PAPER – 3: ADVANCED AUDITING, ASSURANCE AND PROFESSIONAL ETHICS

QUESTIONS

PART A: Multiple Choice Questions

Integrated Case Scenario

ComTeK Limited, a top 1000 listed entity on the BSE by market capitalization for the past two years, sells IT and related equipment directly to consumers through its website.

One day, the CFO of the company received a video call from the Managing Director (MD) instructing him to transfer ₹ 90 lakhs to the bank account of NxT Limited. When questioned by the CFO, the Managing Director explained NxT's products are fast moving and contribute 30% of the company's revenue. Further, the amount of payment is within the approved limit and can easily be remitted without any further approval. Satisfied with the explanations, the CFO made the necessary transfer.

At the end of the month, while preparing the bank reconciliation statement, the CFO realised that five incremental payments of ₹ 90 lakhs each had been made to NxT Limited. These payments were unreconciled and does not have any corresponding entry in the books of account. The CFO explained the situation to the MD, reminding him about the video call that had instructed him such payments. However, the MD denied making any such video call.

The CFO and Managing Director engaged a forensic expert, who observed that the company had cyber-attack using sophisticated AI tools. Investigation further revealed that the video call to the CFO was fake and made from the laptop not owned by the company. The hackers had gained access to the CFO's laptop and have obtained bank details and its authorisation information. The company filed a police complaint and reported the incident to the appropriate authorities.

During the risk assessment process, the auditor of the company determined that the IT environment poses a significant risk. The auditor assessed that the principal financial systems used in the preparation of the financial statements were compromised during the cyber-attack. The auditor also focused on the judgements made by management related to the known security incidents. The auditor made inquiries with Risk Management team and with the Chief Information Officer to understand their assessment of the cybersecurity risk and the measures in place to mitigate this risk, focusing on the principal financial systems used in the preparation of the financial statements. The auditor also communicated with those charged with governance about the cyber incident. After completion of necessary procedures, the auditor felt that it had incurred additional efforts to the tune of 20%. The auditor reviewed, with the assistance of specialists, management's assessment of the potential impact on the principal financial systems used in the preparation of the financial statements.

The management of the company was impressed about the level of detail and diligence employed by the auditor while dealing with the cyber security incident. They particularly appreciated the in-depth knowledge of the auditor, timely involvement of IT specialist by the auditor and experience in dealing with cyber-security incidents. The management felt that the auditor would be the right fit for conducting a thorough audit of the IT systems of the company. In order to leverage the auditor's expertise, the management proposed to engage the auditor to conduct a system audit.

The stakeholders of the company believe that Integrated Reporting, as prescribed by the International Integrated Reporting Council, should be prepared by the management. The primary purpose was to explain to providers of financial capital how the company creates, preserves or erodes value over time. The Integrated Report would provide relevant information, both financial and other for the benefits all stakeholders interested in a company's ability to create value over time, including employees, customers, suppliers, business partners, local communities, legislators, regulators and policy-makers.

On the basis of the above mentioned facts, you are required to answer the following MCQs:

1. In the given case, cyber-attack encountered by the company is known as:

   (a) Spoofing

   (b) Denial of Services Attack

   (c) Malware

   (d) Identity Based Attack

2. The engagement partner is confused as to whether the audit report would be impacted by the cyber-attack instance. What is the appropriate reporting implication:

   (a) No implication in the audit report since the financial loss has already been recognised in the financial statements.

   (b) Qualify audit opinion as the amount of loss due to cyber-attack is incremental and does not emanate from its operating activity.

   (c) Include an Emphasis of Matter paragraph as cyber security incidents are by default fundamental to the attention to the users of the financial statements.

   (d) Report as a Key Audit Matter since the cyber incidence was of most significance in the audit of the financial statements of the current period.

3. The company wants to prepare an Integrated Report as contained in the International Integrated Reporting Council and endorsed by SEBI. The Company Secretary is of the view that Integrated Report is mandatory for a listed entity. Which of the following is correct in this regard?

   (a) The view of Company Secretary is correct since the company meet the qualifying threshold i.e. Top 1000 listed entity by market capitalisation at the end of the previous year.

   (b) The view of company Secretary is incorrect as Integrated Reporting is voluntary for the top 500 listed entities.

(c) The view of Company Secretary is correct as the company meet the qualifying threshold i.e. Top 1000 listed entity by market capitalisation at the end of the current year.

(d) The view of Company Secretary is incorrect since Integrated Reporting is voluntary for the top 1000 listed entities.

4. Integrated Reporting comprises 6 categories of capital. The company observed that it has capitalised intangible assets (patent) and roof top solar equipment in the balance sheet. In the Integrated Report patents and solar equipment should be disclosed respectively as:

(a) Financial Capital and Manufactured Capital.

