during the planning stage requires the extensive use of accounting and business knowledge and experience to assess the potential for material misstatement in the financial statements as a whole, because the key aspect of the task is to identify the relevant risk indicators and to interpret them properly. Furthermore, analytical techniques applied during the planning stage are not generally as precise as the analytical techniques at the substantive stage.

(iii) Evaluating Inherent Risk: To assess inherent risk, the auditor would use professional judgement to evaluate numerous factors such as quality of accounting system, unusual

pressure on management, etc. having regard to his experience of the entity from previous audit engagements of the entity, any controls established by management to compensate for a high level of inherent risk, and his knowledge of any significant changes which, might have taken place since his last assessment.

(iv) Evaluating Internal Control: The auditor's assessment of the control environment is crucial to the decision on whether to make an extended assessment of controls. This is because a good control environment is conducive to the maintenance of a reliable system of accounting and control procedures. For strategy purposes, the auditor should obtain a sufficient understanding of the control environment. The auditor needs an understanding of the accounting systems, regardless of whether the audit strategy will involve an extended assessment of internal accounting controls. This is done by:

(a) considering the results of gathering or updating information about the client; and

(b) making preliminary judgements about materiality, inherent risk and control effectiveness. These will include identification of the system(s) the auditor proposes to subject to an extended assessment of controls.

Thus, the audit strategy is evolved after considering the engagement objectives, the results of the business review, preliminary judgements as to materiality and identified inherent risks. Audit strategy also considers main points relating to planning and controlling the audit or comments on adequacy of the existing arrangements. Thus, the overall audit plan involving determination of timing, manpower, coordination and the directions in which the audit work has to proceed is dependent upon the audit strategy formulated by the audit firm.

Question 11

As an internal auditor of a Cement Manufacturing Company, draft an audit programme for verification of transportation charges for despatches from the factory. (8 Marks, May, 2006)

Answer

Procedure for Audit of Transportation Charges:

(i) Check rates contracted with transporters for carriage of goods.

(ii) Check whether the rates mentioned as per the contract are correctly taken in the transporter's Invoice.

(iii) In case of discrepancy, check whether the same is authorized by the appropriate sanctioning authority.

(iv) Check that the transporter's invoice includes a delivery challan which has customers stamp indicating the receipt of goods.

(v) In case there is no stamp on the delivery challan, check whether the goods are received back and there is a corresponding inward note.

(vi) Check whether all the goods to be dispatched have a transport booking order reference.

(vii) Check whether each transporter's invoice mentions the transport booking order reference.

(viii) Check whether all the transport booking orders have corresponding transporters names.

(ix) Check whether the transport booking orders are pre-numbered.

(x) Check whether all the invoices are correctly booked in the books of accounts.

(xi) In case there is an additional charge by the transporter due to extra carriage, check for the relevant supporting (like material Inward Note/Customer Rejection Note) and necessary authorization by the sanctioning authority.

(xii) Check whether service-tax on the transporters is correctly calculated and accounted.

(xiii) Verify that there is a mechanism for linking all the Transport Bills to the sale invoices.

Question 12

As an internal auditor for a large manufacturing concern, you are asked to verify whether there are adequate records for identification and value of Plant and Machinery, tools and dies and whether any of these items have become obsolescent and not in use. Draft a suitable audit programme for the above. *(10 Marks, May, 2005)*

Answer

The Internal Audit Programme in connection with Plant and Machinery and Tools and dies may be on the following lines:

(i) *Internal Control Aspects:* The following may be incorporated in the audit programme to check the internal control aspects:

   (a) Maintaining separate register for hired assets, leased asset and jointly owned assets.

   (b) Maintaining register of fixed asset and reconciling to physical inspection of fixed asset and to nominal ledger.

   (c) All movements of assets are accurately recorded.

   (d) Authorisation be obtained for –

      (i) a declaring a fixed asset scrapped.

      (ii) selling a fixed asset.

   (e) Check whether additions to fixed asset register are verified and checked by authorised person.

   (f) Proper recording of all additions and disposal.

   (g) Examining procedure for the purchase of new fixed assets, including written authority, work order, voucher and other relevant evidence.

   (h) Regular review of adequate security arrangements.

   (i) Periodic inspection of assets is done or not.

   (j) Regular review of insurance cover requirements over fixed assets.

(ii) *Assets Register*: To review the registers and records of plant, machinery, etc. showing clearly the date of purchase of assets, cost price, location, depreciation charged, etc.

(iii) *Cost Report and Journal Register*: To review the cost relating to each plant and machinery and to verify items which have been capitalised.

(iv) *Code Register*: To see that each item of plant and machinery has been given a distinct code number to facilitate identification and verify the maintenance of Code Register.

(v) *Physical Verification*: To see physical verification has been conducted at frequent intervals.

(vi) *Movement Register*: To verify (a) whether a Movement Register for movable equipments and (b) log books in case of vehicles, etc. are being maintained properly.

(vii) *Assets Disposal Register*: To review whether assets have been disposed off after proper technical and financial advice and sales/disposal/retirement, etc. of these assets are governed by authorisation, sales memos or other appropriate documents.

(viii) *Spare Parts Register*: To examine the maintenance of a separate register of tools, spare parts for each plant and machinery.

(ix) *Review of Maintenance:* To scrutinise the programme for an actual periodical servicing and overhauling of machines and to examine the extent of utilisation of maintenance department services.

(x) *Review of Obsolescence:* To scrutinise whether expert's opinion have been obtained from time to time to ensure purchase of technically most useful efficient and advanced machinery after a thorough study.

(xi) *Review of R&D:* To review R&D activity and ascertain the extent of its relevance to the operations of the organisation, maintenance of machinery efficiency and prevention of early obsolescence.