

RISK MANAGEMENT AND AUDIT – STAGE-5**Q.2 (a)****Risk Assessment Procedures:**

The auditor shall perform risk assessment procedures to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. Risk assessment procedure shall include the following:

- (i) Inquiries of management and of others within the entity who in the auditor's judgment may have information that is likely to assist in identifying risks of material misstatement due to fraud or error.
- (ii) Analytical procedures.
- (iii) Observation and inspection.

(b) Risk Identification:

The method of recognizing possible "Threats and Opportunities" is known as risk identification.

Risk Assessment:

The quantitative and qualitative evaluation of exposures arising from activity. It includes;

1. Risk identification: The identification and classification of what the risks are and their characteristics.
2. Risk measurement and evaluation: The measurement of possible consequences.
3. Risk Prioritization: How the risks are related to each other.

Risk Management:

The process of determining whether or how much of the risk is acceptable and what action should be taken. It includes:

Diversify or avoid the risk: Changing the nature of the activity to spread the exposure over multiple activities.

Sharing the risk: A form of diversification where the parties in the activity take shares of the risk in the activity. Sharing can be with customers, suppliers, or third parties.

Contingency planning: Establishing controls for known risk. **OR**

A branch of management that deals with the consequences of risk. Quite often this function handles the supervision of insurance policies.

(c) Entity's Risk Assessment Process:

A component of internal control that is the entity's process for:

- Identifying business risks relevant to financial reporting objectives;
- Estimating significance of risks;
- Assessing the likelihood of occurrence; and
- Deciding about actions to address those risks.

RISK MANAGEMENT AND AUDIT – STAGE-5**Q.3 (a) Responsibilities up to the date of the audit report**

The auditor is required to carry out specific procedures outlined in ISA 560 (i.e., pro-active responsibility). Such procedures include:

- reviewing management procedures for identifying events
- reviewing minutes of meetings
- reviewing latest financial information
- enquiry of entity's legal advisors
- enquiry of management
- The auditor should consider whether the appropriate amendments/disclosures have been made in the financial statements and whether there is a need to amend the audit report.

Responsibilities After the date of the audit report: (Any one of the following)

- The auditor has no responsibility for further work (passive responsibility). If the auditor becomes aware of facts which materially affect the financial statements, he should consider whether financial statements need amendment, discuss with management and take action appropriate in the circumstances.
- If directors amend financial statements, reissue and re-date audit report.
- If directors refuse to amend, qualify report if not already released to entity.
- If report released, notify those charged with governance not to issue financial statements and audit report to third parties.
- If financial statements released, seek legal advice.

RISK MANAGEMENT AND AUDIT – STAGE-5**(b) List of Audit Procedures to obtain sufficient Appropriate Audit Evidence that "Too Good to be True" is a Going Concern:**

(Any five of the following)

- Perform subsequent event procedures to identify any events that affect the entity's ability to continue as a going concern.
- Analyse and discuss any budget and forecast prepared by directors; especially the assumptions used.
- Analyse and discuss entity's latest interim financial statements.
- Read minutes of the meeting of directors and those charged with governance in connection with financing difficulties that may be faced by the entity.
- Review current situation and events up to the auditor report date which may cast significant doubt about the entity's ability to continue as a going concern.
- Enquire of Too Good to be True's Legal counsel regarding any possible litigation against it.
- Obtain and review reports of regulatory bodies and authorities.
- Determine the adequacy of support for any planned disposals of assets.
- Evaluate the entity's plan to deal with unfilled customer orders.
- Confirm the existence, terms and adequacy of borrowing facilities.
- Confirm the existence, legality and enforceability of arrangements to provide or maintain financial support with related and third parties and assessing the financial ability of such parties to provide additional funds.

(c)**Scenario 1:**

An unqualified and unmodified audit opinion shall be expressed

Scenario 2

As adequate disclosure is made in the financial statement the auditor shall express an unmodified opinion and include an "Emphasis of Matter" paragraph in the auditor's report just above the "opinion paragraph".

Scenario 3

The auditor shall express an "Adverse opinion" as the use of going concern assumption by management is inappropriate

RISK MANAGEMENT AND AUDIT – STAGE-5

Q.4 (a) The technique of verification revolves around following points:

- (i) Physical Existence: Satisfaction as to the existence of an asset or liability
- (ii) Correct valuation: Ensuring that the asset and liabilities are correctly valued
- (iii) Ownership: Ascertaining whether the question of ownership is valid and true in respect of an asset or liability
- (iv) Correct Disclosure: Satisfaction in respect of the fact that each item of asset and liability is being disclosed as legally required under the Companies Ordinance.
- (v) Assets suffering from a charge: Finding out whether any of the assets of the company is suffering from the charge or not and disclosure to that effect.
- (vi) Proper Authorization: Seeing that there is a proper authorization for an acquisition or disposal or any form of movement in respect of assets and liabilities as laid down in the memorandum and articles of association of the company.

(b) Assertions about classes of transactions and events for the period under audit are:

(Any four of the following)

- (i) Occurrence: Transactions that have been recorded have occurred and pertain to the entity.
- (ii) Completeness: All transactions that should have been recorded have been recorded.
- (iii) Accuracy: Amounts and other data relating to recorded transactions have been recorded appropriately.
- (iv) Cutoff: Transactions that have been recorded in the correct accounting period.
- (v) Classification: Transactions and events that have been recorded in the proper accounts.

