

CA Final Advanced Auditing & Professional Ethics

Additional Questions for MAY 2023

Index (Mapping with the CA Sanidhya Saraf's Audit Question Bank)

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Note: Corrigendum at Page no. 41-44

Repetitive questions -only attempt needs to be added. Reference given Page 45.

Chapter 1 -SA

SA 210

Question

(MTP 1 NOV 2022)

NEW Limited is a listed company having its operation across India. NEW Limited appointed Mr. N, Mr. E and Mr. W, as its joint auditors for the year 2021-22. After making sure that all of them are qualified to be appointed as statutory auditor, NEW Limited issued engagement letter to all of them. But Mr. N was not clear on some points, so he requested NEW Limited to slightly change the terms of his engagement. This change will not impact the ultimate opinion on the financial statement. The engagement letter contains the details on objective and scope of audit, responsibilities of auditor and identification of framework applicable. It also contains the reference to expected form and content of report from all three joint auditors. In your opinion what was the discrepancy in the Audit engagement letter issued by NEW Limited?

Answer:

Agreement on Audit Engagement Terms: As per SA 210, “Agreeing the Terms of Audit Engagements”, the auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate.

Subject to prescribed details under Law or Regulations, the agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include:

- (i) The objective and scope of the audit of the financial statements;
- (ii) The responsibilities of the auditor;
- (iii) The responsibilities of management;
- (iv) Identification of the applicable financial reporting framework for the preparation of the financial statements; and
- (v) 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.

In the given scenario, NEW Limited appointed Mr. N, Mr. E and Mr. W, as its joint auditors for the year 2021-22 and issued engagement letter to all of them. The engagement letter contains the details on objective and scope of audit, responsibilities of auditor, identification of framework applicable and reference to expected form and content of report from all three joint auditors. However, engagement letter issued by NEW Ltd. does not specify the responsibilities of management, whereas as per SA 210, it should also specify responsibilities of management.

SA 220 & SQC 1

Question (Important)

(MTP 2 NOV 2022)

Vishudh Sagar & Co. Chartered Accountants have been auditors of JIN Ltd (a listed entity) for the last 8 financial years. CA. Manidhari, partner of the firm, has been handling the audit assignment very well since the appointment. The audit work of CA. Manidhari and his team is reviewed by a senior partner CA. Mahendra Sagar to assure that audit is performed in accordance with professional standards and regulatory and legal requirements. CA. Mahendra was out of India for some personal reasons, so this year CA. Kushal, who is relatively less experienced team member, has been asked to review the audit work. In your opinion, what areas CA. Kushal should consider at the time of review. List any four areas and also comment whether firm is complying with Standard on Quality Control or not.

Answer:

Compliance with Standard on Quality Control on review of audit work - As per SQC 1, “Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements”, review responsibilities are determined on the basis that more experienced engagement team members, including the engagement partner, review work performed by less experienced team members. An engagement quality control review for audits of financial statements of listed entities includes considering the following:

- (i) The work has been performed in accordance with professional standards and regulatory and legal requirements;
- (ii) Significant matters have been raised for further consideration;
- (iii) Appropriate consultations have taken place and the resulting conclusions have been documented and implemented;
- (iv) There is a need to revise the nature, timing and extent of work performed;
- (v) The work performed supports the conclusions reached and is appropriately documented;
- (vi) The evidence obtained is sufficient and appropriate to support the report; and
- (vii) The objectives of the engagement procedures have been achieved.

The firm should establish policies and procedures:

- (i) Setting out criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and
- (ii) For all audits of financial statements of listed entities, requiring the rotation of the engagement partner after a specified period in compliance with the Code.

The familiarity threat is particularly relevant in the context of financial statement audits of listed entities. For these audits, the engagement partner should be rotated after a pre-defined period, normally not more than seven years.

From the facts given in the question and from the above stated paras of SQC 1, it can be concluded that firm is not complying with SQC 1 as Engagement Partner Manidhari is continuing for more than 7 years.

SA 250

Question (Important)

(RTP NOV 2022)

Abhinandan Limited a chemical manufacturing company, having its factory located at Nanded Village, for the year 2021-22 appointed Subahu & Co. as their statutory auditors. During the course of the audit, Subahu & Co. identified that Abhinandan Limited received a show cause notice from National Green Tribunal based on the investigation performed by the regional forest department for violating environmental laws. Upon gathering a further understanding of the said matter, it was identified that Abhinandan Limited was dumping toxic solid waste, without treating it, on the nearby grounds, and because of this, the nearby water bodies were getting polluted. Based on the preliminary investigation performed by the regional forest department under the directions of the National Green Tribunal, it was identified that these practices were carried out since 2009 and a lot of damage has been done to the environment by Abhinandan Limited. A show cause notice was already issued to Abhinandan Limited by the National Green Tribunal for levying the penalty of an amount of ₹ 500 crore. The unaudited profit for the financial year 2021 -22 of Abhinandan Limited was ₹ 35 crore and the unaudited turnover was ₹ 100 crore. Upon inquiry it was identified that Abhinandan Limited has disclosed this matter in the financial statements by way of footnote, the extract of which is provided below:

“The company has received a show cause notice from the National Green Tribunal for some potential violation of environmental laws and the company’s legal department has assessed and found that the judgment would be in favour of the company. Accordingly, no provision has been created for such notices.”

In the light of the above scenario kindly provide what should be the appropriate option for the statutory auditor of the company to report this matter.

Answer :

As per SA 250, “Consideration of Laws and Regulations in an Audit of Financial Statements”, the auditor is required to obtain an understanding and need to evaluate the impact of other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity’s ability to continue its business, or to avoid material penalties (for example, compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations); non-compliance with such laws and regulations may therefore have a material effect on the financial statements.

The auditor shall perform the following audit procedures to help identify instances of non - compliance with other laws and regulations that may have a material effect on the financial statements:

- (a) Inquiring of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations; and

(b) Inspecting correspondence, if any, with the relevant licensing or regulatory authorities

As per Section 143(3)(j) read with Rule 11(a), the auditor is required to report whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement.

As per SA 570, “Going Concern”, if the auditor concludes that management’s use of the going concern basis of accounting is appropriate in the circumstances but a material uncertainty exists, the auditor shall determine whether the financial statements:

- (i) Adequately disclose the principal events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern and management’s plans to deal with these events or conditions; and
- (ii) Disclose clearly that there is material uncertainty related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern and, therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business.

If adequate disclosure about the material uncertainty is not made in the financial statements, the auditor shall (a) Express a qualified opinion or adverse opinion, as appropriate, in accordance with SA 705; and (b) 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.

In the current scenario, Abhinandan Limited has received a show cause notice from the National Green Tribunal of an amount which is more than the net profit and the turnover of the company for the year. In the event of an unfavorable order for Abhinandan Limited, there will be an impact on Abhinandan Limited’s ability to continue as a going concern.

As a result, appropriate disclosure should be provided by management for such events which cast significant doubt on the entity’s ability to continue as a going concern. As no appropriate disclosure has been provided by Abhinandan Limited for such show cause notice, Subahu & Co. should report this matter in their audit report under “Going Concern Para” as per SA 570 and under clause (j) of Section 143(3) of the Companies Act, 2013. Also, the auditor is required to issue an adverse opinion as per SA 705, **“Modifications to the Opinion in the Independent Auditor’s Report”**.

SA 501

Question

(MTP 2 NOV 2022)

The Engagement Partner of the audit team of High Inventory Limited assessed that the inventory is material with respect to the audit of the financial statement for the current period. Upon inquiring with the management, the Engagement Partner identified that the management will be performing an annual physical inventory count at all the warehouses where the entity stores and maintains its inventory. Moreover, management confirmed in its written representation that they will be performing a 100% physical count of inventory for the current period.

As a result, the engagement Partner decided not to perform any physical count of inventory as it will be a duplication of the work. Moreover, he decided that the written representation from management stating “the inventory exists and is in appropriate physical condition” will be sufficient and appropriate with respect to audit evidence to conclude that the inventory balance in the financial statement is free from any material misstatement.

In the light of SA 501, evaluate whether the decision taken by the Engagement Partner is appropriate or not.

Answer:

As per SA 501,” Audit Evidence - Specific Considerations for Selected Items”, when inventory is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of inventory by:

- i. **Attendance at physical inventory counting, unless impracticable, to**
 - 1. Evaluate management’s instructions and procedures for recording and controlling the results of the entity’s physical inventory counting.
 - 2. Observe the performance of management’s count procedures.
 - 3. Inspect the inventory; and.
 - 4. Perform test counts; and
- ii. Performing audit procedures over the entity’s final inventory records to determine whether they accurately reflect actual inventory count results

Attendance at physical inventory counting involves:

- i. Inspecting the inventory to ascertain its existence and evaluate its condition and perform test counts.
- ii. Observing compliance with management’s instructions and the performance of procedures for recording and controlling the results of the physical inventory count; and
- iii. Obtaining audit evidence as to the reliability of management’s count procedures.

Hence in the given case, the approach of Engagement Partner is not appropriate as when inventory is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of inventory. This should be done by performing various audit procedures which also includes attending physical count, observing the count, inspecting the inventory and reperforming physical counts.

SA 530

Question

(RTP NOV 2022)

Chintamani Ltd appoints Chintan & Mani as statutory auditors for the financial year 2021 - 2022. Chintan & Mani seem to have different opinions on Audit approach to be adopted for audit of Chintamani Ltd. Mani is of the opinion that 100% checking is not required and they

can rely on Audit Sampling techniques in order to provide them a reasonable basis on which they can draw conclusions about the entire population.

Chintan is concerned that whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

You are required to guide Chintan about his role if audit sampling has not provided a reasonable basis for conclusions about the population that has been tested in accordance with SA 530.

Answer:

As per SA 530, “Audit Sampling”, the auditor shall evaluate:

- (a) The results of the sample; and
- (b) Whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

If the auditor concludes that audit sampling has not provided a reasonable basis for conclusions about the population that has been tested, the auditor may:

- (I) Request management to investigate misstatements that have been identified and the potential for further misstatements and to make any necessary adjustments; or
- (II) Tailor the nature, timing and extent of those further audit procedures to best achieve the required assurance. For example, in the case of tests of controls, the auditor might extend the sample size, test an alternative control or modify related substantive procedures.

