

Mock Test Paper - Series I: March, 2024

Date of Paper: 14 March, 2024

Time of Paper: 2 P.M. to 5 P.M.

INTERMEDIATE GROUP – II

PAPER – 5: AUDITING AND ETHICS

Time Allowed – 3 Hours

Maximum Marks – 100

Division A- Multiple Choice Questions

Case Scenario 1 carries 10 Marks

Case Scenario 2 carries 8 Marks

Case Scenario 3 carries 6 Marks

General MCQs (3 MCQs x 2 Marks each = 6 Marks)

Total 30 Marks

Case Scenario 1

Dhanush, a CA student undergoing articles, is part of an engagement team conducting audit of Test Enterprises Private Limited. The company is engaged in business of conducting aptitude and language tests every fortnight at centres spread all over major cities of country for Indian students desirous of applying to foreign universities. It also sells books containing model test papers for the benefit of students.

The company has substantial number of computers at each centre to enable seamless experience for students appearing for standardized aptitude and language tests. The company has acquired new identifiable software involving substantial expenditure for conducting tests during the year which is expected to drive company's revenues in coming years. At the time of taking a test, a CD containing software is run in each system for enabling students to take tests. Cost of CD without software is nominal.

The revenue of the company during the year 2023-24 was ₹ 50 crores (₹45 crores from fees charged from students and ₹5 crores from sale of books). Besides, company has also received ₹ 10 lacs as interest on certain investments during the year. The company has a history of profitable operations.

During the course of audit, it is noticed by Dhanush that computers form significant chunk of PPE items in financial statements of company. The company has taken useful life of computers consisting of desktops for 3 years. However, depreciation charged on computers in financial statements of the company is higher than depreciation allowable under Income tax law. It results in lower accounting income as per books of accounts of company as compared with taxable income under Income tax law.

During the course of audit, he notices that cost of CDs along with software cost is treated as an intangible asset by company. It is also part of his responsibility to verify PPE register in accordance with audit programme. On perusing details in PPE register, he finds that some computers have moved from one centre to another

centre to meet business requirements. Further, many computers were disposed or scrapped in earlier years. However, proper details in relation to movement and disposal/scrapping have not been entered in PPE register. When these items were physically verified by the management during the year, it has resulted in material discrepancies. The management has properly dealt with such discrepancies in books of accounts.

Based on above, answer the following questions:

- 1.1 Considering description provided in case scenario regarding accounting income as per books of accounts and taxable income under Income tax law, choose appropriate responsibility of Dhanush:
- (a) To verify deferred tax liability likely created in financial statements in accordance with AS 22
 - (b) To verify deferred tax asset likely created in financial statements in accordance with AS 22
 - (c) To verify deferred tax asset likely created in financial statements in accordance with AS 29
 - (d) To verify deferred tax liability likely created in financial statements in accordance with AS 29
- 1.2 Keeping in view description provided in case scenario, which of following statements is likely to be correct regarding accounting treatment of cost of CDs and software acquired by company to run tests?
- (a) The company's accounting treatment of treating cost of CDs with software costs as intangible assets is not proper. It should have treated such costs as revenue expenditure.
 - (b) The company's accounting treatment of treating cost of CDs with software costs as intangible assets is proper.
 - (c) The company's accounting treatment of treating cost of CDs with software costs as intangible assets is not proper. It should have treated cost of CDs as PPE item and software cost as intangible asset.
 - (d) The company's accounting treatment of treating cost of CDs with software costs as intangible assets is not proper. It should have treated cost of CDs as PPE item and software cost as revenue expenditure.
- 1.3 As regards discrepancies noticed in computer systems on physical verification by management as described in case scenario, which of following statements is most appropriate?
- (a) The management has properly dealt with such discrepancies. However, Dhanush should bring it to light of engagement partner as it may result in modification of auditor's opinion.
 - (b) The management has properly dealt with such discrepancies. However, Dhanush should bring it to light of engagement partner as it entails specific reporting requirement for auditor under Companies Act, 2013.

- (c) The management has properly dealt with such discrepancies. Therefore, Dhanush should not do anything further.
 - (d) The management has properly dealt with such discrepancies. However, Dhanush should bring it to light of engagement partner as it is in nature of misstatement which needs to be communicated and documented by auditor.
- 1.4 Which of following statements meets requirements of law in respect of revenue from operations of the company?
- (a) Revenue from operations of ₹ 50 crores should be shown in Statement of Profit and loss.
 - (b) Revenue from operations of ₹ 50.10 crores should be shown in Statement of Profit and loss. However, revenue from sale of books, fees charged from students and interest on investments should be disclosed separately in notes.
 - (c) Revenue from operations of ₹ 50.10 crores should be shown in Statement of Profit and loss.
 - (d) Revenue from operations of ₹ 50 crores should be shown in Statement of Profit and loss. However, revenue from sale of books and fees charged from students should be disclosed separately in notes.
- 1.5 The company has taken useful life of desktops to be 3 years. Such a requirement is _____
- (a) prescribed under Schedule III to Companies Act, 2013. However, a company can choose useful life different from what is prescribed under Schedule III.
 - (b) is not prescribed under Companies Act, 2013. It depends upon manufacturing specifications of desktops.
 - (c) prescribed under Schedule II to Companies Act, 2013. However, a company can choose useful life different from what is prescribed under Schedule II.
 - (d) is not prescribed under Companies Act, 2013. It needs to be arrived at mandatorily by a management expert.

Case Scenario 2

CDL Limited, a company dealing in FMCG goods, is having 50 branches in India. SKC & Associates (**referred to as company's auditor**) are appointed as statutory auditors of the company for year 2023-24. Further, company has also appointed Mr. D as branch auditor for 5 of its branches.

Since Mr. D is conducting audit of only 5 branches of company, he has not arrived at materiality level in respect of auditee branches. On the same lines, identification and assessment of risk of material misstatement has not been performed. He is of the view that determination of materiality and identifying & assessing risks of material misstatement is done for financial statements of company as a whole. He has mainly performed substantive audit procedures in respect of financial

statements of auditee branches like verification of PPE items, inventories, trade receivables, cash, bank balances and trade payables at auditee branches and maintained documentation of the same.

During the course of audit at two branches dealing in same kind of goods, Mr. D has performed analytical procedures pertaining to inventories. He has arrived at and compared inventory turnover ratio (Cost of goods sold/Average inventory) over a period of years of two branches. The results of analytical procedures are summarized in Table I below:

Table 1

Particulars	Branch	Year 2021-22	Year 2022-23	Year 2023-24
Inventory turnover ratio	I	15	14	12
Inventory turnover ratio	II	4	6	10

The company's auditor has also decided to use work of Mr. D with respect to financial information of 5 branches included in financial information of the company. During the course of audit, company's auditor has advised Mr. D by way of email certain significant accounting, auditing and reporting requirements and has asked him to provide representation as to compliance with them. Irritated and surprised, Mr. D is of the view that such an email is beyond the rights of the company's auditor.

Based on above, answer the following questions:

- 2.1. As regards audit of a branch of CDL Limited as referred to in case scenario is concerned, which of following statements is most appropriate?
- (a) The accounts of a branch shall be audited either by the company's auditor or by any other person qualified for appointment as an auditor of the company and appointed as such under section 139 of the Companies Act, 2013. In case branch accounts are audited by a person other than company's auditor, branch audit report is sent by branch auditor to company's auditor.
 - (b) The accounts of a branch shall only be audited by any other person qualified for appointment as an auditor of the company and appointed as such under section 139 of Companies Act, 2013 except company's auditor. In such a case, branch audit report is sent by branch auditor to members of company.
 - (c) The accounts of a branch shall only be audited by any other person qualified for appointment as an auditor of the company and appointed as such under section 139 of Companies Act, 2013 except company's auditor. In such a case, branch audit report is sent by branch auditor to company's auditor.
 - (d) The accounts of a branch shall be audited either by the company's auditor or by any other person qualified for appointment as an auditor of the company and appointed as such under section 139 of Companies Act, 2013. In case branch accounts are audited by a person other than

company's auditor, branch audit report is sent by branch auditor to members of company.

- 2.2 After reading methodology for carrying out branch audits by Mr. D, which of following statements is likely to be most appropriate?
- (a) Separate determination of materiality and identifying & assessing risk of material misstatement is not required in respect of each of the branches. He is required to perform only substantive procedures as described in the case scenario in respect of auditee branches and maintain documentation of the same.
 - (b) Separate determination of materiality and identifying & assessing risk of material misstatement is required in respect of each of branches. However, documentation for these matters regarding branches is not required. He is required to perform substantive procedures as described in case scenario in respect of auditee branches and also maintain documentation of the same.
 - (c) Separate determination of materiality and identifying & assessing risk of material misstatement is required along with documentation thereof in respect of each of branches. He is required to perform substantive procedures as described in case scenario in respect of auditee branches and also maintain documentation of the same.
 - (d) Identifying & assessing risk of material misstatement is required along with documentation in respect of each of branches. However, materiality is required to be arrived at for financial statements of company as a whole. He is required to perform substantive procedures as described in case scenario in respect of auditee branches and also maintain documentation of the same.
- 2.3 Choose the correct statement regarding results of analytical procedures performed by Mr. D summarized in Table 1 in case scenario.
- (a) During year 2023-24, inventories of Branch I have moved faster in comparison to Branch II.
 - (b) During year 2023-24, inventories of Branch II have moved faster in comparison to Branch I.
 - (c) Comparison of inventory turnover ratio of Branch II over a period of years may indicate that branch's sales have likely been weak with higher inventory holdings in year 2023-24 as compared to previous years.
 - (d) Comparison of inventory turnover ratio of Branch I over a period of years may indicate that branch's sales have likely been strong with lower inventory holdings in year 2023-24 as compared to previous years.
- 2.4 Considering contents of email sent by company's auditor to Mr. D, which of following statements is likely to be in accordance with Standards on Auditing?
- (a) Company's auditor can advise Mr. D regarding certain significant accounting, auditing and reporting requirements and ask him to provide representation as to compliance with them.

- (b) Company's auditor can advise Mr. D certain significant accounting, auditing and reporting requirements. However, asking him to provide representation as to compliance with them is breach of Mr. D's independence.
- (c) Company's auditor cannot advise Mr. D certain significant accounting, auditing and reporting requirements. It is breach of Mr. D's independence.
- (d) Company's auditor can advise Mr. D regarding certain significant accounting, auditing and reporting requirements only when Mr. D makes such a request.

Case Scenario 3

CA B is conducting statutory audit of branch of a nationalized bank. Saurabh, a CA student, is also part of engagement team conducting statutory branch audit. The field of bank branch audit is new to him and he is following instructions as required by engagement partner.

The engagement partner has asked him to prepare a summary of non-funded credit facilities outstanding as on balance sheet date. The following information is appearing in branch's CBS data/records as on 31st March, 2023:

Serial number	Particulars in CBS (Core Banking solution)/records	Amount in ₹ crores
1.	Agricultural term loans	15.00
2.	Staff housing loans	3.50
3.	Staff vehicle loans	0.20
4.	Housing loans-General public	10.00
5.	Letters of credit issued	2.50
6.	Education loans	1.50
7.	Guarantees issued (Fully secured by 100% margin)	1.00
8.	Bills purchased and discounted	2.00
9.	Bills for collection	0.10

On going through listing of housing loans to general public, CA B notices that branch has sanctioned many housing loans of small ticket size ranging between ₹10.00 to ₹ 20 lakhs. Therefore, he has assessed risk of material misstatements to be high. As a consequence, he has designed procedures to perform tests of controls as well as substantive tests.

