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CA INTER (Jan 2026)
GROUP II – PAPER 5
AUDITING AND ETHICS
(Series 3)

Time Allowed: - 3 Hours

Maximum Marks: 100

This question paper comprises two parts, Part I and Part II.
Part I comprises MCQ & Part II comprises questions which require descriptive answers.

PART – I (MCQs)
All MCQs are compulsory

Question no. 1-15 carry 2 marks each

Case Study 1

Sunlight Ltd. is a company engaged in the manufacture of solar panels. It is one of the largest solar panel manufacturing companies in India. With over a decade of experience, the company has implemented projects across the length and breadth of the country in both commercial and residential sectors. For the F.Y. 2023-24, Singhania & Co., an LLP of Chartered Accountants was appointed as the statutory auditors of the company. The audit work for the F.Y. 2023-24 is on the verge of completion.

During the audit, one of the audit team members, Mr. Rishab, was asked by the engagement partner, to verify the ownership assertion of the inventories held by the company. To verify such assertion, Mr. Rishab asked the concerned official of the company to make arrangements for the attendance of the audit team at the physical inventory count being conducted by the company. Mr. Rishab was of the view that only by attending the physical inventory count, the ownership assertion with respect to inventory of the company can be checked. He discussed his view with another audit team member Ms. Soni who had a different point of view for such situation. According to her, the correct course of action in this regard is that Mr. Rishab should verify the purchase requisition, purchase order, receiving reports, vendor invoices, inventory records, payment file etc. as ownership assertion cannot be verified by attending the physical inventory count only.

Further, while verifying the creditors and purchases balances, Ms. Soni decided to check the creditors balance on sample basis with a sample size of 50 creditors as she was satisfied with the Internal Control Procedures applied for the same. She asked the management to provide the list of all the 550 creditors. For deciding the sample, she took the sampling interval of every 11th creditor balance and in this way created a sample size of 50 creditors balance for the purpose of audit.

During the audit, while verifying the share capital balance of the company, Mr. Rishab and Ms. Soni noticed that there has been no change in the share capital raised by the company. Ms. Soni was of the view that since there has been no change in the share capital of the company, the audit team is not required to obtain any evidence with respect to the share capital balance. However, Mr. Rishab opined that they should obtain audit evidence even if there is no change in the company's capital structure during the year. According to him such evidence can be a written confirmation from the accounts manager.

Before finalising the audit report, the Engagement Partner asked Mr. Rishab to coordinate with the client for requesting written representation from the management of the company with respect to the management responsibilities and information provided by the management. Mr. Rishab did not accept the representation given by the management as the same contained a qualifying language to the effect that representations are made to the best of its knowledge and belief, which according to Mr. Rishab was not reasonable to accept.

Since the engagement partner was about to finalise and sign the audit report, Mr. Rishab and Ms. Soni were discussing the various requirements of assembly of the final audit file and the changes that can be made in the audit documentation during the final assembly process. According to Ms. Soni only changes of administrative nature can be made, like deleting superseded documentation, sorting, collating and cross-referencing working papers and changes like recalculation of depreciation etc. should not be made during such final assembly process.

You are required to answer the following:

- 1. While verifying the inventory as asked by the engagement partner, which specific assertion can be best verified by following the specific audit procedure considered appropriate by Mr. Rishab?**
 - (a) Rights and Obligations.
 - (b) Existence and condition.
 - (c) Valuation.
 - (d) Presentation & Disclosure.
- 2. While selecting the sample for verification of creditors, which method of sampling has been applied by Ms. Soni?**
 - (a) Stratified sampling.
 - (b) Haphazard sampling.
 - (c) Systematic sampling.
 - (d) Simple random sampling.
- 3. What is the best course of action to be taken by Mr. Rishab for verifying the assertion with respect to the inventory of the company, as asked by the engagement partner?**
 - (a) Mr. Rishab should attend the physical inventory count as the only audit procedure.
 - (b) Mr. Rishab should agree with Ms. Soni and follow the course of action as suggested by her.
 - (c) Mr. Rishab should ask the management to provide a written representation in this regard as it is a sufficient and appropriate audit evidence.
 - (d) Mr. Rishab should perform test count and inspection while attending the physical inventory count to verify the assertion as requested by the engagement partner.
- 4. With respect to verification of the share capital balance of the company, which of the following is the most appropriate?**
 - (a) The point of view of Ms. Soni is correct.
 - (b) The point of view of Mr. Rishab is correct.
 - (c) The point of view of Mr. Rishab is partly correct as written confirmation should be obtained from the Company Secretary.
 - (d) The point of view of Ms. Soni is partly correct as no evidence is required to be obtained if the same audit firm has conducted the audit of the previous year thereby verifying the closing balance of share capital in the previous year, which becomes the opening balance of

the share capital for the year under audit.