SA 570

Question

(MTP 2 NOV 2022)

CA.K is appointed statutory auditor of SEEK INDIA LTD under Companies Act, 2013 for the first time. The company is preparing its accounts keeping in view applicable requirements of Division II of Schedule III of Companies Act, 2013. On scrutiny of financial statements of company put up for audit, it was noticed that notes to accounts show ageing of trade payables as per amended requirements of Schedule III of the Companies Act, 2013.

The ageing schedule forming part of notes is as under: -

Outstanding for following periods from due date of payment (` In crore)

Particulars	Less than 1 year	1-2 years	2-3 years	More than 3 years	Total
MSME	NIL	NIL	NIL	NIL	NIL
Others	2	4	3	1	10
Disputed dues-MSME	NIL	NIL	NIL	NIL	NIL
Disputed dues-others	NIL	NIL	NIL	NIL	NIL

Besides above, current ratio, debt-equity ratio, trade payables turnover ratio and net profit ratio disclosed in notes to accounts have slipped drastically as compared to last year and from standard norms. Most of the key financial ratios are in red. There is no other relevant information concerning above in notes to accounts.

Further, on reviewing bank statement of cash credit limit (against hypothecation of paid stocks), it was noticed that there is no debit transaction in the month of March, 2022. On inquiry, he came to know that stock audit of company was conducted in the month of January, 2022 and stock auditors have commented vide their report dated 25.2.2022 that company had negative drawing power due to high creditors. Accordingly, the bankers have refused further debits in cash credit account from start of March, 2022. There is no information in this respect in financial statements and notes to accounts.

Discuss how CA K should deal with above for reporting in his audit report under the Companies Act, 2013.

Answer:

In the given situation, it is clear from the ageing schedule that company is not able to pay its creditors on time. Outstanding to creditors for a period of 1 year or more account for 80% of total dues to the creditors of the company from due date of payment. Most of key financial ratios are adverse.

Further, bankers have refused further debits in cash credit account due to negative drawing power from March 2022. Cash credit loans are repayable on demand. There is no other information or disclosure available how the company plans to run its business without bank finance.

All the above factors are indicators that a material uncertainty exists that may cast a significant doubt on the company's ability to continue as going concern. There is no express disclosure of this fact in financial statements.

Therefore, it is a situation where material uncertainty exists which has cast a significant doubt on company's ability to continue as going concern in accordance with SA 570, "Going Concern".

Keeping in view above the fact that although a material uncertainty exists casting a significant doubt on the ability of company to continue as going concern, adequate disclosure of material uncertainty is not made in financial statements, CA K shall give qualified or adverse opinion in accordance with SA-705, "Modifications to the Opinion in the Independent Auditor's Report".

SA 700

Question

(RTP NOV 2022)

How should auditor give description of auditor's responsibilities for the audit of the financial statements when the auditor disclaims an opinion on the financial statements?

Answer:

When the auditor disclaims an opinion on the financial statements due to an inability to obtain sufficient appropriate audit evidence, the auditor shall amend the description of the auditor's responsibilities required by SA 700, "**Forming an Opinion and Reporting on Financial Statements**", to include only the following:

- (i) A statement that the auditor's responsibility is to conduct an audit of the entity's financial statements in accordance with Standards on Auditing and to issue an auditor's report;
- (ii) A statement that, however, because of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and
- (iii) The statement about auditor independence and other ethical responsibilities required in SA 700.

Question

(MTP 1 NOV 2022)

"What constitutes a 'true and fair view' is the matter of an auditor's judgement in particular circumstances of a case." Do you agree? Enlist the requirements you as an auditor will observe to ensure true and fair view.

Answer:

Significance of True and Fair: SA 700 "Forming an Opinion and Reporting on Financial Statements", requires the auditor to form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained; and express clearly that opinion through a written report that also describes the basis for the opinion. The auditor is required to express his opinion on the financial statements that it gives a true and fair view in conformity with the accounting principles generally accepted in India (a) in the case of the Balance Sheet, of the state of affairs of the Company as at March 31, 20XX; (b) in the case of the Statement of Profit and Loss, of the profit/ loss for the year ended on that date; and (c) in the case of the Cash Flow Statement, of the cash flows for the year ended on that date.

In the context of audit of a company, the accounts of a company shall be deemed as not disclosing a true and fair view, if they do not disclose any matters which are required to be disclosed by virtue of provisions of Schedule III to that Act, or by virtue of a notification or an order of the Central Government modifying the disclosure requirements. Therefore, the auditor will have to see that the accounts are drawn up in conformity with the provisions of Schedule III of the Companies Act, 2013 and whether they contain all the matters required to be disclosed

therein. In case of companies which are governed by special Acts, the auditor should see whether the disclosure requirements of the governing Act are complied with.

It must be noted that the disclosure requirements laid down by the law are the minimum requirements. If certain information is vital for presenting a true and fair view, the accounts should disclose it even though there may not be a specific legal provision to do so. Thus, what constitutes a 'true and fair' view is the matter of an auditor's judgment in the particular circumstances of a case. In more specific terms, to ensure true and fair view, an auditor has to see:

- (i) that the assets are neither undervalued or overvalued, according to the applicable accounting principles,
- (ii) no material asset is omitted;
- (iii) the charge, if any, on assets are disclosed;
- (iv) material liabilities should not be omitted;
- (v) the statement of profit and loss discloses all the matters required to be disclosed by Part II of Schedule III
- (vi) the balance sheet has been prepared in accordance with Part I of Schedule III;
- (vii) accounting policies have been followed consistently; and
- (viii) all unusual, exceptional or non-recurring items have been disclosed separately.

SA 701

Question

(MTP 1 NOV 2022)

While auditing the complete set of consolidated financial statements of Moksh Ltd., a listed company, using a fair presentation framework, XYZ & Co., a Chartered Accountant firm, discovered that the consolidated financial statements are materially misstated due to the non-consolidation of one of the subsidiary. The material misstatement is deemed to be pervasive to the consolidated financial statements. The effects of the misstatement on the consolidated financial statements could not be determined because it was not practicable to do so. Thus, XYZ & Co. decided to provide an adverse opinion for the same and further determined that, there are no key audit matters other than the matter to be described in the Basis for Adverse Opinion section. Comment whether XYZ & Co. needs to report under SA 701 'Communicating Key Audit Matters in the Independent Auditor's Report'?

Answer:

SA 700 establishes requirements and provides guidance on forming an opinion on the financial statements. Communicating key audit matters is not a substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation. SA 705, "Modifications to the Opinion in the Independent Auditor's Report", addresses circumstances in which the auditor

concludes that there is a material misstatement relating to the appropriateness or adequacy of disclosures in the financial statements.

When the auditor expresses a qualified or adverse opinion in accordance with SA 705, presenting the description of a matter giving rise to a modified opinion in the Basis for Qualified (Adverse) Opinion section helps to promote intended users' understanding and to identify such circumstances when they occur. Separating the communication of this matter from other key audit matters described in the Key Audit Matters section, therefore, gives it the appropriate prominence in the auditor's report.

Further, when the auditor expresses a qualified or adverse opinion, communicating other key audit matters would still be relevant to enhancing intended users' understanding of the audit, and therefore the requirements to determine key audit matters apply. **However, as an adverse opinion is expressed in circumstances when the auditor has concluded that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements depending on the significance of the matter(s) giving rise to an adverse opinion, the auditor may determine that no other matters are key audit matters.**

In the given situation Moksh Ltd., a listed company, has not consolidated one of its subsidiary. Further, Consolidated Financial Statements of Moksh Ltd. Are materially misstated due to such non-consolidation. The material misstatement is also deemed to be material and pervasive and effect of the failure to consolidate have not been determined. In the given situation it is appropriate to give Adverse Opinion by XYZ & Co., a Chartered Accountant Firm.

Since, in the given case, Adverse Opinion is being expressed thus XYZ & Co. can communicate Key Audit Matter in given below manner:

Key Audit Matters: Except for the matter described in the Basis for Adverse Opinion section, we have determined that there are no other key audit matters to communicate in our report.

SA 705

Question

(RTP NOV 2022)

CA Bahubali is the statutory auditor of Bharat Ltd. for the FY 2021-22. During the course of audit CA Bahubali noticed the following:

- (i) With respect to the debtors amounting to ₹ 240 crore, no balance confirmation was received by the audit team. Further, there have been defaults on the payment obligations by debtors on the due dates during the year under audit. The Company has created a provision for doubtful debts to the tune of ₹40 crore during the year under audit. The Company has stated that the provision is based on receivables which are older than 39 months, which according to the audit team is inadequate and as such the audit team is unable to ascertain the carrying value of trade receivables.
- (ii) In respect of Inventories (which constitutes 38% of the total assets of the company), during the reporting period, the management has not undertaken physical verification of inventories at periodic intervals. Also, the Company has not maintained adequate

inventory records at the factory. The audit team was unable to undertake the physical inventory count as such the value of inventory could not be verified.

Under the above circumstances what kind of opinion should CA Bahubali give? Write the opinion paragraph and basis of opinion paragraph to be included in the Independent Auditor's Report.

Answer:

(a) In the present case, CA Bahubali is unable to obtain sufficient and appropriate audit evidence with respect to the following:

- (i) The balance confirmation with respect to debtors amounting to ₹ 240 crore is not available. Further there has been default in payment by the debtors and the provision so made is not adequate. The audit team is also unable ascertain the carrying value of trade receivables.
- (ii) With respect to 38% of the company's inventory, neither the physical verification has been done by the management nor are adequate inventory records maintained. The audit team is also unable to undertake the physical inventory count as such the value of inventory could not be verified.

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

Thus, CA Bahubali should give a Disclaimer of Opinion.

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

Disclaimer of Opinion

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

Basis for Disclaimer of Opinion

We are unable to obtain balance confirmation with respect to the debtors amounting to ₹ 240 crore. Further, there have been defaults on the payment obligations by debtors on the due dates during the year under audit. The Company has created a provision for doubtful debts to the tune of ₹ 40 crore during the year under audit which is inadequate in the circumstances of the company. The carrying value of trade receivables could not be ascertained.

Further, in respect of Inventories (which constitutes 38% of the total assets of the company), during the reporting period, the management has not undertaken physical verification of inventories at periodic intervals. Also, the Company has not maintained adequate inventory records at the factory. We were unable to undertake the physical inventory count and as such the value of inventory could not be verified.

