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Auditing & Ethics

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- ▶ Questions are arranged Topic Wise as well as Attempt Wise
- ▶ Updated with all Relevant Amendments in Quality Control and Engagement Standards, Company Law etc. (Till 31.08.2023)
- ▶ Includes
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 - (b) Multiple Choice Questions (Approx. 350)
 - (c) Integrated Case Scenario (14)
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CA Pankaj Garg

13th Edition

As per New Syllabus
Group-II Paper-5

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PART I - DESCRIPTIVE QUESTIONS

1.1 - Meaning and Nature of Auditing

Q.1 Lalji Bhai has purchased shares of a company listed on NSE. The audited financial statements of the company provide picture of healthy financial performance having robust turnover, low debt and good profits. On above basis, he is absolutely satisfied that money invested by him is safe and there is no chance of losing his money. Do audited results and audit reports of companies provide such assurance to investors like Lalji Bhai? Is thinking of Lalji Bhai correct?

Ans.: Objectives of Audit:

- An audit does not provide assurance to investor in shares regarding safety of his money. Share prices of securities are affected by range of factors.
- An audit only provides reasonable assurance that financial statements are free from material misstatement whether due to fraud or error.

Conclusion: Thinking of Lalji Bhai is not correct

Q.2 Good deeds Limited is engaged in business of recycling of wastes from dumping grounds of municipal corporation of Indore to usable manure. It is, in this way, also, helping to make the city clean.

During course of audit by Zoha & Zoha, a firm of auditors, it is observed by auditors that company has received a notice from Central Bench of National Green Tribunal for not following certain environmental regulations involving imposition of hefty monetary penalty on the company. The company is yet to reply to the notice. The auditors point out that same is not stated in notes to accounts in financial statements. The company points out that auditors are going beyond scope of their work. Does such a matter fall within scope of audit?

Ans.: Scope of Audit:

An Audit of Financial Statements include within its scope the following:

- (1) **Coverage of all aspects of entity:** Audit of F.S. should be organized adequately to cover all aspects of the entity relevant to the F.S.
- (2) **Reliability and sufficiency of financial information:** Auditor should be reasonably satisfied that information contained in accounting records and other source data (like bills, vouchers, documents etc.) is reliable and provide sufficient basis for preparation of F.S.
- (3) **Proper disclosure of financial information:** Auditor should decide whether relevant information is properly disclosed in F.S in compliance with applicable statutory requirements. For this purpose, auditor is required to study and assess accounting systems and internal controls.

Conclusion: Proper disclosure of financial information is well within scope of audit.

Q.3 A huge fire broke out in NOIDA plant of KT Limited. Plant assets comprising building, machinery and inventories were insured from branch of a public sector insurance company. Apart from an insurance surveyor who was deputed for assessing loss, the regional office of insurance PSU also appointed a CA for verification of books of accounts/financial records of the company and circumstances surrounding the loss. He was also requested to submit an early report. Would the report by CA in nature of audit report?

Ans.: Examination of Books of Accounts for a specific purpose:

- An Audit is independent examination of Financial Information of any entity, whether profit oriented or not, and irrespective of its size or legal form, when such an examination is conducted with a view to expressing an opinion thereon.
- Audit is not an official investigation into alleged wrong doing.
- In this case, CA was appointed for verification of books of accounts/financial records and circumstances surrounding the loss is for a specific objective to determine genuineness of loss and any issue affecting liability of insurance company.

Conclusion: Work performed by CA is nature of investigation and hence his report will not be in nature of audit report.

Q.4 "Choosing of appropriate accounting policies in relation to accounting issues is responsibility of management". Do you agree? Discuss duty of auditor, if any, in relation to accounting policies.

Ans.: Selection of Accounting Policies:

- Choosing of appropriate accounting policies is responsibility of management. Role of auditor lies in evaluating selection and consistent application of accounting policies by management.
- Auditor's duties in relation to accounting policies includes
 - (a) to evaluate whether accounting policies selected by management are proper and
 - (b) whether chosen policy has been applied consistently on a period-to-period basis.

Q.5 RAG is proprietorship firm engaged in the manufacturing of textile and handloom products. It sells its finished products both in the domestic as well as in the international market. The company is making total turnover of ₹ 30 crores. It has also availed cash credit limit of ₹ 5 crores from Canara Bank. In the year 2023-24, proprietor of the firm is worried about the financial position of the company and is under the impression that since he is out of India, therefore firm might run into losses. He approaches a CA about advantages of getting his accounts audited throughout the year so that he may not suffer due to accounting weaknesses. Advise regarding advantages of getting accounts audited. [MTP-March 18, Oct. 18]

Or

The chief utility of audit lies in reliable financial statements on the basis of which the state of affairs may be easy to understand. Apart from this obvious utility, there are other advantages of audit. Some or all of these are of considerable value even to those enterprises and organisations where audit is not compulsory. Explain. [RTP-Nov. 18]

Ans.: Advantage of Audit of Financial Statement:

- (a) Audited accounts provide **high quality information**. It gives confidence to users that information on which they are relying is qualitative and it is the outcome of an exercise carried out by following Auditing Standards recognized globally.

- (b) In case of companies, shareholders may or may not be involved in daily affairs of the company. F.S. are prepared by management consisting of directors. As shareholders are owners of the company, they need an independent mechanism so that financial information is qualitative and reliable. Hence, their interest is safeguarded by an audit.
- (c) Audit acts as a moral check on employees from committing frauds for the fear of being discovered by audit.
- (d) Audited F.S. are helpful to government authorities for determining tax liabilities.
- (e) Audited F.S. can be relied upon by lenders, bankers for making their credit decisions i.e., whether to lend or not to lend to a particular entity.
- (f) Audit may also detect fraud or error or both.
- (g) Audit reviews existence and operations of various controls operating in any entity. Hence, it is useful at pointing out deficiencies.