5. Whether non-acceptance of the written representation by Mr. Rishab is correct?

- (a) The non-acceptance of written representation by Mr. Rishab is not correct as the management of the company has the sole discretion to decide as to which language is used or what limitations are imposed in the written representation provided to the auditor.
- (b) The non-acceptance of written representation by Mr. Rishab is correct as it is not reasonable for the auditor to accept any qualifying language in the written representations given by the management.
- (c) The non-acceptance of written representation by Mr. Rishab is correct as SA 580 requires the auditor to accept the written representation only if it is in the language as used in the letter of audit engagement.
- (d) The non-acceptance of written representation by Mr. Rishab is not correct as it is reasonable for the auditor to accept such qualifying language if the auditor is satisfied that the representations are being made by those with appropriate responsibilities and knowledge of the matters included in the representations.

Case Study 2

Nath Shah & Associates is a firm of Chartered Accountants practicing in Delhi. The firm consists of two partners namely, CA Ajay Nath and CA Ria Shah. The Statutory audit team is generally headed by CA Ajay Nath and his team consists of three articled assistants and one qualified Chartered Accountant, CA Reshu. With respect to the audit work of 4 clients for which the audit team intends to start the audit work, CA Ajay discussed with the team members about the development of audit programmes for individual clients. One of the articled assistants, Mr. Sumit, was of the view that one single audit programme can be developed for all the 4 clients operating in different industries.

With respect to one of the clients namely, Saraswati Ltd., a labour intensive company, CA Ajay asked CA Reshu to compare the amount of wages paid by the company in the current year and last year. Also, she was asked to verify the relationship between the number of employees and wages paid in both the years by the company.

The audit firm started the audit of another client, namely, Sarthak Ltd. having maximum transactions in foreign currency. CA Ajay asked one of the team members, Mr. Rahul, to verify whether the calculations related to conversion of the foreign currency into local currency is proper or not.

While verifying the share issue transactions of one client, namely, Laxman Ltd., CA Reshu found that the company has issued sweat equity shares during the year under audit. She asked one of the articled assistants, Mr. Saurabh, to further verify whether the relevant provisions of the Companies Act 2013, have been complied by the company in this regard. Also, with respect to Sarthak Ltd., there was reduction of share capital during the year. Mr. Saurabh was asked by the engagement partner to verify the compliance of relevant provisions of the Companies Act, 2013 in this regard also. Mr. Saurabh was of the view that there is requirement of passing of Special Resolution by the respective company for both.

While starting the audit work of another client, Rintex Ltd., the audit team noticed that the company has its internal audit team. Mr. Sumit was of the view that the statutory audit team can use and rely on the work of the Internal Auditors of the company and as such there is no requirement for the statutory audit team to perform audit procedures again as the internal audit team must have verified the financial transactions of the company in detail. Further, while verifying the expenses ledger, Mr. Sumit noticed that the company has implemented a system whereby the entries related to expenses incurred during the year can be entered into the accounting system by authorised personnels only. However,

with respect to travelling expenses which constituted about 30% of the total expenses, the entries were made by employees who were not authorised to make such entries.

You are required to answer the following:

- 6. Is the view of Mr. Sumit with respect to the development of audit programme correct?**
- (a) Yes, the view of Mr. Sumit is correct as developing one audit programme for all the clients will avoid duplication of efforts of audit team.
 - (b) No, the view of Mr. Sumit is not correct as all the four clients operate in different industries and evolving one audit programme for all businesses is not practicable.
 - (c) Yes, the view of Mr. Sumit is correct as development of audit programme is not affected by the nature of client business.
 - (d) No, the view of Mr. Sumit is not correct as development of audit programme is not the responsibility of the audit team. The individual clients will develop their respective audit programmes.
- 7. With respect to Saraswati Ltd., Ms. Reshu was asked by CA Ajay to perform which kind of audit procedures?**
- (a) Substantive Analytical Procedures.
 - (b) Test of details.
 - (c) Test of transactions.
 - (d) Test of Controls.
- 8. Whether understanding of Mr. Saurabh regarding the passing of Special Resolution is correct?**
- (a) The understanding of Mr. Saurabh is partly correct as ordinary resolution is required in case of issue of sweat equity shares by the company though special resolution is required to be passed by the company in case of reduction of share capital.
 - (b) The understanding of Mr. Saurabh is partly correct as special resolution is required in case of issue of sweat equity shares by the company though ordinary resolution is required to be passed by the company in case of reduction of share capital.
 - (c) The understanding of Mr. Saurabh is correct as special resolution is required in case of issue of sweat equity shares by the company and reduction of share capital.
 - (d) The understanding of Mr. Saurabh is not correct as ordinary resolution is required in case of issue of sweat equity shares by the company as well as in case of reduction of share capital.
- 9. Is the view of Mr. Sumit correct with respect to using and relying on the work of the Internal Audit team of Rintex Ltd.?**
- (a) Yes, the view of Mr. Sumit is correct.
 - (b) No, the view of Mr. Sumit is not correct as the statutory audit team cannot use the work of the internal audit team of the client company.
 - (c) No, the view of Mr. Sumit is not correct as the statutory auditor has the sole responsibility for the audit opinion expressed.
 - (d) The view of Mr. Sumit is partly correct as the statutory audit team can use and rely on the work of the internal audit team if the same is agreed while signing the engagement letter.
- 10. Which kind of risk is noticed by Mr. Sumit with respect to entries related to travelling expenses entered into the accounting system of Rintex Ltd.?**