Saurabh has been further asked to go through SMA (Special Mention Accounts) jotting as on 30th November, 2022. Such reports are available from system on monthly frequency. Being new to such type of assignment, he is unable to understand relevance of above audit procedure mandated by engagement partner.

Based on above, answer the following questions:

- 3.1 Considering table given in the case scenario, which of the following combinations is appropriate example of non-funded credit facilities provided by branch to its customers?
- (a) Bills purchased and discounted; bills for collection
 - (b) Bills for collection; staff housing loans; letters of credit issued
 - (c) Bills purchased and discounted; letters of credit issued; guarantees issued (fully secured by 100% margin)
 - (d) Letters of credit issued, guarantees issued (fully secured by 100% margin)
- 3.2 CA B's decision to perform both tests of controls as well as substantive tests was taken after he had assessed risk of material misstatement in financial statements to be high due to large number of small ticket size loans. Which Standard on Auditing deals with auditor's responsibility to design such tests?
- (a) SA 500
 - (b) SA 330
 - (c) SA 300
 - (d) SA 315
- 3.3 Saurabh is unable to understand relevance of going through SMA jotting as on 30th November, 2022. Which of following statements is most appropriate in this context?
- (a) It would necessarily help auditor in identifying accounts with significant lending exposure.
 - (b) It would help auditor in identifying accounts which may involve downgrading from Sub-standard asset category to doubtful category.
 - (c) It would help auditor in identifying accounts where substantial recoveries have been received during the year.
 - (d) It would help auditor in identifying accounts which may involve downgrading from standard category to non-performing asset.

MCQs

1. "*We, the people*" is an NGO working for rights of citizens. Due to nature of its activities, its volunteers take part in agitations which acquire political overtones. It also gets money from trusts based in overseas countries.

The government has tightened regulatory mechanism for NGOs receiving foreign funding. The finance and accounts department in NGO is headed by an experienced person, a former volunteer and activist himself. However, he has no professional or legal educational background. CA N is appointed as auditor of above NGO for the first time.

Choose the most appropriate option regarding audit risk inferred by you from above.

- (a) Audit risk in the above situation is low.
 - (b) The situation does not provide quantitative data. Therefore, it is not possible to make a precise measurement of audit risk.
 - (c) Audit risk in the above situation is high.
 - (d) The situation does not provide information affecting all components of audit risk. Therefore, inference cannot be made properly.
2. CA J is in process of planning audit for a large company engaged in business of dealing and manufacturing of pharmaceutical products. Central Drugs Standard Control Organisation (CDSCO), National regulatory Authority under Ministry of Health & Family Welfare is responsible for approval of drugs, conduct of clinical trials and laying down Standards for drugs and control over quality of imported drugs. Auditor is also considering whether to make use of audit evidence obtained in previous audit of the same company. Besides, he is also considering volume of transactions to determine whether it is efficient to rely on internal controls. As part of planning activities, he is also considering extent of substantive audit procedures to be performed. Consider following factors stated from 1 to 5:
- 1. Reporting requirements required by CDSCO, if any
 - 2. Need for specialized knowledge of pharma industry
 - 3. Expected use of audit evidence obtained in previous audit
 - 4. Volume of transactions to consider reliance on internal control
 - 5. Nature and extent of substantive audit procedures
- Choose the most appropriate factor/combination of factors which could be relevant to CA J in establishing audit strategy: -
- (a) 1, 3, 4 and 5
 - (b) 1 only
 - (c) 1, 2, 3 and 4
 - (d) 2 only
3. CA Tarini is in process of formulating audit plan for conducting audit of a company engaged in business of dealing in commodity futures. Which of following is not likely to be an appropriate audit procedure to be included in audit plan for the abovesaid company?
- (a) Verification of turnover of company
 - (b) Verification of cost of raw material consumed
 - (c) Examination of company's accounting policy for revenue recognition
 - (d) Verification of contract notes with brokers

Division B- Descriptive Questions

Question No. 1 is compulsory.

Attempt any **four** questions from the Rest.

1. (a) DOX Limited, a service provider company engaged in providing courier services pan-India as well as internationally, has appointed an internal auditor, Mr. G, in accordance with requirements of the Companies Act, 2013 during financial year 2023-24. The company's annual turnover during year 2022-23 and 2023-24 has been about ₹ 300 crores during each of above years. Business of the company has been profitable. Mr. G heads internal audit department of the company assessing governance activities, assisting in improving risk management activities and reviewing controls. Discuss reporting responsibility of statutory auditor of the company under the Companies Act, 2013 specifically in relation to internal audit and related matters for the year 2023-24. **(4 Marks)**
- (b) Up and High Private Limited has started its export business during the year 2023-24. The company was catering to domestic market only in past years. CA H, statutory auditor of the company, is of the view that the company has understated its revenue by ₹ 50.00 lacs in the year 2023-24 by not complying with requirements of AS 9 relating to revenue recognition.
- (i) Discuss responsibilities of statutory auditor to communicate with management in the above situation in accordance with SA 450. Also explain the usefulness of such communication.
- (ii) If management refuses to correct misstatement as communicated by the statutory auditor, how should he proceed? **(4 Marks)**
- (c) Prudent Enterprises Private Limited has incurred and fully spent for the first time Corporate Social Responsibility (CSR) expenditure amounting to ₹ 14.50 lacs in pursuance to provisions of section 135 of Companies Act, 2013. The expenditure was spent for women empowerment programmes through an implementing agency (not a related party). As per law provisions, it was required to spend ₹ 14.00 lacs during the year. Discuss how such information is required to be disclosed in accordance with requirements of Schedule III to the Companies Act, 2013 in financial statements of the company. **(3 Marks)**
- (d) CA Tripad (engagement partner) based at New Delhi is external auditor of Lap of Nature, a firm, since last three years. The firm is engaged in business of providing tourism services including holiday packages to its club members. It has also provided auditor including his team members free holiday for a week every year in one of its premium resorts in Ooty in the State of Tamil Nadu. The company has also booked free air travel for engagement team members during all these years. Discuss why Chartered Accountant is not acting ethically. How are familiarity threats created in above situation? **(3 Marks)**

2. (a) Mention any four financial events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as going concern. **(4 Marks)**
- (b) Adequate planning benefits the audit of financial statements in several ways. Explain. **(4 Marks)**
- (c) The auditor carries out his work by obtaining audit evidence through performance of audit procedures. However, there are practical and legal limitations on ability of auditor to obtain audit evidence. Give one example each for such practical and legal limitations. **(3 Marks)**
- (d) Goods and Services Tax Network (GSTN) is a not for profit, limited by shares, company. Its 50% shareholding is with Union Government and 50% with different State Governments. The company provides IT infrastructure and services to various stakeholders including governments and tax payers. The company is in operation since past few years and subsequent auditor needs to be appointed during financial year 2023-24. Who appoints statutory auditor of such a company described above in accordance with provisions of Companies Act, 2013? Can any directions be issued to statutory auditors of above company? **(3 Marks)**
3. (a) Suniti, a CA student, is part of an engagement team conducting audit of a company TIM Private Limited. According to audit programme, she is responsible for verifying purchases and PPE items appearing in books of accounts from records/bills of company. Besides, she has also been entrusted responsibility to obtain written representation from management regarding carrying out of physical verification of inventories during the year. During course of her work, she finds that:
- (i) One purchase bill amounting to ₹ 5.00 lacs pertaining to TIM Industries has been entered in books of TIM Private Limited.
- (ii) The management has refused to provide a written representation relating to physical verification of inventories during the year. She has brought it to knowledge of engagement partner who has decided to use lack of such a representation as audit evidence.
- Discuss whether each of above constitutes audit evidence. State reasoning for your answer. **(4 Marks)**
- (b) CA B is statutory auditor of Boom Payments Bank for year 2023-24. During the year, banking regulator has imposed restrictions on Bank from accepting new deposits due to non-compliance in conducting KYC in large number of accounts and violation of rules aimed at preventing money laundering. There is material uncertainty regarding probable outcome of such restrictions on ability of Bank to continue as going concern. However, for year 2023-24, auditor has concluded that use of going concern basis of accounting is appropriate. The financial

statements of Bank do not make adequate disclosure of material uncertainty due to above events in financial statements. What are implications for auditor's report for year 2023-24 in view of above?

(4 Marks)

- (c) Auditor shall develop an audit plan that includes description of audit procedures. Specify requirements in this regard. **(3 Marks)**
- (d) What is meant by audit documentation? What are objectives of an independent auditor in accordance with SA 230? **(3 Marks)**
4. (a) You are part of engagement team conducting audit of an entity engaged in manufacturing business. State few audit procedures you would undertake to perform to verify that recorded sales in financial statements represent goods actually sold during the period and recorded sales are not overstated. **(4 Marks)**
- (b) While performing statutory audit of Contra Industries Private Limited, a company engaged in manufacturing and assembling of LED lights, CA Varun has decided to attend physical inventory count process of the company on 30th and 31st March, 2024. The inventories are lying at three different locations - two such locations A and B are in one city and third location C is in another city. Further, company also sends inventories to some service providers for quality control and testing as such facilities are not available with the company.
- CA Varun is well-versed with this type of industry and has prepared a list of following matters which could be relevant to him in planning attendance at physical inventory count process for discharging his responsibilities in accordance with SAs: -
- Nature of inventories i.e. LED light components, parts, circuits, panels, body, WIP and finished packed LED lights
 - Materiality of inventories at different locations A, B and C
 - Stage of completion of work-in-progress
 - Maintenance of perpetual inventory system by company
 - Materiality of inventories lying with service providers
 - Timing of physical inventory counting i.e. year end
- There are two important matters which do not find place in above list. Without considering these crucial matters, it would be difficult for the auditor to properly plan his attendance at inventory count process in accordance with relevant SA. Discuss such matters. **(4 Marks)**
- (c) The auditor should decide whether relevant information is properly disclosed in the financial statements. Explain with reference to scope of audit. **(3 Marks)**

- (d) SQC 1 dwells upon engagement quality control review (EQCR) as part of system of quality control in a firm. Why is such a review required? For which type of engagements EQCR is mandatory?
What should be approach of firm for engagements for which EQCR is not mandatory? **(3 Marks)**
5. (a) WTE Private Limited is engaged in business of manufacturing a product liable to GST @ 5%. The input raw materials for manufacturing this product are liable to GST @ 12% and 18%. As a result, at the end of financial year, ITC on inputs amounting to ₹ 60 lacs is accumulated in Electronic Credit ledger and refundable to company under provisions of GST law. How would above amount of ₹ 60 lacs be reflected and classified in balance sheet of company? State few audit procedures to be performed by you for verification of abovesaid balance. **(4 Marks)**
- (b) The objective of an auditor in accordance with SA 315 is to identify and assess risks of material misstatement at financial statement level and assertion level. Which specific activities an auditor is required to perform for the purpose of identifying and assessing risks of material misstatement? **(4 Marks)**
- (c) You have been appointed as an auditor of ABC Hotel, a three star hotel, for Financial Year 2022-23. As an auditor what are the special points that need to be considered in verifying the Inventories in the nature of food and beverages? **(3 Marks)**
- (d) Professional Behaviour is one of the fundamental principles governing professional ethics. Explain its meaning. Also, give example of a situation where a Chartered Accountant fails to follow this principle. **(3 Marks)**
6. (a) CA Z is appointed as statutory auditor of BETA Private Limited for the year 2023-24. There exists an internal audit function in the company headed by its Chief Internal Auditor, CA K. Valuation of trade receivables of company is assessed as area of higher risk by statutory auditor. He wants to take direct assistance of Chief Internal Auditor in respect of above matter. Discuss along with reasons whether it would be proper for statutory auditor to: -
- (i) assign checking of accuracy of aging of trade receivables to Chief Internal Auditor?
- (ii) assign evaluation of adequacy of provision based on aging of trade receivables to Chief Internal Auditor? **(4 Marks)**
- (b) The audit of Government expenditure is one of the major components of Government audit. Briefly explain the basic standards set in relation to audit of Government expenditure. **(4 Marks)**

OR

(c) Cinescreen Multiplex Ltd. is operating cinemas in different locations in Mumbai and has appointed you as an internal auditor. What are the areas that need to be verified in relation to receipts from sale of Tickets? **(4 Marks)**

(d) Given below is a table containing Column A and Column B. Column A contains description of certain controls in an automated environment. Complete Column B by stating appropriate type of control.