Q.6 SWM is proprietorship firm engaged in the manufacturing of different kind of yarns. It sells its finished products both in the domestic as well as in the international market. The company is making total turnover of ₹ 30 crores. It has also availed cash credit limit of ₹ 3 crores from Dena Bank. In the year 2023-24. Proprietor of the firm is worried about the financial position of the company and is under the impression that since he is out of India, therefore firm might not run well. He approaches an Internal Auditor about as to what would be covered in Audit. Advice regarding elements to be included in Scope of Audit. [MTP-March 19]

Ans.: Scope of Audit: Refer Answer of Q. No. 2

Q.7 "An audit is independent examination of financial information of any entity, whether profit oriented or not, and irrespective of its size or legal form, when such an examination is conducted with a view to expressing an opinion thereon."

Explain stating clearly how the person conducting this task should take care to ensure that financial statements would not mislead anybody. [MTP-Oct. 19]

Or

The person conducting audit should take care to ensure that financial statements would not mislead anybody. Explain stating clearly the meaning of Auditing. [RTP-May 20, MTP-Oct. 21]

Ans.: Meaning of Audit:

An Audit is independent examination of Financial Information of any entity, whether profit oriented or not, and irrespective of its size or legal form, when such an examination is conducted with a view to expressing an opinion thereon.

This definition has the following implications:

- (a) Audit is independent examination of financial information.
- (b) Requirement of audit applies in case of every entity, whether profit oriented or not (NGO or a Charitable Trust), whatever is business size of entity (Small Size entity or large size entity), whatever is the legal form of the entity (proprietor, partnership, LLP or company).
- (c) Purpose of audit is to express an opinion on the F.S. by means of written audit report.

Points to be ensured that F.S. not misled anybody:

Auditor engaged to perform task of performing audit need to ensure the following:

- (a) Accounts have been drawn up with reference to entries in books of account;
- (b) Entries in books of account are adequately supported by sufficient and appropriate evidence;

	<p>(c) None of the entries in books of account has been omitted in the process of compilation;</p> <p>(d) Information contained in the F.S. is clear and unambiguous.</p> <p>(e) Amounts shown in F.S. are properly classified, described and disclosures are made in conformity with applicable ASs.</p> <p>(f) F.S. reflect true and fair view of financial results and financial position.</p>
Q.8	<p>State the objectives of Audit according to SA 200. [RTP-May 20]</p> <p>Ans.: Objectives of Audit: Refer Answer of Q. No. 10.</p>
Q.9	<p>Both accounting and auditing are closely related with each other. Explain. [RTP-Nov. 20]</p> <p>Ans.: Relationship between accounting and auditing:</p> <ul style="list-style-type: none"> Accounting and auditing are closely related with each other as auditing reviews the financial statements which are nothing but a result of the overall accounting process. Auditing begins when accounting ends. It requires that the auditor must have a thorough and sound knowledge of generally accepted principles of accounting before he can review the financial statements.
Q.10	<p>CA N is the auditor of SR Ltd. The auditor expressed his opinion on the financial statements without ascertaining as to whether the financial statements as a whole were free from material misstatements or not. In your opinion, whether CA N has complied with objectives of audit considering the applicability of relevant SA? [May 22 (3 Marks); MTP-April 23; RTP-Nov. 23]</p> <p>Ans.: Objectives of Auditor:</p> <p>As per SA-200 "Overall Objectives of the Independent Auditor", in conducting an audit of financial statements, the overall objectives of the auditor are:</p> <ol style="list-style-type: none"> To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and To report on the financial statements, and communicate as required by the SAs, in accordance with the auditor's findings. <p>In the given case of SR Ltd., CA N expressed his opinion on the financial statements of SR Ltd. without obtaining reasonable assurance about whether the financial statements as a whole are free from material misstatement or not. Therefore, it can be concluded that CA N did not comply with the objective of audit as stated in SA 200.</p>
Q.11	<p>An audit is distinct from investigation. However, it is quite possible that sometimes investigation results from the prima facie findings of the auditor. Discuss. [RTP-May 23]</p> <p>Ans.: Audit vs. Investigation:</p> <ul style="list-style-type: none"> Audit is distinct from investigation. Investigation is a critical examination of the accounts with a special purpose. For example, if fraud is suspected and it is specifically called upon to check the accounts whether fraud really exists, it takes character of investigation. The objective of audit, on the other hand, is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion.

- Therefore, audit is never started with a pre-conceived notion about state of affairs; about wrongdoing; about some wrong having been committed. The auditor seeks to report what he finds in normal course of examination of accounts.
- However, it is quite possible that sometimes investigation results from the prima facie findings of the auditor. It may happen that auditor has given some findings of serious concern. Such findings may prompt for calling an investigation.

1.2 - Inherent Limitations of Audit

Q.12 Zeeba Products is a partnership firm engaged in trading of designer dresses. The firm has appointed JJ & Co, Chartered accountants to audit their accounts for a year. The auditors were satisfied with control systems of firm, carried out required procedures and necessary verifications. In particular, they carried out sample checking of purchases, traced purchase bills to GST portal and also made confirmations from suppliers. They were satisfied with audit evidence obtained by them as part of audit exercise. An audit report was submitted to the firm giving an opinion that financial statements reflected true and fair view of state of affairs of the firm.