(b) Natural Capital and Financial Capital.

(c) Intellectual Capital and Natural Capital.

(d) Human Capital and Intellectual Capital.

5. Can the auditor accept the system audit as offered by the ComTeK Limited?

(a) Yes, the statutory auditor can accept the assignment of system audit, provided it did not involve any scrutiny/review of financial data and information.

(b) Yes, the statutory auditor can accept the assignment of system audit, provided it involves any scrutiny/review of financial data and information

(c) Yes, the statutory auditor can accept the assignment of system audit, provided the fee for system audit is not more than the audit fee.

(d) No, the statutory auditor cannot accept the assignment of system audit since it did not involve any scrutiny/review of financial data and information.

Independent MCQs

6. CA Vijay qualified as CA in November 2022 started his professional practice in Delhi. Since he has enough time to devote on other activities, he is considering the following four options:

- Part-time tutorship under the coaching organisation of the Institute.
- Editorship of journals other than professional journals.
- Acting as recovery consultant in the banking sector.
- Owning agricultural land and carrying out agriculture activity.

Do you think CA Vijay needs to take any specific and prior permission from the Council for any or all of the above mentioned activities?

(a) Specific and prior permission is required for editorship of journals other than professional journals.

(b) Specific and prior permission is required for part-time tutorship and acting as recovery consultant.

(c) Specific and prior permission is required for acting as recovery consultant and owning agricultural land and carrying out agriculture activity.

(d) Specific and prior permission is required for editorship of journals other than professional journals and carrying out agriculture activity.

7. CA RK, the auditor of Shipra Limited resigned from the post due to personal reasons. CA SP was appointed as the subsequent auditor of the company by the Board of Directors. During the conclusion of the audit for the 2023-24, should CA SP mention CA RK 's resignation in the Companies (Auditor's Report) Order 2020?

(a) No. CARO 2020 does not state any requirements to report resignation of auditor. However, the same needs to be mentioned by CA SP in the Audit Report under Other Matter Paragraph, as per SA 706.

(b) Yes. As per clause (xviii) of para 3 of CARO, CA SP should report the resignation of CA RK and state if he has taken into consideration the issues or objections raised by CA RK.

(c) No. Since the resignation of CA RK is due to his own personal reason, the same need not be reported under CARO.

(d) Yes. As per clause (xxi) of para 3 of CARO, CA SP should report the resignation of CA RK and state if he has taken into consideration the issues or objections raised by CA RK.

8. SMN Limited is a management consultancy firm and in operation for the last 15 years. The company's financial reporting process is sound, and its statutory auditors has issued clean report on the audit of the financial statements of the company since inception. Due to mandatory audit rotation under the Companies Act 2013, MNO & Associates was appointed as the new auditor for the financial year ending 31 March 2024. During the audit, MNO & Associates performed procedures on both the current year's financials and the opening balances. No significant issues have been observed during the audit and the auditors intended to issue a clean report, they included an "Other Matters" paragraph in the draft report, noting that the previous year's financials were audited by a different auditor. The management requested this reference be removed since MNO & Associates audited the opening balances also and such a reference is not required. However, the auditors did not agree with the management. Please advise the auditor or the management whoever is incorrect with the right guidance.

(a) The contention of the management is valid. After performing all the audit procedures, an auditor should not pass on the responsibility to another auditor by including such references in his audit report.

(b) Any auditor has two options, either to perform audit procedures on opening balances or given such reference of another auditor in his report. An auditor cannot mix up the things like this auditor has done. It is completely unprofessional.

(c) In the given situation even if the auditor wants to give such reference, the management and the auditor should have taken approval from the previous auditor at the time of appointment of new auditor. In this case, it cannot be done.

(d) The report of the auditor is correct and is in line with the Standards on Auditing. An auditor is required to include such reference in his report under Other Matter Paragraph which require referencing the previous auditor when applicable.

PART B: DESCRIPTIVE QUESTIONS

Standards on Auditing, Statements and Guidance Notes

Auditing Planning, Strategy and Execution

9. RPS Ltd., at its annual general meeting, appointed Mr. R, Mr. P, and Mr. S as joint auditors to conduct the audit for the financial year 2023-24. For the valuation of the newly constructed infrastructure project of the company, Mr. R, Mr. P, and Mr. S decided to consult their own known engineers. Due to differences of opinion, each joint auditor sought advice from their respective engineers. As a result, significant discrepancies were found in the valuation reports provided by the engineers. However, Mr. R agreed with the report provided by Mr. P's engineer, while Mr. S did not. Mr. R argues that report of Mr. P's engineer should be included in the audit report due to the majority of votes. Now, Mr. S is in a dilemma.