(c) Verification of Directors' Fee:

- Check the Memorandum and Articles of Association of the Company prescribing any limit or amount of Directors fee.
- Check the payment made to the Directors is in-accordance with the limit stated in the Memorandum and Articles of association, after adjusting the taxes etc.
- Check that adequate disclosure of Directors fee is made in the financial statement in-accordance with the disclosure requirements.

RISK MANAGEMENT AND AUDIT – STAGE-5

- Q.5 (a)** As used in the statutory Audit Report by the Auditor, True and Fair View, has been taken to include following:
- Free from prejudice and bias
 - Presentation of an objective picture
 - In accordance with generally accepted accounting principles
 - Consistent and having clarity
 - Not misleading but understandable by the reader of financial statements
- (b)** Quality Control Policies adopted by the Audit Firm include:
- (Any six of the following)**
1. Professional requirements
 2. Skills and Competencies
 3. Assignments
 4. Delegation
 5. Consultation
 6. Acceptance and Retention of Clients
 7. Monitoring.
- (c)** The auditor while planning an audit approach for carrying out any efficient and effective audit, should consider the following factors:
1. Knowledge of the clients^a business:
 - a) its special features , influencing financial statements;
 - b) special statements applicable;
 - c) subsequent changes in clients^f business;
 - d) Changes in commercial environment in which client is operating;
 - e) Changes in applicable legislation and reporting requirements and their impact on clients^g financial statements;
 - f) Specific areas in which audit problems were identified in the past.
 2. Assessment of the clients^f system: Became aware of clients^f system of recording and processing transactions and an assessment of its adequacy as a basis for the preparation of financial statements. Auditor should ascertain and document the clients^h accounting system and assess whether or not proper accounting records have been kept as required by law as he/she specifically has to report in respect of these matters in his/her audit Report.

RISK MANAGEMENT AND AUDIT – STAGE-5

Q.6 (a)

(Any five of the following)

Sr. No.	Cost Auditor	Financial Auditor
1.	Cost audit is conducted by auditor to examine the implementation of costing methods and to see if the expenses have been properly incurred and thus cost statement should show a correct and accurate unit cost.	Financial audit conducted by auditor to check the adequacy and accuracy of the books of accounts of a company and to see whether the balance sheet and profit and loss accounts have been prepared according to the prevalent laws.
2.	The cost auditor not only brings to light the errors and frauds, but also he detects the manipulations in the cost accounts.	As the cost records are not checked in details by financial auditor, there are more chances of concealment of the facts.
3.	The cost auditor has to examine the closing inventory in details in terms of its quality or value.	In case of closing inventory, the financial auditor has to examine whether it has been properly shown and correctly valued for the purpose of balance sheet.
4.	Cost auditor has to see that the material has been issued according to production budget.	Financial auditor is not concerned with the receipts and issuance of raw material during the production period.
5.	The field of cost auditor is wider.	The field of financial auditor is limited.
6.	The main aim of cost auditor is to safeguard the interest of management.	The main aim of financial auditor is to safeguard the interest of shareholders.
7.	The cost auditor checks: (i) the total material purchased; (ii) the materials requisition, issuance and consumption; (iii) the surplus materials returned to the stores; (iv) The proper treatment of scraps whether these are sold at some reasonable price or the company has to incur further amount in its disposal. If scraps have been sold, the auditor has to see whether the amount realized has been credited to the profit and loss account; (v) The treatment of by-products; (vi) The adequacy of wastage; (vii) The authenticity of all documents pertaining to the procurement and issuance of materials	Financial auditor is responsible to check the authenticity of vouchers, receipts, and issuance of notes in respect of purchases and issuance of materials to the production department.

RISK MANAGEMENT AND AUDIT – STAGE-5

Sr. No.	Cost Auditor	Financial Auditor
8.	The cost auditor checks the accuracy of the work in process inventory in terms of its quality and value with reference to the percentage of completion of each job and process.	Financial auditor depends upon a certificate of management in respect of value and quantity of work in process inventory.
9.	The cost auditor examines the following in respect of labour cost: (i) the authenticity and accuracy; (ii) the segregation of labor cost into direct and indirect; (iii) the proper allocation to each job and process.	Financial auditor is only responsible to check that the total payment made to the labour have been properly authorized and accounted for.
10.	It is the duty of cost auditor to check whether the production capacity has been utilized in accordance with the scheduled program.	Financial auditor is not responsible to check the production capacity of a concern.
11.	The cost auditor has to see: (i) the accuracy and adequacy of overheads; (ii) the allocation of overheads; (iii) the reason of over or under applied overheads	Financial auditor is concerned with only to check the accuracy of overheads.

(b) (i) Labour Cost: (Any five of the following)

The cost auditor should examine the following points of labour costs:

- Direct and indirect labour costs on production.
- Total hours worked during the manufacturing period.
- Direct labour rate per man hour or per machine hour.
- Standard labour cost.
- Labour cost variance.
- Basis for differentiating between direct and indirect labour cost.
- Changes in labour cost due to revision in wage rate and new recruitments.

RISK MANAGEMENT AND AUDIT – STAGE-5**(ii) Sales: (Any five of the following)**

The cost auditor should examine the following points with regards to sales:

- Gross rates in terms of quantities and value.
- Sales return and allowances.
- Sale policies
- Price fixation procedures.
- Debtor control
- Follow-up procedures to recover amount from debtors.
- Sales budget.
- Transportation cost of finished goods from the factory to different sales centre.
- Shipping cost in case of export.
- Selling and distribution expenses.
- Soundness of documentation relating to all sales activities.
- Adequacy of control relating to finished goods at different locations, including valuation, physical verification, accounting for differences arising out of physical verification.
- Excise records and procedures.
- Orders and delivery notes files.

THE END