

CA Inter Audit Super Important Questions for Sep 25

Read This Before You Begin -

This list of important questions is curated from a pool of over 700 questions to help you prioritize your revision. It is *not a substitute* for complete syllabus coverage. Questions are selected based on exam trends, frequently tested topics and overall relevance. A few unique questions are included, and don't forget to go through the latest RTPs and MTPs thoroughly

It is not necessary that the questions will come directly from this selection, but they may be based on the concepts covered in it.

Important Note - This list is exclusively for students appearing in Sep 2025 attempt. A separate set of questions will be provided for future attempts.

Checkout Detailed Question Bank Discussion of Chapters 1-4:

<https://youtu.be/4YdYEyLFqCI?si=2zJ6r5a2el6vVor6>

Checkout CA Inter Audit Revision Playlist -

<https://www.youtube.com/playlist?list=PLaGkcEAhgIRuk79GVlc1nGImA-dBh41CZ>

Checkout CA Inter Audit RTPs, MTPs and Exam Paper Analysis Files Links and Discussion Videos -

<https://docs.google.com/document/d/18erqXSSd-9Raj65U0JK92Fp3jL5X2FupN7ZzLMClzYs/edit?usp=sharing>

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Chapter 1 - Nature, Objective and Scope of Audit

Q1.	<p>The person conducting the audit should take care to ensure that financial statements would not mislead anybody. Explain. (MTP1, Nov 2019, 4 Marks) (RTP, May 2020, NA) (MTP1, Nov 2021, 4 marks)</p>
	<p>The person conducting this task should take care to ensure that financial statements would not mislead anybody. This he can do honestly by satisfying himself that:</p> <ol style="list-style-type: none"> 1. the accounts have been drawn up with reference to entries in the books of account; 2. the entries in the books of account are adequately supported by sufficient and appropriate evidence; 3. none of the entries in the books of account has been omitted in the process of compilation and nothing which is not in the books of account has found place in the statements; 4. the information conveyed by the statements is clear and unambiguous; 5. the financial statement amounts are properly classified, described and disclosed in conformity with accounting standards; and 6. the statement of accounts presents a true and fair picture of the operational results and of the assets and liabilities.
Q2.	<p>Good deeds Limited is engaged in the business of recycling of wastes from the dumping grounds of municipal corporation of Indore to usable manure. It is, in this way, also, helping to make the city clean. During the course of audit by Zoha & Zoha, a firm of auditors, it is observed by auditors that the company has received a notice from the Central Bench of National Green Tribunal for not following certain environmental regulations involving imposition of hefty monetary penalty on the company. The company is yet to reply to the notice. The auditors point out that the same is not stated in notes to accounts in financial statements. The company points out that auditors are going beyond scope of their work. Does such a matter fall within scope of audit? (ICAI Study Material- Test Your Understanding)</p>
	<p>Scope of Audit</p> <p>The following points are included in scope of audit of financial statements: -</p> <ol style="list-style-type: none"> 1. Coverage of all aspects of entity : Audit of FSs should be organized adequately to cover all aspects of the entity relevant to the FSs being audited. 2. Reliability and sufficiency of financial information : The auditor should be reasonably satisfied that information contained in underlying accounting records and other source data (like bills, vouchers, documents etc.) is reliable and provide sufficient basis for preparation of financial statements. 3. Proper disclosure of financial information: The auditor must ensure FSs adequately disclose relevant information and comply with statutory requirements, verifying that they accurately summarize recorded transactions and considering management's judgments in their preparation. <p>Conclusion: Proper disclosure of financial information is well within scope of audit.</p>
Q3.	<p>There are practical and legal limitations on the auditor's ability to obtain audit evidence. Explain giving examples. Also explain the difference between audit and investigation. (RTP, Nov 2022, NA)</p>
	<p>The Nature of Audit Procedures: There are practical and legal limitations on the auditor's ability to obtain audit evidence. For example,</p> <ul style="list-style-type: none"> • An auditor does not test all transactions and balances. He forms his opinion only by testing samples. It is an example of practical limitation on auditor's ability to obtain audit evidence. • Management may not provide complete information as requested by auditor. There is no way by which auditor can force management to provide complete information as may be requested by auditor. In case he is not provided with required information, he can only report. It is an example of legal limitation on auditor's ability to obtain audit evidence. • The management may consist of dishonest and unscrupulous people and may be, itself, involved in fraud. It may be engaged in concealing fraud by designing sophisticated and carefully organized schemes which may be hard to detect by the auditor. It may produce fabricated documents before auditor to lead him to believe that audit evidence is valid. However, in reality, such documents could be fake or non-genuine.

	<ul style="list-style-type: none"> It is quite possible that the entity may have entered into some transactions with related parties. Such transactions may be only paper transactions and may not have actually occurred. The auditor may not be aware of such related party relationships or audit procedures may not be able to detect probable wrong doings in such transactions. <p>Difference between audit and investigation</p> <ul style="list-style-type: none"> An audit is not an official investigation into alleged wrongdoing. He does not have any specific legal powers of search or recording statements of witness on oath which may be necessary for carrying out an official investigation. Investigation is a critical examination of the accounts with a special purpose. For example, if fraud is suspected and it is specifically called upon to check the accounts whether fraud really exists, it takes character of investigation. The objective of audit is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion. The scope of audit is general and broad whereas scope of investigation is specific and narrow
Q4.	<p>CA. P Babu is conducting an audit of financial statements of Quick Buy Private Limited. He was not able to obtain external confirmations from certain debtors due to practical difficulties and peculiar circumstances. However, such a procedure is mandated under one of Standards on Auditing. Unable to obtain external confirmations from these debtors, he relied upon sale details to these parties, e-invoices, e-way bills and also traced payments from these parties in bank accounts of the company. He was reasonably satisfied with audit evidence obtained. Is there any other reporting duty cast upon him relating to not following a mandated procedure in one of Standards on Auditing? (ICAI Study Material- Test Your Understanding)</p> <ul style="list-style-type: none"> It is the duty of professional accountants to see that Standards are followed in engagements undertaken by them. Ordinarily, these are to be followed by professional accountants. However, a situation may arise when a specific procedure as required in Standards would be ineffective in a particular engagement. In such a case, professional accountant is required to <ul style="list-style-type: none"> Document how alternative procedures performed achieve the purpose of the required procedure. Reason for departure has to be documented Report should draw attention to such departures <p>Conclusion: Hence, CA. P Babu is required to follow the above procedure.</p>
Q5.	<p>Standards on Auditing (SAs) apply in “audit of historical financial information” whereas Standards on Review Engagements (SREs) apply in “review of historical financial information.” Explain in detail giving examples. (RTP, May 2022, NA) (RTP, May 2024, NA)</p> <p>Standards on auditing apply in “audit” of historical financial information which is a reasonable assurance engagement whereas Standards on Review Engagements apply in “review” of historical financial information which is a limited assurance engagement only.</p> <p>“Historical financial information” means information expressed in financial terms in relation to a particular entity, derived primarily from that entity’s accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.</p> <p>“Audit” and “Review” are two different terms. Audit is a reasonable assurance engagement, and its objective is reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement. However, “review” is a limited assurance engagement, and its objective is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement,</p>

	<p>Standards on Auditing have been issued on wide spectrum of issues in the field of auditing including (but not limited to) overall objectives of independent auditor, audit documentation, planning an audit of financial statements, identifying and assessing risk of material misstatement, audit evidence, audit sampling, going concern and forming an opinion and reporting on financial statements. Some examples of Standards on Auditing are :</p> <ul style="list-style-type: none"> • SA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing • SA 230 Audit Documentation • SA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment • SA 500 Audit Evidence • SA 700 Forming an Opinion and Reporting on Financial Statements <p>Examples of Standards on Review engagements are</p> <ul style="list-style-type: none"> • SRE 2400 (Revised) Engagements to Review Historical Financial Statements • SRE 2410 Review of Interim Financial Information Performed by the Independent Auditor of the Entity
Q6.	<p>RST Ltd., a mid-sized trading company, recently faced challenges in securing a bank loan due to doubts about the reliability of its financial statements. The management realised the importance of having audited accounts to build confidence among lenders and other stakeholders. Elucidate the benefits and need of an audit. (MTP2, Jan 2025, 4 marks)</p> <p>Advantages of audit of Financial statements:</p> <ul style="list-style-type: none"> • Audited accounts provide high quality information. It gives confidence to users that information on which they are relying is qualitative and it is the outcome of an exercise carried out by following Auditing Standards recognized globally. • In case of companies, shareholders may or may not be involved in daily affairs of the company. The FSs are prepared by management consisting of directors. As shareholders are owners of the company, they need an independent mechanism so that financial information is qualitative and reliable. Hence, their interest is safeguarded by an audit. • An audit acts as a moral check on employees from committing frauds for the fear of being discovered by audit. • Audited FSs are helpful to government authorities for determining tax liabilities. • Audited FSs can be relied upon by lenders, bankers for making their credit decisions i.e. whether to lend or not to lend to a particular entity. • An audit may also detect fraud or error or both. • An audit reviews the existence and operations of various controls operating in any entity. Hence, it is useful at pointing out deficiencies.
Q7.	<p>Kriti, a CA student, has joined articles in a reputed audit firm. She considers audit engagement to be an "assurance engagement". Her understanding is that audit engagement is the only kind of assurance engagement in which a practitioner gives a written assurance report in appropriate form. However, her friend Somaya, does not agree with her. She is of the view that assurance engagements are not restricted to audit alone. Besides, Somaya also thinks that assurance engagements can also relate to matters other than historical financial information. Whose view appears to be correct? State with reasons. (RTP, Sep 2024, NA)</p> <ul style="list-style-type: none"> • Audit engagement is an assurance engagement. However, assurance engagements are not restricted to auditing alone. There are other assurance engagements too like review engagements, engagements providing assurance involving prospective financial information, engagements providing assurance on internal controls in an entity. • Assurance engagements provide assurance to users. The difference is of degree. Whereas an audit provides reasonable assurance which is a high level of assurance, review provides lower level of

	<p>assurance as compared to audit.</p> <ul style="list-style-type: none"> There are also assurance engagements which relate to matters other than historical financial information like providing assurance on matters involving prospective financial information and providing assurance on internal controls in an entity. In assurance reports involving prospective financial information, the practitioner obtains sufficient appropriate evidence to the effect that management's assumptions on which the prospective financial information is based are not unreasonable, the prospective financial information is properly prepared on the basis of the assumptions, and it is properly presented, and all material assumptions are adequately disclosed. In the given case, Kriti is of the view that audit engagement is the only kind of assurance engagement in which practitioner gives a written assurance report in appropriate form whereas is Somaya of the view that assurance engagements are not restricted to audit alone. <p>Conclusion: Thus, view of Somaya is correct.</p>
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Chapter 2 - Audit Strategy, Audit Planning and Audit Programme

Q8.	<p>Planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. Adequate planning benefits the audit of financial statements in several ways. Explain clearly those ways. (RTP, Nov 2021, NA) (MTP1, May 2023, 4 marks) (SA, Nov 2018, 5 Marks) (MTP1, Nov 2022, 4 Marks) (RTP, May 2023, NA) (MTP1, May 2024, 4 Marks)</p> <p>Planning an audit involves</p> <ul style="list-style-type: none"> establishing the overall audit strategy for the engagement and developing an audit plan. <p>As per SA 300, "Planning an Audit of Financial Statements", adequate planning benefits the audit of financial statements in several ways, including the following:</p> <ul style="list-style-type: none"> Helping the auditor to devote appropriate attention to important areas of the audit. Helping the auditor identify and resolve potential problems on a timely basis. Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner. Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks, and the proper assignment of work to them. Facilitating the direction and supervision of engagement team members and the review of their work. Assisting, where applicable, in coordination of work done by auditors of components and experts.
Q9.	<p>"Planning is not a discrete phase of an audit, but rather a continual and iterative process." Discuss. (SA, Nov 2018, 5 Marks) (RTP, Nov 2019, NA) (RTP, May 2021, NA) (MTP2, May 2024, 4 Marks) (SA, May 2024, 4 Marks)</p> <p>As per SA 300, "Planning an Audit of Financial Statements", Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement.</p> <p>Planning, however, includes consideration of the timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures. Planning includes the need to consider, prior to the auditor's identification and assessment of the risks of material misstatement, such matters as:</p> <ul style="list-style-type: none"> The analytical procedures to be applied as risk assessment procedures. Obtaining a general understanding of the legal and regulatory framework applicable to the entity and how the entity is complying with that framework. The determination of materiality.

	<ul style="list-style-type: none"> • The involvement of experts. • The performance of other risk assessment procedures.
Q10.	<p>EFG Ltd. has appointed M/s. MN & Co., Chartered Accountants, as the statutory auditors for the year 2024-25. CA N, the engagement partner, completed his risk assessment procedure. However, he is concerned about the management of human resources to be employed to conduct the audit. For this purpose, he wants to establish an overall audit strategy for setting the scope, timing and direction of the audit. Describe how the process of establishment of overall audit strategy will assist him in managing deployment of his human resources for various audit areas. (SA, Sep 2024, 4 marks) (ICAI Study Material- Illustration)(MTP1, May 2018, 5 Marks) (MTP2, Nov 2018, 5 Marks) (RTP, Nov 2018, NA)(SA, May 2019, 4 Marks) (RTP, May 2020, NA)</p> <p>The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. The process of establishing the overall audit strategy assists the auditor to determine, subject to the completion of the auditor's risk assessment procedures, such matters as:</p> <ul style="list-style-type: none"> • The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas or the involvement of experts on complex matters; • The amount of resources to allocate to specific audit areas, such as the number of team members assigned to observe the inventory count at material locations, the extent of review of other auditors' work in the case of group audits, or the audit budget in hours to allocate to high risk areas; • When these resources are to be deployed, such as whether at an interim audit stage or at key cut-off dates; and • How such resources are managed, directed and supervised, such as when team briefing and debriefing meetings are expected to be held, how engagement partner and manager reviews are expected to take place (for example, on-site or off-site), and whether to complete engagement quality control reviews.
Q11.	<p>Lotus Ltd., a rapidly growing manufacturing company, appointed Ridhi & Co., as statutory auditor. The engagement team of Ridhi & Co. identified key areas requiring scrutiny, such as revenue recognition, inventory valuation, and related party transactions. Based on his professional judgment, CA Ravi, the engagement partner, directed the engagement team to focus on these critical areas, emphasising the need for detailed testing to ensure accuracy and compliance. Give some examples of the factors need to be considered by CA Ravi for establishing the audit strategy. (MTP1, Jan 2025, 4 marks) (SA, May 2024, 3 Marks) (MTP2, May 2024, 3 Marks)</p> <p>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 helps auditor in establishing overall audit strategy. More energies need to be devoted to significant matters to obtain desired outcomes. Few examples are listed as under: -</p> <ul style="list-style-type: none"> • Volume of transactions which may determine whether it is more efficient for the auditor to rely on internal control • Significant industry developments such as changes in industry regulations and new reporting requirements. • Significant changes in the financial reporting framework, such as changes in accounting standards. • Other significant relevant developments, such as changes in the legal environment affecting the entity
Q12.	<p>Z Ltd. engaged ABC & Co., Chartered Accountants, to conduct its statutory audit for the F.Y. 2023-24. The audit team developed an overall audit strategy and plan to address the risk. During the audit, several significant changes occurred, including the discovery of a material misstatement in inventory valuation and changes in the scope of audit procedures due to an unexpected acquisition by Z Ltd. The audit documentation for Z Ltd. should reflect these changes but the auditor of a company failed to document the audit strategy and the audit plan. As a senior auditor of the firm briefly outline what should be included in the documentation of audit strategy and audit plan and how should the audit documentation address significant changes made during the audit engagement. (SA, Jan 2025, 5 Marks)</p> <p>The auditor shall document:</p>

	<ul style="list-style-type: none"> the overall audit strategy; the audit plan; and any significant changes made during the audit engagement to the overall audit strategy or the audit plan, and the reasons for such changes. <p>The documentation of the overall audit strategy is a</p> <ul style="list-style-type: none"> record of the key decisions considered necessary to properly plan the audit and to communicate significant matters to the engagement team. <p>The documentation of the audit plan is a</p> <ul style="list-style-type: none"> record of the planned nature, timing and extent of risk assessment procedures and further audit procedures at the assertion level in response to the assessed risks. It also serves as a record of the proper planning of the audit procedures that can be reviewed and approved prior to their performance. The auditor may use standard audit programs and/or audit completion checklists, tailored as needed to reflect the particular engagement circumstances. <p>A record of the significant changes to the overall audit strategy and the audit plan, and resulting changes to the planned nature, timing and extent of audit procedures, explains</p> <ul style="list-style-type: none"> why the significant changes were made, and the overall strategy and audit plan finally adopted for the audit. It also reflects the appropriate response to the significant changes occurring during the audit.
Q13.	<p>XYZ & associates are appointed as the statutory auditors of Fisco Ltd. for the FY 2022 -23. While constructing the audit programme, the engagement partner, CA X, should keep in mind various points. List such points. (RTP, May 2018, NA) (SA, May 2019, 3 Marks)(SA, Nov 2019, 4 Marks) (RTP, Nov 2022, NA)(MTP2, Nov 2022, 4 Marks)</p> <p>For the purpose of programme construction, the following points should be kept in mind:</p> <ul style="list-style-type: none"> Stay within the scope and limitation of the assignment. Prepare a written audit programme setting forth the procedures that are needed to implement the audit plan. Determine the evidence reasonably available and identify the best evidence for deriving the necessary satisfaction. Apply only those steps and procedures which are useful in accomplishing the verification purpose in the specific situation. Include the audit objectives for each area and sufficient details which serve as a set of instructions for the assistants involved in audit and help in controlling the proper execution of the work. Consider all possibilities of error. Co-ordinate the procedures to be applied to related items
Q14.	<p>M/s TP & Co., a firm of Chartered Accountants, is auditor of KSR Ltd. for many 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 or they are required to keep an open mind ? Guide them. (SA, Dec 2021, 4 marks) (MTP2, Sep 2024, 5 marks)</p> <p>In the given situation, 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 assistant to keep an open mind as follows:</p>

- To start with, an auditor having regard to the **nature, size** and **composition** of the business and the dependability of the **internal control** and the given scope of work, should frame a programme which should aim at providing for a **minimum essential work** which may be termed as a standard programme.
- As experience is gained by actually carrying out the work, the programme may be **altered** to take care of situations which were left out originally but are found relevant for the particular concern.
- Similarly, if any work originally provided for proves beyond doubt to be **unnecessary** or irrelevant, it may be **dropped**.
- The assistant engaged in the job should be encouraged to keep an **open mind** beyond the programme given to him. He should be instructed to note and **report significant matters** coming to his notice, to his seniors or to the partners or proprietor of the firm engaged for doing the audit.

Thus, the attitude of assistants of TP & Co. is **not justified**. They should keep an open mind and go beyond the programme to take care of newer areas of the business of KSR Ltd. into which the Company has diversified

- Q15. The assistant of CA K is assigned responsibility of drafting "audit programme" relating to purchases appearing in financial statements of "Broad Industries", a partnership firm. The said firm is a GST registered tax payer and is engaged in manufacturing of packing boxes from a special type of paper taxable under GST. Help him by drafting a sample audit programme for purchases. **(RTP, May 2024, NA) (MTP2, May 2025, 5 Marks)**

Sample audit programme pertaining to purchases:

Name of concern	Broad Industries
Financial year	20XX-XX
Prepared by	Name of person with date
Reviewed by	Name of person with date
Approved by	Name of person with date

S.No	Nature of Procedure	Extent of Check	Basis of sample	Done by
(a)	Vouch few purchase invoices of paper from purchase records of concern			
(b)	Trace these invoices into account books of concern.			
(c)	Verify a few purchase invoices of paper on the GST portal.			
(d)	Trace a few purchase invoices of paper in stock records to ensure that these have been added to stocks of raw material.			

- Q16. CA Tina, the auditor of SKY Ltd., asks its finance and audit head to prepare audit strategy for conducting audit of SKY Ltd. CA Tina also insists him to draw detailed audit procedures. In response to the auditor's request, the finance head of the company completes the audit strategy as well as audit procedures. Subsequently, the auditor realises that the effectiveness of the audit is compromised and it was his responsibility to prepare the overall audit strategy. Comment. **(MTP2, May 2025, 4 Marks)**

- The auditor shall establish an overall audit strategy that sets the **scope, timing and direction of the audit**, and that guides the development of the audit plan. The auditor plans what type of audit procedures are to be performed, their timing and how much work should be done taking into account sample size etc.

- The overall audit strategy and the audit plan remain the **auditor's responsibility**. It is the auditor who is responsible for establishing the overall audit strategy and developing the audit plan. However, auditor **may discuss elements of planning** with the entity's **management without compromising the effectiveness** of audit.
- In the given case, CA Tina, auditor of SKY Ltd. asks its finance and audit head to prepare audit strategy and to draw detailed audit procedures. On the Auditor's request, the finance head completes the audit strategy as well as audit procedures.

In view of above, CA Tina should prepare overall audit strategy and detailed audit procedures. Therefore, **approach of CA Tina was wrong.**

Chapter 3 - Audit Risk and Risk Assessment

- Q17. 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 a 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. (MTP2, Sep 2024, 5 marks)

Misstatement refers to a **difference** between the **amount, classification, presentation, or disclosure** of a **reported** financial statement item and the amount, classification, presentation, or disclosure that is **required** for the item to be in accordance with the applicable financial reporting framework.

In the given situation, there is a difference in amount to be recorded as well as in disclosure of a financial statement item from what is required in accordance with applicable financial reporting framework.

The company should have recorded gross amount of dividend and interest amounting to ₹ 2.00 lakhs and ₹ 3.00 lakhs respectively in its financial statements in accordance with AS 13. Therefore, amount recorded under head "Other income" should have been ₹ 10 lakhs (2 lakhs+3 lakhs+5 lakhs).

Further, in accordance with disclosure requirements of Schedule III of the Companies Act, 2013, other income shall be classified in the above situation as: -

- Interest Income of ₹ 3 lakhs
- Dividend Income of ₹ 2 lakhs
- Net gain on sale of investments of ₹ 5 lakhs

Few examples of misstatements are:

- **Charging** of an item of **capital** expenditure to **revenue** or vice-versa.
- **Difference in disclosure** of a financial statement item vis-à-vis its requirement in the applicable financial reporting framework.
- Selection or application of **inappropriate accounting policies**.
- **Difference** in accounting **estimate** of a financial statement item vis-à-vis its appropriateness in applicable financial reporting framework.
- **Intentional** booking of **fake expenses** in a statement of profit and loss.
- **Overstating** of **receivables** in the financial statements by not writing off irrecoverable debts.
- **Overstating** or **understating inventories**

- Q18. Satranga Foods Private Limited is engaged in manufacturing of pickles. The auditors of the company have

	<p>planned audit procedures in respect of recognition of revenues of the company. Despite that, there is a possibility that misstatements in revenue recognition are not identified by planned audit procedures. Identify and explain that particular risk in detail. (RTP, May 2024, NA)</p> <ul style="list-style-type: none"> There is a possibility that planned audit procedures may not achieve desired result and fail to detect misstatements in revenue recognition. Such a risk is referred to as "detection risk". SA 200 defines detection risk as the risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements. For example, auditor of a company uses certain audit procedures for the purpose of obtaining audit evidence and reducing audit risk, but still there will remain a risk that audit procedures used by the auditor may not be able to detect a misstatement which by nature is material, then that risk is known as detection Risk. Detection risk comprises sampling and non-sampling risk. <ul style="list-style-type: none"> a) Sampling risk is the risk that the auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. It simply means that the sample was not representative of the population from which it was chosen. b) Non-sampling risk is the risk that the auditor reaches an erroneous conclusion for any reason not related to sampling risk. Like an auditor may reach an erroneous conclusion due to application to some inappropriate audit procedure
Q19.	<p>"As part of the risk assessment, the auditor shall determine whether any of the risks identified are, in the auditor's judgment, a significant risk. In exercising judgment as to which risks are significant risks, state the factors which shall be considered by the auditor. Explain the above in context of SA-315." (RTP, May 2018, NA) (RTP, Nov 2021, NA) (MTP1, Nov 2023, 4 marks) (MTP2, Nov 2022, 4 Marks) (SA, May 2023, 3 marks)</p> <p>In exercising judgment as to which risks are significant risks, the auditor shall consider the following-</p> <ul style="list-style-type: none"> Whether the risk is a risk of fraud; Whether the risk is related to recent significant economic, accounting or other developments like changes in regulatory environment etc. and therefore requires specific attention; The complexity of transactions; Whether the risk involves significant transactions with related parties; The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; and Whether the risk involves significant transactions that are outside the normal course of business for the entity or that otherwise appear to be unusual.
Q20.	<p>Auditor or 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 the view of the auditor correct? Specify the other matters due to which the risk of material misstatement is greater for significant non-routine transactions (SA, Dec 2021, 3 Marks) (MTP2, May 2024, 4 Marks) (ICAI Study Material - Test Your Knowledge)</p> <p>Risk of Material Misstatement – Greater for Significant Non-Routine Transactions: Significant risks often relate to significant non- routine transactions or judgmental matters. Non-routine transactions are transactions that are unusual, due to either size or nature, and that therefore occur infrequently.</p> <p>Risks of Material Misstatement– Greater for Significant Non-Routine Transactions Risks of material misstatement may be greater for significant non-routine transactions arising from matters such as the following:</p> <ul style="list-style-type: none"> Greater management intervention to specify the accounting treatment.