   What would be the responsibility of the auditors if the report provided by Mr. P's engineer is later found to be faulty?

Materiality, Risk Assessment and Internal Control

10. AMRO Ltd. is a manufacturing and trading Company of leather goods since last 10 years. You are the internal auditor of the company for the year 2023-24. In order to review internal controls of the company, you visited the departments and noticed:

    (1) The head of procurement, Mr. Amit, has complete control over purchasing, receiving goods, and approving payments to suppliers. His actions are not reviewed by any other person in the company.

    (2) The company's staff has been working in the same roles for over five years without any rotation. The finance manager, Mr. Sachin, in particular, has never had his duties rotated since joining the company.

    (3) The store manager, Mr. Gupta, who is responsible for maintaining the inventory, also keeps the inventory records.

(a) Briefly discuss the general conditions pertaining to the internal check system to be ensure by you as an auditor.

(b) Do you think that general conditions pertaining to the internal check system are violated in the given situation?

Completion and Review

11. Mudit & Associates is appointed as Statutory Auditors of GRF Private Limited for the financial year 2023-24. The company is into the business of Health Club, Fitness Centre and gym costumes. CA M is the Engagement Partner for the audit assignment. CA M observed the following points while auditing:

(i) Customer's base is reducing continuously due to tough competition and discount war existing in the market.

(ii) Payments of creditors are delayed and made with overdue interest.

(iii) Company has not been able to pay the salaries of staff and trainers on time.

(iv) Key financial ratios of the company, like current ratio, debt-service coverage ratio, are in the red and have deteriorated considerably as compared to last year.

(v) The company has requested its bankers to provide it with additional working capital credit facilities of ₹ 1.5 Crores, but bankers are not considering the company's proposal favorably.

What audit procedures should be followed by CA M considering the above circumstances as per SA 570-"Going Concern"? How auditor should deal if the use of going concern basis of accounting is appropriate, but a material uncertainty exists, and adequate disclosure of material uncertainty is made in the financial statements?

Reporting

12. The extract of the financial statements of Nex Limited for the financial year 2023-24 is as follows:

Particulars	Rupees (in Crores)
Trade Receivable - Unsecured considered Good	225.00

Provision for Bad and Doubtful Debts	50.00
Stock of Raw Materials	180.00
Stock of Finished Goods	250.00
Total of Assets	950.00

CA Yash is the statutory auditor of Nex Ltd. for the FY 2023-24. During the course of audit CA Yash noticed the following:

i. With respect to the debtors amounting to ₹ 175 crore, no balance confirmation was received by the audit team. Further, there have been defaults on the payment obligations by debtors on the due dates during the year under audit. The company has created a provision for doubtful debts to the tune of ₹ 50 crore during the year under audit. The company has stated that the provision is based on receivables which are older than 36 months, which according to the audit team is inadequate and as such the audit team is unable to ascertain the carrying value of trade receivables.

ii. Further, in respect of inventories (which constitutes 45% of the total assets of the company), during the reporting period, the management has not undertaken physical verification of inventories at periodic intervals. Also, the company has not maintained adequate inventory records at the factory. The audit team was unable to undertake the physical inventory count as such the value of inventory could not be verified.

What kind of opinion should be given by CA Yash in the given situation? Draft a suitable Opinion and Basis of Opinion paragraph.

Prospective Financial Information and Other Assurance Services

13. Mr. Vineet, an auditor, has been approached by Qub Ltd. to examine the prospective financial information of the company. What factors should an auditor consider before accepting an engagement to examine prospective financial information, and under what conditions should the auditor decline or withdraw from such an engagement? Additionally, what steps should be taken to formalize the terms of the engagement?

Digital Auditing and Assurance

14. Mr. Karan is a consultant tasked with helping a mid-sized manufacturing company modernize its operations by integrating Internet of Things (IoT) technology. The company wants to connect various devices such as manufacturing equipment, smart home security systems for their facility, and inventory management systems. They aim to leverage IoT to improve operational efficiency, predict equipment maintenance needs, and enhance overall security. However, they are concerned about the potential risks and the impact on their audit processes. Describe the key components and benefits of IoT, the risks associated with IoT implementation, and the implications for the company's audit processes. How should the company address these concerns to ensure a smooth transition?

Group Audits

15. You are appointed as an auditor of Imperial Industries Limited, a listed company with a turnover of ₹ 3.5 billion, operating through 15 business units and nearly 200 branches across the country. Imperial Industries Limited is a key supplier to the American building and construction market. As an auditor, how will you draft the report in case:

    (a) When the Component(s) Auditor Reports on Financial Statements under an Accounting Framework Different than that of the Parent?