Column A (Description of control in an automated environment)	Column B (Type of control)
Reasonableness checks	?
Controls over Data centre and network operations	?
Controls over application system acquisition, development and maintenance	?
Program change controls	?

(3 Marks)

(e) An engagement partner takes overall responsibility for maintaining audit quality in an audit engagement in accordance with SA 220. What are his objectives in taking and emphasizing such responsibility? **(3 Marks)**

Mock Test Paper - Series II: April, 2024

Date of Paper: 12 April, 2024

Time of Paper: 2 P.M. to 5 P.M.

INTERMEDIATE GROUP – II

PAPER – 5: AUDITING AND ETHICS

Time Allowed – 3 Hours

Maximum Marks – 100

Division A- Multiple Choice Questions

Case Scenario 1 carries 10 Marks

Case Scenario 2 carries 8 Marks

Case Scenario 3 carries 6 Marks

General MCQs (3 MCQs x 2 Marks each = 6 Marks)

Total 30 Marks

Case Scenario 1

Pluto Limited is engaged in manufacturing and distribution of ergonomic furniture. Such kind of customisable range home office furniture has gained lot of importance in past few years. The company was able to perform well over the years and the same is reflected in their financials.

During year 2023-24, audit firm of S.J. and Associates was reappointed as their auditor. The engagement team consisted of CA Sneha (partner) and five articled assistants. One of the assistants was new to this engagement. Considering huge volume of transactions, the partner asked him to go through files of last year and auditor's report to gain an understanding of issues which arose in last year i.e. 2022-23.

While going through summary page of file of last year, he noticed that below points were under discussion with the partner before audit finalisation:

Point 1: For employee benefit expenses, following points were verified by the team:

- The employee benefit expenses shown in the books were actually incurred during the relevant period.
- The expenses in respect of all personnel were accounted for.
- The expense recognised during year 2022-23 related to this year only.

Point 2: It was noted that dividend to equity shareholders for the year 2022-23, was declared on 15.04.2023. As the dividend related to the year 2022-23, the same was recognised as liability in the same year.

Point 3: Debtors constitute one of the major components of company's financials. As part of audit procedures, verification was made whether company had made allowance for those debtors which were doubtful. In this regard, list of debtors under litigation was also obtained and scrutinized.

Point 4: Asset additions during the year amounted to ₹ 50 lakhs. The payment in respect of these assets were made through bank account of the company. However, on scrutiny, it was found that some of invoices were not in the name of the company but in name of one of directors.

Point 5: The company was maintaining few bank accounts including one foreign currency account. There was included in previous year file a paper converting foreign currency amount held in a bank account to Indian Rupees at closing exchange rate.

Based on above, answer the following questions:

1.1 In point 1 relating to Employee benefits, which among the following assertions are discussed respectively (in same order as described in point 1)?

- (i) Valuation
- (ii) Occurrence
- (iii) Cut-off
- (iv) Completeness

Choose the correct combination from below: -

- (a) (i),(ii) and (iv)
- (b) (ii), (iv) and (iii)
- (c) (ii), (iii) and (iv)
- (d) (i),(ii) and (iii)

1.2 Do you think the amount of dividend recognised as liability in the year 2022-23 as given in point 2 appropriate?

- (a) Yes. As the amount of dividend related to year 2022-23, it should be recognised in the same year irrespective of the year of declaration.
- (b) No. The amount should be recognised equally between two financial years.
- (c) No. The amount should not be recognised as liability in year 2022-23. But it needed to be disclosed in the notes to accounts of that year.
- (d) No. The amount should not be recognised as liability. Further, no disclosure was needed in the financials of that year.

1.3 In relation to matter described in para 3 pertaining to debtors, which of the following assertions was verified by auditors?

- (a) Valuation
- (b) Rights and obligations
- (c) Existence
- (d) Completeness

1.4 Read Point 4 and choose which assertion is not proved in this case.

- (a) Existence

- (b) Rights and obligation
- (c) Completeness
- (d) Measurement/Valuation

1.5 Choose the correct statement from below pertaining to matter described in Point 5.

- (a) The company was required to restate said amount in accordance with requirements of AS 1. By verifying it, auditor had verified existence assertion.
- (b) The company was required to restate said amount in accordance with requirements of AS 11. By verifying it, auditor had verified completeness assertion.
- (c) There was no responsibility of company to restate said amount. It was auditor's responsibility to restate said amount in accordance with requirements of AS 11. No assertion was, therefore, verified by auditor.
- (d) The company was required to restate said amount in accordance with requirements of AS 11. By verifying it, auditor had verified valuation assertion.

(5 MCQs x 2 Marks each = 10 Marks)

Case Scenario 2

Watch IT India Private Limited is a company engaged in business of manufacturing smart watches. The company had a slow start in the beginning as company's products were gaining traction with customers. However, momentum has picked up during the year. The company wants to appoint M/s Tripathi & Associates, a CA firm as their auditor for year 2023-24 by replacing their existing auditors M/s Sreepath and Co. M/s Tripathi & Associates are willing to accept the engagement. They communicated with previous auditors before accepting the engagement. However, M/s Sreepath and Co. have failed to respond.

CA Kishan, partner of M/s Tripathi & Associates explained to his team members about importance of Engagement letter. He also arranged a team discussion on matters relating to acceptance of terms of engagement.

First point of consideration was concerning preconditions for an audit. Mr. Arun, a team member could recollect few of them. Those included determining whether financial reporting framework used in the preparation of financial statement is acceptable, management providing auditor with access to all relevant information and additional information upon auditor's request. It was further elaborated by Arun that management has to provide unrestricted access to employees within entity as may be required by auditor for obtaining audit evidence. Team members were asked to list factors that may necessitate revision of Engagement letter in case of recurring audits. Mr. Kumar, another team member replied that revision may be required in cases involving significant change in ownership, recent changes in senior management, change in financial reporting framework adopted in preparation of financial Statements, modest change in nature or size of the entity's business, change in legal and regulatory requirements etc.

Mr. Ram, one of the team members raised a doubt. He enquired regarding recourse available to incoming auditor in case management makes it clear before acceptance of engagement by auditor regarding its inability in providing support to him in respect of certain procedures expected to be performed during course of audit. In this respect, specific question was raised relating to sending of confirmation requests to material trade payables reflecting in financial statements of a company. Trade payables pertain to material input and input services acquired and utilised by company during the year. Lack of support by management in such a case would, in effect, signify management's refusal to allow auditor to send confirmation requests at the outset before engagement is accepted by auditor.

Based on above, answer the following questions:

- 2.1 As regards doubt of Mr. Ram described in last para of case scenario, which of the following statements is likely to be in accordance with Standards on Auditing?
- (a) The auditor needs to inquire into management's reasons for the refusal and perform alternative audit procedures to obtain relevant and reliable audit evidence.
 - (b) The auditor needs to evaluate implications of management's refusal on auditor's assessment of risk of material misstatement and perform alternative audit procedures to obtain relevant and reliable audit evidence.
 - (c) The auditor should not accept such an engagement.
 - (d) The auditor needs to evaluate implications of management's refusal on risk of fraud and perform alternative audit procedures to obtain relevant and reliable audit evidence.
- 2.2 When CA Kishan, the partner, asked about preconditions for an audit, Mr. Arun could recollect only few of them. Read the passage and find out which among the following points were missed.
- (i) Obtaining management responsibility on specific legal aspects governing the organisation.
 - (ii) Obtaining management responsibility on Standards on Auditing applicable to the organisation.
 - (iii) Obtaining management responsibility for the preparation of financial statements as per applicable financial reporting framework.
 - (iv) Obtaining management responsibility on necessary Internal controls to enable preparation of financial statements which are free from material misstatement whether due to error or fraud.

Choose the correct answer from below options.

- (a) (i), (ii) and (iii)
- (b) (ii), (iii) and (iv)
- (c) (iii) and (iv)
- (d) (i) and (iv)

- 2.3 From what Mr. Kumar replied about the factors requiring a revision of Engagement letter one point was incorrect. Read the passage and find that incorrect factor.
- (a) A significant change in ownership
 - (b) A recent change in management
 - (c) A change in financial reporting framework adopted in preparation of Financial Statements
 - (d) A modest change in nature or size of the entity's business
- 2.4 M/s Sreepath & Co. have failed to respond to incoming auditors. In this regard, choose the most appropriate option: -
- (a) It was unethical on part of outgoing auditors for failing to respond to communication made by incoming auditors. It is violation of principle of objectivity governing professional ethics.
 - (b) It was ethical on part of outgoing auditors for failing to respond to communication made by incoming auditors. It does not involve violation of any of fundamental principles governing professional ethics.
 - (c) It was unethical on part of outgoing auditors for failing to respond to communication made by incoming auditors. It is violation of principle of Professional competence and due care governing professional ethics.
 - (d) It was unethical on part of outgoing auditors for failing to respond to communication made by incoming auditors. It is violation of principle of professional behaviour governing professional ethics.

(4 MCQs x 2 Marks each = 8 Marks)

Case Scenario 3

In accordance with requirements of Standards on Auditing, CA Tina (a freshly qualified professional) wants to obtain sufficient appropriate audit evidence in an audit engagement pertaining to financial statements of a partnership firm for year 2022-23. The firm is trading in FMCG goods. Appointed in May, 2023, she needs evidence to obtain information for arriving at her judgment. Clearly remembering fundamentals that an auditor has to obtain sufficient appropriate audit evidence to draw reasonable conclusions on financial statements, she proceeded in accordance with audit plan prepared by her.