	<ul style="list-style-type: none"> • Greater manual intervention for data collection and processing. • Complex calculations or accounting principles. • The nature of non-routine transactions, which may make it difficult for the entity to implement effective controls over the risks. <p>Keeping in view above, view of the Auditor of Sunshine Ltd is correct.</p>
Q21.	<p>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. Analyse and explain giving examples. (RTP, May 2020, NA) (RTP, Nov 2023, NA) (MTP2, May 2024, 4 Marks)</p> <p>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, for example, when:</p> <ul style="list-style-type: none"> • Assessing risks of material misstatement of the financial statements; • Determining materiality in accordance with SA 320; • Considering the appropriateness of the selection and application of accounting policies; • Identifying areas where special audit consideration may be necessary, for example, related party transactions, the appropriateness of management's use of the going concern assumption, or considering the business purpose of transactions; • Developing expectations for use when performing analytical procedures; • Evaluating the sufficiency and appropriateness of audit evidence obtained, such as the appropriateness of assumptions and of management's oral and written representations.
Q22.	<p>The auditor shall identify and assess the risks of material misstatement at both levels to provide a basis for designing and performing further audit procedures. For the purpose of Identifying and assessing the risks of material misstatement the auditor shall Identify risks, assess the identified risks, relate the identified risks and consider the likelihood of misstatement. Explain the above in detail. (MTP2, Nov 2018, 5 Marks) (RTP, Nov 2020, NA)</p> <p style="text-align: center;">OR</p> <p>Discuss the steps to be taken by the auditor for the purpose of Identifying and assessing the risks of material misstatement as per SA 315. (MTP1, Nov 2022, 4 Marks)</p> <p>Identify and assess the risks of material misstatement:</p> <p>The auditor shall identify and assess the risks of material misstatement at:</p> <ul style="list-style-type: none"> • the financial statement level - • the assertion level for classes of transactions, account balances, and disclosures to provide a basis for designing and performing further audit procedures <p>For the purpose of Identifying and assessing the risks of material misstatement, the auditor shall:</p> <ul style="list-style-type: none"> • Identify risks throughout the process of obtaining an understanding of the entity and its environment, including relevant controls that relate to the risks, and by considering the classes of transactions, account balances, and disclosures in the financial statements; • Assess the identified risks, and evaluate whether they relate more pervasively to the financial statements as a whole and potentially affect many assertions; • Relate the identified risks to what can go wrong at the assertion level, taking account of relevant controls that the auditor intends to test; and • Consider the likelihood of misstatement, including the possibility of multiple misstatements, and whether the potential misstatement is of a magnitude that could result in a material misstatement.

Q23.	<p>CA Srishti, while auditing KSM Private Limited for the first time, utilised software to analyse financial data, comparing amounts recorded in the financial statements for the current audit year with the preceding two years. Her objective was to evaluate the risk of material misstatement. Identify the type of audit procedure performed by CA Srishti in the given case, discuss its relevance, and explain whether an auditor's opinion can solely rely on such procedures. (MTP1, Jan 2025, 4 marks)</p>
	<ul style="list-style-type: none"> • In the given case, CA Srishti is performing analytical procedures as risk assessment procedures. • Analytical procedures performed as risk assessment procedures may identify aspects of the entity of which the auditor was unaware and may assist in assessing the risks of material misstatement in order to provide a basis for designing and implementing responses to the assessed risks. Analytical procedures performed as risk assessment procedures may include both financial and non-financial information. • Analytical procedures may help identify the existence of unusual transactions or events, and amounts, ratios, and trends that might indicate matters that have audit implications. Unusual or unexpected relationships that are identified may assist the auditor in identifying risks of material misstatement, especially risks of material misstatement due to fraud. • Risk assessment procedures are a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels Risk assessment procedures by themselves, however, do not provide sufficient appropriate audit evidence on which to base the audit opinion. • Thus, it can be concluded that auditor's opinion cannot be solely based upon such procedures
Q24.	<p>Much of the information obtained by the auditor's inquiries is obtained from management and those responsible for financial reporting. However, the auditor may also obtain information, or a different perspective in identifying risks of material misstatement, through inquiries of others within the entity and other employees with different levels of authority. Explain the same in view of above. (RTP, Nov 2020, NA) (MTP1, May 2025, 5 Marks)</p>
	<p>Inquiries of Management and Others Within the Entity: Much of the information obtained by the auditor's inquiries is obtained from management and those responsible for financial reporting. However, the auditor may also obtain information, or a different perspective in identifying risks of material misstatement, through inquiries of others within the entity and other employees with different levels of authority.</p> <p>Examples</p> <ul style="list-style-type: none"> • Inquiries directed toward internal audit personnel may provide information about internal audit procedures performed during the year relating to the design and effectiveness of the entity's internal control and whether management has satisfactorily responded to findings from those procedures. • Inquiries of employees involved in initiating, processing or recording complex or unusual transactions may help the auditor to evaluate the appropriateness of the selection and application of certain accounting policies. • Inquiries directed toward in-house legal counsel may provide information about such matters as litigation, compliance with laws and regulations, knowledge of fraud or suspected fraud affecting the entity, warranties, post-sales obligations, arrangements (such as joint ventures) with business partners and the meaning of contract. • Inquiries directed towards marketing or sales personnel may provide information about changes in the entity's marketing strategies, sales trends, or contractual arrangements with its customers. • Inquiries directed to the risk management function may provide information about operational and regulatory risks that may affect financial reporting. • Inquiries directed to information systems personnel may provide information about system changes, system or control failures, or other information system- related risks.

Chapter 3A - Internal Control

Q25.	<p>The auditor of XYZ Ltd, engaged in FMCG (Fast Moving Consumable Goods) obtains an understanding of the control environment. As part of obtaining this understanding, the auditor evaluates whether:</p>
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	<p>i) Management has created and maintained a culture of honesty and ethical behavior; and</p> <p>ii) The strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control.</p> <p>Advise what is included in the control environment. Also explain the elements of the control environment. (RTP, May 2018, NA) (MTP1, May 2018, 6 Marks) (MTP1, Nov 2018, 5 Marks) (MTP1, May 2019, 6 Marks) (MTP1, May 2020, 4 Marks) (RTP, Jan 2025, NA) (ICAI Study Material - Test Your Knowledge)</p>
	<p>What is included in the Control Environment?</p> <p>The control environment includes:</p> <ul style="list-style-type: none"> the governance and management functions and the attitudes, awareness, and actions of those charged with governance and management. <p>The control environment sets the tone of an organization, influencing the control consciousness of its people.</p> <p>Elements of the Control Environment:</p> <ol style="list-style-type: none"> Communication and enforcement of integrity and ethical values – These are essential elements that influence the effectiveness of the design, administration and monitoring of controls. Commitment to competence – Matters such as management's consideration of the competence levels for particular jobs and how those levels translate into requisite skills and knowledge. Participation by those charged with governance – It includes attributes of those charged with governance such as their independence from management, their experience and stature, the extent of their involvement and the information they receive and the scrutiny of activities Management's philosophy and operating style – Characteristics such as management's: <ul style="list-style-type: none"> Approach to taking and managing business risks. Attitudes and actions toward financial reporting. Attitudes toward information processing and accounting functions and personnel. Organisational structure – The framework within which an entity's activities for achieving its objectives are planned, executed, controlled, and reviewed. Assignment of authority and responsibility - Matters such as how authority and responsibility for operating activities are assigned and how reporting relationships and authorisation hierarchies are established. Human resource policies and practices – Policies and practices that relate to, for example, recruitment, orientation, training, evaluation, counselling, promotion, compensation, and remedial actions.
Q26.	<p>The auditor obtains an understanding of the information system, including the related business processes, relevant to financial reporting to gain insight of this important component of internal control. What are the specific areas in respect of which auditor gains such understanding? (MTP1, Nov 2023, 4 marks)(RTP, May 2021, NA) (MTP2, May 2022, 4 marks)</p>
	<p>The auditor shall obtain an understanding of the information system, including the related business processes, relevant to financial reporting, including the following are as:</p> <ul style="list-style-type: none"> The classes of transactions in the entity's operations that are significant to the financial statements; The procedures by which those transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements; The related accounting records, supporting information and specific accounts in the financial statements that are used to initiate, record, process and report transactions; How the information system captures events and conditions that are significant to the financial statements; The financial reporting process used to prepare the entity's financial statements; Controls surrounding journal entries.
Q27.	<p>KR & Associates, an auditor of FDP Ltd., observed that the company has implemented various internal controls addressing financial reporting, operational efficiency, and compliances during their preliminary evaluation. CA</p>

	<p>Karan suggests that all controls should be assessed to mitigate the risk of material misstatement in the financial statements, while CA Rajat is of the view that only those controls deemed relevant to the audit should be assessed based on professional judgment.</p> <p>Comment, whether the auditor should assess all the internal controls or limit the assessment to only those considered relevant by the auditor during the audit. Also, discuss the factors influencing the auditor's judgment on the relevance of controls. (MTP1, Jan 2025, 5 marks) (RTP, May 2021, NA) (MTP1, May 2022, 3 marks) (RTP, Nov 2022, NA)</p> <p>There is a direct relationship between an entity's objectives and the controls implemented to provide reasonable assurance about their achievement. The entity's objectives, and therefore controls, relate to financial reporting, operations and compliance; however, not all of these objectives and controls are relevant to the auditor's risk assessment.</p> <p>Factors relevant to the auditor's judgment about whether a control, individually or in combination with others, is relevant to the audit may include such matters as the following:</p> <ul style="list-style-type: none"> • Materiality. • The significance of the related risk. • The size of the entity. • The nature of the entity's business, including its organisation and ownership characteristics. • The diversity and complexity of the entity's operations. • Applicable legal and regulatory requirements. • The circumstances and the applicable component of internal control. • The nature and complexity of the systems that are part of the entity's internal control, including the use of service organisations. • Whether, and how, a specific control, individually or in combination with others, prevents, or detects and corrects, material misstatement. <p>In the given case, CA Karan suggests that all controls should be assessed to mitigate the risk of material misstatement in the financial statements, while CA Rajat is of the view that only those controls deemed relevant to the audit should be assessed based on professional judgment.</p> <p>Conclusion: It can be concluded that the auditors should assess only those controls deemed relevant to mitigate the risk of material misstatement in FDP Ltd.'s financial statements.</p>
Q28.	<p>So far as the auditor is concerned, the examination and evaluation of the internal control system is an indispensable part of the overall audit programme. The auditor needs reasonable assurance that the accounting system is adequate and that all the accounting information which should be recorded has in fact been recorded. Internal control normally contributes to such assurance. Explain stating clearly the benefits of evaluation of internal control to the auditor. (RTP, May 2019, NA) (RTP, Nov 2022, NA)</p> <p>Benefits of Evaluation of Internal Control to the Auditor</p> <p>The review of internal controls will enable the auditor to know:</p> <ul style="list-style-type: none"> • whether errors and frauds are likely to be located in the ordinary course of operations of the business; • whether an adequate internal control system is in use and operating as planned by the management; • whether an effective internal auditing department is operating; • whether any administrative control has a bearing on his work (for example, if the control over worker recruitment and enrolment is weak, there is a likelihood of dummy names being included in the wages sheet and this is relevant for the auditor); • whether the controls adequately safeguard the assets; • how far and how adequately the management is discharging its function in so far as correct recording of transactions is concerned;

	<ul style="list-style-type: none"> • how reliable the reports, records and the certificates to the management can be; • the extent and the depth of the examination that he needs to carry out in the different areas of accounting; • what would be appropriate audit technique and the audit procedure in the given circumstances; • what are the areas where control is weak and where it is excessive; and • whether some worthwhile suggestions can be given to improve the control system.
Q29.	<p>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? (MTP2, Nov 2022, 3 Marks) (MTP1, Sep 2024, 5 Marks)</p> <p>The Entity's Risk Assessment Process– Component of Control Environment</p> <p>The auditor shall obtain an understanding of whether the entity has a process for:</p> <ul style="list-style-type: none"> • Identifying business risks relevant to financial reporting objectives; • Estimating the significance of the risks; • Assessing the likelihood of their occurrence; and • Deciding about actions to address those risks. <p>The entity's risk assessment process forms the basis for the risks to be managed. If that process is appropriate, it would assist the auditor in identifying risks of material misstatement. Risks can arise or change due to factor such as new technology, new business models, products or activities, changes in operating environment etc. Whether the entity's risk assessment process is appropriate to the circumstances is a matter of judgment.</p>

Chapter 3B - Response to the Assessed Risk

Q30.	<p>A higher level of assurance may be sought about the operating effectiveness of controls when the approach adopted consists primarily of tests of controls. Explain and also state when will the auditor design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls. (RTP, Nov 2018, NA) (RTP, Nov 2020, NA)</p> <p style="text-align: center;">OR</p> <p>SA 330 states that auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to operating effectiveness of relevant controls. Briefly discuss when such tests are to be designed and performed in accordance with SA 330? If an auditor intends to place greater reliance on effectiveness of a control, state its likely effect on audit evidence to be obtained as a result of such tests of controls. Why a higher level of assurance may be sought by an auditor about the operating effectiveness of controls? (MTP1, Jan 2025, 5 marks)</p> <p>The auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls when: -</p> <ol style="list-style-type: none"> 1. The auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively (i.e., the auditor intends to rely on the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures) or 2. Substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level. <p>In designing and performing tests of controls, the auditor shall obtain more persuasive audit evidence, the greater the reliance the auditor places on the effectiveness of a control.</p> <p>A higher level of assurance may be sought about the operating effectiveness of controls when the approach adopted consists primarily of tests of controls, in particular, where it is not possible or practicable to obtain sufficient appropriate audit evidence only from substantive procedures.</p>
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Q31.	<p>Discuss the various points which auditor needs to consider in determining whether it is appropriate to use audit evidence about operating effectiveness of controls obtained in previous audit, and if so, the length of the time period that may elapse before retesting. (SA, Nov 2019, 4 Marks) (MTP2, May 2023, 4 marks)</p>
	<p>In determining whether it is appropriate to use audit evidence about the operating effectiveness of controls obtained in previous audits, and, if so, the length of the time period that may elapse before retesting a control, the auditor shall consider the following: <u>(Simple wording - When deciding whether to rely on past audit evidence of control effectiveness and how long to wait before retesting, the auditor must consider)</u></p> <ul style="list-style-type: none"> • The effectiveness of other elements of internal control, including the control environment, the entity's monitoring of controls, and the entity's risk assessment process; • The risks arising from the characteristics of the control, including whether it is manual or automated; • The effectiveness of general IT-controls; • The effectiveness of the control and its application by the entity, including the nature and extent of deviations in the application of the control noted in previous audits, and whether there have been personnel changes that significantly affects the application of the control; • Whether the lack of a change in a particular control poses a risk due to changing circumstances; and • The risks of material misstatement and the extent of reliance on the control
Q32.	<p>When more persuasive audit evidence is needed regarding the effectiveness of a control, it may be appropriate to increase the extent of testing of the control as well as the degree of reliance on controls. <u>Discuss the matters the auditor may consider in determining the extent of test of controls.</u> (RTP, Nov 2020, NA) (MTP2, Jan 2025, 5 marks)</p>
	<p>When more persuasive audit evidence is needed regarding the effectiveness of a control, it may be appropriate to increase the extent of testing of the control as well as the degree of reliance on controls. Matters the auditor may consider in determining the extent of test of controls include the following:</p> <ul style="list-style-type: none"> • The frequency of the performance of the control by the entity during the period. • The length of time during the audit period that the auditor is relying on the operating effectiveness of the control. • The expected rate of deviation from a control. • The relevance and reliability of the audit evidence to be obtained regarding the operating effectiveness of the control at the assertion level. • The extent to which audit evidence is obtained from tests of other controls related to the assertion

Chapter 3C - Materiality

Q33.	<p>CA Y, statutory auditor of a company, is in process of determining materiality for financial statements while planning an audit. Since materiality is a matter of professional judgment and is affected by the 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? (SA, Nov 2023, 4 marks) (RTP, May 2021, NA) (MTP2, Sep 2024, 4 marks)</p>
	<p>The auditor's determination of materiality is a matter of professional judgment, and is affected by the auditor's perception of the financial information needs of users of the financial statements. In this context, it is reasonable for the auditor to assume that users:</p> <ul style="list-style-type: none"> • Have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence; • Understand that financial statements are prepared, presented and audited to levels of materiality; • Recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment and the consideration of future events; and • Make reasonable economic decisions on the basis of the information in the financial statements.

Q34.	<p>Calen Retail Ltd. is preparing its annual financial statements, and the auditors are tasked with determining materiality. The company has used revenue as the benchmark, as it is a key indicator of performance. However, Calen Retail has recently opened new stores and closed underperforming ones, which could significantly affect both revenue and profitability. As per given case, what factors should the auditors consider when selecting the most appropriate benchmark for materiality?</p> <p>(MTP2, Jan 2025, 4 marks) (SA, May 2023, 3 marks) (RTP, May 2022, NA) (SA, Nov 2020, 4 Marks)</p>
	<p>Determining materiality involves the exercise of professional judgment. A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole. Factors that may affect the identification of an appropriate benchmark include the following:</p> <ul style="list-style-type: none"> • The elements of the financial statements. Example - assets, liabilities, equity, revenue, expenses; • Whether there are items on which the attention of the users of the particular entity's financial statements tends to be focused Example - for the purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets. • The nature of the entity, where the entity is at in its life cycle, and the industry and economic environment in which the entity operates; • The entity's ownership structure and the way it is financed and Example- if an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings); • The relative volatility of the benchmark.

Chapter 3D - Automated Environment

Q35.	<p>Understanding the entity and its automated environment involves understanding how IT department is organised, IT activities, the IT dependencies, relevant risks and controls. Explain stating the points that an auditor should consider to obtain an understanding of the company's automated environment.</p> <p>(RTP, May 2018, NA) (MTP1, Nov 2019, 4 marks) (MTP1, Nov 2023, 3 marks) (MTP2, May 2018, 5 Marks) (SA, May 2018, 5 Marks) (RTP, Nov 2019, NA) (MTP1, Nov 2021, 4 marks) (MTP1, May 2022, 4 Marks) (RTP, Nov 2022, NA) (RTP, Nov 2023, NA)</p>
	<p>Understanding and Documenting Automated Environment:</p> <p>In an audit of financial statements, an auditor is required to understand the entity and its business, including IT as per SA 315. Understanding the entity and its automated environment involves understanding how IT department is organised, IT activities, the IT dependencies, relevant risks and controls.</p> <p>Given below are some of the points that an auditor should consider to obtain an understanding of the company's automated environment</p> <ul style="list-style-type: none"> • Information systems being used (one or more application systems and what they are) • their purpose (financial and non-financial) • Location of IT systems - local vs global • Architecture (desktop based, client-server, web application, cloud based) • Version (functions and risks could vary in different versions of same application) • Interfaces within systems (in case multiple systems exist) • In-house vs Packaged • Outsourced activities (IT maintenance and support) • Key persons (CIO, CISO, Administrators) <p>The understanding of a company's IT environment that is obtained should be documented</p>

Q36.	<p>Companies are increasingly using data analytics for managing their operations. Auditors can also obtain good results by using data analytics. What are the tools and techniques used by auditors in applying the principles of Data Analytics and in which areas data analytics can be used by auditors? (RTP, Sep 2024, NA)</p>
	<p>In today's digital age when companies rely more and more on IT systems and networks to operate business, the amount of data and information that exists in these systems is enormous. A famous businessman recently said, "Data is the new Oil".</p> <p>Data analytics is the combination of processes, tools and techniques that are used to tap vast amounts of electronic data to obtain meaningful information. The companies can benefit immensely from the use of data analytics in terms of increased profitability, better customer service, gaining competitive advantage, more efficient operations, etc., even auditors can make use of similar tools and techniques in the audit process and obtain good results.</p> <p>The tools and techniques that auditors use in applying the principles of data analytics are known as Computer Assisted Auditing Techniques (CAATs)</p> <p>Data analytics can be used in testing of electronic records and data residing in IT systems using spreadsheets and specialized audit tools viz., IDEA and ACL to perform the following,</p> <ul style="list-style-type: none"> • check completeness of data and population that is used in either test of controls or substantive audit tests • selection of audit samples – random sampling, systematic sampling • re-computation of balances – reconstruction of trial balance from transaction data • reperformance of mathematical calculations – depreciation, bank interest calculation. • analysis of journal entries as required by SA 240 • fraud investigation • evaluating impact of control deficiencies
Q37.	<p>Having obtained an understanding of the IT systems and the automated environment of a company, the auditor should consider the risks that arise from the use of IT systems. Explain. (SA, May 2018, 5 Marks) (MTP1, Nov 2018, 5 Marks) (RTP, Nov 2019, NA)</p> <p style="text-align: center;">OR</p> <p>Which are specific risks to the company's internal control having IT environment? (SA, May 2019, 4 Marks) (RTP, Nov 2022, NA)</p>
	<p>Having obtained an understanding of the IT systems and the automated environment of a company, the auditor should now understand the risks that arise from the use of IT systems. Given below are some such risks that should be considered,</p> <ul style="list-style-type: none"> • Inaccurate processing of data, processing inaccurate data, or both • Unauthorized access to data • Direct data changes (backend changes) • Excessive access / Privileged access (super users) • Lack of adequate segregation of duties • Unauthorized changes to systems or programs • Failure to make necessary changes to systems or programs • Loss of data
Q38.	<p>Discuss the impact of IT related risks on Substantive Audit, Controls and Reporting (RTP, May 2018, NA)</p> <p style="text-align: center;">OR</p> <p>Describe how risks in the IT system if not mitigated could have an impact on the audit. (SA, Nov 2020, 3 marks) (RTP, Nov 2021, NA) (MTP2, Nov 2021, 3 marks) (MTP1, Nov 2022, 3 Marks) (MTP1, May 2023, 3 marks)</p> <p style="text-align: center;">OR</p>

	<p>IT related risks can have an impact on audit. In what different ways, such risks can have an impact on audit of financial statements? (RTP, May 2024, NA)</p> <p>Impact of IT related risks:</p> <p>Impact on substantive checking The auditor may not be able to rely on the reports, data obtained from systems where such risk exists. This means all forms of data, information or reports that the auditor obtains from the system for the purpose of audit has to be thoroughly tested and corroborated for completeness and accuracy. It could lead to increased substantive checking i.e., detailed checking.</p> <p>Impact on controls It can lead to non-reliance on automated controls, system calculations and accounting procedures built into applications. It may result in additional audit work.</p> <p>Impact on reporting Due to regulatory requirements in respect of internal financial controls in case of companies, it may lead to modification of auditor's report in some instances</p>
Q39.	<p>Foreceful Limited is a company dealing in mobile spare parts and having its showrooms in almost all the states in the country. For FY 2023-24, the company transferred its accounts from manual to computerized system (SAP). PQR & Co., Chartered Accountants have specialization in the system audit and have been appointed as the system auditor. PQR & Co., at the end of the audit concludes that there are certain findings or exceptions in IT environment and IT controls of the company which needs to be assessed and reported. Mention those points of consideration (SA, July 2021, 3 marks) (MTP2, May 2023, 3 marks)</p> <p style="text-align: center;">OR</p> <p>The Auditor of HK Limited completed the audit of the company in an automated environment. Management of the company requested the auditor to give an idea about any exceptions observed in IT environment that need to be assessed. How the auditor should consider this request and report in light of an audit perspective? (SA, May 2022, 3 Marks)</p> <p>At the conclusion of each audit, it is possible that there will be certain findings or exceptions in IT environment and IT controls of the company that need to be assessed and reported to relevant stakeholders including management and those charged with governance viz., Board of directors, Audit committee.</p> <p>Some points to consider are as follows:</p> <ul style="list-style-type: none"> • Are there any weaknesses in IT controls? • What is the impact of these weaknesses on overall audit? • Report deficiencies to management – Internal Controls Memo or Management Letter. • Communicate in writing any significant deficiencies to Those Charged With Governance. <p>The auditor needs to assess each finding or exception to determine impact on the audit and evaluate if the exception results in a deficiency in internal control.</p>
Q40.	<p>You are appointed as the auditor of a company manufacturing paints. The company has a robust system of internal control. Most of the controls in the company are automated and they are working effectively. However, in certain situations, manual elements in internal controls are more suitable. What are the circumstances where manual elements in internal controls may be more suitable? (SA, May 2024, 3 Marks)</p> <p>Manual elements vs automated elements in entity's internal control: Manual elements in internal control may be more suitable in the following circumstances:</p> <ul style="list-style-type: none"> • Where judgment and discretion are required. • Large, unusual or non-recurring transactions. • Circumstances where errors are difficult to define, anticipate or predict.