    (b) When the Component(s) Auditor Reports under an Auditing Framework Different than that of the Parent?

    (c) Where the financial statements of one or more components are not audited?

Bank Audit

16. Your firm ABC Associates is appointed as Central Statutory Auditors of a Nationalised Bank for the year 2023-24. The Bank follows the financial year as accounting year. During the audit, CA Aadi, the Audit Manager has noticed following issues and placed the same before the team.

Particulars	
Consortium Cash Credit Facilities to Prime Ltd.	₹ 75 crores

Bank's own Share in Cash Credit Facilities	₹ 15 crores
Debits towards Interest in the Last Two Quarters	₹ 2.25 crores
Credits in Prime Ltd.'s Account in the Last Two Quarters	₹ 1.75 crores
Classification of Prime Ltd.'s Account (Based on Lead Bank's Certificate)	Performing Account

As an auditor, how will you deal with the above mentioned matter?

Internal Audit

17. Rishi is appointed as internal auditor for a SPOM Limited, a medium-sized manufacturing company, while CA Nitin is the statutory auditor of the SPOM Limited.

(a) During the review, Rishi notices several discrepancies in the disbursement records and suspects there might be weaknesses in the internal control system. Additionally, there have been recent changes in the company's business policies that he was not informed about. Rishi is concerned about maintaining his independence and objectivity while ensuring that management is aware of these issues. What are the responsibilities of Rishi as an Internal Auditor with respect to the accounting function and financial records of the organisation?

(b) CA Nitin asked Rishi to provide direct assistance to him regarding evaluating the appropriateness of management's use of the going concern assumption. In view of Standards on Auditing, whether Nitin can ask direct assistance from Rishi as stated above?

Due Diligence, Investigation & Forensic Accounting

18. CA. Rajul is designated as the Credit Manager at a branch of APP Bank Limited. PQR Ltd has approached the branch with a request to sanction credit facilities worth ₹ 12 crore for meeting its regular business needs. This is a potential new client for the bank. She has reviewed the company's past history, the background of its promoters and directors, the shareholding pattern, and the nature of its business. She also conducted an assessment of the financial results of past years and future

projections. Additionally, she carried out a SWOT analysis of the company.

She also evaluates the net worth of the directors, checks the CIBIL score, and verifies whether the names of the promoters or directors appear on the RBI defaulters' list. Furthermore, she makes discreet inquiries with a few clients of the branch who are engaged in a similar line of activity regarding the creditworthiness of the company, its promoters, and directors.

Based on the above:

(a) Identify the procedures followed by CA Rajul and discuss its nature.

(b) Would your answer be different if this activity was to be performed by a person not qualified as a Chartered Accountant? Can a non-CA perform such activity? State reason.

(c) Name any three other areas where the identified activity can be undertaken.

Sustainable Development Goals (SDG) & Environment, Social and Governance (ESG) Assurance

19. Kapil is appointed as an external auditor to provide assurance on a company's Business Responsibility and Sustainability Report (BRSR). To ensure the report's accuracy and reliability, he needs to follow a comprehensive methodology that includes several key steps. What methodology should Kapil follow to provide assurance on the BRSR?

Professional Ethics & Liabilities of Auditors

20. (a) CA Vaayu is the auditor of Viva Limited having a turnover of more than ₹ 200 Crores. The audit fee for the year is fixed at ₹ 80 Lakhs. During the year, the company offers CA Vaayu an assignment of representation before Income Tax Appellate Tribunal for certain matter for remuneration of ₹ 1.75 crores. CA Vaayu accepted the assignment. Discuss action of CA Vaayu with reference to the provisions of the Chartered Accountants (Amendment) Act, 2006 and Schedules thereto.

(b) Sanjeev & Associates, a firm of Chartered Accountants responded to a tender from a PF Office, Chembur for filing quarterly e-TDS returns. The terms of tender are as follows:

(i) Earnest Money Deposit of ₹ 7,500/-

(ii) It is open for all categories

(iii) Maximum fees of ₹ 7,500/- per quarter

Discuss whether Sanjeev and Associates can respond to the said tender with reference to provisions of the Chartered Accountants (Amendment) Act, 2006 and Schedules thereto.

SUGGESTED ANSWERS/HINTS

PART A: Answers to Multiple Choice Questions

1. **(a)**

2. **(d)**

3. **(b)**

4. **(c)**

5. **(a)**

6. **(a)**

7. **(b)**

8. **(d)**

PART B: Answers to Descriptive Questions

9. **Using the work of an Auditor's Expert:** As per SA 620 "Using the Work of an Auditor's Expert", the expertise of an expert may be required in the valuation of complex financial instruments, land and buildings, plant and machinery, jewelry, works of art, antiques, intangible assets, assets acquired and liabilities assumed in business combinations and assets that may have been impaired etc., however, the auditor has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the auditor's use of the work of an auditor's expert.