During the year 2022-23, firm was maintaining a current account with a branch of a public sector bank. Her audit plan had included procedure of confirming balance of current account directly from bank. As at 28th March, 2023, the firm had an urgent need to pay its utility bill amounting to ₹1.00 lacs. However, due to insufficiency of funds, it had requested branch manager to get cheque drawn on utility company cleared. Therefore, balance in current account of firm in books of bank branch stood at ₹0.92 lacs (Debit). The firm had also issued cheques in evening of 31st March, 2023 in anticipation of funds on next working day i.e. 3rd April, 2023. It had also certain cheques dated 27th March, 2023 from its debtors lying with it which were deposited in afternoon of 31st March, 2023 in bank branch at request of debtors.

Her plan also included performance of certain procedures pertaining to verification of inventories. Inventories of FMCG goods were material to financial statements. Her assistant, Tisha, had her own notion about understanding of sufficient appropriate audit evidence. She further feels that when audit evidence is obtained from available records of an entity, it is known as internal evidence like purchase bills of FMCG goods, debit notes issued by firm on debtors for GST short charged earlier during the year and credit notes issued by firm during the year on debtors to account for extra price charged in accordance with provisions of GST law. She is also of the view that audit evidence obtained by auditor is final and conclusive.

Based upon above, answer the following questions: -

- 3.1 As regards matter of balance in current account and related issues is concerned, which of following statements is likely to be most appropriate?
- (a) Amount of ₹ 0.92 lac is required to be classified under cash & bank balances in financial statements of firm. Procedure of confirming balance directly from the bank alone is likely to constitute sufficient appropriate audit evidence.
 - (b) Amount of ₹ 0.92 lac is required to be classified under cash & bank balances in financial statements of firm. Procedure of confirming balance directly from the bank alone is not likely to constitute sufficient appropriate audit evidence.
 - (c) Amount of ₹ 0.92 lac is required to be classified under current liabilities in financial statements of firm. Procedure of confirming balance directly from the bank alone is likely to constitute sufficient appropriate audit evidence.
 - (d) Amount of ₹ 0.92 lac is required to be classified under current liabilities in financial statements of firm. Procedure of confirming balance directly from the bank alone is not likely to constitute sufficient appropriate audit evidence.
- 3.2 Considering matter of verification of inventories, which of following statements is based on facts described in the situation and also in essence of Standards on Auditing?
- (a) She should verify subsequent sale invoices of inventory items lying in stocks as at year end. Besides, she should also review stock records of year 2022-23 and subsequent period. Such evidence may constitute sufficient appropriate audit evidence.
 - (b) She should verify subsequent sale invoices of inventory items lying in stocks as at year end. Besides, she should also review stock records of year 2022-23 and subsequent period. She should attend physical inventory count at year end in above situation. Such evidence may constitute sufficient appropriate audit evidence.
 - (c) She should verify purchase invoices of inventory items lying in stocks as at year end. Stock records are not required to be verified. Such evidence is likely to constitute sufficient appropriate audit evidence.

- (d) She should verify purchase invoices of inventory items lying in stocks as at year end. She should attend physical inventory count at year end in above situation. Such evidence may constitute sufficient appropriate audit evidence.

3.3 Identify correct statement on the basis of description provided in case scenario: -

- (a) Purchase bills of FMCG goods, debit notes issued by firm on debtors for GST short charged earlier during the year and credit notes issued by firm during the year on debtors to account for extra price charged in accordance with provisions of GST law are all examples of internal evidence. Audit evidence obtained by auditor is final and conclusive.
- (b) Purchase bills of FMCG goods, debit notes issued by firm on debtors for GST short charged earlier during the year and credit notes issued by firm during the year on debtors to account for extra price charged in accordance with provisions of GST law are all examples of internal evidence. Audit evidence obtained by auditor is persuasive.
- (c) Only debit notes issued by firm on debtors for GST short charged earlier during the year and credit notes issued by firm during the year on debtors to account for extra price charged in accordance with provisions of GST law are examples of internal evidence. Audit evidence obtained by auditor is persuasive.
- (d) Only debit notes issued by firm on debtors for GST short charged earlier during the year is an example of internal evidence. Audit evidence obtained by auditor is persuasive.

(3 MCQs x 2 Marks each = 6 Marks)

MCQs

1. CA D, during the course of audit of a company engaged in export business, notices that credit facilities taken by company during the year from a bank for ₹10 crores have almost been fully utilized during the year. On going through sanction letter provided by bank to company, it is observed that rate of interest stipulated in sanction letter is 8% p.a. Financial statements of company show bank interest amounting to ₹60.00 lacs. Which type of substantive analytical procedure is being used by CA D?
- (a) Trend analysis
- (b) Ratio analysis
- (c) Reasonableness tests
- (d) Structural modelling
2. An auditor of a company has found that accountant of a company has entered bogus purchase bills for ₹50 lacs in its books of accounts. Which of following is most appropriate regarding auditor's duty as far as reporting is concerned under Companies Act, 2013?
- (a) Report the matter to jurisdictional ROC

- (b) Report the matter to Secretary, MCA
 - (c) Report the matter to Board of Directors of company
 - (d) Report the matter to jurisdictional ROC as well as GST authority
3. During course of audit of a company, it is noticed by auditor that Profit before tax of company is Rs. 5 lakhs. Depreciation on building reflected in Schedule of PPE forming part of financial statements has been computed for Rs.10 lacs. The correct depreciation, according to him, should be Rs.25 lacs. The above description as a whole is an example of _____?
- (a) Misstatement
 - (b) Assertion
 - (c) Sampling method
 - (d) Audit risk

Division B - Descriptive Questions

Question No. 1 is compulsory.

Attempt any four questions from the Rest.

1. (a) Sanjeev, an articled clerk in an audit firm, is part of an engagement team conducting audit of a company for year 2023-24. It is a small company having a turnover of about ₹25 crores. During the course of audit, he notices that senior team member has taken following approach for selecting items for testing reflected in financial statements to obtain audit evidence: -
- He has selected to test items debited under the head “Machinery repair & maintenance” as expenditure relating to it during year 23-24 has increased considerably as compared to last year.
 - Out of purchases, he has selected to test purchases from related parties amounting to ₹ 5 crores.
 - He has also selected to test all individual items of expenditure exceeding ₹5 lakhs.
 - Besides, he has also selected amount of ₹0.50 lakhs debited under head “legal expenses” to know purpose of payment made to external legal counsel.
- Sanjeev understands that senior team member is using “audit sampling” for selecting items for testing. Do you agree with him? Which risk is involved in above approach? Discuss with reasons. **(4 Marks)**
- (b) Following is the extract from Schedule no. 10 of Advances as appearing in financial statements of branch of a nationalized bank for year ending 31st March, 2024.

Schedule 10 - Advances

S. No.	Particulars	Amount (In ₹ Crores) rounded off
1.	Bills Purchased and Discounted	50.00
2.	Cash credits, overdrafts and loans repayable on demand	150.00
3.	Term Loans	75.00
	Total	275.00

In carrying out audit of above advances as part of statutory audit of branch, a statutory auditor would obtain evidence about certain matters. State those matters. **(4 Marks)**

- (c) CA J is working as internal auditor in JKL Limited, a non-listed company. The responsibilities of internal auditor include reviewing financial information and performing detailed tests on transactions and balances. He is also responsible for compliance with laws, regulations and external requirements.

During the year 2022-23, services of an employee of company were terminated. The said employee had filed a suit against the company in respect of certain compensation dues amounting to ₹ 10 lakhs which were not paid to him. Based upon advice of legal counsel, the company had made a provision of ₹ 10 lacs in financial statements for year 2022-23. However, somewhere in June 2023, there is an out of court settlement between company and employee for ₹ 6 lakhs. The statutory audit of company is under progress and audit report has not yet been finalized. How internal auditor should have proceeded in situation?

(3 Marks)

- (d) KST Limited is engaged in manufacturing business. It appoints CA T to provide it an assurance report on its financial statements prepared on the basis of historical financial information. The characteristic of such an engagement is that it involves gathering of sufficient appropriate evidence on basis of which limited conclusions can be drawn up by practitioner. Identify type of engagement. Which are two other features of such an engagement? **(3 Marks)**

2. (a) Written representation about management's responsibilities involves confirmation of fulfilment of management's responsibilities in the preparation of the financial statements providing the relevant information and also informing about completeness of transactions. Explain.

(4 Marks)

- (b) Planning includes consideration of the timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures. For example, planning includes the need to

consider, prior to the auditor's identification and assessment of the risks of material misstatement, certain matters. Discuss those matters.

(4 Marks)

- (c) In an initial audit engagement, in the case of inventories, the current period's audit procedures on the closing inventory balance provide little audit evidence regarding inventory on hand at the beginning of the period. Therefore, in such a case, additional audit procedures become necessary so that auditor may obtain sufficient appropriate audit evidence. Discuss those additional audit procedures. **(3 Marks)**
- (d) Internal Control Questionnaire is a comprehensive series of questions concerning internal control. A company is engaged in business of manufacturing of chemicals. It has two plant locations in city "A" and one plant location in city "B" involving huge value of assets. Building at three locations is owned by the company. The company earns handsome profits and does not want to suffer losses due to business interruptions. It has a dedicated department for looking after insurance matters. As an auditor, prepare an internal control questionnaire concerning this department for obtaining staff responses. **(3 Marks)**
3. (a) Tisa Industries Private Limited has prepared its financial statements for year 2023-24. The financial statements and notes to accounts show following information and disclosure in respect of trade receivables of the company: -

S. No.	Particulars	Amount (in ₹ lacs)
1.	Trade Receivables	240.00

Trade receivables ageing schedule.

Outstandings for following periods from due date of payment

(in ₹ lacs)

Particulars	Less than 1 year	1-2 years	2-3 years	More than 3 years	Total
MSME	150.00	30.00	10.00	XXX	190.00
Others	40.00	XXX	XXX	XXX	40.00
Disputed dues-MSME	XXX	XXX	XXX	XXX	XXX
Disputed dues-others	10.00	XXX	XXX	XXX	10.00

You are part of engagement team conducting audit of the company. Point out discrepancies including omissions in above disclosure. (Do not prepare another table). **(4 Marks)**

- (b) Being statutory auditor of JAL Limited, a company engaged in manufacturing of chemicals, CA Gopika has understood that company is expected to have material work-in-progress as on 31st March, 2024.

State few audit procedures to verify existence and valuation assertions for work-in-progress. **(4 Marks)**

- (c) The ascertaining of reporting objectives of engagement helps the auditor to plan timing of different audit procedures and also nature of communications. Give three instances to explain. **(3 Marks)**
- (d) One of the factors affecting the form, content and extent of audit documentation relates to size and complexity of the entity. State six other factors in this respect. **(3 Marks)**
4. (a) It is important to carry out the Tests of Controls for checking effectiveness of internal control over sales as a part of the debtors' audit procedure. In above context, state the points which need to be considered in respect of trade receivables. **(4 Marks)**
- (b) M/s S R & Associates are the Statutory Auditors of Vanee Textile and Garments Ltd., a company engaged in the business of manufacturing of various textile products. The auditor has completed the audit and is in the process of forming an opinion on the financial statements for the F.Y. 2023-2024. CA S, the engagement partner, wants to conclude whether the financial statements as a whole are free from material misstatements, whether due to fraud or error. Guide him about the factors he should consider to reach that conclusion. **(4 Marks)**
- (c) Nature of financial reporting itself is one of causes of inherent limitations of audit of financial statements. Explain. **(3 Marks)**
- (d) Discuss the objective of the auditor as per Standard on Auditing (SA) 705 "Modifications to The Opinion in The Independent Auditor's Report". **(3 Marks)**
5. (a) Column A describes description of certain terms used in banking industry. Complete Column B by suggesting term appropriate to description given.