- In changing circumstances that require a control response **outside** the scope of an existing automated control.
- In monitoring the **effectiveness** of **automated controls**

Chapter 4 - Audit Evidence

SA 500

Q41.	<p>Gap Ltd. possesses some investment for which there is no ready market and to assess its fair market value it hires an expert, the result of which it can use in preparing its financial statement. Being an Auditor of the Company, state the matters which may affect the nature, timing and extent of audit procedure to be adopted by you in the instant case. (Additional Question)</p>
	<p>Matters affecting NTE of Audit procedures in case of information being produced using work of management expert: As per SA 500 "Audit Evidence" if any information is prepared by the entity using the work of management expert and auditor has to consider that information as audit evidence, he is required to evaluate the competence, capability and objectivity of that expert. Matters which may affect nature, timing and extent of audit procedures in such a case are:</p> <ol style="list-style-type: none"> 1. The nature and complexity of the matter to which the management's expert relates. 2. The risks of material misstatement in the matter. 3. The availability of alternative sources of audit evidence. 4. The nature, scope and objectives of the management's expert's work. 5. Whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services. 6. The extent to which management can exercise control or influence over the work of the management's expert. 7. Whether the management's expert is subject to technical performance standards or other professional or industry requirements. 8. The nature and extent of any controls within the entity over the management's expert's work. 9. The auditor's knowledge and experience of the management's expert's field of expertise. 10. The auditor's previous experience of the work of that expert.
Q42.	<p>In the course of audit of SMP Limited for the financial year ended 31st March, 2024 you have observed as an auditor that the company has provided a sum of ₹ 20 Lakhs in the books of account as Gratuity payable to employees based on certificate obtained from an actuary. Give your comments with reference to the Standard on Auditing. (MTP2, Nov 2021, 3 Marks)</p> <p>Certificate from a Management's Expert:</p> <p>In the given case, SMP Limited has provided a sum of ₹ 20 lakh in the books of accounts as gratuity payable on the basis of certificate obtained from an actuary. The liability towards gratuity payable to the employees at the time of cessation of service should be ascertained and provided for in the accounts when the employees are in service, it is an ascertained present liability accruing over the period of service but payable upon cessation of service.</p> <p>The auditor should check the quantification of the gratuity liability. He should ascertain whether the same had been actuarially determined. The auditor should treat the actuary as managements' expert and conduct procedures relevant to checking the opinion of an expert in accordance with SA 500.</p> <p>As per SA 500, "Audit Evidence", when information to be used as audit evidence has been prepared using the work of a management's expert, the auditor shall, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes:</p> <ul style="list-style-type: none"> • Evaluate the competence, capabilities and objectivity of that expert; • Obtain an understanding of the work of that expert; and

	<ul style="list-style-type: none"> Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion.
Q43.	<p>CA Kanika audited books of accounts of Engineering Ltd. for the financial year 2022-2023. The auditor used an audit procedure according to which all the documents and records maintained by the company were checked in detail to obtain audit evidence. Explain the audit procedure used by the auditor. Comment on reliability of audit evidence obtained by performing such an audit procedure in some situations.</p> <p>(RTP, May 2024, NA) (SA, Dec 2021, 3 marks)</p> <p>Audit Procedure:</p> <ul style="list-style-type: none"> Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production. Example of inspection used as a test of controls is inspection of records for evidence of authorisation. Some documents represent direct audit evidence of the existence of an asset, for example, a document constituting a financial instrument such as an inventory or bond. Inspection of such documents may not necessarily provide audit evidence about ownership or value. In addition, inspecting an executed contract may provide audit evidence relevant to the entity's application of accounting policies, such as revenue recognition. Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity's rights and obligations or the valuation of the assets. Inspection of individual inventory items may accompany the observation of inventory counting. In view of above, it can be concluded that CA K used Inspection as an audit procedure
Q44.	<p>Suniti, a CA student, is part of an engagement team conducting an audit of a company TIM Private Limited. According to the audit programme, she is responsible for verifying purchases and PPE items appearing in books of accounts from records/bills of the company. Besides, she has also been entrusted with responsibility to obtain written representation from management regarding carrying out physical verification of inventories during the year. During course of her work, she finds that:</p> <ol style="list-style-type: none"> One purchase bill amounting to ₹ 5.00 lacs pertaining to TIM Industries has been entered in books of TIM Private Limited. The management has refused to provide a written representation relating to physical verification of inventories during the year. She has brought it to the knowledge of the engagement partner who has decided to use lack of such a representation as audit evidence. <p>Discuss whether each of the above constitutes audit evidence. State reasoning for your answer</p> <p>(MTP1, May 2024, 4 Marks)</p> <ul style="list-style-type: none"> Audit evidence comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions. Purchase bill of ₹ 5.00 lacs pertaining to TIM Industries has been entered in books of TIM Private Limited. Therefore, it contradicts management's assertion relating to occurrence of such purchases. Hence, it constitutes audit evidence. Further, the absence of information (for example, management's refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence. In the given case, management has refused to provide a written representation relating to physical verification of inventories during the year. Therefore, absence of information is used by the auditor and it also constitutes audit evidence.
Q45.	<p>Maintaining accounts using accounting software having a feature of recording audit trail can be useful for an auditor. Discuss some of the advantages for such a feature in accounting software for auditors.</p> <p>(ICAI Study Material - Test Your Knowledge)</p> <ul style="list-style-type: none"> An audit trail is a documented flow of a transaction.

	<ul style="list-style-type: none"> It is used to investigate how a source document was translated into an account entry and from there it was inserted into FS of an entity. It is used as audit evidence to establish authentication and integrity of a transaction. Audit trails help in maintaining record of system and user activity. Like, in the case of banks, there is an audit trail keeping track of log-on activity detailing record of log-on attempts and devices used. Audit trails help to enhance internal controls and data security. Audit trails assist in assigning responsibility, reconstructing events, and analyzing issues Audit trails incur costs, both in system expenses and time spent analyzing data. Automated tools can efficiently analyze the large volume of data from audit trails. Audit trails boost auditor confidence by verifying if management's controls work effectively and if authorized personnel performed transactions. They enhance data security, increasing the reliability of audit evidence obtained.
Q46.	<p>The reliability of audit evidence depends on its source, nature, and the circumstances under which it is obtained, including the controls over its preparation and maintenance. Although exceptions may exist, few generalisations can be made about reliability of audit evidence. Considering above, discuss such generalisations that can be made about the reliability of audit evidence. (MTP1, Jan 2025, 5 marks)</p> <p>Reliability of Audit Evidence:</p> <p>SA 500 on "Audit Evidence" provides that the reliability of information to be used as audit evidence, and therefore of the audit evidence itself, is influenced by its source and its nature, circumstances under which it is obtained, including the controls over its preparation and maintenance where relevant. Therefore, generalisations about the reliability of various kinds of audit evidence are subject to important exceptions.</p> <p>While recognising that exceptions may exist, the following generalisations about the reliability of audit evidence may be useful:</p> <ul style="list-style-type: none"> The reliability of audit evidence is increased when it is obtained from independent sources outside the entity. The reliability of audit evidence that is generated internally is increased when the related controls, including those over its preparation and maintenance, imposed by the entity are effective. Audit evidence obtained directly by the auditor (for example, observation of the application of a control) is more reliable than audit evidence obtained indirectly or by inference (for example, inquiry about the application of a control). Audit evidence in documentary form, whether paper, electronic, or other medium, is more reliable than evidence obtained orally (for example, a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed). Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies or facsimiles, or documents that have been filmed, digitized or otherwise transformed into electronic form, the reliability of which may depend on the controls over their preparation and maintenance.
SA 610	
Q47.	<p>Internal audit not only analyses the effectiveness with which the internal control of a company is operating but also improves the effectiveness of internal control. Elucidate the statement. (SA, May 2022, 4 Marks) (RTP, May 2022, NA) (SA, Jan 2021, 3 Marks)</p>

	<p>Objectives and scope of internal audit functions relating to Internal Control are:</p> <ul style="list-style-type: none"> • Evaluation of internal control: The internal audit function may be assigned specific responsibility for reviewing controls, evaluating their operation and recommending improvements thereto. • Examination of financial and operating information: The internal audit function may be assigned to review the means used to identify, recognize, measure, classify and report financial and operating information, and to make specific inquiry into individual items, including detailed testing of transactions, balances and procedures. • Review of operating activities: The internal audit function may be assigned to review the economy, efficiency and effectiveness of operating activities, including non-financial activities of an entity. • Review of compliance with laws and regulations: The internal audit function may be assigned to review compliance with laws, regulations and other external requirements, and with management policies and directives and other internal requirements.
Q48.	<p>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 the company is assessed as area of higher risk by statutory auditor. He wants to take direct assistance from the Chief Internal Auditor in respect of the above matter. Discuss along with reasons whether it would be proper for statutory auditor to: -</p> <ol style="list-style-type: none"> 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? <p>(MTP1, May 2024, 4 Marks)</p> <p>In accordance with SA 610, the external auditor shall not use internal auditors to provide direct assistance to perform procedures that relate to higher assessed risks of material misstatement where the judgement required in performing the relevant audit procedures or evaluating the audit evidence gathered is more than limited.</p> <p>In the given situation,</p> <ul style="list-style-type: none"> • Valuation of trade receivables is assigned as an area of higher risk by statutory auditor. • Judgement required in checking the accuracy of ageing of trade receivables is limited. • Therefore, an external auditor can assign the checking of the accuracy of the ageing to the Chief Internal Auditor providing direct assistance as it involves limited judgement. <p>However, because the evaluation of the adequacy of the provision based on the aging would involve more than limited judgement, it would not be appropriate to assign that latter procedure to Chief Internal Auditor providing direct assistance.</p>
Q49.	<p>CA Mukul is the external auditor of Beige Ltd., a large company, engaged in the manufacturing of fast-moving consumer (FMCG) goods. After assessing the internal audit function of the company, CA Mukul decided to use the internal auditor of the company to provide direct assistance. In this context, what is meant by direct assistance under the relevant Standard on Auditing? Also comment whether prior to using an internal auditor for direct assistance for the purpose of audit, CA Mukul is required to obtain any written agreements or not. Give examples of procedures in which CA Mukul shall not use an internal auditor to provide direct assistance. (RTP, Jan 2025, NA)</p> <p>As per SA 610, "Using the work of Internal Auditor", direct assistance refers to the use of internal auditors to perform audit procedures under the direction, supervision and review of the external auditor.</p> <p>Prior to using internal auditors to provide direct assistance for purposes of the audit, CA Mukul, the external auditor shall: -</p> <ol style="list-style-type: none"> a) Obtain written agreement from an authorized representative of the entity that the internal auditors will be allowed to follow the external auditor's instructions, and that the entity will not intervene in the work the internal auditor performs for the external auditor and

- b) Obtain **written agreement** from the **internal auditors** that they will keep confidential specific matters as instructed by the external auditor and inform the external auditor of any threat to their objectivity.

Examples of procedures in which CA Mukul shall **not use internal auditor** to provide direct assistance to him are: -

- Procedures which involve making **significant judgments** in the audit;
- Procedures relating to **higher assessed risks of material misstatement** where the judgment required in performing the relevant audit procedures or evaluating the audit evidence gathered is more than limited.
- Procedures relating to work with which the **internal auditors** have been **involved** and which has already been, or will be, **reported** to **management** or **TCWG** by the internal audit function; or
- Procedures relating to **decisions** the **external auditor** makes in accordance with this **SA** regarding the internal audit function and the use of its work or direct assistance.

SA 530

- Q50. CA B is appointed as an auditor of M/s. Divine Pharmacy, a wholesale medicine supplier. While auditing for the financial year 2023-24, CA B wants to use a test checking technique. Advise CA B, what kind of precautions should be taken by him in this regard. **(SA, July 2021, 4 Marks) (ICAI Study Material - Test Your Knowledge)**

Precautions to be taken while applying test check techniques are

- Thorough study of the accounting **system** should be done before adopting sampling.
- Proper study of **internal control** systems.
- Areas** which are not **suitable** for **sampling** should be carefully considered. Eg: compliance with statutory provisions, transactions of unusual nature etc.
- Proper **planning** for Sampling methods to be used and explaining the staff,
- Transactions and balances have to be properly **classified** (stratified)
- Sample **size** should be appropriately **determined**.
- Sample should be chosen in **unbiased** way,
- Errors** located in the sample should be analysed properly.

- Q51. CA Shubham, the auditor of Sigma Limited, is performing tests of controls and tests of details using audit sampling. During these procedures, he observed deviations in compliance with management's prescribed procedures for sales transactions of small values of a product at one location during tests of controls. Additionally, misstatements were identified in the sample related to these small-value sales transactions during tests of details. How should he proceed to analyse the nature and cause of the deviations and misstatements observed in the sample results? **(MTP1, Jan 2025, 5 marks)**

In the given case, while performing tests of details on a sample in respect of sales, misstatements have been found by CA Shubham in selected sample pertaining to the sales transactions of small values. This indicates observance of deviations and misstatements while performing tests of controls and tests of details respectively in selected samples.

As per **SA 530, "Audit Sampling"**, in analysing the deviations and misstatements identified, the auditor may observe that many have a common feature, for example, type of transaction, location, product line or period of time.

In such circumstances, the auditor may decide to identify **all items** in the population that possess the common feature, and extend audit procedures to those items. In addition, such deviations or misstatements may be **intentional**, and may indicate the possibility of **fraud**.

Therefore, the auditor shall investigate the **nature** and **causes** of any **deviations** or misstatements identified, and evaluate their **possible effect** on the purpose of the audit procedure and on other areas of the audit.

	<p>In the extremely rare circumstances when the auditor considers a misstatement or deviation discovered in a sample to be an anomaly, the auditor shall obtain a high degree of certainty that such misstatement or deviation is not representative of the population. The auditor shall obtain this degree of certainty by performing additional audit procedures to obtain sufficient appropriate audit evidence that the misstatement or deviation does not affect the remainder of the population.</p>
Q52.	<p>Sampling risk can lead to two types of erroneous conclusions. Explain clearly stating the meaning of sampling risk (RTP, May 2022, NA) (SA, May 2019, 4 Marks) (MTP2, May 2021, 3 Marks) (ICAI Study Material - Test Your Knowledge) (RTP, Nov 2018, NA) (MTP2, May 2019, 3 Marks) (RTP, May 2023, NA)</p> <p>Risk Factors while applying Sampling Techniques:</p> <p>As per SA 530 "Audit Sampling", sampling risk is the risk that the auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. Sampling risk can lead to two types of erroneous conclusions-</p> <ol style="list-style-type: none"> In the case of a test of controls, that controls are more effective than they actually are, or in the case of tests of details, that a material misstatement does not exist when in fact it does. The auditor is primarily concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion. In the case of test of controls, the controls are less effective than they actually are, or in the case of tests of details, that a material misstatement exists when in fact it does not. This type of erroneous conclusion affects audit efficiency as it would usually lead to additional work to establish that initial conclusions were incorrect
Q53.	<p>The level of sampling risk that the auditor is willing to accept affects the sample size required. The lower the risk the auditor is willing to accept, the greater the sample size will need to be. <u>Explain Stating the examples of factors that the auditor may consider when determining the sample size for tests of controls.</u> (MTP1, May 2018, 5 Marks)</p> <p style="text-align: center;">OR</p> <p>The sample size can be determined by the application of a statistically-based formula or through the exercise of professional judgment. When circumstances are similar, the effect on sample size of factors will be similar regardless of whether a statistical or non-statistical approach is chosen. Explain Stating the examples of factors (any four) that the auditor may consider when determining the sample size for tests of controls. (MTP2, Nov 2018, 5 Marks) (MTP1, May 2019, 4 Marks) (MTP1, May 2020, 3 Marks)</p> <p>Factors to be considered while determining the sample size for tests of controls:</p> <p>The level of sampling risk that the auditor is willing to accept affects the sample size required. The lower the risk the auditor is willing to accept, the greater the sample size will need to be. The sample size can be determined by the application of a statistically-based formula or through the exercise of professional judgment. When circumstances are similar, the effect on sample size of factors will be similar regardless of whether a statistical or non-statistical approach is chosen.</p> <p>Examples of Factors Influencing Sample Size for Tests of Controls:</p> <ul style="list-style-type: none"> RELIANCE - An increase in the extent to which the auditor's risk assessment takes into account relevant controls will increase the sample size. (Higher the reliance auditor is placed on the IC, the greater the sample size.) TROD - An increase in the tolerable rate of deviation, will decrease the sample size. EROD - An increase in the expected rate of deviation of the population to be tested, will increase the sample size. Assurance - An increase in the auditor's desired level of assurance that the tolerable rate of deviation is not exceeded by the actual rate of deviation in the population will increase the sample size.
Q54.	<p>The approach to audit and extent of checking are undergoing a progressive change in favour of more attention</p>

towards the questions of principle and controls with a curtailment of non-consequential routine checking. Discuss the given statement. (SA, May 2022, 3 Marks)

- No conscious effort in human society is divested of economic considerations and auditing is no exception. There is a growing realisation that the traditional approach to audit is economically wasteful because all the efforts are directed to check all transactions without any exception. This invariably leads to more emphasis on routine checking, which often is not necessary in view of the **time** and the **cost** involved.
- With the shift in favour of **formal internal controls** in the management of affairs of organisations, the possibilities of routine errors and frauds have greatly **diminished**. Thus, the auditors often find extensive routine checking as **nothing more than a ritual** because it **seldom reveals anything material**. Now the approach to audit and the extent of checking are undergoing a progressive change in favour of more attention towards the **questions of principles** and **controls** with a curtailment of non-consequential routine checking.
- By routine checking, we traditionally think of **extensive checking** and **vouching** of all the entries, **disregarding** the concept of **materiality**. The extent of the checking to be undertaken is primarily a matter of **judgment** of the auditor. There is **nothing statutorily stated** anywhere which specifies **what** work is to be done, **how** it is to be done and to what **extent** it has to be done.
- It is also **not obligatory** that the auditor must adopt the **sampling** technique. What he is to do as an auditor is to **express** his **opinion** on the financial statements and become bound by that.
- To ensure good and reasonable standard of work, he **should adopt standards** and techniques that can lead him to an **informed professional opinion**. This enables the auditor to make conclusions and express fair opinion without having to check all of the items within the financial statements.

Q55. 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 the auditor for selecting samples in such a manner? Additionally, a 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 a partner of CA Z? (MTP2, Sep 2024, 5 marks)

- In the given case, the method of sampling being used in software is known as **interval sampling or systematic sampling**. It is a selection method in which the number of sampling units in the population is divided by the sample size to give a sampling interval.
- Sampling interval = Sampling units in population / Sample size i.e 1000/100
 - **Sampling interval = 10**
 - **Records selected = 100**
 - Software would pick every 10th record from 1 to 1000 records.
- When using this method, the auditor would need to determine that sampling units within the population are not structured in such a way that the sampling interval corresponds with a particular pattern in the population.
- Further, a partner of CA Z suggested him to select the first 200 sales invoices from the sales book for the last month. He is suggesting him **block sampling** for sales, this method involves selection of a block(s) of contiguous items from within the population.

SA 501

Q56.	<p>ABC Ltd is engaged in manufacturing different types of yarns. On going through its financial statements for the past years, it is observed that inventory is material to the financial statements. You as an auditor of the company wanted to obtain sufficient appropriate audit evidence regarding the existence and condition of the inventory as appearing in the financial statements. Discuss, how would you proceed as an auditor.</p> <p>(MTP1, May 2018, 5 Marks) (MTP1, Nov 2018, 5 Marks) (MTP2, Nov 2018, 5 Marks) (MTP1, May 2019, 4 Marks) (MTP1, May 2020, 4 Marks)</p>
	<p>When inventory is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of inventory by:</p> <ul style="list-style-type: none"> • Attendance at physical inventory counting, unless impracticable, to: <ul style="list-style-type: none"> ○ Evaluate management's instructions and procedures for recording and controlling the results of the entity's physical inventory counting; ○ Observe the performance of management's count procedures; ○ Inspect the inventory; and ○ Perform test counts; and • Performing audit procedures over the entity's final inventory records to determine whether they accurately reflect actual inventory count results.
Q57.	<p>Wire Limited, a company engaged in manufacturing of electric equipment, gets some part of its production processes outsourced from third parties. During the audit, the company had sent raw material to third parties for carrying out certain processes on these raw materials and such inventories worth Rs. 1.50 crores (material to financial statements) were lying with different third parties as at year end. How can auditor obtain sufficient appropriate audit evidence in respect of existence and condition of inventories lying with third parties? (MTP2, May 2025, 4 Marks) (RTP, Sep 2024, NA)</p>
	<p>In accordance with requirements of SA 501, "Audit Evidence- Specific Considerations for Selected Items", when inventory under the custody and control of a third party is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of that inventory by performing one or both of the following</p> <ol style="list-style-type: none"> a) Request confirmation from the third party as to the quantities and condition of inventory held on behalf of the entity. b) Perform inspection or other audit procedures appropriate in the circumstances. <p>Other audit procedure may include –</p> <ul style="list-style-type: none"> • Inspecting documentation regarding inventory held by third parties • Requesting confirmation from other parties when inventory has been pledged as collateral. • Attending, or arranging for another auditor to attend, the third party's physical counting of inventory, if practicable. • Obtaining another auditor's report, or a service auditor's report, on the adequacy of the third party's internal control for ensuring that inventory is properly counted and adequately safeguarded.
Q58.	<p>CA Kavita, auditor of Healthify Ltd., while assessing potential risks of material misstatement related to litigations at Healthify Ltd., identified a possible legal claim that could affect the financial statements. She sent a general inquiry letter to the company's external legal counsel, Mohit & Co., seeking clarification. However, Mohit & Co. informed her that their professional rules prohibited them from responding to these general inquiries. Guide CA Kavita that what other option is available to obtain the necessary information for the audit? (MTP2, Jan 2025, 5 marks)</p>
	<p>If the auditor assesses a risk of material misstatement regarding litigation or claims that have been identified, or when audit procedures performed indicate that other material litigation or claims may exist, the auditor shall, in addition to the procedures required by other SAs, seek direct communication with the entity's external legal counsel. The auditor shall do so through a letter of inquiry requesting the entity's external legal counsel to</p>

	<p>communicate directly with the auditor.</p> <p>If law, regulation or the respective legal professional body prohibits the entity's external legal counsel from communicating directly with the auditor, the auditor shall perform alternative audit procedures.</p> <p>If it is considered unlikely that the entity's external legal counsel will respond appropriately to a letter of general inquiry, for example if the professional body to which the external legal counsel belongs prohibits response to such a letter, the auditor may seek direct communication through a letter of specific inquiry. For this purpose, a letter of specific inquiry includes:</p> <ol style="list-style-type: none"> A list of litigation and claims; Where available, management's assessment of the outcome of each of the identified litigation and claims and its estimate of the financial implications, including costs involved; and A request that the entity's external legal counsel confirm the reasonableness of management's assessments and provide the auditor with further information if the list is considered by the entity's external legal counsel to be incomplete or incorrect.
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SA 505

Q59.	<p>CA Rishi is appointed as an auditor of AIR Ltd. for the financial year ending on March 31, 2024. During the audit, he observed that the company's books of accounts reflect a significant number of trade payables and receivables as on the balance sheet date. To verify the accuracy of the trade receivables, CA Rishi decided to send confirmation requests to some of trade receivables. However, the management refused to permit him to send these confirmation requests to the selected parties. How should the auditor proceed in the given situation? (MTP2, Jan 2025, 5 marks) (SA, May 2023, 4 marks) (ICAI Study Material - Illustration) (SA, Nov 2020, 4 Marks)</p>
	<p>As per SA 505, "External Confirmation", if the management refuses to allow the auditor to send a confirmation request, the auditor shall</p> <ul style="list-style-type: none"> Inquire as to management's reasons for the refusal and seek audit evidence as to their validity and reasonableness. Evaluate the implications of management's refusal on the auditor's assessment of the relevant risks of material misstatement, including the risk of fraud, and on the nature, timing and extent of other audit procedures; and Perform alternative audit procedures designed to obtain relevant and reliable evidence. <p>If the auditor concludes that management's refusal to allow the auditor to send a confirmation request is unreasonable, or the auditor is unable to obtain relevant and reliable audit evidence from alternative audit procedures,</p> <ul style="list-style-type: none"> the auditor shall communicate with those charged with governance in accordance with SA 260. The auditor shall also determine the implication for the audit and the auditor's opinion in accordance with SA 705.
Q60.	<p>CA T, the statutory auditor of a company, is in the process of designing external confirmation requests to be sent to trade receivables outstanding as of March 31, 2025. As properly designed confirmation requests are essential to ensure the reliability and effectiveness of the audit evidence obtained. Further, well-structured requests help in reducing the risk of misstatements, nonresponses, or misunderstandings by the recipients. In this context, explain why designing a proper confirmation request is necessary and discuss the key factors an auditor should consider when designing confirmation requests. (MTP1, May 2025, 5 Marks)</p>
	<p>The design of a confirmation request may directly affect the confirmation response rate, and the reliability and the nature of the audit evidence obtained from responses. Therefore, designing a proper confirmation request by an auditor is necessary. Factors to be considered when designing confirmation requests include:</p> <ul style="list-style-type: none"> The assertions being addressed.

- Specific identified **risks** of material misstatement, including fraud risks.
- The **layout** and **presentation** of the confirmation request.
- **Prior experience** on the audit or similar engagements.
- The **method** of communication [for example, in paper form, or by electronic mode (like e-mail) or other medium].
- Management's **authorisation** or encouragement to the confirming parties to respond to the auditor. Confirming parties may only be willing to respond to a confirmation request containing management's authorisation.
- The **ability** of the **intended** confirming **party** to **confirm** or provide the requested information (for example, individual invoice amount versus total balance).