The auditor shall evaluate the adequacy of the auditor's expert's work for the auditor's purposes, including the relevance and reasonableness of that expert's findings or conclusions, and their consistency with other audit evidence as per SA 500.

Further, in view of SA 620, if the expert's work involves use of significant assumptions and methods, then the relevance and reasonableness of those assumptions and methods must be ensured by the auditor and if the expert's work involves the use of source data that is significant to that expert's work, the relevance, completeness, and accuracy of that source data in the circumstances must be verified by the auditor.

In the instant case, Mr. R, Mr. P and Mr. S, jointly appointed as auditors of RPS Ltd., referred their own known engineer for valuation of the newly constructed infrastructure project. Engineers are an auditor's expert as per SA 620. Mr. P's referred Engineer has provided the valuation report, which was later found faulty. Further, Mr. S is not in agreement with this report, therefore, he submitted a separate audit report specifically for such a valuation.

In such a situation, it was the duty of Mr. R, Mr. P and Mr. S, before using the valuation report provided by engineer, to ensure the relevance and reasonableness of assumptions and methods used. They were also required to examine the relevance, completeness and accuracy of source data used for such a report before expressing their opinion.

Mr. R and Mr. P will be held responsible for gross negligence and using such faulty report without examining the adequacy of expert engineer's work whereas Mr. S will not be held liable for the same due to separate opinion expressed by him.

10. **(a)** **Internal Check System:** The general condition pertaining to the internal check system may be summarized as under:

(i) no single person should have complete control over any important aspect of the business operation. Every employee's action should come under the review of another person.

(ii) Staff duties should be rotated from time to time so that members do not perform the same function for a considerable length of time.

(iii) Every member of the staff should be encouraged to go on leave at least once a year.

(iv) Persons having physical custody of assets must not be permitted to have access to the books of accounts.

(v) There should exist an accounting control in respect of each class of assets, in addition, there should be periodical inspection so as to establish their physical condition.

(vi) Mechanical devices should be used, wherever practicable, to prevent loss or misappropriation of cash.

(vii) Budgetary control should be exercised, and wide deviations observed should be reconciled.

(viii) For inventory taking, at the close of the year, trading activities should, if possible be suspended, and it should be done by staff belonging to several sections of the organization.

(ix) The financial and administrative powers should be distributed very judiciously among different officers and the manner in which those are actually exercised should be reviewed periodically.

(x) Procedures should be laid down for periodical verification and testing of different sections of accounting records to ensure that they are accurate.

(b) Yes, in the given situation general conditions pertaining to the internal check system are violated as follows:

(1) The head of procurement, Mr. Amit, having complete control over the procurement process without oversight violates the principle that no single person should control any important aspect of the business operation.

(2) The lack of staff rotation for over five years violates the principle that staff duties should be rotated periodically to prevent any single person from performing the same function for too long.

(3) Allowing Mr. Gupta, the store manager, to maintain inventory records while also having custody of the inventory violates the principle that those with physical custody of assets should not have access to accounting records.

11. As per SA 570, "Going Concern" if events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern, the auditor shall obtain sufficient appropriate audit evidence to determine whether or not a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern through performing additional audit procedures, including consideration of mitigating factors. These procedures shall include:

(a) Where management has not yet performed an assessment of the entity's ability to continue as a going concern, requesting management to make its assessment.

(b) Evaluating management's plans for future actions in relation to its going concern assessment, whether the outcome of these plans is likely to improve the situation and whether management's plans are feasible in the circumstances.

(c) Where the entity has prepared a cash flow forecast, and analysis of the forecast is a significant factor in considering the future outcome of events or conditions in the evaluation of management's plans for future actions:

(i) Evaluating the reliability of the underlying data generated to prepare the forecast; and

(ii) Determining whether there is adequate support for the assumptions underlying the forecast.

(d) Considering whether any additional facts or information have become available since the date on which management made its assessment.

(e) Requesting written representations from management and, where appropriate, those charged with governance, regarding their plans for future actions and the feasibility of these plans.

In the given case, CA M has observed such points that may cast significant doubt on the entity's ability to continue as a going concern. Therefore, CA M should follow audit procedures such as:

- Review of management's assessment of the company's ability to continue as a going concern.
- Examine and challenge the reasonableness of the company's cash flow forecasts and key assumptions.
- Review events after the reporting period that might affect the going concern assumption, such as further financial deterioration or inability to secure financing.
- Analysis of the company's key financial ratios and compliance with loan agreements to assess liquidity and solvency.
- Review of the company's challenges and efforts to secure additional financing and the reasons for the bank's reluctance to provide further credit.
- Assess the impact of declining customer base, delayed payments, and other operational challenges on the company's ability to continue as a going concern.