Column A	Column B
Audit of borrower client of bank carried out at bank's request to verify borrower's current assets	?
Limit up to which an entity can withdraw from sanctioned working capital limit	?
Statutory right of a creditor to adjust debit balance in debtor's account against any credit balance lying in another account of debtor	?
Creation of security in a bank branch by mere delivery of title deeds by a prospective borrower of funds	?

(4 Marks)

- (b) Obtaining an understanding of the entity and its environment, including the entity's internal control, is a continuous, dynamic process of gathering, updating and analysing information throughout the audit. The understanding establishes a frame of reference within which the auditor plans the audit and exercises professional judgment throughout the audit. State few areas in which such an understanding is helpful to auditor. **(4 Marks)**
- (c) You are auditor of a college running different courses operating in your city. During audit of a year, it is noticed that fees concessions to students have been provided in substantial number of cases. Discuss, how, you as an auditor, would proceed to verify the same and also explain two other points to verify fees from students. **(3 Marks)**
- (d) The auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate. The agreed terms of the audit engagement shall be recorded in an audit *engagement letter* or other suitable form of written agreement. Who gives engagement letter to whom and what is included in such a letter? **(3 Marks)**
6. (a) Auditor of Sunshine Ltd. is of the view that due to greater management intervention to specify accounting treatment, the risk of material misstatement is greater for non-routine transactions. Is view of the auditor correct? Specify the other matters due to which the risk of material misstatement is greater for significant non-routine transactions. **(4 Marks)**
- (b) On reviewing internal control over accounting for sales as part of statutory audit of A Ltd, auditor finds certain deficiencies in segregation of duties, authorization of sales orders, preparation of invoices, preparation and authorization of debit/credit notes etc. and non-following of standard procedures as stipulated by the management. The auditor finds these lapses to be significant deficiencies in internal control over sales.
- He points it out to the management in a one-liner as under: -
- “Instructions on internal control related to sales are not properly followed by the staff.”
- Is above communication by the auditor proper? **(4 Marks)**
- OR
- (c) Audit against propriety seeks to ensure that expenditure conforms to certain principles which have for long been recognised as standards of financial propriety. Explain those principles.

- (d) The auditor needs to direct efforts of engagement team towards matters that in his professional judgment are significant. Preliminary identification of material classes of transactions, account balances and disclosures help auditor in establishing overall audit strategy. More energies need to be devoted to significant matters to obtain desired outcomes. Give three examples to explain the above situation.

(3 Marks)

- (e) CA. Ravi Patnaik is conducting audit of a company for which reporting requirements under CARO, 2020 are applicable. He finds that cash credit facilities amounting to ₹ 4 crores were released to the company by branch of a bank for meeting its working capital requirements. He finds that out of above funds, ₹ 1 crore have been used by company for installing effluent treatment plant to meet State pollution control Board requirements.

Is there any reporting obligation upon him under CARO,2020?

(3 Marks)

Mock Test Paper - Series I: July, 2024

Date of Paper: 2nd August, 2024

Time of Paper: 2 P.M. to 5 P.M.

INTERMEDIATE GROUP – II

PAPER – 5: AUDITING AND ETHICS

Time Allowed – 3 Hours

Maximum Marks – 100

PART I - Case Scenario based MCQs (30 Marks)

Write the most appropriate answer to each of the following multiple-choice questions by choosing one of the four options given. All MCQs are compulsory and carries 2 Marks each.

Case Scenario 1

M/s Vishwacharya and Associates, a CA firm based in Orissa, is appointed as an auditor of CBF Bank for the financial year 2023-24. During the course of audit, it came to notice that CBF Bank has sanctioned an overdraft facility of ₹ 75 lakh to Times Ltd. However, as per the stock statement furnished for the last quarter, the drawing power was calculated to be ₹ 50 lakh. It was observed that few advances were guaranteed by the:

- (i) Central Government as part of 'Make in India' initiative. However, the guarantee was not invoked, and the advances were overdue by 95 days. These advances were classified as standard assets and were regarded as NPA for income recognition purpose.
- (ii) State Government as part of power generation initiative. However, the guarantee was not invoked, and the advances were overdue by 80 days. These advances were also classified as standard assets and were regarded as NPA for income recognition purpose.

Additionally, XYZ Ltd., is a borrower availing cash credit facility of ₹ 110 Lakh against security of paid stocks and debtors up to 90 days. Margin stipulated was 25% of stock as and 40% for debtors. Bank has calculated drawing power based on following information provided by XYZ Ltd.

Particulars	Amount (₹)
Value of Stocks (as on 31.12.2023)	130 Lakh
Value of Debtors (as on 31.12.2023)	75 Lakh
Value of stocks (Fully damaged and included in (i) above)	7 Lakh
Value of Debtors (exceeding 90 days included in (ii) above)	10 Lakh
Value of creditors for goods	60 Lakh

Also, the outstanding balance in one of the Loan accounts was ₹ 25 Lakh and the realisable value of the security as assessed by the bank / approved valuers was ₹ 2.25 Lakh. Bank identified the same as erosion in the value of security. It was classified as doubtful category and provision was made for the doubtful assets. A

discussion also took place among the team members regarding issuance of the audit reports after completion of the bank audit and annexure to the same such as Long Form Audit Report, Report on compliance with SLR Requirements, Report on Treasury Operations – as per RBI guidelines, Report on compliance as per Ghosh committee recommendations and Report on adverse credit - lending ratio in the rural areas, etc.

Based on the above facts, answer the following: -

1. With respect to the overdraft facility sanctioned to Times Ltd., the account would be termed as out of order if:
 - (i) The outstanding balance remains continuously in excess of ₹ 75 Lakh.
 - (ii) The outstanding balance remains continuously in excess of ₹ 50 Lakh.
 - (iii) The outstanding balance in the account is less than ₹ 75 Lakh but there are no credits or payments deposited into the account continuously for 90 days as on balance sheet date
 - (iv) The outstanding balance is less than ₹ 50 Lakh.

Choose the correct option from below:

- (a) (i), (ii) and (iii)
 - (b) (i), (iii) and (iv)
 - (c) (ii),(iii) and (iv)
 - (d) (iii) and (iv)
2. Which of the treatment by the bank on the provisioning and income recognition is correct in case of bank guarantee given by the Central Government and State Government?
 - (a) Both (i) and (ii) are correct
 - (b) Only (ii) is correct
 - (c) Only (i) is correct
 - (d) Both (i) and (ii) are incorrect.
3. In the given case drawing power of the borrower XYZ Limited should be:
 - (a) ₹ 86.25 Lakh
 - (b) ₹ 76.35 Lakh
 - (c) ₹ 96.25 Lakh
 - (d) ₹ 85.45 Lakh
4. The Bank has identified an erosion in the value of security and made provision for doubtful assets. Whether the treatment by bank for the doubtful asset is correct?
 - (a) Yes. The security should be classified under doubtful category. It may be either written off or fully provided by the bank.

- (b) No. The existence of such security should be ignored, and the asset should straight away be classified as loss asset. It may be either written off or fully provided by the bank.
 - (c) Yes. The security should be classified under doubtful category and provisioning should be made as applicable for doubtful assets.
 - (d) No. The existence of the security should be ignored, and the asset should straight away be classified as loss asset. Provisioning should be made for doubtful assets.
5. The Statutory Central Auditors of a bank must furnish, in addition to the main audit report, various other audit reports. From the options, choose the audit reports that M/s Vishwacharya and Associates shall furnish.
- (i) Long Form Audit Report
 - (ii) Report on compliance with SLR Requirements
 - (iii) Report on Treasury Operations – as per RBI guidelines
 - (iv) Report on compliance as per Ghosh committee recommendations
 - (v) Report on adverse credit - lending ratio in the rural areas.

Choose the correct answer:

- (a) (i), (ii),(iii),(iv) and(v)
- (b) Only (i),(ii),(iii) and (iv)
- (c) Only (i),(ii) and (iii)
- (d) Only (i),(ii) and (v)

Case Scenario 2

Priority Limited is a large company engaged in manufacturing of terry towels making steady profits on a year-to-year basis. PMR & Associates, statutory auditors of the company since last two years, are in process of establishing audit strategy for conducting statutory audit under Companies Act, 2013 for year 2023-24.

The company has 5 branches which are audited by independent auditors appointed under Companies Act, 2013. It also has a wholly owned subsidiary company which is audited by another audit firm under name of JKL & Associates. The engagement team has noticed that company has maintained several bank accounts and there is substantial movement in fixed deposits during the year leading to risk of misstatement in cash and cash equivalents. The engagement team has planned procedures regarding the same.

- (i) At planning stage, engagement partner is also trying to set materiality for financial statements as a whole. The following information extracted from financial statements is given as under: -

Particulars	(Amount in ₹ crores)
Revenue	100
Total Assets	40

Profit before Tax	8
Total Liabilities (excluding Equity)	30

- (ii) While designing a sample for verifying revenues of company as part of tests of details, engagement partner has determined “tolerable misstatement” for ₹ 5.00 Lakh in order to address the risk that aggregate of individual immaterial misstatements may cause the financial statements to be materially misstated and provide a margin for possible undetected misstatements. One of the newly joined engagement team members has little conceptual understanding of “tolerable misstatement” determined by engagement partner. He also has no idea of the effect of change in tolerable misstatement on sample size.
- (iii) During course of audit, while performing tests of details, engagement team has come across certain misstatements in selected sample pertaining to verification of revenues. The team has projected misstatements to population of revenues. The team wants to comply with the Standards on Auditing strictly.

Based on the above facts, answer the following: -

6. The auditors of company are in process of establishing audit strategy. Which of the following is not a relevant factor in establishing overall audit strategy in the given case scenario?
- Consideration of 5 branches which are audited by independent auditors
 - Consideration of wholly owned subsidiary company audited by another audit firm
 - Expected time of holding AGM in accordance with provisions of Companies Act, 2013
 - Nature, timing and extent of planned procedures for cash and cash equivalents
7. For Priority limited, which benchmark would the engagement partner most likely to use for setting materiality for the financial statements as a whole?
- A percentage of Revenue
 - A percentage of Total assets
 - A percentage of Profit before tax
 - A percentage of Total liabilities (excluding equity)
8. In the given case scenario, assume that the engagement partner has decided to increase tolerable misstatement to ₹ 10.00 Lakh while designing sample described. Select the correct statement.
- It would lead to decrease in sample size.
 - It would lead to an increase in sample size.
 - It would have no effect on sample size.
 - It is not possible to draw inference on sample size due to increase in tolerable misstatement.