However, later on, it was discovered that purchase manager responsible for procuring dresses from one location was also booking fake purchases of small values by colluding with unethical dealers. Payments to these dealers were also made in connivance with accountant through banking channel. The partners of firm blame auditors for futile audit exercise. Are partners of firm correct in their view point? Imagine any probable reason for such a situation.

Ans.: Inherent Limitations of an Audit:

- An Audit suffers from inherent limitations due to which auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the F.S. are free from material misstatement due to fraud or error.
- Circumstances as given in questions is an example of failure of internal controls of the firm. The internal control has not operated due to collusion between employees which is a limitation of internal control itself. The auditor has relied upon internal controls. It is very nature of financial reporting that management is responsible for devising suitable internal controls.

Conclusion: Partners of the firm are not correct. This is an inherent limitation of audit.

Q.13 An audit does not provide absolute assurance. Discuss how nature of audit procedures itself is one of the reasons due to which audit cannot provide absolute assurance.

Ans.: Inherent Limitations of an Audit – Nature of Audit procedures:

There are practical and legal limitations on the auditor's ability to obtain audit evidence. For example:

- (1) Auditor does not test all transactions and balances. He forms his opinion only by testing samples. It is an example of practical limitation on auditor's ability to obtain audit evidence.
- (2) Management may not provide complete information as requested by auditor. There is no way by which auditor can force management to provide complete information as requested. In case he is not provided with required information, he can only report. It is an example of legal limitation on auditor's ability to obtain audit evidence.

The management may consist of dishonest and unscrupulous people and may be, itself, involved in fraud. It may be engaged in concealing fraud by designing sophisticated and carefully organized schemes which may be hard to detect by the auditor. It may produce fabricated documents before

auditor to lead him to believe that audit evidence is valid. However, in reality, such documents could be fake or non-genuine.

It is quite possible that entity may have entered into some transactions with related parties. Such transactions may be only paper transactions and may not have actually occurred. The auditor may not be aware of such related party relationships or audit procedures may not be able to detect probable wrong doings in such transactions.

Q.14 The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit. Explain. [RTP-Nov. 18]

Ans.: Inherent Limitations of Audit:

As per SA 200 "Overall Objectives of the Independent Auditor and the Conduct of an Audit in accordance with Standards on Auditing" the auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit, which may arise from:

(1) **The Nature of Financial Reporting:** Preparation of F.S. involves making many judgments by management. These judgments may involve subjective decisions or a degree of uncertainty. Therefore, auditor may not be able to obtain absolute assurance that F.S. are free from material misstatements due to frauds or errors.

(2) **Nature of Audit Procedures:** There are practical and legal limitations on the auditor's ability to obtain audit evidence. For example:

Auditor does not test all transactions and balances. He forms his opinion only by testing samples. It is an example of practical limitation on auditor's ability to obtain audit evidence.

Management may not provide complete information as requested by auditor. There is no way by which auditor can force management to provide complete information as requested. In case he is not provided with required information, he can only report. It is an example of legal limitation on auditor's ability to obtain audit evidence.

(3) **Not in Nature of Investigation:** Audit is not an official investigation. Hence, auditor cannot obtain absolute assurance that F.S. are free from material misstatements due to frauds or errors.

(4) **Timeliness of Financial Reporting & the Balance between Benefit & Cost:** The relevance of information decreases over time and auditor cannot verify each and every matter. Therefore, a balance has to be struck between reliability of information and cost of obtaining it.

(5) **Future Events:** Future events or conditions may affect an entity adversely. Adverse events may seriously affect ability of an entity to continue its business. The business may cease to exist in future due to change in market conditions, emergence of new business models or products or due to onset of some adverse events.

Q.15 There are practical and legal limitations on the auditor's ability to obtain audit evidence. Explain with examples. [RTP-May 20, MTP-Oct. 20, RTP-Nov. 21, Nov. 23]

Or

There are practical and legal limitations on the auditor's ability to obtain audit evidence. Explain giving examples. Also explain the difference between audit and investigation. [RTP-Nov. 22]

Ans.: Inherent Limitations of an Audit – Nature of Audit procedures: Refer Answer of Q. No. 13.

Difference Between Audit and Investigation:

- Audit is not an official investigation into alleged wrong doing. Auditor does not have any specific legal powers of search or recording statements of witness on oath which may be necessary for carrying out an official investigation.
- Investigation is a critical examination of accounts with a special purpose. For example, if fraud is suspected and it is specifically called upon to check the accounts whether fraud really exists, it takes character of investigation.
- Objective of audit is to obtain reasonable assurance about whether the F.S. as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion.
- Scope of audit is general and broad whereas scope of investigation is specific and narrow.

1.3 – Meaning, Nature and Types of Engagements

Q.16 The management of Exotic Tours and Travels Limited requests its auditor Raja & Co. to provide an assurance report on the financial information for first quarter of a year by skipping required detailed procedures.

Can Raja & Co. provide such a report? What would be nature of such a report? Would it be necessary for them to obtain sufficient appropriate evidence in such a case?

Ans.: Review Engagement:

Raja & Co. can provide a review report in this case. Review is a limited assurance engagement and involves fewer procedures and gathers sufficient appropriate evidence on the basis of which limited conclusions can be drawn up.

Hence Raja & Co. can provide a report as requested by management of Exotic Tours and Travels Limited. Such report would be in nature of "Review".

Raja & Co. will be required to obtain sufficient appropriate evidence based on limited procedures performed.

Q.17 Assurance engagements are not restricted to audit of financial statements alone. Discuss.