- (a) Inherent Risk.
- (b) Detection Risk.
- (c) Control Risk.
- (d) No risk is being noticed.

Case Study 3

A government department has been allocated a budget for infrastructure development. During the audit, the auditor observed several discrepancies that raise concern regarding the management and utilisation of funds. The key findings include:

- Some payments were processed without proper approval from the competent authority.
- A large-scale project was implemented, but no assessment was made to determine whether the expected benefits were achieved or not.
- Funds were utilised from an account for which no budgetary provision had been made.
- Certain expenditures were made without adhering to prescribed financial regulations.
- There were instances of unnecessary spending that did not align with the principles of financial propriety.

You are required to answer the following:

- 11. Which type of audit would most likely identify the issue of payments processed without proper approval from the competent authority?**
 - (a) Audit against Rules & Orders.
 - (b) Audit of Sanctions.
 - (c) Audit against Provision of Funds.
 - (d) Propriety Audit.
- 12. Which type of audit would evaluate whether the expected benefits of a large-scale infrastructure project were achieved?**
 - (a) Propriety Audit.
 - (b) Audit against Rules & Orders.
 - (c) Audit of Sanctions.
 - (d) Performance Audit.
- 13. Out of the following, which audit would address the issue of funds being utilised from an account with no budgetary provision?**
 - (a) Audit against Provision of Funds.
 - (b) Audit of Sanctions.
 - (c) Performance Audit.
 - (d) Audit against Rules & Orders.
- 14. Which audit type would be relevant to detect expenditures made without following prescribed financial regulations?**
 - (a) Performance Audit.
 - (b) Audit against Rules & Orders.

(c) Audit against Provision of Funds.

(d) Audit of Sanctions.

15. What type of audit would most effectively identify instances of unnecessary spending that do not align with financial propriety?

(a) Performance Audit.

(b) Audit of Sanctions.

(c) Propriety Audit.

(d) Audit against Rules & Orders.

PART – II (Descriptive Questions)

This part comprises 6 questions. Question No. 1 is compulsory. Attempt any 4 questions out of the remaining 5 questions.

Question 1A

(5 Marks)

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.

Question 1B

(5 Marks)

You are auditing the financial statements of JEN Ltd., a manufacturing company. During a meeting, Mr. Jai CEO questions the auditor's ability to detect all material misstatements, including those caused by fraud. He insists that since the auditor is a professional, the audit should provide absolute assurance on the accuracy of the financial statements. Is the contention of Mr. Jai correct. Discuss the objectives of auditor in accordance with relevant SA.

Question 1C

(4 Marks)

M/s. PK & Company, Chartered Accountants, are the statutory auditors of JC Limited. CA Tarun, partner of M/s. PK & Company, was entrusted to supervise and verify the inventory items as on 31.03.20XX. During the process of verification, a large chunk of draft inventory sheets were accumulated and then a final inventory sheet was prepared. The audit assistant has kept all these drafts and the final inventory sheet in the audit file. Is the approach of the audit assistant correct? Which papers/ documents may not be included in the audit documentation?

Question 2A

(5 Marks)

Surya and Chand Ltd is a manufacturing company engaged in the production of miscellaneous electrical goods. Trilochan and Co. has been appointed as the auditors to carry out its audit. Auditor thinks that planning an audit would involve establishing the overall audit strategy for the engagement and developing an audit plan. Also, Adequate planning benefits the audit of financial statements in several ways. Analyse and Advise explaining the benefits of adequate planning.

Question 2B

(5 Marks)

Auditor GR and Associates have been appointed to conduct audit of PNG Ltd, a manufacturing company engaged in manufacturing of various food items. While planning an audit, the auditors do not think that it would be necessary to understand internal controls. Advise the auditor in this regard explaining clearly the benefits of understanding the internal control.