BREW Ltd., FMCG Company having its tea gardens in northeastern states of the country is exclusively dealing in blending, processing, packing and selling of various brands of Tea. During the year under audit, the company entered into joint venture for purchasing Tea Gardens in Sri Lanka and Kenya. M/s PM & Associates are the statutory auditors of the company for the financial year 2021-22. During the course of audit, the audit team was unable to obtain sufficient appropriate evidence about a single element of the consolidated financial statement being Joint venture investment in Dharma Ltd. representing over 91% of the group's net assets having both material and pervasive possible effect to the consolidated financial statements. The group's investment in Dharma Ltd. is carried at ` 115 crore in the group's consolidated balance sheet.

Draft the opinion paragraph and basis of opinion paragraph to be included in the Independent Auditor's report.

Answer:

M/s PM & Associates are unable to obtain sufficient appropriate audit evidence about the financial information of a joint venture investment that represents over 91% of the group's net assets. The possible effects of this inability to obtain sufficient appropriate audit evidence are both material and pervasive to the consolidated financial statements. Therefore, the statutory auditor should issue a disclaimer of opinion.

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

Disclaimer of Opinion

We were engaged to audit the accompanying consolidated financial statements of BREW Ltd., (hereinafter referred to as the "Holding Company") and its subsidiaries (the Holding Company and its subsidiaries together referred to as "the Group), which comprise the consolidated balance sheet as at March 31, 2022, the consolidated statement of Profit and Loss, (consolidated statement of changes in equity) and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies (hereinafter referred to as the "Consolidated Financial Statements").

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

Basis for Disclaimer of Opinion

The Group's investment in its joint venture Dharma Ltd. Company is carried at ` 115 crore on the Group's consolidated balance sheet, which represents over 91% of the Group's net assets as at March 31, 2022. We were not allowed access to the management and the auditors of Dharma Ltd. Company, including Dharma Ltd.'s auditors' audit documentation. As a result, we were unable to determine whether any adjustments were necessary in respect of the Group's proportional share of Dharma Ltd.'s assets that it controls jointly, its proportional share of Dharma Ltd.'s liabilities for which it is jointly responsible, its proportional share of Dharma

Ltd.'s income and expenses for the year, (and the elements making up the consolidated statement of changes in equity) and the consolidated cash flow statement.

Question

(MTP 1 NOV 2022)

RST Ltd. has been dealing in tyres since 1995. The Company envisaged to expand its business and wanted to manufacture the tyres besides trading. Accordingly, the machinery was imported, installed and manufacturing operations commenced. The Government also gave certain incentives like power subsidy, land acquisition subsidy, etc. After 2 years of operations, Company received a notice from the Income Tax authorities to pay tax on incentive received in the form of power subsidy. The demand notice was served for ₹ 150.00 Lakhs.

The Company, however, filed an appeal with higher tax authorities against the demand and the matter is undecided as on 31.03.2022. Legal team of the Company anticipated that tax liability might mature. The Company has not made a provision of anticipated tax liability. Considering the provisions of Companies Act, 2013, how an auditor of RST Ltd. should see this matter and report in audit report, if required?

Answer:

Audit report - Legal team anticipated tax liability but the company did not make any provision for that -

The Council of the Institute of Chartered Accountants of India has taken note of the fact that there is a practice prevalent whereby companies do not make provision for tax even when such a liability is anticipated. It has expressed the view that on an overall consideration of the relevant provisions of law, non-provision for tax (where a liability is anticipated) would amount to contravention of the provisions of Sections 128 and 129 of the Companies Act, 2013.

Accordingly, it is necessary for the auditor to qualify his report and such qualification should bring out the manner in which the accounts do not disclose a "true and fair" view of the state of affairs of the company and the profit or loss of the company.

Applying the above to the facts given in the question, auditor should qualify his report.

An example of the manner in which the report on the balance sheet and the Statement of Profit and Loss may be qualified in this respect is given below: "The company has not provided for taxation in respect of its profits and the estimated aggregate amount of taxation not so provided for is ₹including.....for the Year ended onTo the extent of such non-provision for the year, the profits of the Company for the financial year under report have been overstated and to the extent of such aggregate non-provision, the reserves of the company appearing in the said balance sheet have been over-stated and the current liabilities and provisions appearing in the said balance sheet have been understated".

Question**(MTP 2 NOV 2022)**

Difficult Books Limited is engaged in manufacturing of active pharmaceutical ingredients. Due to change in laws and regulations, every company engaged in manufacturing in active pharmaceutical ingredients would now require production capacity license which will restrict the production of companies. Management of the company assessed the impact of the change in law over the financial position of company and appropriately disclosed the same in the financial statement.

Audit Team of the company evaluated management's disclosure and found it appropriate and sufficient. However, considering the said matter as most important and fundamental to users understanding regarding financial statement the audit team decided to disclose the same in Other Matter Paragraph.

You as an Engagement Partner are required to guide the Audit Team with respect to reporting of the said matter in Audit Report.

Answer:

As per SA 706, “Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor’s Report” if the auditor considers it necessary to draw users’ attention to a matter presented or disclosed in the financial statements that, in the auditor’s judgment, is of such importance that it is fundamental to users’ understanding of the financial statements, the auditor shall include an Emphasis of Matter paragraph in the auditor’s report provided:

- (i) The auditor would not be required to modify the opinion in accordance with SA 705 as a result of the matter; and
- (ii) When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor’s report.

In the instant case, since Difficult Books Limited is engaged in manufacturing of active pharmaceutical ingredients, would now require production capacity license which will restrict the production of companies, due to change in laws and regulations. Management of the Difficult Books Limited assessed the impact of the change in law over the financial position of company and appropriately disclosed the same in the financial statement.

Audit team of the Difficult Books Limited evaluated management's disclosure and found it appropriate and sufficient. However, considering the said matter as most important and fundamental to users understanding regarding financial statement the audit team decided to disclose the same.

The said matter is already disclosed and presented appropriately in financial statement and is of such importance that is fundamental to the users understanding of the financial statement and hence, it required to be disclosed under Emphasis of Matter paragraph.

Therefore, decision of audit team to disclose the same in Other Matter Paragraph is not in order, it should be disclosed in Emphasis of Matter Paragraph.

Chapter 2- Company Audit

Question

(RTP NOV 2022)

The Balance Sheet Extract of Siddha Limited, required to prepare financial statement under Ind-AS, as at 31st March, 2022 is as under. Comment on the presentation in terms of Division II of Schedule III to the Companies Act, 2013.

Particulars	As at 31st March, 2022	As at 31st March, 2021
<u>Property Plant and Equipment</u>		
Trademark	XXXX	XXXX
<u>Other Non-current Assets</u>		
Bank deposit with more than 12 months maturity	XXXX	XXXX
<u>Equity</u>		
Share Options Outstanding Account	XXXX	XXXX
<u>Other Current Liabilities</u>		
Application money received for allotment of securities to the extent refundable and interest accrued thereon.	XXXX	XXXX

Answer:

Following Errors have been noticed in presentation, as per Division II of Schedule III:

- “Trademark” is not to be classified under “Property Plant and Equipment” since they are specifically to be disclosed under ‘Other Intangible Assets’ as per Division II of Schedule III.
- “Bank deposit with more than 12 months maturity” is not to be classified under “Other Non-current Assets” since they are specifically to be disclosed under “Other Financial Assets” as per Division II of Schedule III.
- “Share Option Outstanding Accounts” is not to be classified under “Equity”, since it has to be disclosed under “Other Equity” as per Division II of Schedule III.
- Interest accrued thereon” is not to be classified under “Other non-current assets”, since they are specifically to be disclosed under the head “Other Financial Liabilities” as per Division II of Schedule III.

Chapter 3- CARO 2020 (Similar Question)

Question

(RTP NOV 2022)

Gautam Limited had borrowed ₹ 1000 crore from XYZ Bank, the principal of which was repayable after 5 years and interest was payable at the end of each year. For 4 years, Gautam Limited paid the interest amount on time. Gautam Limited defaulted the 5th instalment of interest payment and principal which was due on June 30, 2021. On March 31, 2021, Gautam Limited approached XYZ bank and MNO bank to restructure the existing liability. As a result, the existing principal and outstanding and overdue interest was restructured into a new loan amounting to ₹ 1,100 crore. The management did not provide any disclosure for the default on the loan on the belief that the old loan ceased to exist and the new loan has maturity after 5 years.

During the statutory audit for the financial year 2021-22, KP & Co. identified this transaction and obtained the relevant documents and understanding. Based on the underlying documents, it was identified that the said restructuring agreement was approved and signed on April 8, 2022, by both of the banks. As a result, on March 31, 2022, the restructuring was still not approved.

In the light of the above scenario, kindly guide the statutory auditors in the reporting of this transaction.

Answer:

As per Clause 3(ix) of CARO 2020, the auditor is required to report 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.				

In the given case, the company Gautam Limited defaulted in payment of the principal amount of the loan due of ₹ 1000 crore on 30 June 2021 and the interest instalment of ₹ 100 crore. The said default continued till the end of the year and on 8 April 2022, a restructuring agreement was signed by the banks and company for re-structuring the outstanding loan. Moreover, no disclosure was provided by the company with respect to the said matter.

Hence the auditor is required to report the same matter under Clause (ix) of Para 3 of CARO 2020, i.e., whether the company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, then provide the details of the period and the amount of default. Also, the auditor needs to consider the impact of such non-disclosure and the non-compliance with the financial reporting framework and accordingly the auditor needs to either issue a qualified opinion or an adverse opinion as per SA 705, “Modifications to the Opinion in the Independent Auditor’s Report”.

Chapter 4- Code of Ethics

Clause (6) of Part I of First Schedule

Question	(MTP 2 NOV 2022)
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CA Praful has recently qualified and has obtained certificate of practice. In the initial years, it is taking time to set up his clientele base. He is also conducting audit of few entities. Simultaneously, he plans to provide coaching to CA students online taking advantage of his fresh reservoir of knowledge. Therefore, he advertises his classes on various social media platforms. Comment with reference to the Chartered Accountants Act, 1949, and Schedules thereto.

Answer:

Regulation 190A of Chartered Accountants Regulations, 1988 provides that a chartered accountant in practice shall not engage in any business or occupation other than the profession of accountancy except with the permission granted in accordance with a resolution of the Council.

The Council has passed a resolution under Regulation 190A granting general permission for private tutorship and part time tutorship under coaching organization of the Institute. Such general permission is subject to the condition that direct teaching hours devoted to such activities taken together should not exceed 25 hours a week in order to be able to perform attest functions.