Ans.: Assurance engagements:

- Assurance Engagement is an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria.
- Scope of Assurance Engagements is not restricted to audit of financial statements only; it also extends to examination of Prospective Financial Information (PFI) and examination of internal controls.
- Examples of various assurance engagements that can be rendered by a practitioner includes the following:
 - (1) **Audit of F.S.** - Reasonable assurance engagement
 - (2) **Review of F.S.** - Limited assurance engagement
 - (3) **Examination of PFI** - Provides assurance regarding reasonability of assumptions forming basis of projections and related matters.

	(4) Report on controls operating at an organization - Provides assurance regarding design and operation of controls.
Q.18	<p>An assurance engagement involves a three party relationship. Discuss meaning of three parties in such an engagement.</p> <p>Ans.: Three Party relationship of assurance engagement:</p> <p>An assurance engagement involves three parties – a practitioner, a responsible party, and intended users.</p> <p>(1) Practitioner: Person who provides the assurance. Practitioner is broader than auditor. Audit is related to historical information whereas practitioner may provide assurance not necessarily related to historical financial information.</p> <p>(2) Responsible party: Party responsible for preparation of subject matter.</p> <p>(3) Intended users: Persons for whom an assurance report is prepared. These persons may use the report in making decisions.</p>
Q.19	<p>A Chartered Accountant is specifically asked to check accounts whether fraud exists. State with reasons whether it is an example of reasonable assurance engagement.</p> <p>Ans.: Examination of Accounts for determining existence of Fraud:</p> <ul style="list-style-type: none"> Assurance engagement is an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria. Reasonable Assurance requires a high, but absolute assurance. In this case, a Chartered Accountant is specifically asked to check accounts whether fraud exists. <p>Conclusion: It is not a reasonable assurance engagement. It is in nature of investigation.</p>

1.4 - Qualities of Auditor

Q.20	<p>Explain qualities of Auditor. [RTP-May 19; MTP-March 21, Oct 21]</p> <p>Ans.: Qualities of an Auditor:</p> <ul style="list-style-type: none"> Auditor is concerned with the reporting on financial matters of business and other institutions. Financial matters inherently are to be set with the problems of human fallibility; errors and frauds are frequent. The qualities required are tact, caution, firmness, good temper, integrity, discretion, industry knowledge, judgement, patience, clear headedness and reliability. In short, all those personal qualities that go to make a good businessman contribute to the making of a good auditor. In addition, auditor must have the shine of culture for attaining a great height. He must have the highest degree of integrity backed by adequate independence. Auditor, who holds a position of trust, must have the basic human qualities apart from the technical requirement of professional training and education. He is called upon constantly to critically review F.S. and it is obviously useless for him to attempt that task unless his own knowledge is that of an expert. An exhaustive knowledge of accounting in all its branches is the <i>sine qua non</i> of the practice of auditing. He must know thoroughly all accounting principles and techniques.
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1.5 - Quality Control and Engagement Standards

Q.21 CA. P Babu is conducting audit of financial statements of Quick Buy Private Limited. He was not able to obtain external confirmations from certain debtors due to practical difficulties and peculiar circumstances. However, such a procedure is mandated under one of Standards on Auditing. Unable to obtain external confirmations from these debtors, he relied upon sale details to these parties, e-Invoices, e-way bills and also traced payments from these parties in bank accounts of the company. He was reasonably satisfied with audit evidence obtained. Is there any other reporting duty cast upon him relating to not following a mandated procedure in one of Standards on Auditing?

Ans.: Duties in relation to Engagement and Quality Control Standards:

- It is the duty of professional accountants to see that Standards are followed in engagements undertaken by them.
- However, a situation may arise when a specific procedure as required in Standards would be ineffective in a particular engagement. In such a case, professional accountant is required to ensure the following:
 - (a) Document how alternative procedures performed to achieve the purpose of required procedure;
 - (b) Reason for departure has also to be documented;
 - (c) Report should draw attention to such departures.

Conclusion: CA P Babu is required to document how alternative procedures performed achieve the purpose of required procedure. Reason for departure has to be documented. His report should draw attention to such departure.

Q.22 Standards on Auditing (SAs) apply in "audit of historical financial information" whereas Standards on Review Engagements (SREs) apply in "review of historical financial information." Explain in detail giving examples. [RTP-May 22]

Ans.: Standards on Auditing and Standards on Review Engagements:

- Standards on auditing apply in "audit" of historical financial information which is a reasonable assurance engagement whereas Standards on Review Engagements apply in "review" of historical financial information which is a limited assurance engagement only.
- "Historical financial information" means information expressed in financial terms in relation to a particular entity, derived primarily from that entity's accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.
- "Audit" and "Review" are two different terms. Audit is a reasonable assurance engagement and its objective is reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement. However, "review" is a limited assurance engagement and its objective is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement.
- Standards on Auditing have been issued on wide spectrum of issues in the field of auditing including (but not limited to) overall objectives of independent auditor, audit documentation, planning an audit of financial statements, identifying and assessing risk of material misstatement, audit evidence, audit sampling, going concern and forming an opinion and reporting on financial statements. Some examples of Standards on Auditing are:

	<ul style="list-style-type: none"> (i) SA 200: Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing. (ii) SA 230: Audit Documentation. (iii) SA 315: Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment. (iv) SA 500: Audit Evidence. (v) SA 700: Forming an Opinion and Reporting on Financial Statements. <ul style="list-style-type: none"> • Examples of Standards on Review engagements are: <ul style="list-style-type: none"> (i) SRE 2400: Engagements to Review Historical Financial Statements. (ii) SRE 2410: Review of Interim Financial Information Performed by the Independent Auditor of the Entity.
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PART II - CORRECT/INCORRECT QUESTIONS