SA 510

- Q61. The newly appointed auditor of BTN Limited wants to obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements. What audit procedures should he perform for this purpose? (SA, May 2022, 3 Marks) (MTP2, May 2023, 3 marks) (RTP, May 2024, NA)
- The newly appointed auditor of BTN Ltd shall **read** the most recent financial statements, if any, and the predecessor auditor's report thereon, if any, for information relevant to opening balances, including disclosures. The auditor of BTN Ltd shall obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements by:
- Determining whether the **prior period's closing balances** have been **correctly brought forward** to the current period or, when appropriate, any **adjustments** have been **disclosed** as prior period items in the current year's Statement of Profit and Loss;
 - Determining whether the **opening balances** reflect the **application** of **appropriate accounting policies**; and
 - Performing one or more of the following:
 - Where the prior year financial statements were audited, **perusing** the copies of the audited financial statements including the other relevant documents relating to the prior period financial statements;
 - Evaluating whether audit procedures performed in the current period provide evidence relevant to the opening balances; or
 - Performing specific audit procedures to obtain evidence regarding the opening balances
- Q62. 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 the auditor may obtain sufficient appropriate audit evidence. Discuss those additional audit procedures. (MTP2, May 2024, 3 Marks)
- 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, additional audit procedures may be necessary, and one or more of the following may provide sufficient appropriate audit evidence:
- Observing a **current physical inventory count** and reconciling it to the opening inventory quantities.
 - Performing audit procedures on the **valuation** of the **opening inventory** items.
 - Performing audit procedures on **gross profit** and **cut-off**.

SA 550

- Q63. 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. (MTP1, Sep 2024, 5 Marks) (MTP2, Nov 2023, 4 marks) (RTP, Nov 2021, NA) (MTP2, May 2025, 5 Marks) (ICAI Study Material -

	Illustration)
	<p>During the audit, the auditor should maintain alertness for related party information while reviewing records and documents. He may inspect the following records or documents that may provide information about related party relationships and transactions, for example:</p> <ol style="list-style-type: none"> 1. Entity income tax returns. 2. Information supplied by the entity to regulatory authorities. 3. Documents associated with the entity's filings with a securities regulator e.g, prospectuses) 4. Statements of conflicts of interest from management and those charged with governance. 5. Contracts and agreements with key management or those charged with governance. 6. Significant contracts and agreements not in the entity's ordinary course of business. 7. Significant contracts re-negotiated by the entity during the period. 8. Specific invoices and correspondence from the entity's professional advisors. 9. Internal auditors' reports. 10. Shareholder registers to identify the entity's principal shareholders. 11. Life insurance policies acquired by the entity. 12. Records of the entity's investments and those of its pension plans.

SA 520

Q64.	<p>While conducting the audit of PDP Ltd. for the financial year 2022-23, the statutory auditor identified certain inconsistencies while applying analytical procedures to the financial and non-financial data of PDP Ltd. Can statutory auditor investigate results of Analytical Procedures duly performed in accordance with SA 520 ? Discuss. (SA, Nov 2023, 3 marks) (SA, July 2021, 3 Marks) (RTP, May 2019, NA) (RTP, May 2022, NA) (RTP, May 2023, NA) (MTP2, Nov 2023, 3 marks) (MTP2, May 2018, 5 marks) (ICAI Study Material - Test Your Knowledge)</p>
	<p>As per SA 520 "Analytical Procedures" If while applying analytical procedures in accordance with SA 520, the statutory auditor identifies fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount, the auditor shall investigate such differences by:</p> <ol style="list-style-type: none"> i) Inquiring of management and obtaining appropriate audit evidence relevant to management's responses: Audit evidence relevant to management's responses may be obtained by evaluating those responses taking into account the auditor's understanding of the entity and its environment, and with other audit evidence obtained during the course of the audit. ii) Performing other audit procedures as necessary in the circumstances: The need to perform other audit procedures may arise when, for example, management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate. <p>In the present case, the auditor identifies certain inconsistencies while applying analytical procedures to the financial and non financial data of the company. The auditor should inquire the management of the company and obtain sufficient and appropriate audit evidence relevant to management response. Further, the auditor should also perform other audit procedures if required in the circumstances of the case to obtain further sufficient and appropriate audit evidence.</p>
Q65.	<p>Tree Limited presented its financial statements for the F.Y. 2022-2023 to its auditor for expressing an opinion thereon. The auditor while carrying out the audit started comparing various items of profit and loss account of the year under audit with previous financial years. What is auditor trying to achieve by carrying out those comparisons? (SA, May 2022, 4 Marks) (RTP, Nov 2023, NA)</p> <p>Purpose of Applying Analytical Procedure: Analytical procedures use comparisons and relationships to assess whether account balances or other data appear reasonable. The auditor of Tree Ltd. would achieve the</p>

	<p>following by carrying out the comparison stated in the question:</p> <ul style="list-style-type: none"> • If balances included in the Statement of Profit and Loss of an entity are compared with those contained in the Statement of Profit and Loss with that of the previous period, it would be possible to find out the reasons for increase or decrease in the amount of profits of those years. • By setting up certain expenses' ratios on the basis of balances included in the Statement of Profit and Loss, for the year under audit, comparing them with the same ratios for the previous year, it is possible to ascertain the extent of increase or decrease in various items of expenditure in relation to sales and that of trading profit in relation to sales. • If differences are found to be material, the auditor would ascertain the reasons thereof and assess whether the accounts have been manipulated to inflate or suppress profits. • It would be possible to identify the existence of unusual transactions, amounts, ratios and trends that might indicate matters that have audit implications.
Q66.	<p>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: -</p> <ol style="list-style-type: none"> For testing relationship between sales and cost of sales For testing rights over certain assets forming part of account balances <p>Comment upon his approach along with reasons (MTP2, Sep 2024, 4 marks)</p> <ul style="list-style-type: none"> • Substantive analytical procedures are more appropriate when an account balance or relationships between items of data are predictable. A predictable relationship is one that may reasonably be expected to exist and continue over time. In the given case CA M, auditor of a company, has planned to use substantive analytical procedures for testing the relationship between sales and cost of sales. Hence, the auditor's approach is appropriate in this case. • Using substantive analytical procedures is also affected by nature of assertion. Substantive analytical procedures may be more effective in providing evidence for some assertions (e.g., completeness or valuation) than for others (e.g., rights and obligations). In the given case, CA M has planned to use substantive analytical procedures for testing rights over certain assets forming part of account balances. Such procedures are likely to be less effective in this case.
Q67.	<p>What are the factors that determine the extent of reliance that the auditor places on results of analytical procedures? Explain with reference to SA 520 on "Analytical procedures". (ICAI Study Material - Test Your Knowledge)</p> <p style="text-align: center;">OR</p> <p>CA A, auditor of ABC Ltd. wants to design substantive analytical procedure and for that he wants to check whether the data is reliable or not. Mention the relevant points which he has to consider whether data is reliable for purpose of designing the substantive analytical procedures. (SA, Nov 2019, 3 Marks) (RTP, Nov 2022, NA) (MTP1, May 2018, 5 marks) (MTP2, Nov 2018, 5 marks) (SA, May 2023, 3 marks)</p> <p>The reliability of data is influenced by its source and nature and is dependent on the circumstances under which it is obtained. Accordingly, the following are the relevant points while determining whether data is reliable for purposes of designing substantive analytical procedures:</p> <ul style="list-style-type: none"> • Source of the information available. For example, information may be more reliable when it is obtained from independent sources outside the entity. • Comparability of the information available. For example, broad industry data may need to be supplemented to be comparable to that of an entity that produces and sells specialized products. • Nature and relevance of the information available. For example, whether budgets have been established as results to be expected rather than as goals to be achieved. • Controls over the preparation of the information that are designed to ensure its completeness, accuracy and validity. For example, controls over the preparation, review and maintenance of budgets.

Chapter 5 - Audit of Items of Financial Statements

Q68.	<p>Identify and explain the assertions that the auditor will check by performing the following audit procedures-</p> <ol style="list-style-type: none"> 1. Inventory recognised in the balance sheet actually existed as at the period end. 2. All the items of inventory pertaining to the relevant year shall be included regardless of the location. 3. All goods dispatched prior to the period/ year-end have been invoiced and included in debtors on a test check basis. 4. Examine client correspondence, sales and receivables records, purchase documents. 5. Verifying that the entity has charged depreciation on all items of PPE unless any item of PPE is non-depreciable like freehold land. <p>(MTP2, May 2025, 5 Marks)</p>
	<ol style="list-style-type: none"> 1. The auditor will check the <u>Existence Assertion</u> to ensure Assets, liabilities and equity balances exist as at the period end. 2. The auditor will check the <u>Cut-off assertion</u> to ensure that all assets and liabilities are reported in the appropriate period. 3. The auditor will check <u>Completeness Assertion</u> to ensure all Trade receivable balances that were supposed to be recorded have been recognized in the financial statements. 4. The auditor will check <u>Rights & Obligations</u> assertion to ensure that the entity has valid legal ownership rights over the inventories claimed to be held by the entity and recorded in the financial statements. 5. The auditor will check <u>Valuation assertion</u> to ensure PPE have been valued appropriately and as per generally accepted accounting policies and practices
Q69.	<p>While conducting audit of Air Space Ltd, the auditor observes that it has issued shares at discount to its creditors when its debt is converted into shares in pursuance of debt restructuring scheme in accordance with any guidelines specified by the Reserve Bank of India. Discuss clearly the provisions relating to discount on issue of shares and its verification by the auditor. (RTP, May 2022, NA) (MTP1, May 2022, 3 marks)</p> <p style="text-align: center;">OR</p> <p>Management of D Ltd. has issued shares at a discount to its creditors. Explain the provisions of the Companies Act, 2013 when shares are issued at a discount to creditors ? As an auditor what will be your concern of checking in such a case ? (SA, May 2023, 4 marks)</p>
	<p>Shares issued at a discount:</p> <ul style="list-style-type: none"> • According to Section 53 of the Companies Act, 2013, company shall not issue shares at a discount, except in the case of an issue of sweat equity shares given under Section 54 of the Companies Act, 2013. • Any share issued by a company at a discounted price shall be void. • However, a company may issue shares at a discount to its creditors when its debt is converted into shares in pursuance of any statutory resolution plan or debt restructuring scheme in accordance with any guidelines or directions or regulations specified by the RBI under the Reserve Bank of India Act, 1934 or the Banking (Regulation) Act, 1949. • Where any company fails to comply with the provisions of this section, such company and every officer who is in default shall be liable to a penalty which may extend to an amount equal to the amount raised through the issue of shares at a discount or ₹ 5 lakhs whichever is less, and the company shall also be liable to refund all monies received with interest at the rate of 12% p.a. from the date of issue of such shares to the persons to whom such shares have been issued. <p>The auditor needs to check</p> <ul style="list-style-type: none"> • the movement in share capital during the year and wherever there is any issue, • Verify that Company has not issued any of its shares at a discount by reading the minutes of meeting of its directors and shareholders • Verify that whether the company has issued shares at a discount to its creditors when its debt is converted into shares in pursuance of any statutory resolution plan or debt restructuring scheme in accordance with any guidelines or directions or regulations specified by RBI under RBI Act, 1934 or the

	Banking (Regulation) Act, 1949.
Q70.	<p>The securities premium account may only be applied by the company towards the issue of unissued shares of the company to the members of the company as fully paid bonus shares. Comment. (SA, May 2019, 3 Marks) (MTP2, Nov 2022, 4 Marks)</p> <p>Shares Issued at Premium: Where a company issues shares at a premium, whether for cash or otherwise, aggregate amount of the premium received on those shares shall be transferred to securities premium account.</p> <p>As per Section 52 of the Companies Act, 2013, the securities premium account may be applied by the company for the following purposes:</p> <ol style="list-style-type: none"> issue of unissued shares of the company to the members of the company as fully paid bonus shares; in writing off the preliminary expenses of the Company; in writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company; in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company; or for the purchase of its own shares or other securities under section 68. <p>The auditor needs to verify whether the premium received on shares, if any, has been transferred to a "securities premium account" and whether the application of any amount out of the said "securities premium account" is only for the purposes mentioned above.</p>
Q71.	<p>BNP Ltd has reduced its Share Capital to a greater extent in the year for which you are conducting the audit. State how will you proceed for verifying the reduction of Capital. (MTP1, Nov 2020, 6 Marks)</p> <p>Reduction of Capital: For verifying reduction of capital, the auditor needs to undertake the following procedures:</p> <ul style="list-style-type: none"> Confirm that the shareholders' meeting, which was held to pass the special resolution, was duly convened and that the proposal was circularised in advance to all the shareholders; Check that the Articles of Association authorises reduction of capital; Evaluate that there has been no default w.r.t repayment of deposits accepted by company or payment of interest on such deposits. Reduction of capital shall not be affected if such default exists. Examine the order of the Tribunal confirming the reduction and ensure that a copy of the order and the minutes have been registered and filed with the ROC. Check the Registrar's Certificate as regards to reduction of capital; Vouch the accounting entries recorded to reduce the capital and to write down the assets by reference to the resolution of shareholders and other documentary evidence; Check whether the requirements of Schedule III wrt reduced capital have been complied with. Confirm whether the revaluation of assets has been properly disclosed in the Balance Sheet; Verify the adjustment made in the members' accounts in the Register of Members and confirm that either the paid-up amount shown on the old share certificates has been altered or new certificates have been issued in lieu of the old, and the old ones have been cancelled; Confirm that the words "and reduced", if required by the order of the Tribunal, have been added to the name of the company in the Balance Sheet. Check if the company has complied with all the terms and conditions imposed by the tribunal while confirming reduction of share capital. Verify that the Memorandum of Association of the company has been suitably amended.
Q72.	<p>Droma Shoes Private Limited was established in year 2022-23 for manufacturing of footwear. As funds were needed to carry on its business activities - including for purchase of different raw materials, incurring of regular expenses like power and fuel and payment of wages etc., it had got sanctioned a credit facility amounting to ₹ 2 crores repayable on demand from a bank against primary security of its current assets and collateral security of residential house of one of its directors. Duly signed guarantee documents by directors in favour of bank also form part of bank's loan documentation. Account statement of above facility downloaded from bank's website</p>

	<p>shows debit balance of ₹ 1.85 crores as on 31st March, 2023. The operations in above credit facility are satisfactory. In this regard: -</p> <ol style="list-style-type: none"> Identify the nomenclature of such credit facility given by banks. How would above amount of ₹ 1.85 crores be reflected and classified in financial statements of company as on 31.3.23? Also state specific disclosure requirements of Schedule III of Companies Act, 2013 in relation to above (RTP, May 2024, NA)
	<ol style="list-style-type: none"> The type of credit facilities referred to in above situation given by banks to meet working capital requirements of business which are repayable on demand are known as "cash credit facilities/overdraft" facilities. The amount of ₹ 1.85 crores outstanding as on 31st March, 2023 reflects borrowings of the company and it would be classified as "short-term borrowings" as loans repayable on demand from banks under current liabilities in balance sheet of the company. Borrowings shall further be subclassified as secured Specific disclosure requirements of short-term borrowings under Schedule III to Companies Act, 2013 in given situation are as under: - <ul style="list-style-type: none"> Nature of security i.e. primary security of current assets and collateral security of residential house belonging to a director shall be specified. As loans have been guaranteed by directors, the aggregate amount of such loans shall be disclosed. <p>To be disclosed as Additional Regulatory Information</p> <p>Since the Company has borrowings from bank on the basis of security of current assets, it shall also disclose the following: -</p> <ul style="list-style-type: none"> whether quarterly returns or statements of current assets filed by the Company with banks or financial institutions are in agreement with the books of accounts. if not, summary of reconciliation and reasons of material discrepancies, if any to be adequately disclosed.
Q73.	<p>While auditing books of accounts of SOLAR Ltd., you observed that an amount due from a debtor for invoice issued on 31.03.2024 has not been recognized in the books of accounts. As an auditor, you want to ensure that all trade receivable balances that are supposed to be recorded have been recognized in the financial statements. How will you achieve the stated objective? (SA, Nov 2022, 3 marks)</p>
	<p>Completeness assertion in respect of account balances means that all balances which should have been recorded have been recorded. The auditor needs to satisfy himself about cut off so that there is no understatement or overstatement in account balances of export receivables.</p> <p>In this context, while verifying completeness assertion of export trade receivables, following audit procedures are required: -</p> <ol style="list-style-type: none"> Check that in respect of invoices raised in last few days nearing the cut off date, goods have been actually dispatched and not lying with the company. Check stock records, e-way bill, and transporter receipt regarding actual movement of goods. It would provide assurance that export invoices in respect of which revenue was booked have been actually moved out of company's premises. Ensure that all goods invoiced prior to cut off date/year end have been included in export receivables on test check basis. Ensure that no goods dispatched after year end have been included in export receivables by tracing entries in export sales, stock records of next year. The same can be verified from e-way bills also. Match invoices to dispatch/shipping details. Further match invoices dates to dispatch dates to see if sales are being recorded in correct accounting period. Test invoices in a receivable report. Select invoices from ageing report of export receivables and compare them with supporting documentation to ensure that these are billed with correct names, dates and amounts.
Q74.	<p>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</p>

	<p>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? (MTP1, Sep 2024, 4 Marks)</p> <p>CA D should ensure that BRS is signed by the authorized personnel so that he is able to assign responsibility in case of any errors. Verification of BRS shall entail the following: -</p> <ul style="list-style-type: none"> • Tallying the balance as per bank book to the bank confirmation/ statement. • Checking of all material reconciling items included under cheques issued but presented for payment to the underlying bank book forming part of books of account. In addition, the auditor should request for bank statements of subsequent period and should verify if the cheques issued have subsequently been cleared by the bank. For all cases where cheques have become stale i.e. 3 months or more have lapsed since the issue date, the same should not appear in the BRS and should instead be taken back to liabilities. • Checking of all material reconciling items included under cheques deposited but not credited by bank by requesting for bank deposit slips, duly acknowledged by bank and verifying if the balances were credited by bank subsequently by tallying to the bank statement of subsequent period. For any instances related to cheques not cleared beyond reasonable time, the auditor should seek brief descriptions from the management and in case such explanations are found to be unsatisfactory, the auditor should verify the revenue recognition related to such parties was in order and as per the Company's revenue recognition policy. • Checking of all material reconciling items included under amounts or charges debited/ credited by bank but not accounted for by requesting for bank statements for the period under audit and tallying the same. If the amounts are found to be material, the auditor should ensure that the management records the adjustments for the same in its books of account.
Q75.	<p>As the statutory auditor of Ginni Ltd., you need to verify if the company has valid legal ownership rights over the inventories recorded in the balance sheet as on March 31, 2025. What audit procedures should you perform to verify the company's ownership of the inventories, including items stored at third-party locations? (MTP1, Jan 2025, 4 marks)</p> <p>The statutory auditor of Saturn Ltd. should perform the following audit procedures to verify if the company has valid legal ownership rights over the inventories recorded in the balance sheet as on 31.03.2024. The auditor should:</p> <ul style="list-style-type: none"> • vouch recorded purchases to underlying documentation (purchase requisition, purchase order, receiving report, vendor invoice and cancelled cheque or payment file). • evaluate the consigned goods. • examine client correspondence, sales and receivables records, purchase documents. • determine the existence of collateral agreements. • review consignment agreements. • review material purchase commitment agreements. • examine invoices for evidence of ownership i.e. the invoices shall be in the name of the client. • obtain confirmation for significant items of inventory as per SA 501. • For instances of inventory held by third party, the auditor should insist on obtaining declaration from the third party on its business letterhead and signed by an authorized personnel of that third party confirming that the items of inventory belong to the entity and are being held by such third party on behalf of and for the benefit of the entity under audit.
Q76.	<p>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. (MTP1, Sep 2024, 5 Marks)</p>

	<p>Audit procedures to be followed by the statutory auditor of Zed Limited to ensure that only the inventories held by entity have been recorded in the financial statements and do not include any inventories that belong to third parties but does include inventories owned by the entity and lying with a third party are as under: -</p> <ul style="list-style-type: none"> • Perform analytical procedures (comparison tests with industry averages, budgets, prior years, trend analysis, etc.). <ul style="list-style-type: none"> ◦ Compute inventory turnover ratio (COGS/ average inventory) ◦ Perform vertical analysis (inventory/ total assets) ◦ Compare budgetary expectations vis-à-vis actuals • Examine non-financial information related to inventory, such as weights and other measurements. • Perform purchase and sales cut-off tests. Trace shipping documents (bills of lading and receiving reports, warehouse records, and inventory records) to accounting records immediately before and after year-end. • With respect to tagged inventory, perform tests for omitted transactions and tests for invalid transactions. • Verify the clerical and arithmetical accuracy of inventory listings. • Reconcile physical inventory amounts with perpetual records. • Reconcile physical counts with ledger control totals. • Reconcile inventories which belong to client but are held with third parties like transporters, warehouses, port authorities etc. • Goods received on a consignment basis have been properly segregated from other items of inventory.
Q77.	<p>During the audit of Rapid Industries Private Limited, CA Akshat notices that inventories of raw materials & consumables and work-in- progress amounting ₹ 2.50 crores and ₹ 0.25 crores appear in the financial statements of the company as on March 31st, 2025. He wants to verify that the above-mentioned inventories have been valued appropriately and as per generally accepted accounting policies and practices. How should he proceed to verify the above? (RTP, Jan 2025, NA)</p> <p>For Raw materials and consumables:</p> <ul style="list-style-type: none"> • Ascertain what elements of cost are included e.g. carriage inward, nonrefundable duties etc. • If standard costs are used, enquire into basis of standards; how these are compared with actual costs and how variances are analyzed and accounted for/ treated in accounting records. • Test check cost prices used with purchase invoices received in the month(s) prior to counting. • Follow up valuation of all damaged or obsolete inventories noted during observance of physical counting with a view to establishing a realistic net realizable value <p>For Work in Progress:</p> <ul style="list-style-type: none"> • Ascertain how the various stages of production/ value add are measured and in case estimates are made, understand the basis for such estimates. • Ascertain what elements of cost are included. If overheads are included, ascertain the basis on which they are included and compare such basis with the available costing and financial data/ information maintained by the entity. • Ensure that material costs exclude any abnormal wastage factors
Q78.	<p>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. (MTP2, Sep 2024, 5 marks) (MTP2, Nov 2022, 6 Marks)</p> <p>To verify whether the entity has valid legal ownership rights over the PPE claimed to be held by the entity and recorded in the financial statements -</p> <ul style="list-style-type: none"> • In addition to the procedures undertaken for verifying completeness of additions to PPE during the period under audit, the auditor while performing testing of additions should also verify that all PPE purchase invoices are in the name of the entity that entitles legal title of ownership to the respective entity.