However, Clause 6 of Part I of the First Schedule to the Chartered Accountants Act, 1949 states that Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he solicits clients or professional work either directly or indirectly by circular, advertisement, personal communication or interview or by any other means;

Further, an advertisement of online coaching activities through social media platforms amounts to indirect solicitation as well as solicitation by another means and is, therefore, violative of Clause 6 of Part I of the First Schedule to Chartered Accountants Act, 1949.

Therefore, although a member in practice can engage in private tutorship subject to Council Guidelines but he cannot advertise by any means for coaching activities as it amounts to indirect solicitation of clients and professional work.

In the given case, CA Praful is providing coaching to CA students online and also advertising his classes on various social media platforms. In view of above, CA. Praful is guilty of

professional misconduct under Clause (6) of Part I of First Schedule to the Chartered Accountants Act 1949 for advertising his classes on various social media platforms.

Question

(RTP NOV 2022)

Clause (4) of Part I of Second Schedule

Comment on the following with reference to the with reference to the Chartered Accountants Act, 1949 and Schedules thereto:

CA Dev started practice in Punjab in the year 2019. CA Dev issued 'Turnover Certificate' for M/s. ASAUS Traders to be forwarded to the Bank for the purpose of availing cash credit facility and machinery term loan. Brother of CA Dev was proprietor of M/s. ASAUS Traders.

Answer:

As per **Clause (4) of Part I of Second Schedule** to the Chartered Accountants Act, 1949, a Chartered Accountant in practice is deemed to be guilty if he expresses his opinion on financial statements of any business or enterprise in which he, his firm, or a partner in his firm has a substantial interest.

Further, it is not permissible for a member to undertake the assignment of certification, wherein the client is relative of the member. The "relative" for this purpose would refer to the definition mentioned in Accounting Standard (AS) - 18.

In the given situation, CA Dev started practice in Punjab in the year 2019. CA Dev issued Turnover certificate for M/s. ASAUS Traders to be forwarded to the Bank for the purpose of obtaining Loan. Brother of CA Dev is proprietor of M/s. ASAUS Traders. Brother is very well covered in the definition of relative mentioned in Accounting Standard (AS)-18.

Hence, CA Dev is guilty of professional misconduct.

Clause (7) of Part I of Second Schedule

Question

(RTP NOV 2022)

Comment on the following with reference to the with reference to the Chartered Accountants Act, 1949 and Schedules thereto:

Aagam Private Limited requested CA Sheetal, a practicing Chartered Accountant, to digitally sign the form related to resignation of Mr. Rohit, one of the Director of Aagam Private Limited, along with the copy of Resignation Letter to be uploaded on the website of Registrar of Companies. The signature of Mr. Rohit was simply copied and pasted by another Director of Aagam Private Limited. CA Sheetal, without verifying the genuineness of the resignation letter, digitally signed the form and the said form was uploaded on the website of Registrar of Companies.

Answer:

As per **Clause (7) of Part I of Second Schedule** to the Chartered Accountants Act, 1949, a Chartered Accountant in practice is deemed to be guilty if he does not exercise due diligence or is grossly negligent in the conduct of his professional duties.

In the given case, Aagam Private Limited requested CA Sheetal, a practicing-chartered accountant, to digitally sign the form related to resignation of Mr. Rohit, one of the Directors of Aagam Private Limited, along with the copy of Resignation Letter to be uploaded on the website of Registrar of Companies. The signature of Mr. Rohit was simply copied and pasted by another Director of Aagam Private Limited.

CA Sheetal, without verifying the genuineness of the Resignation Letter, digitally signed the Form and the said form was uploaded on the website of Registrar of Companies.

Due to forged resignation letter, the resignation of Mr. Rohit from directorship of the Aagam Private Limited had been occurred. It was noted that CA Sheetal had not taken any step to verify forged signature on resignation letter which anyone would have taken in normal circumstances.

Consequently, CA. Sheetal would be held liable for professional misconduct as per Clause (7) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

Council General Guidelines (add towards the end of chapter)**Question****(MTP 1 NOV 2022)**

AJ & Associates and PK & Co., chartered accountant firms have joined the Network firm A to Z & Associates registered with Institute. AJ & Associates was statutory auditor of B Ltd. for last 10 years. Due to rotation of auditor as per section 139 (2) of Companies Act, 2013, B Ltd. retires AJ & Associates and appoints PK & Co., as auditor for the year 2020 -21. Comment as per Chartered Accountant Act, 1949 - Guidelines for Networking.

Answer:

As per Council General Guidelines, 2008, Chapter XV, Guidelines for Networking, once the relationship of network arises, it will be necessary for such a network to comply with all applicable ethical requirements prescribed by the Institute from time to time in general and the following requirements in particular in those cases where rotation of firms is prescribed by any regulatory authority, no member firm of the network can accept appointment as an auditor in place of any member firm of the network which is retiring.

In the given situation, AJ & Associates was statutory auditor of B Ltd. For last 10 years and due to rotation of auditor as per section 139(2) of the Companies Act, 2013 B Ltd., retires AJ & Associates and appoints PK & Co. as auditor for the year 2020-21.

It may be considered that AJ & Associates and PK & Co., chartered accountant firms have joined the network firm namely A to Z & Associates registered with Institute. In view of above Guidelines for Networking PK & Co., is disqualified for appointment as an auditor of B Ltd.

Chapter 6 - Risk Assessment and Internal Control

Question

(RTP NOV 2022)

Arihant Limited was engaged in the business of owning and managing hotels and resorts, selling tourism packages and performing airline bookings for corporate and individuals. It appointed Upadhyay & Co. as its statutory auditor for the financial year 2021-22. While planning the audit, the audit team decided that the risk of improper revenue recognition from hotel business should not be treated as a fraud risk. This conclusion was based on the assessment of earlier years, wherein no fraud was identified in revenue recorded from such business. While testing the internal financial controls over the process of revenue recognition, it was identified that the controls are not properly designed to mitigate the risk of fraud and risk of improper revenue recognition. As a result, the audit team decided to perform additional substantive testing. However, the audit team still were to the conclusion that there is no risk of fraud in revenue recognition. During the course of substantive testing, it was identified that the management did not account for revenue received from corporate hotel bookings amounting to ₹ 35 crore. These amounts were partially received in the company's bank accounts and partially received in the CFO's personal account. The amounts received in the bank account of the company were disclosed as advances received against the future bookings.

In the light of above scenario, kindly guide the statutory auditors with respect to their responsibility relating to fraud in an audit of a financial statement.

Answer:

As per SA 240, "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements" and SA 315, "Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment", the auditor shall identify and assess the risks of material misstatement due to fraud at the financial statement level, and at the assertion level for classes of transactions, account balances and disclosures. When identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions or assertions give rise to such risks.

In accordance with SA 240, "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements" and 330, "The Auditor's Responses to Assessed Risks" the auditor shall determine overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level and assertion level.

The presumption that there are risks of fraud in revenue recognition may be rebutted. For example, the auditor may conclude that there is no risk of material misstatement due to fraud relating to revenue recognition in the case where there is a single type of simple revenue transaction, for example, leasehold revenue from a single unit rental property. However, when there is a complex revenue structure or when there is lack of controls on revenue recognition, then there is a high probability of fraud risk in revenue recognition.

Obtaining an understanding of the entity and its environment, including the entity's internal control (referred to hereafter as an "understanding of the entity"), is a continuous, dynamic process of gathering, updating and analysing information throughout the audit.

In the current scenario, the company was earning revenue from multiple streams. Also, it was identified that the controls are not properly designed to mitigate the risk of fraud and risk of improper revenue recognition. During the year it was identified that the management did not account for revenue from corporate hotel bookings amounting to ₹ 35 crore. These amounts were partially received in the company's bank accounts and partially received in the CFO's personal account. The amounts received in the bank account of the company were disclosed as advances received against future bookings.

Therefore, the auditor while performing the risk assessment procedures should consider the complexity and nature of the revenue for determining the fraud risks in revenue recognition. Also, there were no adequate controls addressing the risk of improper revenue recognition or fraud risk, the audit team rebutted the fraud risk. Moreover, the audit team should have recognised fraud risk by identifying the deficiencies of internal control over the revenue recognition process and should have treated the risk of improper revenue recognition as a significant risk. Also, as per Section 143(12), the auditor is required to report all the frauds identified during the course of the audit involving amounts above ₹ 1 crore within the prescribed time frame to the Central Government.

Chapter 9- Internal, Management and Operational Audit (similar question)

Question

(RTP NOV 2022)

Write a short note on Management audit questionnaire

Answer:

A management audit questionnaire is an important tool for conducting a management audit. It is through these questionnaires that the auditors make an inquiry into important facts by measuring current performance. Such questionnaires aim at a comprehensive and constructive examination of an organisation's management and its assigned tasks. Overall, it is concerned with the appraisal of management actions in accomplishing the organisation's objectives.

Management Audit Questionnaire

Its primary objective is to highlight weaknesses and deficiencies of the organisation. It includes a review of how well or badly the management functions of planning, organising, directing and controlling are being performed. The questionnaire provides a means for evaluating an organisation's ongoing operations by examining its major functional areas. There are three possible answers to the management audit questions-

- **Yes-** It indicates that the specific area, function or aspect under study is functioning in an acceptable manner. No written application is needed in that case.
- **No-** It indicates unacceptable performance & should be explained in writing.
- **Not applicable-** It indicates that the question doesn't apply.

Thus, management audit questionnaire for this part of the audit not only serves as a management tool to analyse the current situation; more importantly, it enables the management auditors to synthesis those elements that are causing organisational difficulties and deficiencies.

Question

(MTP 2 NOV 2022)

ABC Pvt Ltd was involved in the business of manufacturing pipes and holdings. For financial year 2020-21 the company had the following turnover from its various segments and product:

Segment Name	Turnover	Profit
Steel / Iron Pipe Manufacturing	140 Crore	10 Crore
Holdings and Civil Structure Accessories	25 Crore	50 Lakh
PVC / Yellow Pipe Manufacturing	65 Crore	8 Crore

During Financial Year 2021-22, the company's performance was considerably lower compared to FY 2020-21 due to competition and high prices. Turnover and Profit of the company for FY 2021-22 is given hereunder:

Segment Name	Turnover	Profit
Steel / Iron Pipe Manufacturing	60 Crore	2 Crore
Holdings and Civil Structure Accessories	15 Crore	35 Lakh
PVC / Yellow Pipe Manufacturing	35 Crore	3 Crore

The company was fully financed through its own capital during both years. Kindly assess whether the company was required to appoint internal auditor as per section 138 read with Rule 13 of the Companies (Accounts) Rules, 2014 for FY 2021-22.