1	<p>The basic objective of audit does not change with reference to nature, size or form of an entity.</p> <p>Ans.: Statement is Correct.</p> <p>An audit is an independent examination of financial information of any entity, whether profit oriented or not, and irrespective of its size or legal form, when such an examination is conducted with a view to expressing an opinion thereon.</p> <p>It is clear that the basic objective of auditing, i.e., expression of opinion on financial statements does not change with reference to nature, size or form of an entity.</p>
2	<p>The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. [MTP-March 23]</p> <p>Ans.: Statement is Correct.</p> <p>As per SA 200 "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing", the purpose of an audit is to enhance the degree of confidence of intended users in the financial statements.</p> <p>This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable FRF.</p>
3	<p>The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error.</p> <p>Ans.: Statement is Correct.</p> <p>As per SA 200 "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing", the auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error.</p> <p>This is because there are inherent limitations of an audit, which result in most of the audit evidence on which auditor draws conclusions and bases auditor's opinion being persuasive rather than conclusive.</p>

4	<p>Mr. S, one of the new team members of the auditor of Extremely Effective Limited was of the view that for the purpose of conducting an audit, only knowledge of direct tax is required whereas no knowledge of indirect tax is required.</p>
	<p>Ans.: Statement is incorrect.</p> <p>The viewpoint of Mr. S is incorrect because for the purpose of conducting an audit, proper knowledge of both direct tax as well as indirect tax is required.</p>
5	<p>According to Mr. H, one of the team members of the auditor of Very Essential Limited was of the view that no relation exists between accounting and auditing from the point of view of a company.</p>
	<p>Ans.: Statement is incorrect.</p> <p>The viewpoint of Mr. H is incorrect because there exists a proper relation between accounting and auditing from the point of view of a company. Audit is conducted for financial statements of a company and those F.S. are prepared with the help of books of accounts of that company.</p> <p>In order to properly conduct an audit of a company, an auditor is required to be aware of accounting principles and accounting policies of that company.</p>
6	<p>The term "Engagement Standards" refer to Standards on Auditing only.</p>
	<p>Ans.: Statement is incorrect.</p> <p>Engagement Standards refer not only to Standards on auditing but also to Standards on review engagements, Standards on assurance engagements and Standards on related services.</p>
7	<p>The objective of audit is to obtain absolute assurance and to report on the financial statements.</p> <p style="text-align: right;">[RTP-May 18, MTP-March 19]</p>
	<p>Ans.: Statement is incorrect.</p> <p>Objective of audit is to express an opinion on true and fair view of the financial statements. In this reference. SA-200 "Overall Objectives of the Independent Auditor and conduct of audit in accordance with Standards on Auditing" provides that in conducting an audit of financial statements, the overall objectives of the auditor are:</p> <ol style="list-style-type: none"> (a) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement; and (b) To report on the financial statements, and communicate as required by the SAs, in accordance with the auditor's findings.
8	<p>The preparation of financial statements does not involve judgment by management in applying the requirements of the entity's applicable financial reporting framework to the facts and circumstances of the entity.</p> <p style="text-align: right;">[RTP-Nov. 18, May 19]</p>
	<p>Ans.: Statement is incorrect.</p> <ul style="list-style-type: none"> • The preparation of F.S. involves judgment by management in applying the requirements of the entity's applicable financial reporting framework to the facts and circumstances of the entity. • In addition, many F.S. items involve subjective decisions or assessments or a degree of uncertainty, and there may be a range of acceptable interpretations or judgments that may be made.
9	<p>An audit is an official investigation into alleged wrongdoing.</p> <p style="text-align: right;">[RTP-Nov. 18, May 19]</p>
	<p>Ans.: Statement is incorrect.</p> <ul style="list-style-type: none"> • An audit is not an official investigation into alleged wrongdoing. • Accordingly, the auditor is not given specific legal powers, such as the power of search, which may be necessary for such an investigation.

10	<p>Management of the organisation is solely responsible for the compliance of auditing standards while preparing financial statements. [Nov. 18 (2 Marks)]</p>
	<p>Ans.: Statement is incorrect.</p> <ul style="list-style-type: none"> • Responsibility for the compliance of Auditing Standards is of Auditor. While carrying out the audit, auditor is required to ensure that audit is been performed in accordance with Standards on Auditing and appropriate Report is issued. • Management is responsible for the compliance of Accounting Standards.
11	<p>The auditor is expected to and can reduce audit risk to zero. [MTP-May 20, Oct. 21]</p>
	<p>Ans.: Statement is incorrect.</p> <ul style="list-style-type: none"> • As per SA 200 "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing", the auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. • This is because there are inherent limitations of an audit, which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive.
12	<p>The Auditor is expected to, reduce audit risk to zero and can therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. [Jan. 21 (2 Marks)]</p>
	<p>Ans.: Statement is incorrect.</p> <ul style="list-style-type: none"> • As per SA 200 "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing", the auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. • This is because there are inherent limitations of an audit.
13	<p>There are inherent limitations of an audit, which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being conclusive rather than persuasive. [MTP-April 21]</p>
	<p>Ans.: Statement is incorrect.</p> <ul style="list-style-type: none"> • As per SA 200, the auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. <p>This is because there are inherent limitations of an audit, which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive.</p>
14	<p>The preparation of financial statements involves judgment by management. [MTP-Nov. 21]</p>
	<p>Ans.: Statement is correct.</p> <p>The preparation of financial statements involves judgment by management in applying the requirements of the entity's applicable FRF to the facts and circumstances of the entity.</p> <p>In addition, many financial statement items involve subjective decisions or assessments or a degree of uncertainty, and there may be a range of acceptable interpretations or judgments that may be made.</p>