Further, as per SA 570 if adequate disclosure about the material uncertainty is made in the financial statements, the auditor shall express an unmodified opinion and the auditor's report shall include a separate section under the heading "Material Uncertainty Related to Going Concern" to:

(a) Draw attention to the note in the financial statements that discloses the matters set out in paragraph 19; and

(b) State that these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the auditor's opinion is not modified in respect of the matter.

12. In the present case, CA Yash is unable to obtain sufficient and appropriate audit evidence with respect to the following:

i. The balance confirmation with respect to debtors amounting to ₹ 175 crores are not available. Further there has been default in payment by the debtors and the provision so made is not adequate. The audit team is also unable to ascertain the carrying value of trade receivables.

ii. With respect to 45% of the company's inventory, neither the physical verification has been done by the management nor adequate inventory records are maintained. The audit team is also unable to undertake the physical inventory count as such the value of inventory could not be verified.

In the above two circumstances the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

Thus, CA Yash should give a Disclaimer of Opinion.

The relevant extract of the Disclaimer of Opinion Paragraph and Basis for Disclaimer of Opinion paragraph is as under:

Disclaimer of Opinion

We do not express an opinion on the accompanying financial statements of Nex Ltd. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for Disclaimer of Opinion

We are unable to obtain balance confirmation with respect to the debtors amounting to ₹ 175 crore. Further, there have been defaults on the payment obligations by debtors on the due dates during the year under audit. The company has created a provision for doubtful debts of ₹ 50 crore during the year under audit which is inadequate in the circumstances of the company. The carrying value of trade receivables could not be ascertained.

Further, in respect of inventories (which constitute 45% of the total assets of the company), during the reporting period, the management has not undertaken physical verification of inventories at periodic intervals. Also, the company has not maintained adequate inventory records at the factory. We were unable to undertake the physical inventory count and as such the value of inventory could not be verified.

13. Before accepting an engagement to examine prospective financial information, the auditor would consider, amongst other things:

- The intended use of the information;
- Whether the information will be for general or limited distribution;
- The nature of the assumptions, that is, whether they are best estimates or hypothetical assumptions;
- The elements to be included in the information; and
- The period covered by the information.

The auditor should not accept, or should withdraw from, an engagement when the assumptions are clearly unrealistic or when the auditor believes that the prospective financial information will be inappropriate for its intended use. The auditor should consider the extent to which reliance on the entity's historical financial information is justified.

To formalize the terms of the engagement, it is essential to agree on the terms with the client by sending an engagement letter, like in other engagements.

14. **Internet of Things:** IoT is the concept of connecting any device (cell phones, coffee makers, washing machines, and so on) to the internet.

Key components of IoT are data collection, analytics, connectivity, and people and process. IoT not only changes the business model, but also affects the strategic objectives of the organisation. The risk profile of the entity changes with exposure to new laws and regulations.

Example

(i) Connected Cars, connected manufacturing equipment's, smart home security, (The options for home security from doorbell cameras or outdoor cameras - users can view video feeds when they are away from home).

(ii) Data from machines can be used to predict whether equipment will break down, giving manufacturers advance warning to prevent long stretches of downtime.

(iii) Refrigerator placing an order with a grocery store whenever the supply of eggs falls below a certain number.

(iv) Smart oven works by scanning QR or bar codes and connecting to Wi-Fi, which it then uses to determine the best temperature and time to cook the food to avoid undercooking or burning.

(v) Researchers use IoT devices to gather data about customer preferences and behavior, though that can have serious implications for privacy and security.

Common risks of IoT:

The key risks associated with IoT including, device hijacking, data siphoning, denial of service attacks, data breaches and device theft.

Audit Implications

A shift to connected devices and systems may result in auditors not being able to rely only on manual controls. Instead, auditors may need to scope new systems into their audit. Audit firms may need to train and upskill auditors to evaluate the design and operating effectiveness of automated controls.

Consumer-facing tools that connect to business environments in new ways can impact the flow of transactions and introduce new risks for management and auditors to consider. Consider payment processing tools that allow users to pay via credit card at a retail location through a mobile device. This could create a new path for incoming payments that may rely, in part, on a new service provider supplying and routing information correctly. Auditors would need to consider the volume of those transactions, and the processes and controls related to it.