Answer:

As per section 138 of the Companies Act, 2013, such class or classes of companies as may be prescribed shall be required to appoint an internal auditor, who shall either be a chartered accountant or a cost accountant, or such other professional as may be decided by the Board to conduct an internal audit of the functions and activities of the company.

As per Rule 13 of the Companies (Accounts) Rules, 2014, the following class of companies shall be required to appoint an internal auditor which may be either an individual or a partnership firm or a body corporate, namely:

- every listed company.
- every unlisted public company having-

- o paid up share capital of fifty crore rupees or more during the preceding financial year; or
- o turnover of two hundred crore rupees or more during the preceding financial year; or
- o outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more at any point of time during the preceding financial year; or
- o outstanding deposits of twenty-five crore rupees or more at any point of time during the preceding financial year; and
- every private company having-
 - o turnover of two hundred crore rupees or more during the preceding financial year; or
 - o outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more at any point time during the preceding financial year:

In the current scenario, the company is a private limited company with having turnover of ₹ 230 Crore in FY 2020-21 and ₹ 110 Crore in FY 2021-22. As per Rule 13, every private company with a turnover of two hundred crore rupees or more during the preceding financial year must appoint an internal auditor who may be either an individual, a partnership firm or a body corporate. Hence, ABC Pvt Ltd is required to appoint Internal Audit for FY 2021 -22.

Chapter 11- Peer Review

Question

(RTP NOV 2022)

Prabhu & Co LLP is a large firm of Chartered Accountants based out of Mumbai. Prabhu & Co. LLP is subject to peer review which was last conducted 3 years back. For the peer review of the financial year ended 31st March 2021, the firm got an intimation on 29th May 2021. The process of peer review got started and was completed on 27th September 2021. In view of peer reviewer, the systems and procedures of Prabhu & Co. LLP are deficient / non-compliant. The peer reviewer did not share any of his observations with Prabhu & Co LLP as draft and final report was submitted to the Board. Comment.

Answer:

Peer Review Report of Reviewer: After completing the on-site Review, the Peer Reviewer, before making his Report to the Board, **shall communicate his findings in the Preliminary Report to the Practice Unit** if in his opinion, the systems and procedures are deficient or non-compliant with reference to any matter that has been noticed by him or if there are other matters where he wants to seek clarification.

The Practice Unit shall within 15 days after the date of receipt of the findings, make any submissions or representations, in writing to the Reviewer. (i.e. Response to the Preliminary Report).

At the end of an on-site Review if the Reviewer is satisfied with the reply received from the Practice Unit, he shall submit a Peer Review Report to the Board along with his initial findings, response by the Practice Unit and the manner in which the responses have been dealt with. A copy of the report shall also be forwarded to the Practice Unit.

In case the Reviewer is of the opinion that the response by the Practice Unit is not satisfactory, the Reviewer shall accordingly submit a modified Report to the Board incorporating his reasons for the same. The Reviewer shall also submit initial findings **(i.e. Preliminary Report), response by the Practice Unit (Response to Preliminary Report)** and the manner in which the responses have been dealt with. A copy of the report shall also be forwarded to the Practice Unit.

In case of a modified report, The Board shall order for a **“Follow On”** Review after a period of one year from the date of issue of report as mentioned above. If the Board so decides, the period of one year may be reduced but shall not be less than six months from the date of issue of the report.

In the instant case, in view of Peer Reviewer systems and procedures in Prabhu & Co. LLP are deficient, therefore, Peer Reviewer should not submit the report directly to the Board. Thus, contention of Prabhu & Co. LLP is correct.

Question (MTP 2 NOV 2022)

CA. Vimal wants to apply in the empanelment of peer reviewer. He was into employment till 2012 since then he shifted from industry and started his own practice. Below is his experience and employment record from 1995 to 2012.

Name of Company	Designation	From Date	To Date
Parshav Ltd	Project Implementation Manager	1-4-1995	31-3-1998
Supersaver Ltd	Financial Reporting Senior Manager (Assisting in Audits)	1-4-1998	31-3-2007
Parasnath Ltd	Project & Improvement Director	1-4-2007	31-3-2012
Own Practice – Sole Prop	Audit & Taxation	1-4-2012	31-3-2022

Kindly assess whether CA. Vimal can apply and is qualified to get admitted in the empanelment of Peer Reviewer.

Answer:

As per Peer Review Statement,

1. A Peer Reviewer shall: -

a) Shall be a member in practice with at least 7 years of audit experience.

- b) In case a member has moved from industry to practice and is currently in practice he should have at least 10 years of audit experience in industry and at least 3 years audit experience in practice.
 - c) Should have undergone the requisite training and cleared the requisite test for Peer Review as prescribed by the Board.
2. A member on being appointed as a Reviewer shall be required to furnish-
- (a) a declaration as prescribed by the Board, at the time of Empanelment as a Peer Reviewer.
 - (b) a Declaration of Confidentiality as per Annexure A to this Statement while giving consent for appointment as a Peer Reviewer.
3. A member shall not be eligible for being appointed as a Reviewer of a Practice Unit, if -
- (i) any disciplinary action / proceeding is pending against him;
 - (ii) he has been found guilty of professional or other misconduct by the Council or the Board of Discipline or the Disciplinary Committee at any time
 - (iii) he has been convicted by a competent court whether within or outside India, of an offence involving moral turpitude and punishable with imprisonment,
 - (iv) he or his partners have any obligation or conflict of interest in the Practice Unit.
 - (v) He has undergone training/articleship under any of the partner of Practice Unit.
4. A Reviewer shall not accept any professional assignment from the Practice Unit for a period of next two years from the date of appointment. Further, he should not have accepted any professional assignment from the Practice Unit for a period of two years before the date of appointment as reviewer of that Practice Unit.

In the current scenario, CA. Vimal was in employment for a period from 1 -4-95 to 31-3-12 i.e., 17 years. Out of which, he was having audit experience for 9 years. However, he is in practice since 10 years i.e. 2012 to 2022. Hence, he will be eligible for Peer Reviewer by virtue of the condition stipulating that a Peer Reviewer shall be a member in practice with at least 7 years of audit experience.

Chapter 12- Audit of NBFC (Similar Ques ,Important for practice)

Question

(RTP NOV 2022)

Sudarshan Ltd. is a company registered under the Companies Act, 2013. The company is engaged in the business of loans and advances, acquisition of shares / stocks / bonds / debentures/securities issued by Government or local authorities. For the year ended 31st March, 2022 following are some extracts from the financial statements:

(i)	Paid-up share capital	₹ 40.53 Cr.
(ii)	Non-Current Assets - Loans & Advances	₹ 75.50 Cr.
(iii)	Current Assets - Loans and advances	₹ 294.33 Cr.
(iv)	Total assets of the company	₹ 618.55 Cr.
(v)	Intangible assets	₹ 6.35 Cr.
(vi)	Profit for the Year	₹ 8.15 Cr.
(vii)	Income from interest and dividends	₹ 62.31 Cr.
(viii)	Gross income	₹ 111.23 Cr.

Directors intend to apply for registration as Non-Banking Financial Company (NBFC) under Section 45-IA of the Reserve Bank of India (Amendment) Act, 1997. Advise.

Answer

In order to identify a particular company as Non-Banking Financial Company (NBFC), it will consider both assets and income pattern as evidenced from the last audited balance sheet of the company to decide its principal business. The company will be treated as NBFC when a company's

- (i) Financial assets constitute more than 50 per cent of the total assets (netted off by intangible assets) and
- (ii) Income from financial assets constitute more than 50 per cent of the gross income.

A company which fulfils both these criteria shall qualify as an NBFC and would require to be registered as NBFC by RBI.

In the given case, applying the Criteria (i) Financial assets constitute more than 50 per cent of the total assets (netted off by intangible assets),

A. Financial Assets of Sudarshan Ltd. are =

Non-Current Assets - Loans & Advances	₹ 75.50 Cr.
Add: Current Assets - Loans and advances	₹ 294.33 Cr.

Total Financial Assets	₹ 369.83 Cr.
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B. Total Assets (netted off by intangible assets) of Sudarshan Ltd. are=

Total assets of the company	₹ 618.55 Cr.
Less: Intangible assets	₹ 6.35 Cr.
Total Assets (netted off by intangible assets)	₹ 612.20 Cr.

In view of above, Financial assets of Sudarshan Ltd. constitute more than 50 per cent of the total assets (netted off by intangible assets).

Applying the Criteria (ii) Income from financial assets constitute more than 50 per cent of the gross income.

Income from financial assets = ₹ 62.31 Cr

Gross Income = ₹ 111.23 Cr

From the above, it is clear that Sudarshan Ltd.'s financial assets constitute more than 50 per cent of the total assets (netted off by intangible assets) and income from financial assets constitutes more than 50 per cent of the gross income. Hence, Sudarshan Ltd. fulfills both these criteria to qualify as an NBFC.

Thus Sudarshan Ltd. can apply for registration under Section 45-IA of Reserve Bank of India (Amendment) Act, 1997 in prescribed form along with the necessary documents.

Question

(MTP 1 NOV 2022)

Shreyansh & Co LLP, a firm of Chartered Accountants, was appointed as auditor of an NBFC. The audit work has been completed. The audit team which was involved in the fieldwork came across various observations during the course of audit of this NBFC and have also limited understanding about the exceptions which are required to be reported in the audit report. They would like to understand in detail regarding the obligations on the part of an auditor in respect of exceptions in his report so that they can conclude their work. Briefly explain.

Answer:

Obligation of auditor to submit an exception report to the RBI:

(I) Where, in the case of a non-banking financial company, the statement regarding any of the items referred to in paragraph 3 above, is unfavorable or qualified, or in the opinion of the auditor the company has not complied with:

(a) the provisions of Chapter III B of RBI Act (Act 2 of 1934); or

(b) Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 2016; or

(c) Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016 and Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

It shall be the obligation of the auditor to make a report containing the details of such unfavorable or qualified statements and/or about the non-compliance, as the case may be, in respect of the company to the concerned Regional Office of the Department of Non-Banking Supervision of the RBI under whose jurisdiction the registered office of the company is located as per first Schedule to the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 2016.