15	<p>There is no difference between "audit" and "review." [RTP-Nov. 22]</p> <p>Ans.: Statement is Incorrect.</p> <ul style="list-style-type: none"> • "Audit" and "Review" are two different terms. • Audit is a reasonable assurance engagement, and its objective is reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement. • However, "review" is a limited assurance engagement, and its objective is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement.
16	<p>For auditor's opinion, reasonable assurance is an absolute level of assurance. [RTP-Nov. 22]</p> <p>Ans.: Statement is Incorrect.</p> <p>Reasonable assurance is a high level but not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive.</p>
17	<p>Historical Financial information relates to financial information based on assumptions about occurrence of future events and possible actions by an entity. [Nov. 22 (2 Marks)]</p> <p>Ans.: Statement is Incorrect.</p> <p>"Historical financial information" means information expressed in financial terms in relation to a particular entity, derived primarily from that entity's accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.</p>
18	<p>As per SA 200 "Overall Objectives of the Auditor", in conducting an audit of financial statements, the overall objectives of the auditor is to obtain absolute assurance about whether the financial statements as a whole are free from material misstatement due to fraud. [RTP-May 23]</p> <p>Ans.: Statement is Incorrect.</p> <p>As per SA-200 "Overall Objectives of the Independent Auditor", in conducting an audit of financial statements, the overall objectives of the auditor are:</p> <ol style="list-style-type: none"> To obtain reasonable assurance about whether the F.S. as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the F.S. are prepared, in all material respects, in accordance with applicable FRF; and To report on the F.S., & communicate as required by the SAs, in accordance with the findings.

PART III - MULTIPLE CHOICE QUESTIONS

1	<p>Which of the following is not an advantage of audit?</p> <ol style="list-style-type: none"> It provides high quality financial information. It acts as a moral check on employees. It enhances risk of management bias. It helps in safeguarding interests of shareholders
2	<p>Which of the following is NOT TRUE about an assurance engagement?</p> <ol style="list-style-type: none"> It relates to providing assurance about historical financial information only. The practitioner obtains sufficient appropriate evidence.

	<p>(c) There is some information to be examined by practitioner.</p> <p>(d) A written assurance report in appropriate form is issued by practitioner.</p>
3	<p>Which of the following is TRUE about Engagement Standards?</p> <p>(a) Engagement standards ensure proper rights to practitioners in course of performance of their duties.</p> <p>(b) Engagement standards ensure preparation and presentation of financial statements in a standardized manner.</p> <p>(c) Engagement standards ensure uniformity by practitioners in course of performance of their duties.</p> <p>(d) Engagement standards ensure savings in resources of clients.</p>
4	<p>Consider following statements in relation to "Limited assurance engagement":-</p> <p>Statement I - It involves obtaining sufficient appropriate evidence to draw reasonable conclusions.</p> <p>Statement II - Review of interim financial information of a company is an example of limited assurance engagement.</p> <p>(a) Statement I is correct. Statement II is incorrect.</p> <p>(b) Both Statements I and II are correct.</p> <p>(c) Both Statements I and II are incorrect.</p> <p>(d) Statement I is incorrect. Statement II is correct.</p>
5	<p>Which of the following is TRUE about Standards on auditing?</p> <p>(a) These deal mainly with voluntary responsibilities of auditors.</p> <p>(b) These deal mainly with mandatory responsibilities of auditors.</p> <p>(c) Their sole purpose is to help government authorities in augmenting revenues.</p> <p>(d) These deal mainly in carrying out audit according to legal provisions.</p>
6	<p>The auditor of Delicious Sweets Limited was of the opinion that objective of audit of financial statements of a company is to provide reasonable assurance that financial statements of that company are free from misstatements. Which type of misstatements are mentioned by auditor of Delicious Sweets Limited:</p> <p>(a) Simple.</p> <p>(b) Material.</p> <p>(c) Easy.</p> <p>(d) Competent.</p>
7	<p>_____ framework means a framework adopted in the preparation and presentation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation.</p> <p>(a) Financial reporting</p> <p>(b) Applicable financial reporting</p> <p>(c) Financial verification</p> <p>(d) Financial analysis</p>
8	<p>No business or institution can effectively carry on its activities without the help of proper _____:</p> <p>(a) Audit</p> <p>(b) Record and accounts</p> <p>(c) Neither (a) nor (b)</p> <p>(d) Both (a) and (b)</p>

Chapter 1

9	<p>_____ along with other disciplines such as accounting and law, equips you with all the knowledge that is required to enter into auditing as a profession.</p>
<ul style="list-style-type: none"> (a) Auditing (b) Taxation (c) Finance (d) Law 	
10	<p>As per SA-200 "Overall Objectives of the Independent Auditor", in conducting an audit of financial statements, the overall objectives of the auditor are:</p>
<ul style="list-style-type: none"> (a) To obtain reasonable assurance (b) To report on the financial statements (c) Both (a) and (b) above (d) To obtain absolute assurance. 	
11	<p>Which of the following is not correct?</p>
<ul style="list-style-type: none"> (a) SA 230 - Audit Documentation (b) SA 500 - Audit Evidence (c) SA 505 - Written Representation (d) SA 560 - Subsequent Events 	
12	<p>An employee of Fruits and Vegetables Limited was of the opinion that auditor of a company is required to express an opinion. On which one of the following the auditor of a company is required to express an opinion:</p>
<ul style="list-style-type: none"> (a) Only Balance Sheet of the Company. (b) Financial Statements of the Company. (c) Only Profit and Loss Account of the Company. (d) Only Cash Flow Statement of the Company. 	
13	<p>Choosing of appropriate accounting policies in relation to various accounting issues like choosing method of charging depreciation on fixed assets or choosing appropriate method for valuation of inventories are responsibilities of:</p>
<ul style="list-style-type: none"> (a) Statutory Auditor (b) Internal Auditor (c) Legal counsel (d) Management 	
14	<p>As explained in SA 200, "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing", _____ is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (i.e., the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level.</p>
<ul style="list-style-type: none"> (a) absolute assurance (b) limited assurance (c) reasonable assurance (d) reasonable or absolute assurance 	