9. While performing procedures on designed sample, the engagement team identified certain misstatements in selected sample and projected these to the entire population of revenues. According to the requirements of the Standards on Auditing, which statement is correct in this regard?
- (a) Anomalous misstatement is auditor's best estimate of misstatement in population.
 - (b) The projected misstatement plus anomalous misstatement, if any, is best estimate of misstatement in population.
 - (c) When projected misstatement exceeds tolerable misstatement, sample provides a reasonable basis for conclusion about tested population.
 - (d) When projected misstatement plus anomalous statement, if any, exceeds tolerable misstatement, sample provides a reasonable basis for conclusion about tested population.

Case Scenario 3

Bandhu Charitable Trust is considering appointment of MNO & Associates, Chartered Accountants, as independent auditors of its financial statements. The Trust is engaged in providing affordable healthcare services. It is in interest of both auditor and client to issue an engagement letter so that the possibility of misunderstanding is reduced to a great extent. It is, therefore, important that each party should be clear about nature of engagement. It should exactly specify the scope of work. Such an "engagement letter" is exchanged between Trust management and auditors.

While performing audit procedures, it is noticed by auditors that bills of two vehicles are not in name of Trust but in name of trustees. However, payment of these vehicles was made from bank account of Trust. The said vehicles are used for activities of Trust.

It is also noticed that a sum of ₹ 50.00 Lakh is reflected in Trust's financial statements in name of Gamma Instrument and Equipment in schedule of creditors. The said amount is outstanding since two years. The auditors sent confirmation request to the said supplier and seek management's co-operation in this regard. However, management of the Trust informs the auditor regarding certain dispute going on with the supplier of equipment due to some quality issues. It is further informed that dispute is near settlement and it would not be proper to send confirmation request as it can affect negotiation process.

Based on the above facts, answer the following: -

10. As regards exchange of engagement letter between Trust management and auditors is concerned, which of following statements is likely to be true?
- (a) Engagement letter is sent by MNO & Associates to Bandhu Charitable Trust. It includes reference to the expected form and content of report to be issued by them and a statement that there may be circumstances in which such report may differ from its expected form and content.
 - (b) Engagement letter is sent by Bandhu Charitable Trust to MNO & Associates. It includes reference to the expected form and content of

report to be issued by auditors. However, it does not include a statement that such report may differ from its expected form and content.

- (c) Engagement letter is sent by MNO & Associates to Bandhu Charitable Trust. It includes reference to expected form and content of report to be issued by them. However, it does not include a statement that such a report may differ from its expected form and content.
 - (d) Engagement letter is sent by MNO & Associates to Bandhu Charitable Trust. It does not include reference to the expected form and content of report to be issued by them.
11. Considering the issues related to vehicles as described in the case study, identify the most appropriate statement.
- (a) Auditors have identified misstatement concerning “Existence” assertion made by Trust management.
 - (b) Auditors have identified misstatement concerning “Rights and Obligations” assertion made by Trust management.
 - (c) Auditors have identified misstatement concerning “Accuracy” assertion made by Trust management.
 - (d) Auditors have identified misstatement concerning “Completeness” assertion made by Trust management.
12. What course of action should the auditor take regarding the amount payable to the equipment supplier when management has communicated that sending a confirmation request could negatively impact the negotiation process?
- (a) The auditor should issue adverse opinion in auditor’s report.
 - (b) The auditor should seek audit evidence as to the validity and reasonableness of the reasons for refusal and perform alternative audit procedures.
 - (c) The auditor should withdraw from engagement as Trust management’s refusal is a limitation on scope of independent audit.
 - (d) The auditor should disclaim opinion in auditor’s report.

MCQs

13. CA Prince, after developing the audit strategy for Vedika Limited, develops an audit plan but finds a need to revise the materiality levels set earlier and therefore, a deviation from the already set audit strategy is felt necessary. In this case, he should
- (a) Drop the audit and withdraw from the engagement.
 - (b) Devise a new audit plan and then, change the strategy as per the Revised Plan.
 - (c) First Modify the audit strategy and thereafter, prepare the audit plan according to the modified strategy.
 - (d) Continue with the Audit Plan without considering the Audit Strategy.

14. Jasmine was of the view that audited financial statements are not a guarantee against probable wrong doings in the financial matters of companies. What kind of assurance does audit of financial statements provide?
- It provides reasonable assurance meaning a low level of assurance.
 - It provides reasonable assurance meaning a high level of assurance.
 - It provides reasonable assurance meaning an absolute level of assurance.
 - It provides reasonable assurance meaning a moderate level of assurance.
15. CA Raman instructed his article Raju to verify whether employee benefit expense of Prep Limited has been fairly allocated between the operating expense incurred in production activities and general expense. Which of the following assertions is being addressed by this instruction?
- Completeness
 - Presentation and Disclosure
 - Measurement
 - Occurrence

PART II - Descriptive Questions

Question No. 1 is compulsory.

*Attempt any **four** questions from the Rest.*

1. (a) Subodh has recently joined an audit firm as an articled clerk. He was in process of assembling audit working papers in audit file of Cop Limited, as per the instructions of his senior. While assembling, he noticed following working paper in audit file: -

Timing of Audit Activities

Activity	Expected Timing
Audit Planning	July 1, 2023 - July 5, 2023
Review by EQCR	July 6, 2023 - July 7, 2023
Audit Field Work	July 10, 2023 - August 20, 2023
Review by Manager	August 21, 2023
Review by Engagement Partner	August 22, 2023 - August 25, 2023
Review by EQCR	August 26, 2023 - August 27, 2023
Response on Audit Memo	August 28, 2023
Review by Partners – internally post response on audit memo	August 29, 2023
Review by EQCR	August 30, 2023

Finalization of Audit Report and Financial Statements	September 01, 2023 - September 02, 2023
Issuance of Audit Report and Financial Statements	September 03, 2023

The above working paper lists certain factors which are considered by the auditor while establishing audit strategy. Explain how these considerations highlighted in above working paper could have helped the auditor? **(5 Marks)**

- (b) CA Tina, while inspecting financial statements of a company, notices that gross profit ratio of company has increased from 14% in year 2022-23 to 24% in year 2023-24. Considering the above, she has assessed the risk of material misstatement to be high with respect to assertions relating to revenue and various direct expenses. CA Tina wants to know few possible reasons which could have led to abnormal jump in gross profit ratio.

During the discussion among engagement team members, her junior Ms. Tisha, expressed her view that detection risk in this engagement should be kept at high level.

- (i) List out a few possible reasons which could have led to abnormal jump in gross profit ratio.
- (ii) Do you agree with viewpoint of Tisha? Provide reasons for your answer. **(5 Marks)**

- (c) Expert Industries Limited is engaged in petrochemical business. Due to nature of its business, the company has hired PQR Associates, a reputed firm of chartered engineers, to determine the quantity and valuation of inventories for preparation of financial statements. The auditor of Expert Industries Limited want to use the same as audit evidence. Before using the work of PQR Associates, management's expert, what aspects should be taken care by auditor? **(4 Marks)**

2. (a) Stay fit Private Limited is a start-up that has been in business for about two years. It runs an application which provides valuable information pertaining to nutrition and helps its clients to access customized healthy food. The company's revenues are expected to grow in the coming period. Although company has reflected net losses in its financial statements for the last two years, it has managed to meet its financial commitments. The financial statements for last two years were prepared on going concern basis of accounting. The management of company wants to follow the same basis of accounting for the current year. Is the view of management appropriate? How does the "going concern" affect the preparation of financial statements? **(5 Marks)**

- (b) PQR & Associates and MNO & Co., both firms of Chartered Accountants, have been appointed as joint auditors of Gama and Beta Limited. Before the commencement of the audit, the joint auditors should discuss and

develop a joint audit plan. In developing the joint audit plan, the joint auditors should identify division of audit areas and common audit areas. Explain stating the other relevant considerations in this regard with reference to the Standards on Auditing. **(5 Marks)**

- (c) The management of Cool Drinks Limited suspects that some employees of the company may be involved in making fraudulent payments to dummy workers at its various plants in the country. Therefore, they are considering appointment of a firm of auditors to conduct audit involving detailed examination of accounts. However, one senior person among Board members, Mr. P, objects to use of word "audit" in proposed assignment. Comment. Also, discuss how audit is different from investigation. **(4 Marks)**
3. (a) Mr. Chetan is appointed as an auditor of Spot Limited, a small company. Mr. Chetan is aware that CARO 2020 is not applicable to small company. List out the classes of companies that are specifically exempt from the applicability of CARO 2020. **(5 Marks)**
- (b) Zed Limited is engaged in the manufacturing and export of shoes. The statutory auditor of the company wants to reasonably ensure that only the inventories recorded in the financial statements are exclusively owned by the company and do not include any inventories that belong to third parties but includes inventories owned by the company but lying with third party. Advise the auditor on the audit procedures to be performed to achieve this assurance. **(5 Marks)**
- (c) SQC 1 requires assumption of leadership responsibilities for quality within firm. Are such leadership responsibilities required for audit engagements only? Who assumes such leadership responsibilities within firm? How it is important for audit quality? **(4 Marks)**
4. (a) CA X is contemplating the use of negative confirmation requests as the sole substantive audit procedure to verify certain accounts payable balances reflected in financial statements of a company. Which conditions need to be met to use negative confirmation requests as stated above? Additionally, CA X is of the view that negative confirmations provide same level of persuasive audit evidence as in case of positive confirmations. Do you agree with his viewpoint? Provide reasons for your answer. **(5 Marks)**
- (b) CA H has been offered audit of financial statements of a society engaged in promoting social causes, such as setting up of drug de-addiction centres for misguided youth and rehabilitating such young people by helping them find avenues of gainful employment. However, CA H failed to send audit engagement letter to the society's governing body and proceeded to conduct the audit. In the absence of this letter, the governing body is of the view that purpose of such an audit is to provide absolute assurance against probable errors and frauds in the financial statements. Does it constitute violation of fundamental principles governing professional ethics? State reasons for the same. **(5 Marks)**

- (c) While verifying cash and cash equivalents of a company, CA D engagement partner, is very particular that Bank reconciliation statement (BRS) prepared by the management in respect of bank account maintained by the company is proper to rule out misstatements in cash and cash equivalents reflected in the financial statements of the company. The company does not use net banking and prefers to issue cheques to its creditors and receives substantial payments locally through account payee cheques. Which aspects need to be taken care of and verified by CA D in respect of BRS? **(4 Marks)**
5. (a) CA Sumit has been appointed as statutory auditor of Core Limited. List out some matters that he may consider in determining whether a deficiency or combination of deficiencies in internal control constitutes a “significant deficiency”. **(5 Marks)**
- (b) While conducting the audit of Zeena Limited, CA E is trying to obtain understanding of different components of internal controls of the company. Such an understanding is necessary and is required to be documented in accordance with Standards on Auditing. In this context, how he shall obtain understanding of the risk assessment process of the company and how is this understanding important for the auditor? **(5 Marks)**
- (c) Section 72(1) of the Multi-State Co-operative Societies Act, 2002 states that only a person who is a Chartered Accountant within the meaning of the Chartered Accountants Act, 1949 can be appointed as an auditor of a multi-state co-operative society. Who, according to Section 72(2), is disqualified from being appointed as auditors of a multi-state co-operative society? **(4 Marks)**
6. (a) National Bank has advanced cash credit facility of ₹ 25 Lakh to Sun Industries. Following is the extract of account of Sun Industries reflecting in CBS of Bank from December 1, 2023 to March 31, 2024: -

Date	Particulars	Dr.	Cr.	Balance (Dr.)
01/12/2023	To Transfer	45,000		24,75,000
31/12/2023	By Clearing		1,00,000	23,75,000
31/12/2023	To Interest	25,000		24,00,000
31/01/2024	To Interest	24,700		24,24,700
29/02/2024	To Interest	24,800		24,49,500
31/03/2024	To Inspection charges	1,000		24,50,500
31/03/2024	To Interest	24,900		24,75,400

Drawing power during the above period was consistent at ₹ 25 Lakh. The account was classified as “Standard asset” as on 31.12.2023 in books of Bank. The security charged with the bank remains intact throughout this period.