(II) The duty of the Auditor under sub-paragraph (I) shall be to report only the contraventions of the provisions of RBI Act, 1934, and Directions, Guidelines, instructions referred to in sub- paragraph (1) and such report shall not contain any statement with respect to compliance of any of those provisions.

Chapter 13- Audit of Public Sector Undertaking

Question

(RTP NOV 2022)

Comptroller & Auditor General appointed Sambhav & Associates, a chartered accountant firm, to conduct Performance audit of MAP Ltd., a public sector undertaking of Government of India. The firm conducted the audit with a view to check all the expenses of the unit are in conformity with the public interest and publicly accepted customs. The audit report submitted by audit firm was rejected by C&AG. Give your opinion on the action of C&AG.

Answer:

In the given scenario, C&AG appointed Sambhav & Associates, a chartered accountant firm, to conduct Performance Audit of MAP Ltd., a PSU of Government of India. The firm conducted audit with a view to check all the expenses of the unit are in conformity to the public interest and publicly accepted customs which is not Performance Audit.

A performance audit is an objective and systematic examination of evidence for the purpose of providing an independent assessment of the performance of a government organization, program, activity, or function in order to provide information to improve public accountability and facilitate decision-making by parties with responsibility to oversee or initiate corrective action.

Performance audit in PSUs is conducted by the C&AG (Supreme Audit Institutions) through various subordinate offices of Indian Audit and Accounts Department (IAAD). In conducting performance audit, the subordinate offices are guided by manual and auditing standards prescribed by C&AG.

Therefore, the objectives of performance auditing are evaluation of economy, efficiency, and effectiveness of policy, programmes, organization and management. It also promotes

accountability by assisting those charged with governance and oversight responsibilities to improve performance; and transparency by affording taxpayers, those targeted by government policies and other stakeholders an insight into the management and outcomes of different government activities.

Performance auditing focuses on areas in which it can add value which have the greatest potential for development. It provides constructive incentives for the responsible parties to take appropriate action.

Regulations on Audit and Accounts issued by C&AG lay down that the responsibility for the development of measurable objectives and performance indicators as also the systems of measurement rests with the Government departments or Heads of entities. They are also required to define intermediate and final outputs and outcomes in measurable and monitorable terms, standardise the unit cost of delivery and benchmark quality of outputs and outcomes.

Thus, rejection of audit report (submitted by audit firm) by C&AG is in order as audit with a view to mere check all the expenses of the unit are in conformity to the public interest and publicly accepted customs done by audit firm is not performance audit in all aspects.

Chapter 14- Audit under Fiscal Law

Question

(RTP NOV 2022)

Billimoria & Billimoria, a partnership firm, is engaged in providing engineering consultancy services to insurance corporates in automobile sector. The firm conducts risk inspection of vehicles and submit their reports to insurance companies. Both the partners are Chartered Engineers. The following information is culled out from the account books of the company for financial year 2021 -22 by the firm:

Particulars	Rupees in Crore
Turnover	8.50
Receipt on account of sales/debtors	6.00
Cash receipt from debtors	0.10
Expenditure during year	7.00
Cash expenditure	0.21
Cash loan repayment	0.05

The partner of said firm informs you that due to changes in income-tax laws, their firm is not liable for audit under section 44 AB of Income tax Act (commonly called as tax audit). How would you deal with the matter? Is contention of partner in accordance with law?

Answer:

Section 44 AB(a) of the Income Tax Act, 1961 prescribes that a person carrying on business shall get his accounts audited if his total sales, turnover or gross receipts exceed ₹ 1 crore in

any previous year. However, this limit was enhanced to ₹ 10 crore in the following case where:

-

- (a) aggregate of all amounts received including amount received for sales, turnover or gross receipts during the previous year, in cash, does not exceed five per cent of the said amount; and
- (b) aggregate of all payments made including amount incurred for expenditure, in cash, during the previous year does not exceed five per cent of the said payment.

However, section 44 AB(b) of the Income Tax Act, 1961 states that in case of profession, every person shall get his accounts audited, if his gross receipts in profession exceed ₹ 50 lakh. The above said firm is engaged in providing engineering consultancy services to insurance corporates. Hence, the benefit of enhanced threshold limit is not available to persons engaged in professional activities.

The information regarding cash receipt and payment although falling within 5% of total receipts/payments is not relevant in the instant case.

Hence, contention of partner is not correct, and firm is required to get its accounts audited under income tax law.

Question

(MTP 1 NOV 2022)

While conducting the tax audit of Rajul Ltd. you observed that company has timely filed ETDS return for TDS deducted on salary under section 192 of the Income Tax Act, 1961 in form 24Q in respect of fourth quarter period from 1st January 2022 to 31st March 2022. The company has not furnished list of details which are not reported in the statement of tax deducted at source under the pretext that TDS statements are furnished within the prescribed time. As a Tax Auditor of Rajul Ltd. how you would deal and report?

Answer:

As per Clause 34 (b) of the Form 3CD, the auditor has to report whether the assessee is required to furnish the statement of tax deducted or tax collected. If yes, please furnish the details:

Tax deduction and collection Account Number (TAN)	Type of Form	Due date for furnishing	Date of furnishing, if furnished	Whether the statement of tax deducted or collected contains information about all transactions which are required to be reported	If not, please furnish list of details/transactions which are not reported

Accordingly, clause 34 (b) requires, a list of details/transactions which are not reported in the statement of tax deducted at source and statement of tax collected at source are required to be

furnished. The reporting requirement is notwithstanding the fact that the assessee has furnished the statements of tax deducted at source and tax collected at source within the prescribed time.

In the given situation, Rajul Ltd., has timely filed ETDS return for TDS deducted on Salary under section 192 of the Income Tax Act in Form 24Q in respect of 4th quarter. The company has not furnished list of details which are not reported in the statement of tax deducted at source under the pretext that TDS Statements are furnished within the prescribed time. Therefore, in view of above, Rajul Ltd. is required to furnish list of details which are not reported in the statement of tax deducted at source.

Question

(MTP 2 NOV 2022)

Gautam Ltd. is engaged in the manufacturing of textile products having an annual capacity of producing 2,30,000 units of garments. Gautam Ltd. is covered under the provisions of Goods and Service Tax Law with an applicable rate of 12%. During the financial year 2021-2022, Gautam Ltd. received a demand notice of ` 17.00 Lacs pertaining to the F.Y 2015-16 when the provisions of Central Excise Act were applicable. Gautam Ltd. deposited the demand amount after discussing with its legal department. Comment whether a tax auditor of Gautam Ltd. is required to report the same.

Answer:

Gautam Ltd. is a manufacturer of textile products and is covered under GST Law. During financial year 2021-2022 Gautam Ltd. has received a demand notice of 17 lakh which pertains to financial year 2015-2016 when the Central Excise Act was prevalent.

As a tax auditor of Gautam Ltd., reporting would be under Clause 41 which is given hereunder:

“Please furnish the details of demand raised or refund issued during the previous year under any tax laws other than Income Tax Act, 1961 and Wealth tax Act, 1957 along with details of relevant proceedings. “

It may be noted that even though the demand/refund order is issued during the previous year, it may pertain to a period other than the relevant previous year. In such cases also, reporting has to be done under this clause. If there is any adjustment of refund against any demand, the auditor shall also report the same under this clause.

In this case, liability is of excise duty i.e. under Central Excise Act, other than Income Tax Act and Wealth Tax Act, thus this clause gets attracted and the reporting has to be done as per format:

S No.	Name of the Applicable Act	Demand/ Refund Order no., if any	Date of demand raised/refund issued	Financial year to which the demand/refund relates	Amount of demand/raised /refund issued	Adjustment of refund against demand, if any	Remarks

Chapter 15- Audit of Consolidated Financial Statements

Question

(RTP NOV 2022)

Jambu & Sudharma Investments Ltd. is a company having paid up share capital of ₹ 1 crore, it has a subsidiary, Investors Fund Management Ltd. Major business of Jambu & Sudharma Investments Ltd. is to pool money from investors on a collective basis and invest this money in various funds. This company pooled ₹ 12 crore from a number of clients, which represent the Company's shareholders.

While auditing books of accounts of Jambu & Sudharma Investments Ltd. CA Vardhman observed that whole amount of ₹ 12 crore pooled has been invested in shares and debentures of various companies and profit earned due to appreciation of the prices of these shares has been distributed to various shareholders of the company. Performance of all of its investments is measured on fair value basis.

Now, CA Vardhman raised an issue while auditing financial statements of Jambu & Sudharma Investments Ltd. whether the consolidated financial statements are required as per Section 129(3) of the Companies Act, 2013? Analyse the above issue and give your opinion.

Answer:

According to Section 129(3) of the Companies Act, 2013, where a company has one or more subsidiaries, including associate company and joint venture, it shall, in addition to its own financial statements prepare a consolidated financial statement of the company and of all the subsidiaries in the same form and manner as that of its own.

As per sub-section 6 of the section 129 of the Companies Act, 2013, the Central Government may, on its own or on an application by a class or classes of companies, by notification, exempt any class or classes of companies from complying with any of the requirements of section 129 or the Rules made thereunder.

An investment entity is an entity that:

- (a) obtains funds from one or more investors for the purpose of providing those investor(s) with investment management services;
- (b) commits to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and
- (c) measures and evaluates the performance of substantially all of its investments on a fair value basis.

An investment entity need not present consolidated financial statements if it is required, in accordance with paragraph 31 of Ind AS 110, to measure all of its subsidiaries at fair value through profit or loss. A parent shall determine whether it is an investment entity.

However, as per paragraph 33 of Ind AS 110, parent of an investment entity shall consolidate all entities that it controls, including those controlled through an investment entity subsidiary, unless the parent itself is an investment entity.

Applying the above to the given case of Jambu & Sudharma Investments Ltd., which fulfils all the conditions stated above, it is an investment entity. By applying Para 31 and 33 of Ind AS

110, it can be concluded that Jambu & Sudharma Investments Ltd. is not required to consolidate as per Section 129 (3) of the Companies Act, 2013.