15	<p>Which of the following is correct?</p> <p>(a) The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error.</p> <p>(b) The auditor is expected to and can reduce audit risk to zero and can therefore obtain absolute assurance.</p> <p>(c) The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain reasonable assurance that the financial statements are free from material misstatement due to fraud or error.</p> <p>(d) The auditor is expected to and can reduce audit risk to zero and can therefore obtain reasonable assurance that the financial statements are free from material misstatement due to fraud or error.</p> <p style="text-align: right;">[MTP-April 19]</p>
16	<p>M/s. KYC & Co. is a reputed Audit firm in Mumbai. They are appointed as Statutory Auditors of Blessed Ltd. Which of the below is the responsibility of M/s. KYC & Co.</p> <p>(a) Preparation of financial statements</p> <p>(b) Designing, implementation and maintenance of internal control system</p> <p>(c) Reporting on true and fair view of financial statements</p> <p>(d) Compliance with the applicable law and regulation</p> <p style="text-align: right;">[RTP-Nov. 20]</p>
17	<p>Owing to the _____ limitations of an audit, there is _____ risk that some material misstatements of the financial statements will not be detected, even though the audit is properly planned and performed in accordance with the SAs.</p> <p>(a) Inherent, unavoidable</p> <p>(b) Inherent, complete</p> <p>(c) Management, unavoidable</p> <p>(d) Regulatory, control</p> <p style="text-align: right;">[MTP-March 22]</p>
18	<p>Which of the following is the responsibility of the auditor:</p> <p>(a) Preparation and presentation of the financial statements in accordance with applicable financial reporting</p> <p>(b) Design, implementation and maintenance of internal controls</p> <p>(c) Express an opinion on the Financial Statements</p> <p>(d) To obtain limited assurance.</p> <p style="text-align: right;">[MTP-April 22]</p>
19	<p>With respect to auditing, which of the following statement is correct:</p> <p>(a) Audited financial statements are absolutely free from all material misstatement due to fraud or error.</p> <p>(b) An audit is an official investigation into alleged wrongdoing and auditor has specific legal powers to conduct investigation.</p> <p>(c) The auditor can obtain only a reasonable assurance about whether the financial statement as a whole are free from material misstatement and report on it.</p> <p>(d) An auditor's opinion is an assurance as the future viability of the enterprise or the efficiency or effectiveness of the management.</p> <p style="text-align: right;">[MTP-April 23]</p>

Chapter 1

Answer Key	
Q. No.	Answer
1	(c) It enhances risk of management bias.
2	(a) It relates to providing assurance about historical financial information only.
3	(c) Engagement standards ensure uniformity by practitioners in course of performance of their duties.
4	(d) Statement I is incorrect. Statement II is correct.
5	(b) These deal mainly in carrying out audit according to legal provisions.
6	(b) Material
7	(b) Applicable financial reporting
8	(b) Record and accounts
9	(a) Auditing
10	(c) Both (a) and (b) above
11	(c) SA 505- Written Representation
12	(b) Financial Statements of the Company.
13	(d) Management
14	(c) reasonable assurance
15	(c) The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain reasonable assurance that the financial statements are free from material misstatement due to fraud or error.
16	(c) Reporting on true and fair view of financial statements
17	(a) Inherent, unavoidable
18	(c) Express an opinion on the Financial Statements
19	(c) The auditor can obtain only a reasonable assurance about whether the financial statement as a whole are free from material misstatement and report on it.

PART IV - CASE STUDY

Case Study 1

Rohit, Gurpreet, Ali and Goreti are friends since their school days based in Mumbai. They have cleared CA foundation exams in the same attempt and now plan to appear for CA Intermediate exams. All of them are avid news listeners and regularly keep track of business news even on social media.

They are trying to understand new subjects including auditing. Rohit, Gurpreet and Ali have also started attending Live Coaching Classes (LCC) being conducted by Board of studies of ICAI. Goreti has not been able to join Live Coaching Classes yet as she was away on a holiday with her parents. However, she plans to catch it up with her friends very soon. Ali had also joined the classes but he had skipped some lectures.

During one informal get together, their discussions centred around new subject of auditing. They discussed many things regarding its nature, scope, benefits and other general practical issues. Goreti was regular in keeping track of audited results of companies being published in leading newspapers. Her view was that audited financial statements of companies give 100% guarantee to different stake holders. It is the main reason behind so much reliance upon auditing. But she could not understand why wrong doings in financial matters are being discovered after many years have gone by.

Ali also concurred with her view and added that when financial statements are audited, each and every transaction appearing in books of accounts is verified. However, he could not give clarity to Goreti. Gurpreet was of the opinion that audit was conducted on the basis of sample checking. He was also of the view that audited financial statements are not a guarantee against probable wrong doings in financial matters of the companies. Not to be left behind, Rohit also jumped in the fray. He supported Gurpreet and also added something of his own.