Comment on “asset classification” of above account as on 31st March 2024 in books of Bank in accordance with RBI norms. **(5 Marks)**

- (b) While performing audit of financial statements of a listed company, statutory auditor needs to maintain an attitude of professional skepticism for related party information. State examples of the records or the documents that may provide information about related party relationships and transactions. **(5 Marks)**
- (c) Sanjana is of the view that there exist some disadvantages in the use of audit programmes but most of these can be removed by following some concrete steps. Do you agree with her perspective? Comment. **(4 Marks)**

OR

BOTS is a manufacturing entity having material Property, Plant and Equipment (PPE) items in its financial statements. The auditor of the entity wants to verify that PPE items have been valued appropriately as per generally accepted accounting policies and practices. Comment on significance of such verification. Suggest a few audit procedures in this regard. **(4 Marks)**

Mock Test Paper - Series II: August 2024

Date of Paper: 22nd August 2024

Time of Paper: 2 P.M. to 5 P.M.

INTERMEDIATE GROUP – II

PAPER – 5: AUDITING AND ETHICS

Time Allowed – 3 Hours

Maximum Marks – 100

PART I - Case Scenario based MCQs (30 Marks)

Write the most appropriate answer to each of the following multiple-choice questions by choosing one of the four options given. All MCQs are compulsory and carries 2 Marks each.

Case Scenario 1

DLP & Associates, a firm of Chartered Accountants, are in midst of conducting audit of Twist and Spin Limited. The company is in business since last 15 years and have appointed DLP & Associates as their auditor for the first time for a term of 5 years beginning from financial year 2023-24. While identifying and assessing the risk of material misstatement at assertion level, the engagement team had assessed risk of material misstatement for revenues and trade receivables to be high.

The team is considering to send negative confirmation requests as sole substantive procedure to some business entities representing trade receivables appearing in the financial statements of the company. The company had made sales to these business entities in January, 2024. Such business entities are few and have quite large balances as on 31st March, 2024. However, team members are not on the same page regarding sending negative confirmation requests.

Besides considering sending of confirmation requests, engagement team has planned certain audit procedures pertaining to trade receivables. These procedures include: -

1. Verification of invoices issued during last 7 days of financial year 2023-24 to verify that goods have been despatched by the company.
2. Selection of a few invoices from ageing report of the month March 2024 for verification of correctness of the billed amounts, to correct customers and on correct dates.
3. Preparation of schedule of movement of bad debts.
4. Review of the process of providing discounts to ensure that it is in accordance with company policy.

Another junior team member, S, observed that “Share Options Outstanding Account” reflected in the financial statements of the company. He started searching classification requirements of Schedule III of Companies Act, 2013 in this regard.

The engagement team wants to ensure that only the inventories held by company have been recorded in the financial statements and do not include any inventories belonging to third parties. They are keen to verify completeness assertion for inventories. The team has planned following audit procedures in this respect: -

1. Comparison of inventory turnover ratio of current period with previous years;
2. Vertical analysis of current period with previous years;
3. Comparison of budgetary expectations vis-à-vis actuals;
4. Performing purchase and sales cut-off tests

During the course of audit, R, a team member concluded that company has followed a particular accounting policy for revenue recognition during year 2023-24 which is in accordance with Accounting Standards and applicable financial reporting framework, but it was not consistently applied in preceding period having an impact upon opening balances of trade receivables of current year 2023-24. R is confused regarding the possible implications on auditor's report on this issue.

Based upon above, answer the following questions: -

1. The engagement team members are not able to take decision on sending negative confirmation requests to some entities described in case scenario. Which of the following statements is in accordance with Standards on Auditing?
 - (a) It would be appropriate for engagement team to send negative confirmation requests to these business entities.
 - (b) It would be inappropriate for engagement team to send negative confirmation requests to these business entities.
 - (c) Sending negative confirmation requests depends upon auditor's professional judgment and Standards on Auditing do not spell out any confirmation requirements in this respect.
 - (d) Business entities are more likely to respond in case of disagreement. Therefore, sending negative confirmation requests always provides better qualitative audit evidence as compared to other confirmation modes.
2. Which of the planned audit procedure(s) pertaining to trade receivables described in case scenario is/are not related to verification of "Completeness assertion"?
 - (a) 2 only
 - (b) 2 and 3
 - (c) 3 only
 - (d) 1 and 3
3. Guide team member S by selecting the correct option with respect to "Share Options Outstanding Account":
 - (a) It is required to be classified under head "Current liabilities".

- (b) It is required to be classified under Shareholder funds under “Share Capital”. Further, it is to be classified separately under “Paid up Share Capital”.
 - (c) It is required to be classified under Shareholder funds under “Reserves & Surplus”. Further, it is to be classified separately as such under “Reserves & Surplus”.
 - (d) It is required to be classified under Shareholder funds under “Reserves & Surplus”. However, it is shown as part of Capital Reserve. No Separate disclosure is mandated under Schedule III of Companies Act, 2013.
4. Which of the planned audit procedures in relation to the inventories described in the case scenario is/are not in nature of analytical procedure(s)?
- (a) 2 and 3
 - (b) 3 only
 - (c) 2 and 4
 - (d) 4 only

Case Scenario 2

CA J is nearing completion of audit of Cheap Cost Private Limited, a manufacturing company for the year 2023-24. The draft financial statements of the company show a profit before tax of ₹ 5 crores. Materiality for financial statements as a whole has been determined @ 5% of Profit before Tax. At the end of June 2024, he is considering following issues flagged during the course of audit which remain uncorrected: -

- A fire took place in one of the premises of the company on 1st May, 2024 resulting in damages to all the inventories lying there amounting to ₹ 1 crores. The inventories of affected premises are insured with Quick Bima Limited for ₹ 50 lakhs and company has also lodged a claim with it which is still to be settled.
- The company has debited ₹ 10 lakhs under “Machinery Account” whereas expenditure relates to normal wear and tear of high-speed automated machinery. The amount has been wrongly capitalised under “Machinery account”. (Ignore depreciation effect)
- The company has not properly accounted for necessary elements of cost in arriving at work in progress. Further, estimates regarding various stages of production have not been made properly. All such factors have resulted in overstatement of work in progress inventories by ₹ 20 lakhs.

No other issues except as stated above merit attention. Besides, written representation letter has also been obtained on matters concerning management’s responsibilities regarding fulfilment of responsibilities for preparation of financial statements and providing access to all information to CA J. However, written representation provided to CA J begins in the below stated manner:

“This representation letter is provided in connection with your audit of the financial statements of Cheap Cost Private Limited for the year ended March 31, 2024, for

the purpose of expressing an opinion as to whether the financial statements give a true and fair view in accordance with the applicable accounting standards in India. We confirm that (to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves)

Based upon above, answer the following questions: -

5. Which of following statements is most appropriate as regards to fire incident?
 - (a) The auditor should ask management to adjust financial statements for period under audit and book a loss of ₹ 50 lakhs in its Statement of Profit and Loss.
 - (b) The auditor should ask management to adjust financial statements for period under audit and book a loss of ₹ 1 crores in its Statement of Profit and Loss.
 - (c) The auditor should ask management to disclose it in notes to accounts.
 - (d) The auditor has no responsibility regarding described fire incident.
6. Identify the correct option regarding materiality of uncorrected misstatements relating to wrong capitalisation under “Machinery Account” and overstatement of inventories of work in progress.
 - (a) The uncorrected misstatements are not material in context of audit of financial statements as a whole as these are below materiality level determined by auditor.
 - (b) The uncorrected misstatements are material in context of audit of financial statements as a whole and their effect on opinion should be considered by auditor.
 - (c) The uncorrected misstatements are not material in context of audit of financial statements as a whole as these are in nature of management’s judgment.
 - (d) The uncorrected misstatements are material in context of audit of financial statements as a whole and auditor should correct these.
7. The auditor has performed certain audit procedures described in case scenario relating to inventories of work in progress. Such procedures are related to verification of _____ assertion.
 - (a) Completeness
 - (b) Valuation
 - (c) Existence
 - (d) Rights and obligations
8. Which of the following statements is correct in respect to manner of providing written representations by management?
 - (a) The extract of written representations provided in case scenario is proper.

- (b) The use of words “having made such enquiries” is not permitted.
- (c) The use of words “to the best of our knowledge and belief” is not permitted.
- (d) The use of both kind of words “having made such enquiries” and “to the best of our knowledge and belief” is not permitted.

Case Scenario 3

MPM & Associates, a firm of Chartered Accountants, have received offer letter from PST Bank for carrying out statutory audit of their Chandigarh branch for the financial year 2023-24. The offer letter, inter alia, requests audit firm to give an undertaking in writing that firm is not disqualified under Section 141(3)(d)(ii) of Companies Act, 2013. Such provision relates to disqualification of a person as auditor of a company if he, his relative or partner is indebted to the company subject to certain prescribed conditions. Before accepting the said audit, the firm checks out whether it complies with law requirements. However, there is a difference of opinion among firm personnel whether such an undertaking can be given in case of banks.

The offer letter also contains following declaration to be signed by the auditors in case they choose to accept the appointment: -

“We declare that we will not communicate or allow to be communicated to any person, not legally entitled thereto, any information relating to the affairs of PST Bank or to the affairs of the person having any dealing with the Bank, nor will we allow any such person to inspect or have access to any books or documents belonging to or in possession of the Bank relating to the business of any person having any dealing with the Bank.”

The audit firm has also received a document kit provided by Statutory Central Auditors of Bank. It relates to scope of audit, areas of special consideration while performing audit and requires audit firm to confirm certain matters like adherence to RBI Master Circulars for income recognition, asset classification & provisioning and adequacy of checking of books of accounts based on sample etc. to them by way of a letter.

The document kit received also requires MPM & Associates to consider adverse comments made by stock auditors of borrowers enjoying cash credit facilities in their reports for purpose of reporting. It also contains specific instructions to check foreign letter of credits (FLCs) issued during the year in compliance with sanction terms of the respective borrowers and to verify income recognized in respect of FLCs.

9. Which of the following statements is likely to be most appropriate regarding required undertaking in accordance with the Companies Act, 2013?
- (a) The referred provision mainly addresses self-interest threats to independence of auditors. The audit firm can give such an undertaking after verifying if it complies with such requirements.
 - (b) The referred provision mainly addresses self-review threats to independence of auditors. The audit firm can give such an undertaking after verifying if it complies with such requirements.