	<ul style="list-style-type: none"> For all additions to land, building in particular, the auditor should obtain copies of conveyance deed/ sale deed to establish whether the entity is mentioned to be the legal and valid owner. The auditor should insist and verify the original title deeds for all immovable properties held as at the balance sheet date. In case the entity has given such immovable property as security for any borrowings and the original title deeds are not available with the entity, the auditor should request the entity's management for obtaining a confirmation from the respective lenders that they are holding the original title deeds of immovable property as security. In addition, the auditor should also verify the register of charges, available with the entity to assess that any charge has been created against the PPE. <p>The auditor has to ensure whether PPE has been valued appropriately and as per generally accepted accounting policies and practices -</p> <p>It is a common understanding that the value of fixed assets/ PPE depreciates due to efflux of time, use and obsolescence. The diminution of the value represents an item of cost to the entity for earning revenue during a given period. Unless this cost in the form of depreciation is charged to the accounts, the profit or loss would not be correctly ascertained, and the values of PPE would be shown at higher amounts. Therefore, such verification is significant.</p> <p>While verifying the PPE of the client entity, the auditor also needs to consider whether the PPE has been valued appropriately and as per the generally accepted accounting principles and practices. The auditor should:</p> <ul style="list-style-type: none"> Verify that the entity has charged depreciation on all items of PPE unless any item of PPE is non-depreciable like freehold land; Assess that the depreciation method used reflects the pattern in which the asset's future economic benefits are expected to be consumed by the entity. It could be Straight line method, diminishing value method, unit of production method, as applicable The auditor should also verify whether the management has done an impairment assessment to determine whether an item of property, plant and equipment is impaired as per the requirements of AS 28 - Impairment of Assets.
Q79.	<p>You are an auditor of PQR Ltd. which has spent ₹10 lakhs on Research activities of the product during period under audit. Board of Directors want to recognize it as an internally generated intangible assets. Advise and discuss the conditions necessary to be fulfilled to recognize the intangible assets in the financial statements. (SA, May 2019, 4 marks) (MTP1, Nov 2020, 3 marks) (MTP1, May 2021, 4 marks) (MTP2, May 2023, 3 marks)</p> <p>No Intangible asset arising from research (or from the research phase of an internal project) shall be recognised. Expenditure on research shall be recognised as an expense when it is incurred since in the research phase of an internal project, an entity cannot demonstrate that an intangible asset exists that will generate probable future economic benefits.</p> <p>Thus, the board of directors cannot recognize the expense as an internally generated intangible asset.</p> <p>An intangible asset shall be recognised if, and only if:</p> <ul style="list-style-type: none"> the said asset is identifiable; the entity controls the asset i.e. the entity has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits; it is probable that future economic benefits associated with the asset will flow to the entity; the cost of the item can be measured reliably.
Q80.	<p>CA Tripti is in the midst of conducting an audit of a company engaged in manufacturing of range of bicycles in an industrial township located in a North Indian state. As part of its activities, the company procures bicycle components from various small and medium sized enterprises. Besides, the company imports a few bicycle components from China on credit terms. The auditor notices that the company has huge trade payables</p>

	<p>reflected in its financial statements. He wants to be sure that all trade payables reflected in financial statements have been valued appropriately. Suggest a few audit procedures to be performed in this respect. (RTP, May 2025, NA)</p> <p>Audit procedures to be performed to verify that all trade payables reflected in financial statements have been valued appropriately are:</p> <ul style="list-style-type: none"> Review the process followed by the Company to identify if any old creditor balance needs to be written back. This will include a consistency comparison with the method used in the last year, and a determination of whether the method is appropriate for the underlying business environment. Obtain the ageing of payable balances, and the list of vendors with whom the Company has disputes and any claims from customers, under litigation and compare with previous year. Check that write backs in the trade payable balances assessed as no longer payable have been approved by an appropriate and authorised member of senior management, for example, CEO/MD. Check that the restatement of foreign currency trade payables has been done properly in accordance with AS 11. Understand management's process to identify the principal amount and the interest due thereon (if any) remaining unpaid to any Micro, Small and Medium Sized Enterprises suppliers at the end of accounting year. Test check the management process to assess if the auditor could rely on the management process.
Q81.	<p>CA Q, the auditor of XYZ Ltd, while conducting an audit observes that the company has made various provisions in the books of account. What are the audit procedures that CA Q will follow to verify the existence, completeness, and valuation of the provisions made ? (SA, May 2023, 3 marks)</p> <p>Audit procedures that CA Q will follow to verify the existence, completeness, and valuation of the provisions made are:</p> <p>Existence</p> <ul style="list-style-type: none"> Obtain a list of all provisions and compare them with balances in the ledger. Inspect the underlying agreements like agreements with customers to assess warranty commitments, any legal and other claims on the entity i.e. litigations. <p>Valuation</p> <ul style="list-style-type: none"> Wherever required, obtain the expert's report, calculation and underlying working for the provision amount. For example - for warranty involving complex calculations, some entities get that valued through an actuary. In such a case, the auditor may request the management to share the actuarial valuation report and in case of any matter under legal dispute, the auditor should request for assessment made by a legal expert in relation to likelihood of a liability devolving on the entity i.e. whether probable or possible or remote as defined above. The auditor should then verify the underlying assumptions used by the expert with the data shared by the management. <p>Completeness</p> <ul style="list-style-type: none"> Obtain the underlying working and the basis for each of the provisions made from the management and verify whether the same is complete and accurate. The auditor shall obtain a written representation from the management that it has made all the provisions which were required to be made as per the recognized accounting principles.
Q82.	<p>How will you vouch/verify Provision for income tax? (ICAI Study Material- Test Your Knowledge)</p> <p>Provision for Income Tax:</p> <ul style="list-style-type: none"> Obtain the computation of income and income tax prepared by the entity and verify whether it is as per the Income-tax Act, 1961 and Rules made thereunder. Review adjustments, expenses, disallowed special rebates, etc. with particular reference to the last available completed assessment.

	<ul style="list-style-type: none"> Examine relevant records and documents pertaining to advance tax, self-assessment tax and other demands. Compute tax payable as per the latest applicable rates in the Finance Act. Ensure that overall provisions on the date of the balance sheet is adequate having regard to current year provision, advance tax paid, assessment orders, etc. Ensure that the requirements of AS 22 on Accounting for Taxes on Income have been appropriately followed for the period under audit
Q83.	<p>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. (MTP1, May 2024, 4 Marks)</p> <p>CA X, having doubts about fictitious sales being recorded by Joyful Ltd would ensure that revenue is not overstated by performing following audit procedures:</p> <ul style="list-style-type: none"> Check whether a single sales invoice is recorded twice or a cancelled sales invoice could also be recorded. Test check a few invoices with their relevant entries in the sales journal. Obtain confirmation from few customers to ensure genuineness of sales transaction Whether any fictitious customers and sales have been recorded. Whether any shipments were done without the consent and agreement of the customer, especially at the year end to inflate the sales figure Whether unearned revenue recorded as earned. Whether any substantial uncertainty exists about collectability Whether customer obligations are contingent on other actions (financing, resale etc.)
Q84.	<p>Discuss the audit procedures generally required to be undertaken by the auditor while auditing Goods sent out on Sale or Return Basis. (SA, Nov 2020, 3 Marks) (MTP1, Nov 2023, 3 marks)</p> <p>Goods Sent Out on Sale or Return Basis:</p> <ol style="list-style-type: none"> Check whether a separate memoranda record of goods sent out on sale or return basis is maintained. The party accounts are debited only after the goods have been sold and the sales account is credited. Verify that the price of such goods is unloaded from the sales account and the trade receivables record. Check the memoranda record to confirm that on the receipt of acceptance from each party, his account has been debited and the sales account correspondingly credited. Ensure that the goods in respect of which the period of approval has expired at the end of the year, have either been received back or customers' accounts have been debited. Confirm that the inventory of goods sent out on approval, the period of approval in respect of which had not expired till the end of the year lying with the party, has been included in the closing inventory.
Q85.	<p>ABC limited appointed XYZ & Company, Chartered Accountants, as a Statutory Auditor of the Company for the year 2023-24. CA X, partner of XYZ & Company, was looking after the audit of other income of the company which consists of interest income on fixed deposits. As a Statutory Auditor how would CA X verify interest income on fixed deposits for the year 2024-25? (SA, Nov 2020, 4 Marks)</p> <p>CA X, partner of XYZ & Company, would carry out the following audit procedure for verifying interest income on fixed deposits of ABC Limited:</p> <ol style="list-style-type: none"> Obtain a listing of fixed deposits opened during the period under audit along with the applicable interest rate and the number of days for which the deposit was outstanding during the period. Verify the arithmetical accuracy of the interest calculation made by the entity by recomputing i.e. multiplying the deposit amount with the applicable rate and number of days during the period under audit. For deposits still outstanding as at the period- end, trace the same to the direct confirmations obtained from the respective bank/ financial institution.

	<p>iv) Obtain a confirmation of interest income from the bank and verify that the interest income as per bank reconciles to the calculation shared by the entity.</p> <p>v) Obtain a copy of Form 26AS and reconcile the interest reflected therein to the calculation shared by client.</p>
Q86.	<p>As a Statutory Auditor of the company list out audit procedure required to be undertaken for the recognition of following other income:</p> <p>i) Interest income from fixed deposit</p> <p>ii) Dividend income</p> <p>iii) Gain/(loss) on sale of investment in mutual funds.</p> <p>(SA, Jan 2021, 3 marks)</p> <p>Statutory auditor would perform the following audit procedure for recognition of different items given in the question:</p> <p>i) Interest income on fixed deposits is recognized on a time proportion basis taking into account the amount outstanding and the applicable interest rate.</p> <p>ii) Dividends are recognised in the statement of profit and loss only when:</p> <ul style="list-style-type: none"> the entity's right to receive payment of the dividend is established; it is probable that the economic benefits associated with the dividend will flow to the entity; and the amount of the dividend can be measured reliably. <p>iii) Gain/(loss) on sale of investment in mutual funds is recorded as other income on transfer of title from the entity and is determined as the difference between the redemption price and carrying value of the investments.</p>
Q87.	<p>During the audit of Grace Pvt. Ltd., CA Tanu notices that significant amount of depreciation and amortisation charges are reflected in financial statements of the company. Which attributes need to be considered by him while verifying such depreciation and amortisation charges? (MTP2, May 2025, 5 Marks) (SA, Jan 2021, 4 marks) (MTP2, Nov 2023, 4 marks) (SA, May 2018, 5 Marks)</p> <p>Depreciation and amortisation generally constitute an entity's significant part of overall expenses and have direct impact on the profit/ loss of the entity, hence auditors need to verify and ensure that such expenditure is appropriate, accurately calculated and has been accounted as per applicable provisions of Companies Act or other statutes, to the extent applicable on the respective industry and as per generally accepted accounting principles.</p> <p>Auditor needs to consider the following attributes while verifying for depreciation and amortisation expenses:</p> <p>i) Obtain the understanding of the entity's accounting policy related to depreciation and amortisation.</p> <p>ii) Ensure that the Company's policy for charging depreciation and amortisation is as per the relevant provisions of Companies Act and applicable accounting standards.</p> <p>iii) The accounting policy has been applied consistently year on year. Any change in the accounting policy has been adequately disclosed</p> <p>iv) Whether the depreciation has been calculated after making adjustment of residual value from the cost of the assets.</p> <p>v) Whether depreciation and amortisation charges are valid.</p> <p>vi) Whether depreciation and amortisation charges are accurately calculated and recorded.</p> <p>vii) Whether all depreciation and amortisation charges are recorded in the appropriate period.</p> <p>viii) Ensure the parts (components) of each item of property, plant and equipment that are to be depreciated separately has been properly identified.</p> <p>ix) Whether the most appropriate depreciation method for each separately depreciable component has been used.</p>
Q88.	<p>"While the auditor may choose to analyse the monthly trends for expenses like rent, power and fuel but for other expenses, an auditor generally prefers to verify other attributes." Mention those attributes.</p>

	<p>(SA, Nov 2018, 5 Marks) (MTP1, Nov 2021, 4 Marks)</p> <p style="text-align: center;">OR</p> <p>Profit and Loss account of an organisation shows various types of expenses like rent, power and fuel, repairs and maintenance, insurance, travelling, miscellaneous expenses etc., that are essential and incidental to running of business operations. What are the attributes that an auditor generally prefers for vouching these types of expenses ? (SA, Dec 2021, 3 Marks)</p> <p style="text-align: center;">OR</p> <p>M/s SS & Associates have been appointed as statutory auditors of Green Limited, a company engaged in the business of manufacturing of hardware products. They are analyzing the monthly trends for other expenses like rent, power and fuel, repairs, etc. and are also verifying attributes of such types of expenses. List down the attributes for verifying such expenses.</p> <p>(SA, Nov 2022, 4 marks) (MTP2, Jan 2025, 5 marks)</p>
	<p>An entity in addition to making purchases and incurring employee benefit expenses, also incurs other expenditures like rent, power and fuel, repairs and maintenance, insurance, travelling, miscellaneous expenses etc., that are essential and incidental to running of business operations</p> <p>While the auditor may choose to analyse the monthly trends for expenses like rent, power and fuel, an auditor generally prefers to vouch for other expenses to verify following attributes:</p> <ol style="list-style-type: none"> Whether the expenditure pertained to current period under audit; Whether the expenditure qualified as a revenue and not capital expenditure; Whether the expenditure had a valid supporting like travel tickets, insurance policy, third party invoice etc.; Whether the expenditure has been classified under the correct expense head; Whether the expenditure was authorised as per the delegation of authority matrix; Whether the expenditure was in relation to the entity's business and not a personal expenditure
Q89.	<p>Proceedings have been initiated against False Limited for holding benami property under the Benami Transactions (Prohibition) Act, 1988 (45 of 1988) and the rules made thereunder, but such property is not recorded in books of accounts. As a consultant to the company, what will you advice to the company as far as disclosure requirements are concerned in relation to said proceedings? (SA, May 2022, 4 marks) (RTP, May 2024, NA) (MTP2, May 2022, 4 marks)</p> <p>Details of Benami Property held</p> <p>Where any proceedings have been initiated or pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act, 1988 (45 of 1988) and the rules made thereunder, the company shall disclose the following:-</p> <ol style="list-style-type: none"> Details of such property, including year of acquisition, Amount thereof, Details of Beneficiaries, If property is in the books, then reference to the item in the Balance Sheet, If property is not in the books, then the fact shall be stated with reasons, Where there are proceedings against the company under this law as an abetter of the transaction or as the transferor then the details shall be provided, Nature of proceedings, status of same and company's view on same.
Q90.	<p>What are the required disclosures for cash & Cash equivalents to be made by the company as per Schedule III (Part I) to Companies Act, 2013? (RTP, May 2023, NA) (MTP1, May 2023, 4 marks) (SA, Dec 2021, 3 Marks) (ICAI Study Material- Test Your Knowledge)</p> <p>The following are the disclosure requirements as per Schedule III to the Companies Act, 2013, with respect to the cash & cash equivalents held by the company: Cash and cash equivalents</p>

- i) Cash and cash equivalents shall be classified as:
 - a) Balances with **banks**;
 - b) **Cheques**, drafts on hand;
 - c) Cash on **hand**;
 - d) **Others** (specify nature)
- ii) **Earmarked balances** with banks (for example, for unpaid dividend) shall be separately stated.
- iii) Balances with banks to the extent held as **margin money** or security against the borrowings, guarantees, other commitments shall be disclosed separately
- iv) **Repatriation restrictions**, if any, in respect of cash and bank balances shall be separately stated.
- v) Bank **deposits** with **more than 12 months'** maturity shall be disclosed separately.

Q91. Following is extract of notes to accounts of financial statements of STU Private Limited listing some ratios. Discuss, whether disclosure, given in following manner meets requirements of Schedule III of the Companies Act, 2013. Ignore other ratios which are not listed in extract given below:

Name of ratio	31.3.2023	31.3.2022
Current ratio	2.50	2.30
Inventory turnover ratio	3.00	6.00
Trade receivables turnover ratio	1.75	5.00
Net profit ratio (in%)	13%	10%

(RTP, May 2024, NA)

The disclosure given in the question does **not** meet requirements of Schedule III to Companies Act, 2013. Schedule III requires that the company shall explain the items included in numerator and denominator for computing the ratios. Further explanation shall be provided for any change in the ratio by **more than 25% as compared to the preceding year**.

In the given table, the company has not explained the items included in numerator and denominator for computing ratios. Further, variations in ratios as compared to preceding year are as under: -

Name of ratio	31.3.2023	31.3.2022	Variation
Current ratio	2.50	2.30	8.69%
Inventory turnover ratio	3.00	6.00	50%
Trade receivables turnover ratio	1.75	5.00	65%
Net profit ratio (in%)	13%	10%	30%

As calculated above, there is **change in inventory turnover ratio, trade receivables turnover ratio and net profit ratio by more than 25%** as compared to preceding year. Therefore, explanations for such changes have also to be provided where there are changes by more than 25% as compared to preceding year

Chapter 6 - Audit Documentation

Q92. During an audit of MNT Ltd., CA Shubh, the auditor discovers an issue with stock valuation. To ensure the accuracy and reliability of his observations, CA Shubh needs to document the audit procedures, evidence collected, and his observations thoroughly. In this situation, how does audit documentation help CA Shubh support his findings in audit in accordance with Standards on Auditing? (MTP1, May 2025, 4 Marks)

The following are the purpose of Audit documentation:

- Assisting the engagement team to **plan** and **perform** the audit.
- Assisting members of the engagement team to **direct** and **supervise** the audit work, and to discharge their **review** responsibilities.

	<ul style="list-style-type: none"> Enabling the engagement team to be accountable for its work. Retaining a record of matters of continuing significance to future audits. Enabling the conduct of quality control reviews and inspections in accordance with SQC 1. Enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements.
Q93.	<p>M/s KSJS & Associates are the statutory auditors of Moon Ltd. for the financial year 2023-24. During an audit briefing, CA Sanket, the engagement partner, explained that the auditor must assemble the audit documentation in an audit file and complete the administrative process of finalising the audit file on a timely basis after the date of the auditor's report. He also highlighted the requirements of SQC 1 regarding establishment of policies and procedures for the retention of engagement documentation in a firm. Explain the requirements related to the timely assembly and retention of audit files in accordance with relevant Engagement and Quality Control Standards. (MTP1, Jan 2025, 5 marks) (RTP, May 2023, NA) (RTP, May 2022, NA) (SA, Nov 2019, 3 Marks) (RTP, Nov 2019, NA) (MTP1, May 2018, 5 Marks) (RTP, Nov 2018, NA) (MTP1, May 2019, 4 Marks) (RTP, Nov 2023, NA)</p> <ul style="list-style-type: none"> The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report. SQC 1 "Quality Control for Firms that perform Audits and Review of Historical Financial Information, and other Assurance and related services", requires firms to establish policies and procedures for the timely completion of the assembly of audit files. An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor's report. The completion of the assembly of the final audit file after the date of the auditor's report is an administrative process that does not involve the performance of new audit procedures or the drawing of new conclusions. Changes may, however, be made to the audit documentation during the final assembly process, if they are administrative in nature. Examples of such changes include: <ul style="list-style-type: none"> Deleting or discarding superseded documentation. Sorting, collating and cross referencing working papers. Signing off on completion checklists relating to the file assembly process. Documenting audit evidence that the auditor has obtained, discussed and agreed with the relevant members of the engagement team before the date of the auditor's report. After the assembly of the final audit file has been completed, the auditor shall not delete or discard audit documentation of any nature before the end of its retention period. SQC 1 requires firms to establish policies and procedures for the retention of engagement documentation. The retention period for audit engagements ordinarily is no shorter than seven years from the date of the auditor's report, or, if later, the date of the group auditor's report.
Q94.	<p>The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor to understand significant matters arising during the audit. Explain the above statement and also give examples of significant matters. (RTP, Nov 2022, NA)</p> <p>The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions. Judging the significance of a matter requires an objective analysis of the facts and circumstances.</p> <p>Examples of significant matters include:</p> <ul style="list-style-type: none"> Matters that give rise to significant risks. Results of audit procedures indicating <ul style="list-style-type: none"> that the financial statements could be materially misstated, or

	<ul style="list-style-type: none"> ○ a need to revise the auditor's previous assessment of the risks of material misstatement and the auditor's responses to those risks. ● Circumstances that cause the auditor significant difficulty in applying necessary audit procedures. ● Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter Paragraph in the auditor's report.
Q95.	<p>The form, content and extent of audit documentation depends upon a number of factors. List out such factors. (ICAI Study Material - Test Your Knowledge)</p> <p>Form, Content and Extent of Audit Documentation: Working papers should record the audit plan, nature, timing and extent of auditing procedures performed, and the conclusions drawn from the evidence obtained.</p> <p>The form, content and extent of audit documentation depend on factors such as:</p> <ul style="list-style-type: none"> ● The size and complexity of the entity. ● The nature of the audit procedures to be performed. ● The identified risks of material misstatement. ● The significance of the audit evidence obtained. ● The nature and extent of exceptions identified. ● The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained. ● The audit methodology and tools used.

Chapter 7 - Completion and Review

Q96.	<p>During the audit of Jimjam Ltd., CA Arjun, the auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report, that requires adjustment of, or disclosure in, the financial statements have been identified. With reference to Standards on Auditing, what specific audit procedures should CA Arjun include in his risk assessment to address subsequent events effectively?</p> <p>(MTP2, May 2025, 4 Marks) (SA, July 2021, 4 Marks) (RTP, May 2019, NA)</p> <p>Audit Procedure Regarding Events Occurring Between The Date Of The Financial Statements And The Date Of The Auditor's Report</p> <p>The auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements have been identified.</p> <p>The auditor shall take into account the auditor's risk assessment which shall include the following:</p> <ul style="list-style-type: none"> ● Obtaining an understanding of any procedures management has established to ensure that subsequent events are identified. ● Inquiring of management and, where appropriate, TCWG as to whether any subsequent events have occurred which might affect the financial statements. ● Read the minutes of meeting of board of directors, executive committee, meeting of shareholders held after balance sheet date ● Reading the entity's latest subsequent interim financial statements, if any.
Q97.	<p>S Ltd., a large textile manufacturing company, due to heavy recession in the market was unable to collect amount of huge receivables in time and also holding large amounts of stock of raw materials and finished goods since last 9 months of the Financial Year 2023-24. From your primary observations of audit evidences you feel that there is a material uncertainty exists about going concern. How will you deal in your audit report ? What will be the effect on your audit opinion in the following situations ?</p> <p>a) If adequate disclosure of such material uncertainty is already made in the financial statements.</p>

	<p>b) If adequate disclosure of such material uncertainty is not made in the financial statements" (SA, May 2023, 4 marks) (RTP, Nov 2021, NA)</p> <p>Use of the Going Concern Basis of Accounting is Appropriate but a Material Uncertainty Exists:</p> <p>The identification of a material uncertainty is a matter that is important to users' understanding of the financial statements. The use of a separate section with a heading that includes reference to the fact that a material uncertainty related to going concern exists alerts users to this circumstance.</p> <p>a) Adequate Disclosure of a Material Uncertainty is Made in the Financial Statements</p> <p>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."</p> <p>b) Adequate Disclosure of a Material Uncertainty is Not Made in the Financial Statements</p> <p>If adequate disclosure about the material uncertainty is not made in the financial statements, the auditor shall:</p> <ul style="list-style-type: none"> Express a qualified opinion or adverse opinion, as appropriate, in accordance with SA 705 (Revised); and In the Basis for Qualified (Adverse) Opinion section of the auditor's report, state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter.
Q98.	<p>Up and High Private Limited has started its export business during the year 2023-24. The company was catering to the 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.</p> <p>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.</p> <p>ii) If management refuses to correct misstatement as communicated by the statutory auditor, how should he proceed?</p> <p>(MTP1, May 2024, 4 Marks)</p> <ul style="list-style-type: none"> The above situation is an example of misstatement relating to noncompliance with requirements of AS 9 identified during audit. In accordance with requirements of SA 450, the auditor shall communicate on a timely basis all misstatements accumulated during the audit with the appropriate level of management, unless prohibited by law or regulation. The auditor shall request management to correct those misstatements. Timely communication of misstatements to the appropriate level of management is important as it enables management to evaluate whether the items are misstatements, inform the auditor if it disagrees and take action as necessary. The correction by management of all misstatements, including those communicated by the auditor, enables management to maintain accurate accounting books and records and reduces the risks of material misstatement of future financial statements because of the cumulative effect of immaterial uncorrected misstatements related to prior periods. If management refuses to correct some or all of the misstatements communicated by the auditor, the auditor shall obtain an understanding of management's reasons for not making the corrections and shall take that understanding into account when evaluating whether the financial statements as a whole are free from material misstatement.
Q99.	<p>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" (MTP1, Sep 2024, 5 Marks) (ICAI Study Material - Test Your Knowledge)</p> <ul style="list-style-type: none"> The likelihood of the deficiencies leading to material misstatements in the financial statements in the

	<p>future.</p> <ul style="list-style-type: none"> • The susceptibility to loss or fraud of the related asset or liability. • The subjectivity and complexity of determining estimated amounts, such as fair value accounting estimates. • The financial statement amounts exposed to the deficiencies. • The volume of activity that has occurred or could occur in the account balance or class of transactions exposed to the deficiency or deficiencies. • The importance of the controls to the financial reporting process, for example: <ul style="list-style-type: none"> ○ General monitoring controls (such as oversight of management). ○ Controls over the prevention and detection of fraud. ○ Controls over the selection and application of significant accounting policies. ○ Controls over significant transactions with related parties. ○ Controls over significant transactions outside the entity's normal course of business. ○ Controls over the period-end financial reporting process (such as controls over non-recurring journal entries). • The cause and frequency of the exceptions detected as a result of the deficiencies in the controls. • The interaction of the deficiency with other deficiencies in internal control
Q100.	<p>Auditors are required to obtain an understanding of internal control relevant to the audit when identifying and assessing its effectiveness and risk of material misstatement. PDC Ltd. appointed CA Nikhil as auditor for the F.Y. 2023-24. During the audit, he observed that significant deficiency exists in the internal control system and he wants to ascertain the same. Elucidate the various indicators of significant deficiencies which will help you in assessing the efficiency of internal control system of the organisation. (MTP2, May 2025, 5 Marks)</p> <p>As per SA 265, "Communicating Deficiencies in Internal Control to Those Charged with Governance and Management", Indicators of significant deficiencies in internal control include, for example:</p> <ol style="list-style-type: none"> Evidence of ineffective aspects of the control environment, such as: <ol style="list-style-type: none"> Indications that significant transactions in which management is financially interested are not being appropriately scrutinised by those charged with governance. Identification of management fraud, whether or not material, that was not prevented by the entity's internal control. Management's failure to implement appropriate remedial action on significant deficiencies previously communicated. Absence of a risk assessment process within the entity where such a process would ordinarily be expected to have been established. Evidence of an ineffective entity risk assessment process, such as management's failure to identify a risk of material misstatement that the auditor would expect the entity's risk assessment process to have identified. Evidence of an ineffective response to identified significant risks (e.g., absence of controls over such a risk). Misstatements detected by the auditor's procedures that were not prevented, or detected and corrected, by the entity's internal control. Disclosure of a material misstatement due to error or fraud as prior period items in the current year's Statement of Profit and Loss. Evidence of management's inability to oversee the preparation of the financial statements.
Q101.	<p>UVW & Associates are the statutory auditors of Moon Ltd., a listed company, for the financial year 2023-24. CA Udhav is the engagement partner for the audit assignment. He was of the understanding that as per the requirement of one of the SAs he has a responsibility to communicate following matters to those charged with governance:</p> <ol style="list-style-type: none"> The auditor's responsibilities in relation to the financial statement audit.

- b) Planned scope and timing of the audit.
- c) Auditor independence

Which of the matters is not included in the list prepared by CA Udhav. Discuss such matter in detail.