Question

(MTP 2 NOV 2022)

T Ltd. is holding 68% share of B Ltd, 51% share of C Ltd. RS & Co. Chartered Accountants are the statutory auditors of T Ltd. MN & Co. Chartered Accountants are the statutory auditors of B Ltd. and C Ltd. MN & Co have qualified the report of B Ltd. due to material discrepancies in standalone financial statement. While framing the opinion on Consolidated Financial Statement of T Ltd., RS & Co. (Principal Auditor) have ignored the qualification of B Ltd. considering it not material at Group Level. Comment.

Answer:

In carrying out the audit of the standalone financial statements, the computation of materiality for the purpose of issuing an opinion on the standalone financial statements of each component would be done component-wise on a standalone basis. However, with regard to determination of materiality during the audit of consolidated financial statements (CFS), the auditor should consider the following:

- The auditor is required to compute the materiality for the group as a whole. This materiality should be used to assess the appropriateness of the consolidation adjustments (i.e. permanent consolidation adjustments and current period consolidation adjustments)
- The parent auditor can also use the materiality computed on the group level to determine whether the component's financial statements are material to the group to determine whether they should scope in additional components, and consider using the work of other auditors as applicable.
- The principal auditor also computes materiality for each component and communicates to the component auditor, if he believes is required for true and fair view on CFS.
- The principal auditor also obtains certain confirmations from component auditor like independence, code of ethics, certain information required for consolidation and disclosure requirements etc.

However, while considering the observations (for instance modification and /or emphasis of matter in accordance with SA 705/706) of the component auditor in his report on the standalone financial statements, the principles of SA 600 needs to be considered., The parent auditor should comply with the requirements of SA 600, "Using the Work of Another Auditor". Therefore, the concept of materiality would be considered while considering the observations of the component auditor.

Hence RS & Co. cannot ignore the qualification of B Ltd. while framing the opinion on consolidated financial statements of T Ltd.

Chapter 18 - Audit of Insurance Companies

Question

(RTP NOV 2022)

Write a short note on Free look Cancellation (FLC).

Answer:

Free Look Cancellation (FLC) : As per clause 6(2) of IRDA (Protection of Policyholders Interest) Regulations, 2002, “the insurer shall inform by the letter forwarding the policy that he has a period of 15 days from the date of receipt of the policy document to review the terms and conditions of the policy and where the insured disagrees to any of those terms or conditions, he has the option to return the policy stating the reasons for his objection, when he shall be entitled to a refund of the premium paid, subject only to a deduction of a proportionate risk premium for the period on cover and the expenses incurred by the insurer on medical examination of the proposer and stamp duty charges”.

Accordingly, FLC is an option provided to the policyholder wherein he has a period of 15 days from the date of receipt of the policy document to review the Terms & Conditions of the policy and in case of disagreement to any of the terms & conditions, he/ she has the option to return the policy stating the reason for policy's cancellation. FLC requests can be received through any mode –e-mail, fax and letters depending on insurer's policy. In case of written letters, the signature of the policy holder should be matched with the original proposal form. FLC request is processed only when the policy holder is not satisfied with the terms and conditions of the policy document and not for any other reasons. FLC refund is paid either by cheque or in case the policy holder wants direct credit, then consent for direct credit along with cancelled cheque for bank account details is submitted.

Chapter 19- Audit of Banks

Question

(RTP NOV 2022)

CA Prachi was conducting statutory audit of branch of a nationalized bank for the year 2021-22. While reviewing operations and documents/papers of a borrower enjoying overdraft credit facilities of ₹ 50 crore (availed against security of stocks and book debts), following observations were jotted down by her: -

- (i) The balance in overdraft credit facility as on 31st March, 2022 was ₹ 55.65 crore. The balance in account exceeded sanctioned limit during the whole month of March 2022.
- (ii) As per terms of sanction letter, stock/book debt statements were required to be submitted monthly. Latest available stock/book debt statement for the month of February, 2022 showed drawing power of ₹ 48.50 crore only. However, stock/book debt statements of previous months showed adequate drawing power.
- (iii) Stock audit of borrower was also conducted during the year by one of empanelled stock auditors of the bank. Stock audit report dated 31st December, 2021 placed on the record showed adequate drawing power in the account. However, it has commented adversely on the declining turnover of borrower in year 2021 -22 (till the date of stock audit report) as compared to proportionate turnover in preceding year.

- (iv) The renewal of overdraft facilities was due on 20th October, 2021. The account was short renewed by competent authority for a period of 3 months pending submission of complete papers.

However, borrower has not submitted complete renewal papers till 31st March, 2022. There is a request letter from borrower on record stating that valuation report of a property located at a faraway location was taking time.

The branch has classified the account as 'Standard Asset'. Considering above, CA Prachi is in dilemma relating to proper classification of above advance. Guide her.

Answer:

The borrower was enjoying overdraft credit facilities of ₹ 50 crore against security of stocks and debts. Further, though latest available stock statement for the month of February, 2022 showed inadequate drawing power, there was adequate drawing power available throughout the year. Stock audit report dated 31.12.2021 also reflected adequate drawing power. Hence, it shows that borrower had adequate drawing power during the year. Further, comment on declining sales is of general informative value to management for making credit decisions.

The fact of over drawings in account during the month of March, 2022 and inadequate drawing power in a month are in nature of temporary deficiencies and do not require account to be classified as NPA in accordance with asset classification and provisioning norms of RBI.

RBI instructions lay down that ordinarily credit limits need to be reviewed not later than three months from the due date. As per Guidance note on Audit of Banks, in case of constraints such as non-availability of financial statements and other data from the borrowers, the branch should furnish evidence to show that renewal/ review of credit limits is underway and would be completed soon. In any case, delay beyond six months is not considered desirable as a general discipline. Hence, an account where the credit limits have not been reviewed/ renewed within 180 days from the due date will be treated as NPA.

It would be pertinent to note that the counting of 180 days would be required to be done from the date of original due date for renewal and not from the date of expiry of short reviews / technical reviews. In the instant case, the original date of renewal was 20th October, 2021 and period of 180 days has still not expired as on balance sheet date.

Keeping in view all above factors, CA Prachi should accept classification of account as 'Standard Asset' made by branch.

Question

(MTP 2 NOV 2022)

You are part of engagement team conducting statutory audit of a branch of nationalized bank. During the course of audit, it has come to your notice that there are large number of cash credit accounts in the branch. Many of the cash credit accounts are only partially utilized during substantial part of year. However, in the month of March, the accounts are fully utilized. On further scrutiny, it is observed that these account holders have made fixed deposits from these utilized amounts at the end of year. These deposits have been liquidated in first week of April

of next financial year. Comment upon how this situation would be dealt by you as a statutory branch auditor?

Answer:

In the given case, many of the cash credit accounts in the branch of a nationalized bank are only partially utilized during substantial part of year. However, in the month of March, the accounts are fully utilized. On further scrutiny, it is observed that these account holders have made fixed deposits from these utilized amounts at the end of year. These deposits have been liquidated in first week of April of next financial year.

This is an example of **window dressing**. The branch is resorting to window dressing by artificially boosting its advances and deposits. Utilization of advances and placing of fixed deposits at end of year in branch and again liquidation of deposits early next year indicate that branch is resorting to window dressing to inflate its advances as well as deposits artificially.

The auditor has to verify whether the unavailed portion of the credit facilities (overdraft, cash credit) are used to boost the loans and deposits which might tantamount to window dressing.

The relevant regulatory guidelines also prohibit such type of practices and these might involve penal action in terms of Banking Regulation Act, 1949.

The same needs to be suitably reported in audit report and commented in LFAR also. In appropriate cases, making a suitable qualification in the main audit report has also to be considered

Chapter 21- Audit in an Automated Environment

Question

(RTP NOV 2022)

M/s RST & Associates have been appointed as auditors of ADI Ltd. for the financial year 2021-22. The processes, operations, accounting and decisions are carried out by using computers in ADI Ltd. M/s RST & Associates understand that there are several aspects that they should consider to determine the level of automation and complexity in the business environment of ADI Ltd. While planning the audit work, the engagement partners discussed with the audit staff about the various types of controls in the automated environment that are put in place to mitigate the IT risks and to maintain the confidentiality, integrity, availability and security of data such as General IT Controls; Application Controls; and IT-Dependent Controls.

You are required to briefly explain:

- (i) General IT Controls.
- (ii) Application Controls.
- (iii) IT-Dependent Controls.

Answer:

The controls that are put in place to mitigate the IT risks and to maintain the confidentiality, integrity, availability and security of data are General IT Controls, Application Controls and IT-Dependent Controls.

General IT Controls: “General IT controls are policies and procedures that relate to many applications and support the effective functioning of application controls. They apply to mainframe, miniframe, and end-user environment. General IT controls that maintain the integrity of information and security of data commonly include controls over the following:” (SA 315)

- Data center and network operations;
- System software acquisition, change and maintenance
- Program change;
- Access security;
- Application system acquisition, development, and maintenance (Business Applications).

These are IT controls generally implemented to mitigate the IT specific risks and applied commonly across multiple IT systems, applications and business processes. Hence, General IT controls are known as “pervasive” controls or “indirect” controls.

Application Controls: Application controls include both automated or manual controls that operate at a business process level. Application controls can be preventive as well as detective in nature and are designed to ensure the integrity of the accounting records. application controls relate to procedures used to initiate, record, process and report transactions or other financial data. These controls help ensure that transactions occurred, are authorised, and are completely and accurately recorded and processed. Automated Application controls are embedded into IT applications viz., ERPs and help in ensuring the completeness, accuracy and integrity of data in those systems. Examples of automated applications include edit checks and validation of input data, sequence number check, limit check, format check, range check, reasonableness check, mandatory data fields, existence check etc.

IT dependent controls: IT dependent controls are basically manual controls that make use of some form of data or information or report produced from IT systems and applications. In this case, even though the control is performed manually, the design and effectiveness of such controls depend on the reliability of source data.

Due to the inherent dependency on Information Technology, the effectiveness and reliability of Automated application controls and IT dependent controls require the General IT Controls to be effective.

Chapter 22- Quality Review

Question

(RTP NOV 2022)

What are the important areas for evaluation while conducting quality reviews in terms of SQC -1 Standard on Quality Control?

Answer:

Evaluating the professional judgment exercised by the auditor: It is also important for the Technical Reviewer (hereinafter referred as TR) to understand that “professional judgment”, as defined in SA 200, “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing” is an integral concept in the context of an audit and application of SAs in real life audit scenarios. SA 200 defines professional judgment as “the application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the course of action that is appropriate in the circumstances of the audit engagement.”