- (c) The referred provision mainly addresses self-interest threats to independence of auditors. However, the audit firm can't give such an undertaking as such provisions are applicable to companies and not to banks.
 - (d) The referred provision mainly addresses self-review threats to independence of auditors. However, the audit firm can't give such an undertaking as such provisions are applicable to companies and not to banks.
10. The declaration relating to non-communication of information related to affairs of Bank is related to adherence to which fundamental principle governing professional ethics?
- (a) Objectivity
 - (b) Confidentiality
 - (c) Independence
 - (d) Professional Competence and due care
11. MPM & Associates are required to report on adverse comments made by stock auditors of borrowers of branch enjoying cash credit facilities. Which of the following statements is most appropriate in this regard?
- (a) Stock auditors make comments in their reports on valuation of security and calculation of drawing power.
 - (b) Stock auditors make comments in their reports on valuation of security only. However, no comments are made on calculation of drawing power.
 - (c) Stock auditors make comments in their reports on valuation of security, documentation made by bank in respect of sanctioned credit facilities, leakage of revenue and calculation of drawing power only.
 - (d) Stock auditors make comments in their reports on calculation of drawing power only.
12. Keeping in view matter of foreign letters of credits (FLCs) described in case scenario, consider following statements: -
1. Foreign letter of credit issued by branch is a non-funded loan.
 2. Branch earns interest on issuance of foreign letter of credit which is credited in interest earned account of profit and loss account of branch.
 3. The bank which receives foreign letter of credit is known as beneficiary bank.

Which of following statement(s) is/are true?

- (a) Only statement 1 is correct.
- (b) Only statements 1 and 3 are correct.
- (c) Only statements 1 and 2 are correct.
- (d) Only statements 2 and 3 are correct.

MCQs

13. CA Y has started planning for audit of a listed company. In this respect, he is considering all the matters relating to acceptance of client, assessment of compliance with ethical requirements including independence, consideration regarding the use of analytical procedures to be performed as risk assessment procedures and to have common understanding regarding terms of engagement with management. Which of the following does not fall under the preliminary engagement activities of planning process?
- (a) Considering all matters relating to acceptance of client.
 - (b) Assessing ethical requirements including independence.
 - (c) Using analytical procedures to be performed as risk assessment procedures.
 - (d) Establishing common understanding regarding terms of engagement.
14. A practicing Chartered Accountant is appointed by a company to perform certain agreed-upon procedures relating to its trade payables. Such agreed upon procedures include verifying listing with books of accounts, sending confirmation letters and reporting factual discrepancies to company management. Which of statements is correct in this context?
- (a) The practicing CA shall perform work in accordance with Standards on Related Services and SA 220.
 - (b) The practicing CA shall perform work in accordance with Standards on Related Services and SQC 1.
 - (c) The practicing CA shall perform work in accordance with Standards on Auditing including SA 220.
 - (d) The practicing CA shall perform work in accordance with Standards on Assurance Engagements and SQC 1.
15. The audit of government expenditure is one of the major components of government audit. In this regard, what is meant by "Audit against rules and orders"?
- (a) That the expenditure is incurred with due regard to broad and general principles of financial propriety.
 - (b) That there is sanction, either special or general, accorded by competent authority authorising the expenditure.
 - (c) That there is a provision of funds out of which expenditure can be incurred and the same has been authorised by competent authority.
 - (d) That the expenditure incurred conforms to the relevant provisions of the statutory enactment and in accordance with the financial rules and regulations framed by the competent authority.

PART II - Descriptive Questions

Question No. 1 is compulsory.

Attempt any **four** questions from the Rest.

1. (a) CDE Private Limited, a manufacturing company, had made investment in shares of some blue-chip companies. Additionally, it had temporarily deposited some of its extra funds in fixed deposits with a scheduled bank. Dividend from shares amounting to ₹ 1.80 lakhs (net of TDS, TDS = ₹ 0.20 lakhs) and bank interest of ₹ 2.70 lakhs (net of TDS, TDS = ₹ 0.30 lakhs) were credited in bank account of the company. During the year 2023-24, it has also sold some shares resulting in net gain of ₹ 5 lakhs. The company has shown above incomes under head "Other income" for consolidated amount of ₹ 9.50 lakhs in the statement of Profit and Loss. No other information is furnished in the financial statements put up for audit. As the auditor of the company, discuss whether the above situation constitutes "misstatement" in the financial statements of the company. Also state, few examples of misstatements. **(5 Marks)**
- (b) During the audit of a company, CA Z is using a software to select samples pertaining to sales records of the company. While performing this process, a window opens in software prompting the user to enter certain information. CA Z is in the process of entering information in this regard as given under: -

Selection Interval	?
Number of records to select	100
Starting record number to select	1
Ending record number to select	1000
File name	Sales

Going through the above fields, which method of sampling is likely being used in the software? Discuss. Which foremost consideration should be kept in mind by auditor for selecting samples in such a manner?

Additionally, partner of CA Z suggested him to select the first 200 sales invoices from the sales book of the last month. Which method of sampling is being suggested by partner of CA Z? **(5 Marks)**

- (c) Truthful Products Private Limited is engaged in trading stationery items. During the year 2023-24, there was a huge fire in one storage location of the company resulting in loss of inventories of ₹ 5 crores. As a result, the operations of the company were badly affected for about two months. Unfortunately, the insurance claim of the company was rejected due to certain defects in the policy issued and loss was booked by company in the year 2023-24 itself. There was no change in nature of business of company in relation to the last year. The draft financial statements of the company reflect following information:

(Figures in ₹ crores)

Particulars	FY 2022-23	FY 2023-24
Revenue from Operations	80	100
Net profit before tax	6	10

CA D who has been the statutory auditor for past three years, has decided to rely upon the same tests of details as performed in previous years. In the given situation what is lacking on part of the auditor? Discuss. **(4 Marks)**

2. (a) “Assurance engagement” means an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria. In this context, give three examples of assurance engagements highlighting difference in nature of assurance provided by such engagements. **(5 Marks)**
- (b) Pure Services Limited is into the litigation relating to some legal action initiated by the industry regulator. The matter has reached jurisdictional High Court. Keeping in view uncertainty related to future outcome of matter, statutory auditor of the company has decided to include Emphasis of Matter (EOM) Paragraph in auditor’s report.
- (i) Briefly discuss the considerations to be taken care of by the statutory auditor when EOM paragraph is included in auditor’s report.
- (ii) State any two examples of circumstances where the auditor may consider it necessary to include an EOM paragraph. **(5 Marks)**
- (c) CA Y, statutory auditor of a company, is in process of determining materiality for financial statements while planning audit. Since materiality is a matter of professional judgment and is affected by auditor’s perception of financial information needs of users of financial statements, he is reasonably making certain assumptions about users of financial statements. Which reasonable matters are likely to be assumed by him in respect of users? **(4 Marks)**
3. (a) During the course of statutory branch audit of a nationalized bank, CA Amrish is performing audit procedures in relation to the advances. He has verified the selected sample of borrower accounts representing advances and found nothing unusual. In a banking environment, there exist documentary evidence containing observations/comments on advances which can be useful to the statutory branch auditor in performing an effective audit. List out few such documentary evidence which can be made use of by CA Amrish. **(5 Marks)**

- (b) While auditing the financial statements of Bro Traders LLP, CA L is carefully going through LLP agreement. Briefly discuss the key points CA L should pay attention in the LLP agreement and the reporting responsibilities of CA L concerning the financial statements of Bro Traders LLP? **(5 Marks)**
- (c) CA N, statutory auditor of Rock Limited, is in the process of final assembly of audit file. Under what circumstances, a statutory auditor can make changes to audit documentation during final assembly process of audit file? Give a few examples of such changes. **(4 Marks)**
4. (a) CA J is appointed as statutory auditor of Sigma and Beta Limited for the year 2023-24. During the audit he observed trade receivables amounting to ₹ 50 crores are reflected in the financial statements of the company. He wants to obtain sufficient appropriate evidence to conclude that trade receivables have been valued appropriately. Suggest few audit procedures in this regard. **(5 Marks)**
- (b) While planning the audit of Me Limited, CA M has planned nature, timing and extent of risk assessment procedures to identify and assess risks of material misstatements. How risk should be assessed by the auditor CA M? It is also well known that assessment of risks is a matter of professional judgment.
- Which specific matters are not included in audit risk? Additionally, CA K, one of the team members of CA M, is of the view that Materiality and Audit Risk are only considered at planning stage of an audit. Comment. **(5 Marks)**
- (c) CA D is planning an audit of a listed company. List specific documentation requirements in accordance with SA 300 in relation to planning such an audit. How such planning documentation is useful? **(4 Marks)**
5. (a) Section 143(1) of Companies Act, 2013 states that every auditor of a company shall have access to books of accounts and vouchers of company and shall be entitled to require from officers of company such information and explanation as considered necessary and shall inquire into certain matters. State those matters to be inquired. **(5 Marks)**
- (b) M/s Veer and Associates is appointed as auditor of KMP limited. During the audit, auditor wants to verify that trade payables and liability balances that were supposed to be recorded have been recognized in the financial statements. Which assertion auditor wants to ensure and what audit procedures should be followed by him in this regard? **(5 Marks)**
- (c) CA M, auditor of a company, has planned to use substantive analytical procedures during course of audit. In this regard, he has decided to use such procedures in following areas: -

- (i) For testing relationship between sales and cost of sales
- (ii) For testing rights over certain assets forming part of account balances

Comment upon his approach along with reasons. **(4 Marks)**

6. (a) Mr. Vaayu is appointed as the auditor of PRISM Limited for the year 2023-24. He wants to ensure that the PPE has been valued appropriately and as per generally accepted accounting policies and practices and also that PRISM Limited has valid legal ownership rights over the PPE claimed to be held by the company and recorded in the financial statements. Explain how the auditor will verify the same. **(5 Marks)**
- (b) M/s TP & Co., a firm of Chartered Accountants, has been conducting audit of KSR Ltd. since last 4 years. KSR Ltd. has diversified their business into newer areas during the last year. The senior member of the audit team handed over the standard audit programme of earlier years to the audit assistants and instructed them to follow the same. The assistants are conducting the audit accordingly. Whether the attitude of the audit assistants is justified? Guide them. **(5 Marks)**
- (c) As per SA 560, when after the date of the auditor's report but before the date the financial statements are issued, a fact becomes known to the auditor that had it been known to the auditor at the date of the auditor's report, it may have caused the auditor to amend the auditor's report. In this context, what is meant by "Date the financial statements are issued"? Can it be later than the date of providing auditor's report to the entity? **(4 Marks)**

OR

CA N, statutory auditor of QST Limited, appointed for a term of 5 years has completed audit for the first financial year ending on 31st March 2024. In compliance with requirements of professional standards, an audit file has been assembled. After about a period of six months from date of issue of audit report, he gets a call from CFO of the company to share complete audit file so that financial reporting of company can be improved upon in coming periods. Is it mandatory for statutory auditors to share audit files with client? What are the requirements for making audit documentation available to clients? **(4 Marks)**