15. **(a)** **When the Component(s) Auditor Reports on Financial Statements under an Accounting Framework Different than that of the Parent:** The parent may have components located in multiple geographies outside India applying an accounting framework (GAAP) that is different than that of the parent in preparing its financial statements. Foreign components prepare financial statements under different financial reporting frameworks, which may be a well-known framework (such as US GAAP or IFRS) or the local GAAP of the jurisdiction of the component. Local component auditors may be unable to report on financial statements prepared using the parent's GAAP because of their unfamiliarity with such GAAP.

When a component's financial statements are prepared under an accounting framework that is different than that of the framework used by the parent in preparing group's consolidated financial statements, the parent's management perform a conversion of the components' audited financial statements from the framework used by the component to the framework under which the consolidated financial statements are prepared. The conversion adjustments are audited by the principal auditor to ensure that the financial information of the component(s) is suitable and appropriate for the purposes of consolidation.

A component may alternatively prepare financial statements on the basis of the parent's accounting policies, as outlined in the group accounting manual, to facilitate the preparation of the group's consolidated financial statements. The group accounting manual would normally contain all accounting policies, including relevant disclosure requirements, which are consistent with the requirements of the financial reporting framework under which the group's consolidated financial statements are prepared. The local component auditor can then audit and issue an audit report on the components financial statements prepared in accordance with "group accounting policies".

When applying the approach of using group accounting policies as the financial accounting framework for components to report under, the principal/parent auditors should perform procedures necessary to determine compliance of the group accounting policies with the GAAP applicable to the parent's financial statements. This ensures that the information prepared under the requirements of the group accounting policies will be directly usable and relevant for the preparation of consolidated financial statements by the parent entity, eliminating the need for auditing by the auditor, the differences between the basis used for the component's financial statements and that of the consolidated financial statements. The Principal auditor can then decide whether or not to rely on the components' audit report and make reference to it in the auditor's report on the consolidated financial statements.

(b) **When the Component(s) Auditor Reports under an Auditing Framework Different than that of the Parent:** Normally, audits of financial statements, including consolidated financial statements, are performed under auditing standards generally accepted in India ("Indian GAAS").

In order to maintain consistency of the auditing framework and to enable the parent auditor to rely and refer to the other auditor's audit report in their audit report on the consolidated financial statements, the components' financial statements should also be audited under a framework that corresponds to Indian GAAS.

(c) **Where the financial statements of one or more components are not audited:** The financial statements of all components included in consolidated financial statements should be audited or subjected to audit procedures in the context of a multi-location group audit. Such audits and audit procedures can be performed by the auditor reporting on the consolidated financial statements or by the components' auditor.

Where the financial statements of one or more components continue to remain unaudited, the auditor reporting on the consolidated financial statements should consider unaudited components in evaluating a possible modification to his report on the consolidated financial statements. The evaluation is necessary because the auditor (or other auditors, as the case may be) has not been able to obtain sufficient appropriate audit evidence in relation to such consolidated amounts/balances. In such cases, the auditor should evaluate both qualitative and quantitative factors on the possible effect of such amounts remaining unaudited when reporting on the consolidated financial statements using the guidance provided in SA 705, “Modifications to the Opinion in the Independent Auditor’s Report”.

16. The bank is a consortium member of cash credit facilities of ₹ 75 crores to Prime Ltd. Bank's own share is ₹ 15 crores only. During the last two quarters against a debit of ₹ 2.75 crores towards interest, the credits in X Ltd.’s account are to the tune of ₹ 1.75 crores only. Sometimes, several banks form a group (the 'consortium') under the leadership of a 'lead bank' to make advance to a large customer on same conditions and security with proportionate rights. In such cases, each bank may classify the advance given by it according to its own experience of recovery and other factors. Since in the last two quarters, the amount remains outstanding and, thus, interest amount should be reversed. This is despite the certificate of lead bank to classify that the account as performing. Accordingly, the amount should be shown as non-performing asset (NPA).

17. **(a)** In the given case, Rishi notices several discrepancies in the disbursement records and suspects there might be weaknesses in the internal control system. He is concerned about maintaining his independence and objectivity while ensuring that management is aware of these issues.

Responsibilities of Rishi as an Internal Auditor with respect to the accounting function and financial records of the organisation include:

- to ascertain adequacy of system of internal control by a continuous examination of accounting procedures, receipts and disbursements, and to provide adequate safeguards against misappropriation of assets.
- to operate independently of the accounting staff and must not in any way divest any of the responsibilities placed upon him.
- not to involve in the performance of executive functions in order that the objective outlook does not get obscured by the creation of the vested interest.

- to observe facts and situations and bring them to notice of authorities who would otherwise never know them; also, critically appraise various policies of the manage-ment and draw its attention to any deficiencies, wherever these require to be corrected.
- to associate closely with management and keep knowledge up to date by being informed about all important occurrences and events affecting the business, as well as the changes that are made in business policies.
- at all times, the internal auditor must enjoy an independent status.