(Additional Question)

SA 260 "Communication with Those Charged with Governance" deals with auditor's responsibility to communicate with TCWG in relation to an audit of FS. Among various matters as included by CA Udhav in his list, one of the matters that is not mentioned in the list is **Significant findings from the audit**. With respect to such matter, the auditor shall communicate with those charged with governance: -

- a) The auditor's views about significant **qualitative aspects** of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures. When applicable, the auditor shall explain to TCWG why the auditor considers a significant accounting practice, that is acceptable under the AFRR, not to be most appropriate to the particular circumstances of the entity;
- b) **Significant difficulties**, if any, encountered during the audit;
- c) Unless all of TCWG are involved in managing the entity: -
 - i) **Significant matters** arising during the audit that were discussed, or subject to correspondence, with management;
 - ii) **Written representations** the auditor is requesting
- d) **Circumstances** that affect the form and **content** of the auditor's report, if any and
- e) Any **other significant matters** arising during the audit that, in the auditor's professional judgment, are relevant to the oversight of the financial reporting process.

The communication of findings from the audit may include requesting further information from TCWG in order to complete the audit evidence obtained. For example, the auditor may confirm that TCWG have the same understanding of the facts and circumstances relevant to specific transactions or events.

- Q102. 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?

(MTP1, Sep 2024, 5 marks)

- As per **SA 570, "Going Concern"**, going concern is one of the **fundamental accounting** assumptions. The enterprise is normally viewed as a going concern, that is, as continuing in operation for the foreseeable future.
- It is **assumed** that the enterprise has **neither** the **intention** nor the **necessity** of **liquidation** or of curtailing materially the scale of the operations.
- Under the going concern basis of accounting, the financial statements are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future.
- General purpose financial statements are prepared using the going concern basis of accounting, **unless** management either
 - **intends** to **liquidate** the entity or to cease operations, or
 - has **no realistic alternative** but to do so.
- In the given situation, company has reflected net losses in financial statements of last two years but is able to meet its financial commitments signifying its ability to carry on business/trade. The revenue of company is also expected to grow in the coming period. It shows that management has neither the intention nor the necessity of liquidation or of curtailing materially the scale of operations.
- Therefore, view of the management for following going concern basis of accounting in current year is **appropriate**.
- Further, the significance of going concern is due to its effect on the preparation of financial statements. Ability or otherwise of an enterprise to be viewed as going concern affects its preparation of financial statements.

	<ul style="list-style-type: none"> When the use of the going concern basis of accounting is appropriate, assets and liabilities are recorded on the basis that the entity will be able to realise its assets and discharge its liabilities in the normal course of business. When an enterprise is not viewed as a going concern, the financial statements are prepared on liquidation basis. For example, inventories may need to be written down as these may be sold for a lower price. Assets may have to be recorded at the likely prices they will fetch
Q103.	<p>ABC Pvt. Ltd., a manufacturing company, is facing significant financial difficulties due to downfall in market and increase in cost of production. CA Ram, the auditor of ABC Pvt. Ltd. has identified the following conditions:</p> <ul style="list-style-type: none"> The company has defaulted on a major loan repayment. Current liabilities exceed current assets by 50%. Sales revenue has declined by 30% compared to the previous year. <p>Management has not yet performed an assessment of the company's ability to continue as a going concern, but they provided assurance for implementing corrective measures, including cost-cutting initiatives and discussions with creditors for restructuring the loan. Which additional audit procedures need to be performed by CA Ram in accordance with SA 570 when such events or conditions are identified? (MTP2, Jan 2025, 5 marks)</p> <p>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.</p> <p>These procedures shall include:</p> <ul style="list-style-type: none"> 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. 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. 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: <ul style="list-style-type: none"> Evaluating the reliability of the underlying data generated to prepare the forecast; and Determining whether there is adequate support for the assumptions underlying the forecast. Considering whether any additional facts or information have become available since the date on which management made its assessment. Requesting written representations from management and, where appropriate, those charged with governance, regarding their plans for future actions and the feasibility of these plans.
Q104.	<p>Udit & Co. is the statutory auditor of Fun Journey Ltd., a company engaged in the tours and travel business. The company has an annual turnover of ₹ 1,200 crores and profits of ₹ 150 crores. While planning, the auditors discussed the requirement for a written representation letter from management for confirming that:</p> <ol style="list-style-type: none"> The auditor is provided with all relevant information and access as agreed in the terms of the audit engagement; and All transactions have been recorded and are reflected in the financial statements <p>As the audit was near to completion, the auditor disagreed with the management on one of the matters including need of written representation contending that verbal confirmations given during the audit should be sufficient. Thus, separate written representation is not required. Udit & Co., however, explained that under SA 580 obtaining a formal written statement from management is mandatory. Fun Journey Ltd. refuses to provide a written representation letter, despite the auditor's several requests.</p> <p>a. Whether the contention of auditor for seeking written representation letter is justified?</p>

- b. What should be the form of such written representation?
 c. How should the auditor proceed if management refuses to provide the written representation?

(Additional Question)

(a) As per **SA 580, "Written Representations"**, the auditor shall request management to provide a written representation that it has fulfilled its responsibility for the preparation of the financial statements in accordance with AFRF, including where relevant their fair presentation, as set out in the terms of the audit engagement.

Further, the auditor shall request management to provide a written representation that:

- i. It has provided the auditor with all **relevant information** and access as agreed in the terms of the audit engagement
- ii. All transactions have been **recorded** and are **reflected** in the financial statements.

In the given case, Fun Journey Ltd. refuses to provide a written representation letter, despite the auditor's several requests. Thus, in view of above the **contention of auditor is correct**

(b) The written representations as per SA 580, shall be in the form of a **representation letter** addressed to the auditor. If law or regulation requires management to make written public statements about its responsibilities, and the auditor determines that such statements provide some or all of the representations required, the relevant matters covered by such statements need not be included in the representation letter.

(c) As per **SA 580**, if management does not provide one or more of the requested written representations, the auditor shall:

- i) Discuss the **matter with management**;
- ii) **Re-evaluate the integrity** of management and evaluate the effect that this may have on the reliability of representations (oral or written) and audit evidence in general; and
- iii) Take **appropriate actions**, including determining the possible effect on the opinion in the auditor's report in accordance with **SA 705 (Revised)**.

Furthermore, the auditor shall disclaim an opinion on the financial statements in accordance with SA 705 (Revised) if the auditor concludes that there is sufficient doubt about the integrity of management such that the written representations required are not reliable or management does not provide the written representations required.

Thus, refusal to provide a written representation could impact the auditor's ability to obtain sufficient appropriate audit evidence, potentially leading to a modified audit report.

Chapter 8 - Audit Report

- Q105. M/s S & Associates are the Statutory Auditors of Real Ltd., a company engaged in the business of manufacturing of garments. 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 K, the engagement partner, wants to conclude that whether the financial statements as a whole are free from material misstatements, whether due to fraud or error. What factors he should consider to reach that conclusion?

(SA, Dec 2021, 4 marks) (MTP1, Nov 2023, 4 marks) (MTP2, May 2024, 4 Marks) (ICAI Study Material - Test Your Knowledge)

Factors to be considered to form an opinion:

The auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

In order to **form** that **opinion**, the auditor shall **conclude** as to whether the auditor has obtained **reasonable**

	<p>assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. That conclusion shall take into account:</p> <ul style="list-style-type: none"> • The auditor's conclusion, in accordance with SA 330, whether sufficient appropriate audit evidence has been obtained • The auditor's conclusion, in accordance with SA 450, whether uncorrected misstatements are material, individually or in aggregate. • The evaluations required <ul style="list-style-type: none"> ○ The auditor shall evaluate whether the financial statements are prepared in accordance with the requirements of the applicable financial reporting framework. ○ This evaluation shall include consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgments
Q106.	<p>The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion". Explain what is included in this "Basis for Opinion" section. (ICAI Study Material - Test Your Knowledge) (RTP, Nov 2019, NA) (RTP, Nov 2020, NA) (MTP2, Nov 2023, 3 marks)</p> <p>Basis for Opinion: The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that:</p> <ul style="list-style-type: none"> • States that the audit was conducted in accordance with Standards on Auditing; • Refers to the section of the auditor's report that describes the auditor's responsibilities under the SAs; • Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. • States whether the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's opinion.
Q107.	<p>"An auditor is required to make specific evaluations while forming an opinion in an audit report." State them. (ICAI Study Material - Test Your Knowledge) (SA, Nov 2018, 5 marks) (MTP2, May 2021, 4 marks) (MTP1, Nov 2021, 3 marks) (MTP1, May 2023, 4 marks)</p> <p style="text-align: center;">OR</p> <p>The auditor shall evaluate whether the financial statements are prepared in accordance with the requirements of the applicable financial reporting framework. Explain stating clearly specific evaluations made by the auditor. (RTP, May 2022, NA)</p> <p>Specific Evaluations by the auditor: In particular, the auditor shall evaluate whether :</p> <ul style="list-style-type: none"> • The financial statements adequately disclose the significant accounting policies selected and applied; • The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate; • The accounting estimates made by management are reasonable; • The information presented in the financial statements is relevant, reliable, comparable, and understandable; • The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and • The terminology used in the financial statements, including the title of each financial statement, is appropriate.
Q108.	<p>The auditor of PQR LTD. is unable to obtain sufficient appropriate audit evidence and also the auditor thinks that the possible effects of undetected misstatements on the financial statements would be both material and pervasive. The auditor perceives the situation involving multiple uncertainties there and the auditor concludes that it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements. Advise and explain the type of opinion the auditor would issue in the given circumstances. You are also required to explain the meaning of</p>

	<p>pervasive in this regard. (MTP2, May 2018, 5 marks)</p> <p>The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.</p> <p>The auditor shall disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.</p> <p>Meaning of Pervasive – A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence.</p> <p>Pervasive effects on the financial statements are those that, in the auditor's judgment:</p> <ul style="list-style-type: none"> • Are not confined to specific elements, accounts or items of the financial statements • Even if it is confined to a specific element the effect can be considered as pervasive if it represent a substantial proportion of financial statements • In relation to disclosures, are fundamental to users' understanding of the financial statements.
Q109.	<p>While conducting audit of VED Ltd., you as an auditor are not only prevented in completing certain audit procedures but also are not able to obtain audit evidence even by performing alternative procedures. How you will deal with this situation? (MTP1, May 2022, 4 marks)</p> <p>As per SA 705, "Modifications to the Opinion in the Independent Auditor's Report", if, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall request that management remove the limitation.</p> <p>If management refuses to remove the limitation, the auditor shall communicate the matter to those charged with governance, unless all of those charged with governance are involved in managing the entity and determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence.</p> <p>If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall determine the implications as follows:</p> <ul style="list-style-type: none"> • If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive, the auditor shall qualify the opinion; or • If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall: <ul style="list-style-type: none"> ○ Withdraw from the audit, where practicable and possible under applicable law or regulation; or ○ If withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements. <p>If the auditor withdraws, before withdrawing, the auditor shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion.</p>
Q110.	<p>The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements." SA 200 explains the premise, relating to the responsibilities of management and, where</p>

	<p>appropriate, those charged with governance, on which an audit in accordance with SAs is conducted. Explain (ICAI Study Material - Test Your Knowledge) (RTP, Nov 2018, NA) (MTP2, May 2019, 4 marks) (MTP1, May 2020, 4 marks) (MTP2, May 2021, 4 marks) (MTP2, May 2023, 4 marks) (MTP1, May 2025, 5 Marks)</p> <p>Responsibilities for the Financial Statements: The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements."</p> <p>SA 200 explains the premise, relating to the responsibilities of management and, where appropriate, TCWG, on which an audit in accordance with SAs is conducted. Management and, where appropriate, TCWG accept responsibility for the preparation of FS. Management also accepts responsibility for such internal control as it determines is necessary to enable the preparation of FS that are free from material misstatement, whether due to fraud or error. The description of management's responsibilities in the auditor's report includes reference to both responsibilities as it helps to explain to users the premise on which an audit is conducted.</p> <p>This section of the auditor's report shall describe management's responsibility for:</p> <ol style="list-style-type: none"> Preparing FS in accordance with AFRF, and for such internal control as management determines is necessary to enable the preparation of FS that are free from material misstatement, whether due to fraud or error and Assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern. The explanation of management's responsibility for this assessment shall include a description of when the use of the going concern basis of accounting is appropriate.
Q111.	<p>Pure Services Limited is into litigation relating to some legal action initiated by the industry regulator. The matter has reached the jurisdictional High Court. Keeping in view uncertainty related to the future outcome of the matter, the statutory auditor of the company has decided to include the Emphasis of Matter (EOM) Paragraph in the auditor's report.</p> <ol style="list-style-type: none"> Briefly discuss the considerations to be taken care of by the statutory auditor when the EOM paragraph is included in the auditor's report. State any two examples of circumstances where the auditor may consider it necessary to include an EOM paragraph. <p>(MTP2, Sep 2024, 5 Marks)</p> <ol style="list-style-type: none"> When the auditor includes an Emphasis of Matter (EOM) paragraph in the auditor's report, the auditor shall:- <ol style="list-style-type: none"> include the paragraph within a separate section of the auditor's report with an appropriate heading that includes the term "Emphasis of Matter" include in the paragraph a clear reference to the matter being emphasized and to where relevant disclosures that fully describe the matter can be found in the financial statements. The paragraph shall refer only to information presented or disclosed in the financial statements and indicate that the auditor's opinion is not modified in respect of the matter emphasized. Examples of circumstances where the auditor may consider it necessary to include an Emphasis of Matter (EOM) paragraph are: <ol style="list-style-type: none"> An uncertainty relating to the future outcome of exceptional litigation or regulatory action. A significant subsequent event that occurs between the date of the financial statements and the date of the auditor's report. Early application (where permitted) of a new accounting standard that has a material effect on the financial statements. A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position

Q112.	<p>The senior member of the firm Kaur & Associates, Chartered Accountants, informed to its auditing staff that at the time of audit reporting regarding corresponding figures, when corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in specified circumstances. What are those exceptional circumstances?</p> <p>(SA, May 2022, 4 Marks) (MTP2, May 2025, 5 Marks) (SA, Nov 2019, 4 marks) (MTP1, Nov 2018, 5 Marks) (MTP1, Nov 2022, 4 Marks)</p>
	<p>When corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in the following circumstances.</p> <ul style="list-style-type: none"> • If the auditor's report on prior period FS was modified and the subject of modification is still unresolved, the auditor shall modify the current audit report also. In the Basis for Modification paragraph in the auditor's report, the auditor shall either <ul style="list-style-type: none"> ◦ Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or ◦ In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the <u>comparability</u> of the current period's figures and the corresponding figures. • If the auditor obtains audit evidence that a material misstatement exists in the prior period FS on which an unmodified opinion has been previously issued, the auditor shall verify whether the misstatement has been dealt with as required under the applicable financial reporting framework and, if that is not the case, the auditor shall express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, modified. • Prior Period Financial Statements Not Audited- If the prior period financial statements were not audited, the auditor shall state in an Other Matter paragraph in the auditor's report that the corresponding figures are unaudited. Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements
Q113.	<p>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. (MTP2, Sep 2024, 5 marks) (MTP1, Nov 2020, 6 Marks) (RTP, Nov 2018, NA) (MTP1, Nov 2018, 5 Marks)</p> <p>Reporting requirement relating to matters stated in section 143(1)</p> <p>Under section 143(1), auditor shall inquire into following matters given as under: -</p> <ol style="list-style-type: none"> a) whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members; b) whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company; c) where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other securities have been sold at a price less than that at which they were purchased by the company; d) whether loans and advances made by the company have been shown as deposits; e) whether personal expenses have been charged to revenue account; f) where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading.

	The auditor should make a report to the members in case he finds an answer to any of these matters in adverse .
Q114.	<p>ABC Ltd is a company incorporated in India. It has branches within and outside India. Explain who can be appointed as an auditor of these branches within and outside India. Also explain to whom branch auditor is required to report. (ICAI Study Material - Test Your Knowledge) (RTP, May 2020, NA)</p> <p>Branch Auditor:</p> <ul style="list-style-type: none"> • Section 143(8) of the Companies Act, 2013, prescribes the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor. • Where a company has a branch office, the accounts of that office shall be audited either by <ul style="list-style-type: none"> ○ the auditor appointed for the company i.e. company's auditor ○ any other person qualified for appointment as an auditor of the company under this Act ○ where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country • The branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary. • Further as per rule 12 of the Companies (Audit and Auditors) Rules, 2014, the branch auditor shall submit his report to the company's auditor and reporting of fraud by the auditor shall also extend to such branch auditor to the extent it relates to the concerned branch.
Q115.	<p>CA E was appointed statutory auditor of XYZ Private Limited in AGM held in the month of August, 2023 for the first time for audit of financial statements of the company from year 2023-24 onwards. Since he is new to the company, he wants to be sure about the integrity of accounting records. In this regard, he wants to ensure that software used by company for maintenance of its books of accounts is capable of tracking user activities and changes made to entries in books of accounts, if any, during the course of year. What CA E is looking for in the given situation? Discuss the reporting requirements for CA E in this matter to be included in audit report to be issued under the Companies Act, 2013. (MTP2, Nov 2023, 3 marks)</p> <p style="text-align: center;">OR</p> <p>As per 11(g) of the Companies (Audit and Auditors) Rules, 2014 auditor's report should state whether the accounting software used for maintaining its books of account has a feature of recording audit trail (edit log) facility. What are the reporting requirements under Rule 11(g)? (SA, Nov 2023, 3 marks)</p> <p>In the given situation, the auditor is looking for a feature of "audit trail" in software used by a company for maintenance of books of accounts. Under section 143(3) of Companies Act, 2013, it has to be reported by the auditor as under: -</p> <p>Whether the company has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and</p> <ul style="list-style-type: none"> • same has been operated throughout the year for all transactions recorded in the software and • audit trail feature has not been tampered with and • audit trail has been preserved by the company as per the statutory requirements for record retention.
Q116.	<p>Mr. A is appointed as statutory auditor of a company for the Financial Year ended 31st March, 2025. During the course of the audit, it was found that a few doubtful transactions had been committed by the finance manager who retired in March, 2025. The fraud was going on since last 2 -3 years and the total amount misappropriated exceeding ₹ 100 lakhs. As a statutory auditor, what would be the reporting responsibilities of Mr. A? (SA, May 2018, 5 marks) (MTP1, May 2021, 4 marks)</p> <p>Reporting Fraud to Central Government:</p> <ul style="list-style-type: none"> • As per section 143(12) of the Companies Act, 2013 read with Rule 13 of the Companies (Audit and

	<p>Auditors) Rules, 2014, if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of ₹ 1 crore or above, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as prescribed.</p> <ul style="list-style-type: none"> • However, in case of a fraud involving lesser than the specified amount, i.e. below ₹ 1 Cr., the auditor shall report the matter to the audit committee constituted u/s 177 or to the Board in other cases within such time and in such manner as may be prescribed • The companies, whose auditors have reported frauds to the audit committee or the Board but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as may be prescribed.
Q117.	<p>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 the years 2022-23 and 2023-24 has been about ₹ 300 crores during each of the above years. Business of the company has been profitable. Mr. G heads the 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. (MTP1, May 2024, 4 Marks)</p> <p>DOX Limited is in the business of providing courier services. As name of the company and given facts suggest: -</p> <ul style="list-style-type: none"> • It is not a small company under section 2(85) of Companies Act, 2013. • It is not a private company. • It is not a one person company. • It is not a banking or insurance company. • It is not a Section 8 company as it does not have charitable objects etc. <p>Therefore, it does not qualify for any exemption from applicability of CARO, 2020. Hence, reporting requirements under CARO, 2020 are applicable.</p> <p>While reporting under CARO, 2020, statutory auditor is required to report under clause (xiv) of paragraph 3 as under</p> <ul style="list-style-type: none"> • whether the company has an internal audit system commensurate with the size and nature of its business • whether the reports of the internal auditors for the period under audit were considered by the statutory auditor
Q118.	<p>State the matters to be included in the auditor's report as per CARO, 2020 regarding-</p> <ol style="list-style-type: none"> 1. in case the company has accepted deposits 2. Nidhi company <p>(MTP2, May 2018, 4 Marks)</p> <ol style="list-style-type: none"> 1. In case the company has accepted deposits [Clause (v)] in respect of deposits accepted by the company or amounts which are deemed to be deposits, whether the directives issued by RBI and the provisions of sections 73 to 76 or any other relevant provisions of the Companies Act and the rules made thereunder, where applicable, have been complied with, if not, the nature of such contraventions be stated; if an order has been passed by Company Law Board or National Company Law Tribunal or RBI or any court or any other tribunal, whether the same has been complied with or not; 2. Nidhi company [Clause (xii)] <ul style="list-style-type: none"> • whether the Nidhi Company has complied with the Net Owned Funds to Deposits in the ratio of 1:20 to meet out the liability;

- whether the Nidhi Company is maintaining **10% unencumbered term deposits** as specified in the Nidhi Rules, 2014 to meet out the liability;
- whether there has been any **default** in payment of **interest** on deposits or repayment thereof for any period and if so, the details thereof;

Q119.

ABC Ltd. is a public company, which has availed various loans and cash credit facilities from Banks and other financial institutions. The company has defaulted in repayments of such borrowings during the year under audit. What are the reporting requirements in this regard under the Companies (Auditor's Report) Order, 2020 ?

(SA, May 2023, 4 marks)

Repayment of loans or borrowing to a financial institution, bank, Government or dues to debenture holders
[Clause (ix) of Para 3 of CARO 2020]

a) whether the company has **defaulted** in **repayment** of **loans** or **other** borrowings or in the **payment** of **interest** thereon to any lender, if **yes**, the **period** and the **amount** of default to be reported as per the format below:-

Nature of borrowing, including debt securities	Name of lender	Amount not paid on due date	Whether principal or interest	No. of days delay or unpaid	Remarks, if any
	lender wise details to be provided in case of defaults to banks, financial institutions and Government.				

b) whether the company is a declared **wilful defaulter** by any bank or financial institution or other lender;

c) whether **term loans** were **applied** for the **purpose** for which the loans were obtained; if **not**, the **amount** of loan so **diverted** and the **purpose** for which it is used may be **reported**;

d) whether funds raised on **short term basis** have been utilized for long term purposes, if yes, the **nature** and **amount** to be indicated;

e) whether the company has taken any **funds** from any entity or person on account of or to meet the **obligations** of its **subsidiaries, associates or joint ventures**, if so, **details** thereof with **nature** of such transactions and the **amount** in each case;

f) whether the company has raised loans during the year on the **pledge** of **securities** held in its subsidiaries, joint ventures or associate companies, if so, give **details** thereof and also **report** if the company has **defaulted** in repayment of such loans raised;

Chapter 9 - Special Features of Audit of Different Types Of Entities

Q120.	<p>The Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971 provides certain powers to the C& AG in connection with performance of his duties. Discuss (MTP2, Nov 2021, 4 marks) (MTP2, Nov 2023, 4 marks) (MTP2, May 2020, 4 marks) (SA, May 2019, 3 marks) (MTP2, May 2023, 3 marks)</p> <p>The C&AG Act gives the following powers to the C&AG in connection with the performance of his duties-</p> <p>a) To inspect any office of accounts under the control of the Union or a State Government including office responsible for the creation of the initial or subsidiary accounts.</p> <p>b) To require that any accounts, books, papers and other documents which deal with or are otherwise relevant to the transactions under audit, be sent to specified places.</p> <p>c) To put such questions or make such observations as he may consider necessary to the person in charge of the office and to call for such information as he may require for the preparation of any account or report</p>
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	<p>which is his duty to prepare.</p> <p>d) In carrying out the audit, the C&AG has the power to dispense with any part of detailed audit of any accounts or class of transactions and to apply such limited checks in relation to such accounts or transactions as he may determine.</p>
Q121.	<p>Define Government Audit & explain its objectives. (ICAI Study Material - Test Your Knowledge) (SA, July 2021, 4 marks) (MTP2, Nov 2022, 4 Marks)</p> <p style="text-align: center;">OR</p> <p>Government audit has not only adopted the basic essentials of auditing as known and practised in the profession to suit the requirements of governmental transactions but has also added new concepts, techniques and procedures to the audit profession. Explain stating clearly the definition of Government auditing as discussed in U.N. Handbook on Govt Auditing and Developing Countries and also state Objectives of Govt audit. (RTP, May 2021, NA) (MTP2, May 2022, 4 marks)</p> <p>Government auditing is</p> <ul style="list-style-type: none"> the objective, systematic, professional and independent examination of financial, administrative and other operations of a public entity made subsequently to their execution for the purpose of evaluating and verifying them, presenting a report containing explanatory comments on audit findings together with conclusions and recommendations for future actions by the responsible officials and in the case of examination of financial statements, expressing the appropriate professional opinion regarding the fairness of the presentation <p>OBJECTIVES:</p> <ul style="list-style-type: none"> Accounting for Public Funds: Government audit serves as a mechanism or process for public accounting of government funds. Appraisal of Government policies: It also provides public accounting of the operational, management, programme and policy aspects of public administration as well as accountability of the officials administering them. Base for Corrective actions: Audit observations based on factual data collection also serve to highlight the lapses of the lower hierarchy, thus helping supervisory level officers to take corrective measures Administrative Accountability: The main objective of audit is a combination of ensuring accountability of administration to legislature and functioning as an aid to administration.
Q122.	<p>Audit against rules and orders aims to ensure that the expenditure conforms to the relevant provisions of the Constitution and of the laws and rules made thereunder. The job of audit is to see that these rules, regulations and orders are applied properly by the subordinate authorities. It is, however, not the function of audit to prescribe what such rules, regulations and orders shall be. Analyse and Explain (RTP, Nov 2020, NA) (MTP2, May 2022, 4 marks)</p> <p>Audit against Rules & Orders:</p> <p>Audit against rules and orders aims to ensure that the expenditure conforms to the relevant provisions of the Constitution and of the laws and rules and orders issued by a competent authority</p> <p>These rules, regulations and orders against which regularity audit is conducted mainly fall under the following categories:</p> <ol style="list-style-type: none"> Rules and orders regulating the powers to incur and sanction expenditure from the Consolidated Fund of India or of a State Rules and orders dealing with the mode of presentation of claims in general the financial rules prescribing the detailed procedure to be followed by government servants in dealing with government transactions; Rules and orders regulating the conditions of service, pay and allowances, and pensions of government