The concept of “professional judgment” underscores the fact that Standards, particularly, Standards on Auditing are written to lay down the fundamental principles that would apply to an audit situation. Hence, no Standard can have straight jacketed application/solutions for all audit scenarios. Above all, the Standards on Auditing issued by the Institute of Chartered Accountants of India are principle based rather than rule based. Hence, almost all the SAs envisage exercise of professional judgment by the auditor in their application in real life audit scenarios.

The TR would need to appreciate that the exercise of professional judgment in any particular case is based on the facts and circumstances that are known to the auditor as at the time of exercising that professional judgment. Normally, exercise of professional judgement by an auditor is preceded by consultation on the relevant matters both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm.

In evaluating the professional judgment exercised by the auditor, the TR should consider the following factors:

- whether the judgment reached reflects a due consideration and application of the relevant auditing and accounting principles; and
- whether the judgment is appropriate in the light of, and consistent with, the facts and circumstances that were known to the auditor up to the date of the auditor’s report. Hence, the TR and the QR Team should not, under any circumstance, use “hindsight” (i.e. perception or retrospection) in their evaluation of exercise of professional judgment by the auditor.

Since the auditor needs to exercise professional judgment throughout the audit, the latter also needs to be appropriately documented. Hence, the TR can expect to find such audit documentation as a part of the audit engagement file. It is important to note that professional judgment cannot be used by an auditor as a justification for decisions that are not otherwise supported by the facts and circumstances of the engagement or sufficient appropriate audit evidence.

Chapter 23- Forensic Audit

Question

(RTP NOV 2022)

Write a short note on Services rendered by Forensic Auditors.

Answer:

Services rendered by Forensic Auditors are:

- Crafting questions to be posed
- Responding to questions posed
- Identifying documents to be requested and/or subpoenaed
- Identifying individuals to be most knowledgeable of facts
- Conducting research relevant to facts of the case
- Identifying and preserving key evidence
- Evaluating produced documentation and information for completeness
- Analysing produced records and other information for facts
- Identifying alternative means to obtain key facts and information
- Providing questions for deposition and cross examination of fact and expert witnesses

Corrigendum

Chapter 1- SA

1. SA 220 Question 10 (Replace the answer with this)

Question 10

HK & Co. Chartered Accountants have been auditors of SAT Ltd (a listed entity) for the last 8 financial years. CA. H, partner of the firm, has been handling the audit assignment very well since the appointment. The audit work of CA. H and her team is reviewed by a senior partner CA. K to assure that audit is performed in accordance with professional standards and regulatory and legal requirements. CA. K was out of India for some personal reasons, so this year CA. G has been asked to review the audit work. In your opinion, what areas CA. G should consider at the time of review. List any four areas and also comment whether firm is complying with Standard on Quality Control or not.

Answer:

Compliance with Standard on Quality Control on review of audit work -

As per SQC 1, an engagement quality control review for audits of financial statements of listed entities includes considering the following:

- (i) The work has been performed in accordance with professional standards and regulatory and legal requirements;
- (ii) Significant matters have been raised for further consideration;
- (iii) Appropriate consultations have taken place and the resulting conclusions have been documented and implemented;
- (iv) There is a need to revise the nature, timing and extent of work performed;
- (v) The work performed supports the conclusions reached and is appropriately documented;
- (vi) The evidence obtained is sufficient and appropriate to support the report; and
- (vii) The objectives of the engagement procedures have been achieved.

The firm should establish policies and procedures:

- (i) Setting out criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and
- (ii) For all audits of financial statements of listed entities, requiring the rotation of the engagement partner after a specified period in compliance with the Code.

The familiarity threat is particularly relevant in the context of financial statement audits of listed entities. For these audits, the engagement partner should be rotated after a pre- defined period, normally not more than seven years.

From the facts given in the question and from the above stated paras of SQC 1, it can be concluded that firm is not complying with SQC 1 as Engagement Partner H is continuing for more than 7 years.

2. SA 700 Question 5 (Replace the answer with this)

Question

CA S has been appointed as Statutory Auditor of SRT Ltd. for the financial year 2020-2021. The Company while preparing financial statements for the year under audit prepared one additional profit and loss account that disclosed specific items of expenditure and included the same as an appendix to the financial statements. CA. S has not been able to understand this as the additional profit and loss account is not covered under applicable financial reporting framework. Guide him as to how he should deal with this issue while reporting on the financial statements of SRT Ltd.

Answer:

If supplementary information that is not required by the applicable financial reporting framework is presented with the audited financial statements, the auditor shall evaluate whether, in the auditor's professional judgment, supplementary information is nevertheless an

integral part of the financial statements due to its nature or how it is presented. When it is an integral part of the financial statements, the supplementary information shall be covered by the auditor's opinion.

If supplementary information that is not required by the applicable financial reporting framework is not considered an integral part of the audited financial statements, the auditor shall evaluate whether such supplementary information is presented in a way that sufficiently and clearly differentiates it from the audited financial statements. If this is not the case, then the auditor shall ask management to change how the unaudited supplementary information is presented.

If management refuses to do so, the auditor shall identify the unaudited supplementary information and explain in the auditor's report that such supplementary information has not been audited.

When an additional profit and loss account that discloses specific items of expenditure is disclosed as a separate schedule, included as an appendix to the financial statements, the auditor may consider this to be supplementary information that can be clearly differentiated from the financial statements.

Thus, additional profit and loss account is not considered an integral part of the audited financial statements and the auditor shall evaluate that supplementary information is presented in a way that sufficiently and clearly differentiates it from the audited financial statements.

Chapter 23- Forensic Audit

Question 10 – Replace the answer of the forensic auditor should necessarily possess the following **characteristics and skills: (there is mistake in Institute answer.)**

Question

BR Construction was into the business of building roads and other infrastructure facilities for government contracts. Mr. Tiwari, one of the senior official, was looking after the procurement of cement required at the construction sites. There was a substantial increase in the price of cement bags bought as compared to those bought prior to the appointment of Mr. Tiwari. The management of the company decides to get a forensic audit done for the transactions handled by Mr. Tiwari. What points should be kept in mind by the management while appointing a forensic auditor?

Answer:

A Forensic Auditor is often retained to analyze, interpret, summarize and present complex financial and business-related issues in a manner which is both understandable and properly supported. Forensic Accountants are trained to look beyond the numbers and deal with the business reality of the situation. Forensic auditor needs to have an understanding on various frauds that can be carried off and how evidence need to be collected.

While appointing a forensic auditor, the Management of BR Construction must initially consider whether the firm has the necessary skills and experience to accept the work. In view

of above, Management of BR Construction should ensure **that the forensic auditor should necessarily possess the following characteristics and skills:**

Characteristics- Forensic Auditor	Skills - Forensic Auditor should possess
<ul style="list-style-type: none"> i. Out of the Box Thinking ii. Strong Visualization and Imagination iii. Curiosity iv. Persistence v. Detail-oriented vi. Inquisitiveness vii. Creativity viii. Discretion ix. Skepticism x. Confidence xi. Sound professional judgement xii. Objectivity and credibility 	<ul style="list-style-type: none"> i. Auditing standards, procedures and related methodologies ii. Accounting & Business reporting systems iii. Information Technology iv. Data Analytics v. Criminology vi. Legal Framework vii. Litigation processes & procedures viii. Investigative Techniques ix. Evidence gathering x. Network of professional contacts in related fields' viz. enforcement, regulatory bodies, law, industry, peers etc.

Repetitive questions -only attempt needs to be added.

Sr.no.	Chapter	Remarks
1.	1. SA	SA 220 – Ques 3 Add only this question by putting or Question: NEMI Limited (manufacturer of textile goods) got an order of manufacturing of PPE kits in December 2021. But there was shortage of machinery and manpower to accomplish the ordered requirement of PPE kits. NEMI Limited approached another manufacturing unit Rathnemi Limited for purchase of the unit. Rathnemi Limited was interested in the sale of unit, so the deal went through, and NEMI Limited acquired ninety five percent shares of Rathnemi Limited. The new management of Rathnemi Limited proposed and appointed Mani Associates, Chartered Accountants, (already auditors of NEMI Limited) as new auditors of Rathnemi Limited. Mani Associates accepted the assignment without considering information whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate. Comment with respect to appropriate Standard on Auditing what type of information assists the engagements partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate or not? (MTP 1 Nov 2022)
2.	1. SA	SA 402 ,Question 6 (Add MTP 1 Nov 2022)
3.	1. SA	SA 200 Question 9 (Add MTP 1 Nov 2022)
4.	4. Code of ethics	Ques 61 (Add MTP 1 Nov 2022)
5	4. Code of ethics	Ques 112 (Add MTP 1 Nov 2022)
6.	8. Audit Committee and Corporate Governance	Ques 27 (Add MTP 1 Nov 2022)
7.	9. Internal, Management and Operational Audit	Ques 21 (Add MTP 1 Nov 2022)
8.	9. Internal, Management and Operational Audit	Ques 36 (Add MTP 1 Nov 2022)
9.	16. Liabilities of Auditors	Ques 6 (Add MTP 1 Nov 2022)
10.	18. Audit of Insurance Companies	Ques 19 (Add MTP 1 Nov 2022)
11.	19.Audit of Banks	Ques 36 (Add MTP 1 Nov 2022)
12.	23.Forensic Audit	Ques 6 (Add MTP 1 Nov 2022)

13.	21. Audit in an Automated Environment	Ques 9 - Add only question by putting OR as the answer is exactly same. Question Generating and preparing meaningful information from raw system data using processes, tools, and techniques is known as Data Analytics and the data analytics methods used in an audit are known as Computer Assisted Auditing Techniques or CAATs.” You are required to give illustration of a suggested approach to get the benefit from the use of CAATs. (Add MTP 2 Nov 2022)
14.	10. Investigation and Due Diligence	Ques 22 (Add MTP 2 Nov 2022)
15.	4.Code of ethics	Ques 4 (Add MTP 2 Nov 2022)
16.	4.Code of ethics	Ques 93 (Add MTP 2 Nov 2022)
17.	12.Audit of NBFC	Ques 17 (Add MTP 2 Nov 2022)
18.	18. Audit of Insurance Companies	Ques 27 (Add MTP 2 Nov 2022)
19.	1.SA	SA 265 Ques 4 (Add MTP 2 Nov 2022)