Question 2C

(4 Marks)

Management's assessment of the entity's ability to continue as a going concern involves making a

judgement about inherently uncertain future outcomes of events or conditions. What are relevant factors to that judgement?

Question 3A

(5 Marks)

Money Ltd. is a listed company engaged in the business of manufacturing. During the financial year 2024–25, the company has given loans to its subsidiary and provided a corporate guarantee on behalf of a related party.

State the reporting responsibilities of the auditor under Clause (iii) of Paragraph 3 of CARO, 2020.

Question 3B

(5 Marks)

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

Timing of Audit Activities

Activity	Expected Timing
Audit Planning	July 1, 20XX - July 5, 20XX
Review by EQCR	July 6, 20XX - July 7, 20XX
Audit Field Work	July 10, 20XX - August 20, 20XX
Review by Manager	August 21, 20XX
Review by Engagement Partner	August 22, 20XX - August 25, 20XX
Review by EQCR	August 26, 20XX - August 27, 20XX
Response on Audit Memo	August 28, 20XX
Review by Partners-internally post response on audit memo	August 29, 20XX
Review by EQCR	August 30, 20XX
Finalization of Audit Report and Financial Statements	September 01, 20XX - September 02, 20XX
Issuance of Audit Report and Financial Statements	September 03, 20XX

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

Question 3C

(4 Marks)

M/s S R & Associates are the Statutory Auditors of Vanee Textile and Garments Ltd., a company engaged in the business of manufacturing of various textile products. The auditor has completed the audit and is in the process of forming an opinion on the financial statements. CA S, the engagement partner, wants to conclude whether the financial statements as a whole are free from material misstatements, whether due to fraud or error. Guide him about the factors he should consider to reach that conclusion.

Question 4A

(5 Marks)

Mr. Piyush, the Bank Manager develops controls to aid in managing key business and financial risks.

Discuss the various requirements for an effective risk management system in a bank.

Question 4B

(5 Marks)

CA Rimi is appointed as an auditor of ASI Pvt. Ltd. During the audit, she decided to use various audit procedures to gather sufficient and appropriate audit evidence such as:

- i. While verifying the fixed asset, she examined factory equipment and verified the presence of each item.
- ii. To verify the company's accounts receivable, she directly sends balance confirmations to some of the customers.
- iii. CA Rimi examined purchase invoices, contracts, and authorisation records to assess the validity of payments and the approval process.
- iv. She independently performs the bank reconciliation that was originally carried out by the accounts department.
- v. She also checked the accuracy of depreciation calculations made by the client.

Identify and explain the type of abovementioned audit procedure performed by CA Rimi in accordance with relevant SA.

Question 4C

(4 Marks)

CA Y, statutory auditor of a company, is in process of determining materiality for financial statements while planning audit. Since materiality is a matter of professional judgment and is affected by auditor's perception of financial information needs of users of financial statements, he is reasonably making certain assumptions about users of financial statements. Which reasonable matters are likely to be assumed by him in respect of users?

Question 5A

(5 Marks)

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?

Question 5B

(5 Marks)

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 relevant Standard on Auditing? Also comment whether prior to using 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.

Question 5C

(4 Marks)

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.

Question 6A

(5 Marks)

CA Jatin is auditor of XYZ Pharma, his brother-in-law's Partnership Firm. His family relationship creates a conflict of interest that could unduly influence his professional judgment, making it difficult for him to provide an unbiased opinion on the firm's financial statements.

In another assignment of Tax Audit of a company, CA Jatin is also required to prepare the company's tax return. He fails to check the latest provision of the Income-tax Act which allows for a major new deduction resulting in the client overpaying income tax.

CA Jatin is also preparing GST returns of one of his clients. The client instructs him to intentionally understate the sales figures to reduce the tax liability.

Identify and explain the fundamental principles of professional ethics involved in above situations.

Question 6B

(5 Marks)

JB Limited has invested huge sums of money on establishment of new Property, Plant and Equipment during the year under audit. They have incurred an amount of ₹ 5,70,000 on dismantling of an old plant, which had become obsolete, so that a new plant can be set up at the existing location. The Auditor is in the process of verifying the cost incurred towards addition to Property, Plant and Equipment. What should be the accounting treatment of the amount spent on dismantling of old plant in the financial statements? Which elements of cost should be considered for valuing Property, Plant and Equipment?

Question 6C

(4 Marks)

Proceedings have been initiated against False Limited for holding benami property under law relating to prohibition of benami transactions and the rules made thereunder but such property is not recorded in books of accounts. As a consultant to the company, what will you advise the company as far as disclosure requirements are concerned in financial statements in relation to said proceedings?