(b) As per SA 610 "Using the Work of Internal Auditor", the external auditor shall not use internal auditors to provide direct assistance to perform procedures that involve making significant judgments in the audit.

Since the external auditor has sole responsibility for the audit opinion expressed, the external auditor needs to make significant judgments in the audit engagement.

Significant judgments include the following:

- Assessing the risks of material misstatement;
- Evaluating the sufficiency of tests performed;
- Evaluating the appropriateness of management's use of the going concern assumption;
- Evaluating significant accounting estimates; and
- Evaluating the adequacy of disclosures in the financial statements, and other matters affecting the auditor's report.

In view of the above, CA. Nitin cannot ask direct assistance from internal auditors regarding evaluating the appropriateness of management's use of the going concern assumption in accordance with SA 610.

18. **(a)** The activity described in the situation is Due diligence. Due diligence is a measure of prudence activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent person under the particular circumstance, not measured by any absolute standard but depending upon the relative facts of the case. It involves a careful study of financial and non-financial possibilities. It implies a general duty to take care in any transaction.

Due diligence is a process of investigation, performed by investors, into the details of a potential investment such as an examination of operations and management and the verification of material facts. It entails conducting inquiries for the purpose of timely, sufficient and accurate disclosure of all material statements/information or documents, which may influence the outcome of the transaction. Due diligence involves a careful study of the financial as well as non-financial possibilities for successful implementation of restructuring plans.

Due diligence involves an analysis carried out before acquiring a controlling interest in a company to determine that the conditions of the business conform with what has been presented about the target business. Also, due diligence can apply to recommendation for an investment or advancing a loan/credit.

(b) There would be no difference in answer if above activity was to be performed by a person who is not a Chartered Accountant. The activity would remain due diligence. Due diligence can be performed by any person. It is not necessary that due diligence can only be carried out by a Chartered Accountant. As due diligence involves exercise of prudence and general duty to take care in any transaction, it can be undertaken by any person.

(c) The areas where due diligence may be undertaken are: -

(i) Corporate restructuring

(ii) Venture capital financing

(iii) Public offerings

19. Methodology that should be followed by Kapil to provide assurance on BRSR is:

- Preliminary Review of ESG report, parameters
- On-site Assessment / Verification of ESG Report
- Issuance of Assessment Report and Assessment Statement
- Review of the responses and clarifications on the findings
- Submission of findings of the on-site assessment and document review
- Preparation of Assessment / Verification report including final results of Assessment

20. (a) As per the Council General Guidelines 2008, under Chapter IX on appointment as statutory auditor a member of the Institute in practice shall not accepts the appointment as a statutory auditor of a PSUs'/Govt company(ies)/Listed company(ies) and other public company(ies) having a turnover of ₹ 50 crores or more in a year and where he accepts any other work(s) or assignment(s) or service(s) in regard to same undertaking(s) on a remuneration which in total exceeds the fee payable for carrying out the statutory audit of the same undertaking. For this purpose, the other work/services include Management Consultancy and all other professional services permitted by Council excluding audit under any other statute, Certification work required to be done by the statutory auditor and any representation before an authority.

In the given case, the company offers CA Vaayu, the statutory auditor, an assignment of representation before Income Tax Appellate Tribunal for remuneration of ₹ 1.75 Crores.

Conclusion: In view of the above provision, it would not be misconduct on Vaayu's part if he accepts the assignment of representation before Income Tax Appellate Tribunal for remuneration of ₹ 1.75 crore.

(b) As per Clause 6 of Part I of the First Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice shall be guilty of professional misconduct if he solicits clients or professional work either directly or indirectly by circular, advertisement, personal communication or interview or by any other means.

Provided that nothing herein contained shall be construed as preventing or prohibiting -

(i) Any Chartered Accountant from applying or requesting for or inviting or securing professional work from another chartered accountant in practice; or

(ii) A member from responding to tenders or enquiries issued by various users of professional services or organisations from time to time and securing professional work as a consequence.

However, as per the Guidelines issued by the Council of the Institute of Chartered Accountants of India, a member of the Institute in practice shall not respond to any tender issued by an organisation or user of professional services in areas of services which are exclusively reserved for chartered accountants, such as audit and attestation services. However, such a restriction shall not be applicable where minimum fee of the assignment is prescribed in the tender document itself or where the areas are open to other professionals along with the Chartered Accountants.

In the given case, Sanjeev & Associates responded to a tender from a PF Office, Chembur for filing quarterly e-TDS returns.

Conclusion: Sanjeev & Associates can respond to the said tender as the tender is open for all the categories i.e. it is open to other professionals along with the Chartered Accountants.