	<p>servants.</p> <p>It is the function of the executive government to frame rules, regulations and orders, which are to be observed by its subordinate authorities. The job of audit is to see that these rules, regulations and orders are applied properly by the subordinate authorities. It is, however, not the function of audit to prescribe what such rules, regulations and orders shall be.</p> <p>But, it is the function of audit to carry out examination of the various rules, regulations and orders issued by the executive authorities to see that:</p> <ul style="list-style-type: none"> • they are not inconsistent with any provisions of the Constitution or any laws made thereunder; • they are consistent with the essential requirements of audit and accounts as determined by the C&AG; • they do not come in conflict with the orders of, or rules made by, any higher authority; and • in case they have not been separately approved by competent authority, the issuing authority possesses the necessary rule-making power.
Q123.	<p>Audit against the propriety seeks to ensure that expenditure conforms to certain principles. Explain (MTP1, Nov 2019, 4 marks)</p> <p style="text-align: center;">OR</p> <p>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. (MTP2, May 2024, 4 Marks)</p> <p>Audit against propriety seeks to ensure that expenditure conforms to these principles which have been stated as follows:</p> <ol style="list-style-type: none"> The expenditure should not be prima facie more than the occasion demands. Every public officer is expected to exercise the same vigilance in respect of expenditure incurred from public moneys as a person of ordinary prudence would exercise in respect of expenditure of his own money. No authority should exercise its powers of sanctioning expenditure to pass an order which will be directly or indirectly to its own advantage. Public moneys should not be utilised for the benefit of a particular person or section of the community unless: <ol style="list-style-type: none"> the amount of expenditure involved is insignificant; or a claim for the amount could be enforced in a Court of law; or the expenditure is in pursuance of a recognised policy or custom; and the amount of allowances, such as travelling allowances, granted to meet expenditure of a particular type should be so regulated that the allowances are not, on the whole, sources of profit to the recipients.
Q124.	<p>Before commencing the Audit of Local Bodies, a Chartered Accountant employee in firm of XYZ & Co., firm of Chartered Accountants seeks assistance of Mr. X, partner, in preparation of audit programme for local bodies. How Mr. X should advise to him in this connection? (MTP2, Nov 2023, 4 marks)</p> <p>Audit Programme for local bodies</p> <ol style="list-style-type: none"> The Local Fund Audit Wing of the State Government is generally in-charge of the audit of municipal accounts. Sometimes bigger municipal corporations e.g. Delhi, Mumbai etc have power to appoint their own auditors for regular external audit. So the auditor should ensure his appointment. The auditor while auditing the local bodies should report on the <ul style="list-style-type: none"> • fairness of the contents and presentation of financial statements, • strengths and weaknesses of system of financial control, • adherence to legal and/or administrative requirements; • whether value is being fully received on money spent. • His objective should be to detect errors and fraud and misuse of resources. The auditor should ensure that the expenditure incurred conforms to the relevant provisions of the law and is in accordance with the financial rules and regulations framed by the competent authority.

	<p>iv) He should ensure that all types of sanctions, either special or general, accorded by the competent authority.</p> <p>v) He should ensure that there is a provision of funds and the expenditure is incurred from the provision and the same has been authorized by the competent authority.</p> <p>vi) The auditor should check that the different schemes, programmes and projects, where large financial expenditure has been incurred, are running economically and getting the expected results.</p>
Q125.	<p>On 1st May 2022, NGO has been founded with the objective of disaster relief registered under section 8 of the Companies Act, 2013. In addition to corpus contribution, substantial foreign contributions also have been received by NGO. You have been appointed as the first auditor of the said NGO for the F.Y. 2022-23. While planning the audit of NGO which points you will focus upon ? Mention any four such points. (SA, Nov 2023, 4 marks) (RTP, Nov 2021, NA) (MTP2, May 2025, 5 marks) (ICAI Study Material - Test Your Knowledge) (RTP, Nov 2018, NA)</p> <p>While planning the audit, the auditor may concentrate on the following:</p> <ol style="list-style-type: none"> Knowledge of the NGO's work, its mission and vision, areas of operations and environment in which it operate. Updating knowledge of relevant statutes especially with regard to recent amendments, circulars, judicial decisions viz. Foreign Contribution (Regulation) Act 2010, Societies Registration Act, 1860, Income Tax Act 1961 etc. and the Rules related to the statutes. Reviewing the legal form of the Organisation and its Memorandum of Association, Articles of Association, Rules and Regulations. Reviewing the NGO's Organisation chart, then Financial and Administrative Manuals, Project and Programme Guidelines, Funding Agencies Requirements and formats, budgetary policies if any. Examination of minutes of the Board/Managing Committee/Governing Body/ Management and Committees thereof to ascertain the impact of any decisions on the financial records. Study the accounting system, procedures, internal controls and internal checks existing for the NGO and verify their applicability. Setting of materiality levels for audit purposes. The nature and timing of reports or other communications. The involvement of experts and their reports. Review the previous year's Audit Report.
Q126.	<p>You are appointed as an auditor of M/s Shine & Co., a partnership firm. During your review, you observed that:</p> <ul style="list-style-type: none"> The audit appointment was informal and not documented properly. The firm started a new business activity which is not covered in the partnership deed. Major financial decisions were made without proper records. <p>As an auditor, briefly explain the matters that should be specially considered by you while auditing the accounts of the partnership firm, M/s Shine & Co. (RTP, Sep 2025, NA)</p> <p>While auditing the accounts of M/s Shine & Co., a partnership firm, it is important to ensure that they have formal appointment. Further, deviation from the partnership deed, and absence of documentation for key decisions raise concerns about the validity, transparency, and legal compliance of the firm's operations. Thus, the auditor should specially consider the following matters in the audit of accounts of a partnership:</p> <ul style="list-style-type: none"> Letter of Appointment: Confirming that the letter of appointment, signed by a partner, duly authorised, clearly states the nature and scope of audit contemplated by the partners, specially the limitation, if any. Partnership Documents: Studying the minute book, if any, maintained to record the policy decision taken by partners specially the minutes relating to authorisation of extraordinary and capital expenditure, raising of loans; purchase of assets, extraordinary contracts entered into and other such matters as are not of a routine nature. Objects of Partnership: Verifying that the business in which the partnership is engaged is authorised by the partnership agreement; or by any extension or modification thereof agreed to subsequently.

	<ul style="list-style-type: none"> • Books of Account: Examining whether books of account appear to be reasonable and are considered adequate in relation to the nature of the business of the partnership. • Mutual Interest: Verifying generally that the interest of no partner has suffered prejudicially by an activity engaged in by the partnership which, it was not authorised to do under the partnership deed or by any violation of a provision in the partnership agreements. • Provision for Taxes: Confirming that a provision for the firm's tax payable by the partnership has been made in the accounts before arriving at the amount of profit divisible among the partners. • Division of Profits: Verifying that the profits and losses have been divided among the partners in their agreed profit-sharing ratio.
Q127.	<p>CA B is appointed as the auditor of a Public Charitable Trust. Guide him the focus area of attention relating to the vouching and verification of expenditure of charitable institution (SA, May 2023, 3 marks)</p> <p>Audit of Expenditure of Charitable Institution:</p> <ul style="list-style-type: none"> • Vouching payment of grants, also verifying that the grants have been paid only for a charitable purpose or purposes falling within the purview of the objects for which the charitable institution has been set up and that no trustee, director or member of the Managing Committee has benefited there from either directly or indirectly. • Verifying the schedules of securities held, as well as inventories of properties both movable and immovable by inspecting the securities and title deeds of property and by physical verification of the movable properties on a test- basis. • Verifying the cash and bank payments. • Ascertaining that any funds contributed for a special purpose have been utilised for the purpose.
Q128.	<p>You have been appointed as an auditor of a health care service provider. Briefly discuss the special points that should be kept in mind as an auditor for developing an audit programme. (SA, July 2021, 4 marks) (MTP1, May 2022, 6 marks) (MTP1, Nov 2021, 4 marks) (SA, Nov 2019, 4 marks) (MTP1, May 2019, 6 marks) (MTP1, May 2018, 5 marks) (MTP1, Nov 2018, 5 marks) (MTP2, Nov 2018, 5 marks) (ICAI Study Material - Test Your Knowledge)</p> <p>The special steps involved in such an audit are stated below</p> <ol style="list-style-type: none"> 1. Register of Patients: Vouch the Register of patients with copies of bills issued to them. Verify bills for a selected period with the patients' attendance record to see that the bills have been correctly prepared. Also see that bills have been issued to all patients from whom an amount was recoverable according to the rules of the hospital. 2. Collection of Cash: Check cash collections as entered in the Cash Book with the receipts, counterfoils and other evidence for example, copies of patients bills, counterfoils of dividend and other interest warrants, copies of rent bills, etc. 3. Income from Investments, Rent etc: See with reference to the property and Investment Register that all income that should have been received by way of rent on properties, dividends, and interest on securities have been collected. 4. Legacies and Donations: Ascertain that legacies and donations received for a specific purpose have been applied in the manner agreed upon. 5. Reconciliation of Subscriptions: Trace all collections of subscription and donations from the Cash Book to the respective Registers. Reconcile the total subscriptions due (as shown by the Subscription Register and the amount collected and that still outstanding). 6. Authorisation and Sanctions: Vouch all purchases and expenses and verify that the capital expenditure was incurred only with the prior sanction of the Trustees or the Managing Committee and that appointments and increments to staff have been duly authorised. 7. Grants and TDS: Verify that grants, if any, received from Government or local authority has been duly accounted for. Also, that refund in respect of taxes deducted at source has been claimed. 8. Budgets: Compare the totals of various items of expenditure and income with the amount budgeted for them and report to the Trustees or the Managing Committee, significant variations which have taken place.

	<p>9. Internal Check: Examine the internal check as regards the receipt and issue of stores; medicines, linen, apparatus, clothing, instruments, etc. so as to ensure that purchases have been properly recorded in the Inventory Register and that issues have been made only against proper authorisation.</p> <p>10. Depreciation: See that depreciation has been written off against all the assets at the appropriate rates.</p> <p>11. Registers: Inspect the bonds, share scrips, title deeds of properties and compare their particulars with those entered in the property and Investment Registers.</p> <p>12. Inventories: Obtain inventories, especially of stocks and stores as at the end of the year and check a percentage of the items physically; also compare their total values with respective ledger balances.</p> <p>13. Management Representation and Certificate: Get proper Management Representation and Certificate with respect to various aspects covered during the course of audit.</p>
Q129.	<p>You have been appointed as internal auditor of 'City Club' in Delhi. The receipts of the club were ₹ 50 lakhs during the previous year ending 2023-24. You are required to mention special points of consideration while auditing such receipts of the club. (SA, Jan 2021, 4 marks) (MTP2, May 2018, 5 marks) (ICAI Study Material - Test Your Knowledge) (MTP1, May 2023, 4 marks)</p> <p style="text-align: center;">OR</p> <p>You are appointed as an auditor of "The Prestigious Township Club". As the auditor of "The Prestigious Township Club" for the financial year 2023-24, what are the key points you would consider while auditing the income and expenditure items of the club? (MTP1, Jan 2025, 5 marks)</p> <p>The special steps involved in an audit of club are stated below-</p> <ol style="list-style-type: none"> Entrance Fee: Vouch the receipt on account of entrance fees with members' applications, counterfoils issued to them, as well as on a reference to minutes of the Managing Committee. Subscriptions: Vouch members' subscriptions with the counterfoils of receipt issued to them, trace receipts for a selected period to the Register of Members; also reconcile the amount of total subscriptions due with the amount collected and that outstanding. Arrears of Subscriptions: Ensure that arrears of subscriptions for the previous year have been correctly brought over and arrears for the year under audit and subscriptions received in advance have been correctly adjusted. Arithmetical accuracy: Check totals of various columns of the Register of members and tally them across. Irrecoverable Member Dues: See the Register of Members to ascertain the Member's dues which are in arrear and enquire whether necessary steps have been taken for their recovery; the amount considered irrecoverable should be mentioned in the Audit Report. Pricing: Verify the internal check as regards members being charged with the price of foodstuffs and drinks provided to them and their guests, as well as, with the fees chargeable for the special services rendered, such as billiards, tennis, etc. Member Accounts: Trace debits for a selected period from subsidiary registers maintained in respect of supplies and services to members to confirm that the account of every member has been debited with amounts recoverable from him. Purchases: Vouch purchase of sports items, furniture, crockery, etc. and trace their entries into the respective inventory registers Margins earned: Vouch purchases of foodstuffs, cigars, wines, etc., and test their sale price so as to confirm that the normal rates of gross profit have been earned on their sales. The inventory of unsold provisions and stores, at the end of year, should be verified physically and its valuation checked. Management Powers: Examine the financial powers of the secretary and, if these have been exceeded, report specific case for confirmation by the Managing Committee.
Q130.	<p>You have been appointed as an auditor of ABC Hotel, a three star hotel, for Financial Year 2023-24. As an auditor what are the special points that need to be considered in verifying the Inventories in the nature of food and beverages?</p> <p>(RTP, Nov 2022, NA) (MTP2, Nov 2023, 4 Marks) (MTP1, May 2024, 4 Marks) (MTP1, Nov 2022, 4 Marks)</p>

	<p>Verification of inventories in the nature of food and beverages: The inventories in any hotel are both readily portable and saleable particularly the food and beverage inventories. It is therefore extremely important that all movements and transfers of such inventories should be properly documented to enable control to be exercised over each individual stores' areas and sales point. The auditor should carry out tests to ensure that all such documentation is accurately processed. Therefore, following points may be noted in this regard:</p> <ol style="list-style-type: none"> All movement and transfer of inventories must be properly documented. Areas where inventories are kept must be kept locked and the key retained by the departmental manager. The key should be released only to trusted personnel and unauthorized persons should not be permitted in the stores area. Many hotels use specialized professional valuers to count and value the inventories on a continuous basis throughout the year The auditor should ensure that all inventories are valued at the year end and that he should himself be present at the year-end physical verification, to the extent practicable, having regard to materiality consideration and nature and location of inventories.
Q131.	<p>Pilfering is one of the greatest problems in any hotel and the importance of internal control cannot be undermined. Explain. (RTP, May 2022 ,NA) (MTP2, Nov 2023, 4 marks) (RTP, May 2024, NA) (MTP1, Nov 2022, 3 Marks)</p> <ul style="list-style-type: none"> Pilfering is one of the greatest problems in any hotel and the importance of internal control cannot be undermined. It is the responsibility of management to introduce controls which will minimise the leakage as far as possible. Evidence of their success is provided by the preparation of regular perhaps weekly, trading accounts for each sales point and a detailed scrutiny of the resulting profit percentages, with any deviation from the anticipated form being investigated. The auditor should obtain these regular trading accounts for the period under review, examine them and obtain explanations for any apparent deviations. The auditor should verify a few restaurant bills by reference to K.O.T.s (Kitchen Order Tickets) or basic record. This would enable the auditor to ensure that controls regarding revenue cycle are in order. The auditor should satisfy himself that all taxes collected from occupants on food and occupation have been paid over to the proper authorities. If the internal control in a hotel is weak or perhaps breaks down, then a very serious problem exists for the auditor. As a result of the transient nature of many of his clients' records, the auditor must rely to a very large extent on the gross margin shown by the accounts. As a result, the scope of his audit tests will necessarily be increased and, in the event of a material margin discrepancy being unexplained, he will have to consider qualifying his audit report
Q132.	<p>CA. Z, a Chartered Accountant is the Senior manager of a Multi-State co-operative society in Mumbai. He is proposed to be appointed as an auditor of the said Multi-State Co-operative society. Analyse the provisions of the Multi-State Co-operative Societies Act, 2002 and comment on validity of proposed appointment (SA, May 2023, 4 marks) (MTP1, Sep 2024, 4 Marks) (MTP1, Nov 2018, 5 marks)</p> <p>Section 72 of the Multi-State Co-operative Societies Act, 2002 states that a person who is a Chartered Accountant within the meaning of the Chartered Accountants Act, 1949 can only be appointed as auditor of Multi-State co-operative society. However the following persons are not eligible for appointment as auditors of a Multi- State co-operative society-</p> <ol style="list-style-type: none"> A body corporate. An officer or employee of the Multi-State co-operative society. A person who is a member or who is in the employment of an officer or employee of the Multi-State co-operative society. A person who is indebted to the Multi-State co-operative society or who has given any guarantee or provided any security in connection with the indebtedness of any third person to the Multi-State co-operative society for an amount exceeding ₹ 1000

	<p>In the given case, CA. Z, a Chartered Accountant is the Senior manager of a Multi-State co-operative society who is proposed to be appointed as an auditor of the said Multi-State Co-operative society.</p> <p>Conclusion: The person who is an employee of the MultiState co-operative society is not eligible for appointment as auditor of a Multi-State cooperative society. The proposed appointment is not valid.</p>
Q133.	<p>No inspection under Section 79 of Multi-State Co-operative Societies Act, 2002 shall be made unless a notice has been given to the multi-state co-operative society. Explain stating clearly when and how such inspection can be made. Also state the powers available with the Central Registrar in this regard along with provisions relating to communication of the inspection report under the said section (RTP, May 2022, NA) (MTP1, May 2025, 5 Marks)</p> <p>Inspection of Multi-State Co-operative societies under Section 79</p> <ol style="list-style-type: none"> When: The Central Registrar may, on a request from <ul style="list-style-type: none"> federal co-operative to which a Multi- State Co-operative society is affiliated or a creditor or not less than one-third of the members of the board or not less than one-fifth of the total number of members of a Multi-State co-operative society How: By general or special order in writing in this behalf inspect or direct any person authorized by him by order in writing in this behalf to make an inspection into the constitution, working and financial condition of a Multi- State co-operative society. Opportunity of Being heard: No inspection shall be made unless a notice of not less than 15 days has been given to the multi-state co-operative society. Powers available: The Central Registrar or the person authorized by him shall have the following powers: <ol style="list-style-type: none"> He shall at all times have access to all books, accounts, papers, vouchers, securities, stock and other property of that society and may, in the event of serious irregularities discovered during inspection, take them into custody and shall have power to verify the cash balance of the society and subject to the general or special order of the central registrar to call a meeting of the society where such general meeting is, in his opinion necessary. Every officer or member of a Multi-State Co-operative society shall furnish such information with regard to the working of the society as the central registrar or the person making such inspection may require. Inspection Report: A copy of the report of inspection under this section shall be communicated to the Multi-State Co-operative society within a period of 3 months from the date of completion of such inspection.
Q134.	<p>Central Govt. hold 55% of the paid up share Capital in Kisan Credit Co-operative Society, which is incurring huge losses. Advise when the Central Government can direct Special Audit under Section 77 of the Multi State Co-operative Society Act. (SA, May 2019, 3 marks) (MTP2, May 2023, 3 marks)</p> <p style="text-align: center;">OR</p> <p>Section 77 of Multi-State Cooperative Societies Act, 2002 states that the Central Government may at any time by order direct that a special audit of the Multi-State Cooperative Society's accounts for such period or periods as may be specified in the order, shall be conducted. Further, it may by the same or a different order appoint either a Chartered Accountant or the Multi-State Cooperative Society's auditor himself to conduct special audit. Under which circumstances such power can be exercised by the Central Government? (RTP, Sep 2024, NA)</p> <p>Central Government shall order for special audit only if that Government or the State Government either by itself or both hold 51% or more of the paid-up share capital in such Multi-State co-operative society.</p> <p>Under section 77 of the Multi-State Co-operative Societies Act, 2002, where the Central Government is of the opinion:</p>

- a) that the **affairs** of any Multi-State co-operative society are **not being managed** in accordance with self-help and mutual deed and co-operative principles or prudent commercial practices or with sound business principles; or
- b) that any Multi-State co-operative society is being **managed** in a manner likely to **cause serious injury** or damage to the interests of the trade industry or business to which it pertains; or
- c) that the **financial position** of any Multi-State co-operative society is such as to endanger its solvency.

Thus, in the given case since the Central Govt is holding 55% shares and the financial position of Kisan Credit co-operative society is in danger, the Central government can **direct for special audit**.

Chapter 10 - Audit of Banks

- Q135. "The engagement team should hold discussions to gain better understanding of the bank and its environment, including internal control, and also to assess the potential for material misstatements of the financial statements. All these discussions should be appropriately documented for future reference". Explain.
(ICAI Study Material - Test Your Knowledge) (MTP1, May 2018, 5 marks) (MTP1, May 2019, 4 Marks) (SA, May 2019, 4 Marks) (SA, Nov 2019, 3 Marks)

All personnel performing an engagement, including any experts contracted by the firm in connection with that engagement are known to be the "Engagement Team".

The engagement team should hold discussions

- to gain better understanding of the bank and its environment, including internal control, and also
- to assess the potential for material misstatements of the financial statements.

All these discussions should be appropriately documented for future reference. These discussions are ordinarily done at the planning stage of an audit.

Matters to be discussed:

- **Errors** that may be more **likely** to occur;
- **Errors** which have been identified in **prior years**;
- Method by which **fraud** might be perpetrated by bank personnel or others within particular account balances and/or disclosures;
- Audit **responses** to Engagement Risk, Pervasive Risks, and Specific Risks;
- Need to maintain professional **skepticism** throughout the audit engagement;
- **Need to alert** for information or other conditions that indicates that a material misstatement may have occurred

- Q136. During the audit of Smile Bank, CA Sweety focused on understanding the risk management process of the bank. She reviewed how management developed controls and used performance indicators to monitor key business and financial risks. CA Sweety also assessed whether the risk management system effectively identified and mitigated risks in required areas. How should CA Sweety evaluate the adequacy of the bank's risk management controls? (MTP2, Jan 2025, 5 marks) (SA, May 2019, 4 Marks) (RTP, May 2023, NA) (MTP1, Nov 2022, 4 Marks)

An effective risk management system in a bank generally requires the following:

1. **Oversight and involvement in the control process by those charged with governance:**

- Those charged with governance (BOD/Chief Executive Officer) should approve **written risk management policies**.
- The policies should be **consistent** with the **bank's business objectives** and strategies, capital strength, management expertise, regulatory requirements and the types and amounts of risk it regards as acceptable.

2. **Identification, measurement and monitoring of risks:** Risks that could significantly impact the achievement of a bank's goals should be **identified, measured** and **monitored** against **pre-approved limits** and **criteria**.
3. **Control activities:** A bank should have **appropriate controls** to manage its risks, including effective segregation of duties, accurate measurement and reporting of positions, verification and approval of transactions, reconciliation of positions and results, setting of limits, reporting and approval of exceptions, physical security and contingency planning.
4. **Monitoring activities:** Risk management **models, methodologies** and **assumptions** used to measure and manage risk should be regularly assessed and updated. This function may be conducted by the **independent risk management unit**.
5. **Reliable information systems:** Banks require reliable information systems that provide adequate **financial, operational** and **compliance** information on a **timely** and **consistent** basis. Those charged with governance and management require risk management information that is easily understood and that enables them to **assess** the changing nature of the **bank's risk profile**

Q137. Advances generally constitute the major part of the assets of the bank. There are a large number of borrowers to whom a variety of advances are granted. The audit of advances requires the major attention from the auditors. In carrying out audit of advances, the auditor is primarily concerned with obtaining evidence about, among other points, the amounts included in the balance sheet in respect of advances are outstanding at the date of the balance sheet. Explain

(RTP, Nov 2019, NA) (RTP, May 2021, NA) (RTP, Nov 2022, NA) (RTP, Nov 2023, NA)

OR

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. (MTP2, May 2024, 4 Marks)

In carrying out audit of advances, the auditor is primarily concerned with obtaining evidence about the following:

- **Amounts** included in the balance sheet in respect of advances are **outstanding** at the date of the balance sheet.
- Advances represent the **amount due to the bank**.
- Amounts due to the bank are appropriately **supported by Loan documents** and **other** documents as applicable to the **nature** of advances.
- There are **no unrecorded advances**.
- The stated basis of **valuation** of advances is appropriate and properly applied, and that the recoverability of advances is recognised in their valuation.
- The advances are **disclosed, classified** and **described** in accordance with recognised accounting policies and practices and relevant statutory and regulatory requirements.

	<ul style="list-style-type: none">Appropriate provisions towards advances have been made as per the RBI norms, Accounting Standards and generally accepted accounting practices																				
Q138.	<p>Explain "Advances under Consortium" in the context of Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances. (SA, Jan 2021, 4 Marks) (MTP2, Nov 2021, 4 Marks) (MTP1, Nov 2023, 3 marks)</p> <p>Advances under Consortium:</p> <ul style="list-style-type: none">Consortium advances should be based on the record of recovery of the respective individual member banks and other aspects having a bearing on the recoverability of the advances.Where the remittances by the borrower under consortium lending arrangements are pooled with one bank and/or where the bank receiving remittances is not parting with the share of other member banks, the account should be treated as not serviced in the books of the other member banks and therefore, an NPA.The banks participating in the consortium, therefore, need to arrange to get their share of recovery transferred from the lead bank or to get an express consent from the lead bank for the transfer of their share of recovery, to ensure proper asset classification in their respective books.																				
Q139.	<p>During the course of statutory branch audit of a nationalised 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 exists 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. (MTP2, Sep 2024, 5 marks)</p> <p>In a banking environment, there exists documentary evidence containing observations/comments on advances which can be useful to the statutory branch auditor in performing an effective audit. CA Amrish, the auditor should take into account the adverse comments, if any, on advances appearing in the following:-</p> <ul style="list-style-type: none">Previous year's audit reports.Latest internal inspection reports of bank officials.Reserve Bank's latest inspection report.Concurrent / Internal audit report.Report on verification of security.Any other internal reports specially related to particular accounts.Manager's charge-handing-over report when incumbent is changed																				
Q140.	<p>Agrim, a CA student, is part of an engagement team conducting an audit of the Madurai branch of ARB Bank. CA Bhuvan, engagement partner, has asked him to verify provision made by branch as on March 31st, 2024 in respect of the following non-performing assets: -</p> <table><tr><th>Name of Account</th><th>NPA classification</th><th>Outstanding amount as on March 31st, 2024 (In ₹ lakhs)</th><th>Amount of provision made (In ₹ lakhs)</th></tr><tr><td>AK Industries</td><td>Doubtful (D1)</td><td>10.00</td><td>5.00</td></tr><tr><td>Jupiter Traders</td><td>Substandard asset</td><td>50.00</td><td>7.50</td></tr><tr><td>VT & Co.</td><td>Doubtful (D2)</td><td>30.00</td><td>30.00</td></tr><tr><td>ASD & Sons</td><td>Loss</td><td>1.00</td><td>1.00</td></tr></table> <p>The engagement partner has already verified NPA classification. Outstanding amounts as on March 31st, 2024, relating to each NPA account listed above (except ASD & Sons) are fully secured. However, only personal guarantee of proprietor (Net worth of proprietor ₹ 50 lakhs) is available in account of ASD & Sons. Comment on the correctness of the above provisions.</p>	Name of Account	NPA classification	Outstanding amount as on March 31st, 2024 (In ₹ lakhs)	Amount of provision made (In ₹ lakhs)	AK Industries	Doubtful (D1)	10.00	5.00	Jupiter Traders	Substandard asset	50.00	7.50	VT & Co.	Doubtful (D2)	30.00	30.00	ASD & Sons	Loss	1.00	1.00
Name of Account	NPA classification	Outstanding amount as on March 31st, 2024 (In ₹ lakhs)	Amount of provision made (In ₹ lakhs)																		
AK Industries	Doubtful (D1)	10.00	5.00																		
Jupiter Traders	Substandard asset	50.00	7.50																		
VT & Co.	Doubtful (D2)	30.00	30.00																		
ASD & Sons	Loss	1.00	1.00																		

Agrim is in dilemma regarding classification of above accounts as NPA although these are fully secured or guaranteed. Guide him. (RTP, Jan 2025, NA)

The auditor is required to ensure that provision for NPA is made as per its classification in different categories which are given as under:

Categories of Non-Performing Assets:	Provision required
<ul style="list-style-type: none"> Substandard Assets: Would be one, which has remained NPA for a period less than or equal to 12 months. 	15%
<ul style="list-style-type: none"> Doubtful Assets: Would be one which has remained in the substandard category for a period of 12 months. Sub-categories: Doubtful up to 1 Year (D1) Doubtful 1 to 3 Years (D2) Doubtful more than 3 Years (D3) 	(Secured + Unsecured) 25% + 100% 40% + 100% 100% + 100%
<ul style="list-style-type: none"> Loss Assets 	100%

From the above provision, it can be concluded that in case of:

AK Industries- It has been classified as **Doubtful (D1) category**. Therefore, it requires provision of 25% of secured amount. That is provision of ₹ 2.50 lakh (i.e 25% of ₹10 lakh) should be made instead of ₹ 5 lakh.

Jupiter Traders- It has been classified as **Substandard asset**. It requires provision of 15% of outstanding amount (i.e 15% of ₹ 50 lakhs) which comes to ₹ 7.50 lakh. Therefore, provision made by the branch is **correct**.

VT & Co.- It has been classified as **Doubtful (D2) category**. It requires provision of 40% of secured amount. That is, a provision of ₹ 12.00 lakh (40% of ₹ 30 lakhs) should be made instead of ₹ 30 lakh.

ASD & Sons- It has been classified as a **loss asset** which requires **provision** of **100%** of outstanding amount. Therefore, the provision made by the branch is correct.

Classification as NPA should be based on the record of **recovery**. Availability of **security** or **net worth** of borrower/guarantor is **not to be taken** into **account** for the purpose of treating an advance as NPA or otherwise.

Hence, these accounts have been **classified** as **NPA** on the record of recovery although these are fully secured or guaranteed.

Q141. Ramjilal & Co. had been allotted the branch audit of a nationalized bank for the year ended 31st March, 2025. In the audit planning, the partner of Ramjilal & Co., observed that the allotted branches are predominantly based in rural areas and major portion of the advances were for agricultural purpose."

Now he needs your assistance on the following points so as to incorporate them in the audit plan:

- for determination of NPA norms for agricultural advances
- for accounts where there is erosion in the value of security/frauds committed by the borrowers.

(SA, Nov 2018, 5 marks)

NPA norms for Agricultural Advances:

- As per the guidelines, Agricultural Advances are of two types:

- Agricultural Advances for **“long duration”** crops; and
- Agricultural Advances for **“short duration”** crops.
- The “long duration” crops would be crops **with a crop season longer than one year** and crops, which are not “long duration” crops would be treated as “short duration” crops.
- The crop season for each crop, which means the **period up to harvesting of the crops raised**, would be as determined by the State Level Bankers’ Committee in each State.
- The following NPA norms would apply to agricultural advances (including Crop Term Loans):
 - A loan granted for **short duration crops** will be treated as **NPA**, if the instalment of principal or interest thereon remains overdue for **two crop seasons**; and
 - A loan granted for **long duration crops** will be treated as NPA, if the instalment of principal or interest thereon remains overdue for **one crop season**.

NPA norms where there is erosion in the value of security/frauds committed by borrowers:

In case there arises erosion in the value of security or any frauds committed by borrowers, banks can straightaway classify these accounts as doubtful or loss assets, as appropriate.

- Erosion in the value of security can be reckoned as significant when the **realisable value of the security is less than 50%** of the value assessed by the bank or accepted by RBI at the time of last inspection, as the case may be. Such NPAs may be straightaway classified under **doubtful category** and provisioning should be made as applicable to doubtful assets.
- If the realizable value of the security, as assessed by the bank/ approved valuers/ RBI is **less than 10% of the outstanding in the borrowal accounts**, the existence of security should be ignored and the asset should be straightaway classified as a **loss asset**. It may be either written off or fully provided for by the bank.

Q142. The auditor should examine the efficacy of various internal controls over advances in case of Banks to determine the nature, timing and extent of his substantive procedures. Explain what is included in the internal controls over advances
(RTP, Nov 2018, NA) (SA, Nov 2018, 5 Marks) (RTP, May 2019, NA) (MTP2, May 2019, 4 Marks) (MTP1, May 2022, 4 marks)

The auditor should examine the efficacy of various internal controls over advances to determine the nature, timing and extent of his substantive procedures. The internal controls over advances include the following:

- i) The bank should make an advance only after evaluating **credit worthiness** of the borrower and after obtaining **sanction** from the appropriate **authorities** of the bank.
- ii) **All the necessary documents** such as agreements, demand promissory notes, letters of hypothecation, etc. should be executed by the parties before advances are made.
- iii) The **compliance** with the **terms** of sanction and **end use** of funds should be ensured.
- iv) Sufficient margin as specified in the sanction letter should be kept against securities taken so as to **cover** for any **decline** in the value thereof. The availability of sufficient margin needs to be ensured at regular intervals.
- v) If the securities taken are in the nature of shares, debentures, etc., the **ownership** of the same should be **transferred** in the name of the **bank** and the effective control of such securities be retained as a part of documentation.
- vi) All securities requiring registration should be **registered** in the **name** of the **bank** or otherwise accompanied by documents sufficient to give title to the bank.
- vii) In the case of goods in the possession of the bank, **contents** of the packages should be **tested** at the time of receipt. The godowns should be frequently **inspected** by **responsible officers** of the branch concerned, in addition to the inspectors of the bank.
- viii) Drawing Power Register should be **updated every month** to record the value of securities hypothecated and entries should be checked by an officer.
- ix) The accounts should be kept within **both** the **drawing power** and the **sanctioned limit**.
- x) All the accounts which exceed the sanctioned limit or drawing power or are otherwise **irregular** should be brought to the **notice** of the controlling authority regularly.

	xi) The operation of each advance account should be reviewed at least once a year .
Q143.	<p>In carrying out audit of income, the auditor is primarily concerned with obtaining reasonable assurance that the recorded income arose from transactions, which took place during the relevant period and pertained to the bank, there is no unrecorded income and the income is recorded at appropriate amount. Explain the Audit Approach and Procedures regarding following points in the above context :</p> <ol style="list-style-type: none"> RBI's Directions Materiality Revenue Certainty Revenue Uncertainty <p>(MTP2, May 2022, 4 marks)</p> <p>Audit Approach and Procedures:</p> <ol style="list-style-type: none"> RBI's Directions: RBI has advised that in respect of any income which exceeds one percent of the total income of the bank if the income is reckoned on a gross basis or one percent of the net profit before taxes if the income is reckoned net of costs, should be considered on accrual as per AS 9. Materiality: If any item of income is not considered to be material as per the above norms, it may be recognised when received and the auditors need not qualify their report in that situation. Revenue Certainty: Banks recognise income (such as interest, fees and commission) on accrual basis, i.e., as it is earned. It is an essential condition for accrual of income that it should not be unreasonable to expect its ultimate collection. In modern day banking, the entries for interest income on advances are automatically generated through a batch process in the CBS system. Revenue Uncertainty: In view of the significant uncertainty regarding ultimate collection of income arising in respect of non-performing assets, the guidelines require that banks should not recognize income on non-performing assets until it is actually realised. When a credit facility is classified as non-performing for the first time, interest accrued and credited to the income account in the corresponding previous year which has not been realised should be reversed or provided for. This will apply to Government guaranteed accounts also.
Q144.	<p>In carrying out an audit of interest expense, the auditor is primarily concerned with assessing the overall reasonableness of the amount of interest expense. Analyse and explain stating the audit approach and procedure in regard to interest expense.</p> <p>(RTP, May 2020, NA) (RTP, Nov 2021, NA)</p> <p>Audit approach and procedure in regard to interest expense:</p> <ul style="list-style-type: none"> Obtain from the bank an analysis of various types of deposits outstanding at the end of each quarter. From such information, the auditor may work out a weighted average interest rate. The auditor may then compare this rate with the actual average rate of interest paid on the relevant deposits as per the annual accounts and enquire into the difference, if material. Compare the average rate of interest paid on the relevant deposits with the corresponding figures for the previous years and analyse any material differences. The auditor should, on a test check basis, verify the calculation of interest and ensure that: <ul style="list-style-type: none"> Interest has been provided on all deposits upto the date of the balance sheet; Interest rates are in accordance with the bank's internal regulations, the RBI directives and agreements with the respective deposit holder; Interest on savings accounts are in accordance with the rules framed by the bank/RBI in this behalf. Interest on inter-branch balances has been provided at the rates prescribed by the head office/RBI Ascertain whether there are any changes in interest rate on saving accounts and term deposits during the period
Q145.	K Ltd is availing cash credit limit of ₹ 25 crores from LMN Bank Ltd. The drawing power of the company ranged between ₹22 crores and ₹25 crores during the year 2024-25. The limit availed by the company remained less

	<p>than ₹20 crores during all the days of the financial year 2024-25. The company has not deposited any amount in the cash credit account and there are no other credits to this account during the last two quarters. How will this account be classified in the books of LMN Bank Ltd. as on 31-03-2025? Explain. (SA, Sep 2024, 3 marks)</p>
	<p>An account should be treated as 'out of order' if:-</p> <ul style="list-style-type: none"> the outstanding balance remains continuously in excess of the sanctioned limit/drawing power or In cases where the outstanding balance in the principal operating account is less than the sanctioned limit/drawing power, but there are no credits continuously for 90 days as on the date of Balance Sheet ; or credits are not enough to cover the interest debited during the same period <p>In the given case, K Ltd. is availing cash credit limit of ₹ 25 crores from LMN Bank Ltd and the drawing power of the company range between ₹ 22 crores and ₹ 25 crores during the year 2024-25. The limit availed by K Ltd. remained less than ₹ 20 crores during all the days of the financial year 2024 - 25 and the company has not deposited any amount in the cash credit account and there are no other credits to this account during the last two quarters.</p> <p>Thus, account should be treated as out of order in the books of LMN Bank Ltd. as the outstanding balance in the principal operating account (₹ 20 crore) is less than the sanctioned limit/drawing power (₹ 22 cores and ₹ 25 crores), but there are no credits continuously for 90 days as on the date of Balance Sheet.</p>

Chapter 11 - Ethics and Terms of Audit Engagements

Q146.	<p>Professional skepticism refers to an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence. The auditor shall plan and perform an audit with professional skepticism recognising that circumstances may exist that cause the financial statements to be materially misstated. Explain giving examples. (RTP, Nov 2020, NA) (MTP1, Nov 2023, 4 marks)</p>
	<p>The auditor shall plan and perform an audit with professional skepticism recognising that circumstances may exist that cause the financial statements to be materially misstated.</p> <p>Professional skepticism includes being alert to, for example:</p> <ul style="list-style-type: none"> Audit evidence that contradicts other audit evidence obtained. Information that brings into question the reliability of documents and responses to inquiries to be used as audit evidence. Conditions that may indicate possible fraud. Circumstances that suggest the need for audit procedures in addition to those required by the SAs. Maintaining professional skepticism throughout the audit is necessary if the auditor is to reduce the risks of: <ul style="list-style-type: none"> Overlooking unusual circumstances. Over generalizing when drawing conclusions from audit observations. Using inappropriate assumptions in determining the nature, timing, and extent of the audit procedures and evaluating the results thereof.
Q147.	<p>CA Sudhakar has been appointed as the auditor of AMRO Ltd. Before accepting the appointment, he learns that his cousin, who held shares in the company and recently passed away without children, named him as the nominee for these shares, which have substantial value. Although holding such shares through a distant relative does not violate legal provisions or affect his independence, this unexpected inheritance places him in a dilemma. Advise CA Sudhakar on how he should deal with this situation and safeguard his independence. (RTP, Jan 2025, NA)</p>
	<p>Chartered Accountants have a responsibility to remain independent by taking into account the context in which they practice, the threats to independence and the safeguards available to address the threats.</p>

	<p>Safeguards are actions, individually or in combination, that the professional accountant takes that effectively reduce threats to comply with the fundamental principles to an acceptable level. To address the issue, the following guiding principles are to be applied: -</p> <ol style="list-style-type: none"> 1. For the public to have confidence in the quality of audit, it is essential that auditors should always be and appears to be independent of the entities that they are auditing. 2. Before taking on any work, an auditor must conscientiously consider whether it involves threats to his independence. 3. When such threats exist, the auditor should either desist from the task or eliminate the threat or at the very least, put in place safeguards which reduce the threats to an acceptable level. All such safeguards measures need to be recorded in a form that can serve as evidence of compliance with due process. 4. If the auditor is unable to fully implement credible and adequate safeguards, then he must not accept the work. <p>Considering above, holding of shares of the same company for which he is offered appointment as auditor constitutes threat to his independence. Therefore, CA Sudhakar should take steps to eliminate the threat by selling shares immediately before accepting the appointment and in the absence of same, he should not accept the appointment as an auditor.</p>
Q148.	<p>ABC & Associates, an audit firm, has been approached by a prospective company client that has been in business for about 10 years to conduct an audit of its financial statements. Before accepting the audit engagement, the firm wants to assess the integrity of prospective clients. With regard to the assessment of integrity, which matters should be considered by the audit firm? (RTP, Sep 2024, NA)</p> <p>With regard to the integrity of a client, matters that ABC & Associates should consider include, for example:</p> <ul style="list-style-type: none"> • The identity and business reputation of the client's principal owners, key management, related parties and those charged with its governance. • The nature of the client's operations, including its business practices. • Information concerning the attitude of the client's principal owners, key management and those charged with its governance towards such matters as aggressive interpretation of accounting standards and the internal control environment. • Whether the client is aggressively concerned with maintaining the firm's fees as low as possible. • Indications of an inappropriate limitation in the scope of work. • Indications that the client might be involved in money laundering or other criminal activities.
Q149.	<p>CA M is the engagement partner of the firm M/s YZZ LLP and he is auditing the financial statements of a listed entity ABC Ltd. The audit firm has determined that an engagement quality control review is required for this assignment. Discuss the responsibilities of CA M as an engagement partner for engagement quality control review as per SA-220. (SA, May 2024, 4 Marks)</p> <p>Engagement Performance:</p> <p>As per SA 220, for audits of financial statements of listed entities, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required, the engagement partner shall:</p> <ol style="list-style-type: none"> i) Determine that an engagement quality control reviewer has been appointed. ii) Discuss significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer. iii) Not date the auditor's report until the completion of the engagement quality control review. iv) If differences of opinion arise within the engagement team, with those consulted or, where applicable, between the engagement partner and the engagement quality control reviewer, the engagement team shall follow the firm's policies and procedures for dealing with and resolving differences of opinion.
Q150.	<p>The engagement partner shall consider the results of the firm's monitoring process as evidenced in the latest information circulated by the firm and, if applicable, other network firms and whether deficiencies noted in that</p>

	<p>information may affect the audit engagement. Explain the key aspects that the engagement partner should consider and document as part of an audit engagement under a system of quality control.</p> <p>(Additional Question)</p>
	<p>An effective system of quality control includes a monitoring process designed to provide the firm with reasonable assurance that its policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively.</p> <p>The engagement partner shall consider the results of the firm's monitoring process as evidenced in the latest information circulated by the firm and, if applicable, other network firms and whether deficiencies noted in that information may affect the audit engagement. The engagement partner should document following matters pertaining to an audit engagement: -</p> <ul style="list-style-type: none"> (a) Issues identified with respect to compliance with relevant ethical requirements and how they were resolved. (b) Conclusions on compliance with independence requirements that apply to the audit engagement, and any relevant discussions with the firm that support these conclusions. (c) Conclusions reached regarding the acceptance and continuance of client relationships and audit engagements. (d) The nature and scope of, and conclusions resulting from, consultations undertaken during the course of the audit engagement.
Q151.	<p>SS Ltd. is a company listed in India. The Company has appointed M/s Z & Co. as auditors. Mr. Q, a CA has recently joined the firm and has been appointed as the engagement partner for the first time. He understands that it is necessary to ensure the compliance of independence for the audit team as per standard audit practices. But he could not find as such, any policies and procedures available with the firm in documented form. Why do you think that the firm should have policies and procedures to ensure the independence of the firm in every assignment? How does an engagement partner ensure the compliance of independence? Discuss with reference to relevant SAs. (Additional Question)</p> <p>As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements," the firm should establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, others subject to independence requirements (including experts contracted by the firm and network firm personnel), maintain independence where required by the Code. Such policies and procedures should enable the firm to:</p> <ul style="list-style-type: none"> i) Communicate its independence requirements to its personnel and, where applicable, to others subject to them; and ii) Identify and evaluate circumstances and relationships that create threats to independence, and to take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement. <p>Further, as per SA 220, "Quality Control for an Audit of Financial Statements", the engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall:</p> <ul style="list-style-type: none"> i) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate circumstances and relationships that create threats to independence; ii) Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for the audit engagement; and iii) Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is permitted by law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action.

Q152.	<p>CA Paras has accepted an audit of financial statements of an entity. According to the Standards on Auditing, the auditor is required to send an audit engagement letter to the entity. What are the key areas that should be included in the audit engagement letter? Under what circumstances is the auditor not required to record the terms of engagement in such a written agreement? (MTP1, Jan 2025, 5 marks)</p>
	<p>The auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate. The audit engagement letter is sent by the auditor to his client. It is in the interest of both the auditor and the client to issue an engagement letter so that the possibility of misunderstanding is reduced to a great extent. Such a letter includes:</p> <ol style="list-style-type: none"> The objective and scope of the audit of the financial statements The responsibilities of the auditor The responsibilities of management Identification of the applicable financial reporting framework for the preparation of the financial statements and Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content. <p>If law or regulation prescribes in sufficient detail the terms of the audit engagement, the auditor need not record them in a written agreement, except for the fact that such law or regulation applies and that management acknowledges and understands its responsibilities.</p>
Q153.	<p>A Chartered accountant is conducting an audit of a client for the last two years. Before proceeding to start the audit for next year, he notices that there is substantial change in management. Besides, client has ventured into areas of business activity which were not present at time of accepting initial audit engagement. Discuss responsibility of auditor in this regard in context of SA 210. (ICAI Study Material - Test Your Knowledge)</p> <p>As per SA 210, "Agreeing the terms of audit engagements", recurring audit is an audit which is performed by an auditor over years. In case of recurring audits, the auditor shall assess whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms of the audit engagement.</p> <p>The auditor may decide not to send a new audit engagement letter or other written agreement each period. However, the following factors may make it appropriate to revise the terms of the audit engagement or to remind the entity of existing terms:</p> <ul style="list-style-type: none"> Any indication that the entity misunderstands the objective and scope of the audit. Any revised or special terms of the audit engagement A recent change of senior management. A significant change in ownership. A significant change in nature or size of the entity's business. A change in legal or regulatory requirements. A change in the financial reporting framework adopted in the preparation of the financial statements. A change in other reporting requirements. <p>In the given case, the auditor noticed that there is substantial change in management and client has ventured into areas of business activity which were not present at time of accepting initial audit engagement. Thus, the auditor may decide to send a new audit engagement letter.</p>
Q154.	<p>A professional accountant is expected to comply with the fundamental principles of professional ethics at all times. Explain which fundamental principle governing professional ethics is violated in the following situations?</p> <ol style="list-style-type: none"> 1) A chartered accountant in practice accepted the appointment as an auditor of a firm in which his sister was a partner.

- 2) A chartered accountant in practice was approached by his friend to seek some insider information about a company, which was a client of the chartered accountant. He could not refuse his friend's request.
- 3) A chartered accountant in practice failed to inform his client about the change in laws applicable to his client

(SA, May 2024, 3 Marks)

Fundamental Principles:

- 1) **Objectivity:** The principle of objectivity requires that a professional accountant shall **not undertake** a professional activity if a **circumstance** or relationship **unduly** influences the accountant's professional judgment regarding that activity. Objectivity principle will be violated in the given situation where a chartered accountant in practice accepted the appointment as an auditor of a firm in which his sister was a partner.
- 2) **Confidentiality:** Confidentiality principle requires a professional accountant to **respect** the confidentiality of information acquired as a result of professional or business relationships. Confidentiality principle will be violated in the given situation where a chartered accountant in practice could not refuse his friends requested to seek some insider information about a client company of the chartered accountant.
- 3) **Professional Competence and Due care:** A professional accountant shall comply with the principle of professional competence and due care, which requires an accountant to **attain** and **maintain** professional **knowledge** and **skill** at the level required to ensure that a client or employing organization receives **competent professional service**, based on current technical and professional standards and relevant legislation; and **act diligently** and in accordance with applicable technical and professional standards. Professional Competence and Due Care principle will be violated in the situation where a chartered accountant in practice failed to inform his client about the change in laws applicable to his client.

- Q155. Professional integrity and independence are considered essential characteristics of all the professions. There are two interlinked perspectives of independence of auditors, one, independence of mind and two, independence in appearance. Explain. (RTP, May 2023, NA)

Professional integrity and independence are considered essential characteristics of all the professions but are more so in the case of accountancy profession. Independence implies that the judgment of a person is **not subordinate** to the wishes or direction of another person who might have engaged him.

It is **not** possible to **define** "independence" **precisely**. Independence is a condition of mind as well as personal character. It should not be confused with the superficial and visible standards of independence which are sometimes imposed by law.

Independence of mind and independence in appearance are interlinked perspectives of Independence of auditors.

- a) **Independence of mind** – the state of mind that permits the **provision** of an **opinion without** being **affected** by **influences** that compromise professional judgment, **allowing** an individual to **act** with **integrity**, and exercise **objectivity** and professional **skepticism**; and
- b) **Independence in appearance** – the **avoidance** of **facts** and **circumstances** that are so **significant** that a reasonable and informed **third party**, having knowledge of all relevant information, including any safeguards applied, would reasonably **conclude** a firm's, or a member of the assurance team's, **integrity**, **objectivity** or professional **skepticism** had been **compromised**.

Independence of the auditor has not only to exist in fact, but also appears to so exist to all reasonable persons.