Based on above, answer the following questions:

Q.1	<p>Gurpreet was of the view that audited financial statements are not a guarantee against probable wrong doings in financial matters of companies. What kind of assurance does audit of financial statements provide?</p> <p>(a) It provides reasonable assurance meaning a moderate level of assurance. (b) It provides reasonable assurance meaning a low level of assurance. (c) It provides reasonable assurance meaning a high level of assurance. (d) It provides reasonable assurance meaning an absolute level of assurance.</p>
Q.2	<p>Rohit added that auditor can force an employee of the company to provide him required information and documents. Can he do so?</p> <p>(a) Yes, he can do so. It is necessary to obtain audit evidence. (b) Yes, he can do so. There are express rights given to him in this respect. (c) No, he cannot do so. He can only request for providing him with necessary information and documents. But it cannot be forced by him. (d) No, he cannot do so. He has no right of seeking information and documents. Therefore, question of forcing does not arise.</p>
Q.3	<p>Ali had listened in one of the classes that audit covers all aspects of an entity and concluded that each and every transaction of entity is verified by auditor.</p> <p>Goreti also seemed to be in agreement with him but she was of the view that besides this, it also meant that audit should be so organized to cover all areas of an entity. Which of following statements is appropriate in this regard?</p> <p>(a) Only view of Ali is correct. (b) Only view of Goreti is correct. (c) Views of both Ali and Goreti are correct. (d) Views of both Ali and Goreti are incorrect.</p>
Q.4	<p>All of them also discussed about benefits of auditing. Which of the following is not a likely benefit of auditing?</p>

	<p>(a) Since auditing is connected to future events, audited information can be easily relied upon by users.</p> <p>(b) Errors or frauds may be discovered during audit.</p> <p>(c) Government authorities can make use of audited accounts for different purposes.</p> <p>(d) It can help in bringing out deficiencies in maintenance of financial records.</p>
Q.5	<p>Goreti told her friends that she had read a news report about how a company had misled its auditors by producing some fabricated documents. Which of following statements seems to be appropriate in this regard?</p> <p>(a) It was wrong on the part of auditor to rely upon fabricated documents. He must have discovered it as the same falls within the scope of his duties.</p> <p>(b) Although it was wrong on the part of auditor to rely upon fabricated documents, he cannot do anything in the matter. He has to report on the basis of documents provided to him. He has no duty in this regard.</p> <p>(c) Auditor has to conduct audit by exercising professional skill. But he is not an expert in discovering genuineness of documents. Hence, management consisting of dishonest persons may have led him to rely upon fabricated documents deliberately.</p> <p>(d) Management cannot mislead auditor due to high level of knowledge and expertise possessed by him. The above is an outlier case-one of the rare odd cases.</p>

Answer - Case Study 1

Q. No.	Answer
1	(c) It provides reasonable assurance meaning a high level of assurance.
2	(c) No, he cannot do so. He can only request for providing him with necessary information and documents. But it cannot be forced by him.
3	(d) Views of both Ali and Goreti are incorrect.
4	(a) Since auditing is connected to future events, audited information can be easily relied upon by users.
5	(c) Auditor has to conduct audit by exercising professional skill. But he is not an expert in discovering genuineness of documents. Hence, management consisting of dishonest persons may have led him to rely upon fabricated documents deliberately.

Case Study 2

Me and You Private Limited has been newly incorporated. The plant of the company has recently started production with the help of funds provided by a bank for purchase and installation of machinery. Further, the company is also utilizing working capital credit facilities from the same bank for meeting its day to day working capital requirements like for purchase of raw materials, labour payment etc. However, just within six months of its operations, the management feels that working capital funds are inadequate and situation is creating liquidity issues in the company.

The management of the company has approached its bankers and requested for enhancement in working capital credit facilities. The bank manager is insisting upon financial statements of the company for half year along with report providing assurance in this respect duly signed by Chartered Accountant as audit is far away. It also requires projected financial statements for coming years along with a report from CA providing assurance regarding these projections to consider request of management.

The management approaches CA P, who has qualified recently and started practising. Reports providing assurance for half yearly results and projected financial statements are sought from CA P. The Management provides necessary information and records to him in this regard.

Assume, in above case, the company only provides trial balance, financial statements in draft/preliminary form along with accompanying records for the relevant half year to CA P and requests him to provide duly signed financial statements with a report for mutually agreed professional fees.

Based on above, answer the following questions:

- Q.1** The management of company has engaged CA P to issue a duly signed report for half year. Which of the following standards, if any, issued by ICAI are relevant for CA P?
- (a) Standards on Review Engagements
 - (b) Standards on Auditing
 - (c) Standards on Related Services
 - (d) There are no standards for issuing report in such situation.

- Q.2** Which of the following statements is MOST APPROPRIATE in given case situation?
- (a) CA P can assist management in preparation of financial statements of the company. However, issue of a report in such a case is outside the scope of work.
 - (b) CA P can assist management in preparation of financial statements of the company and he can issue an audit report.
 - (c) CA P can assist management in preparation of financial statements of the company and he can issue a compilation report in this respect.
 - (d) The responsibility of preparation of financial statement is of company's management. CA P cannot assist management in preparation of financial statements of the company. However, he can issue a review report.

- Q.3** In the above said scenario for issuance of signed financial statements for half year by CA P, as discussed in last para of Case Study, identify the MOST APPROPRIATE statement:
- (a) Standard on Quality control (SQC 1) is not applicable as CA P cannot issue audit report.
 - (b) Standard on Quality Control (SQC 1) is not applicable as CA P cannot issue review report.
 - (c) Standard on Quality Control (SQC 1) is applicable in such type of engagement.
 - (d) Standard on Quality Control (SQC 1) is not applicable as CA P is barred from issuing any report in such type of engagement.

- Q.4** The banker of company has also requested for projected financial statements for coming years along with a report from CA regarding these projections to consider request of management. Which of the following standards issued by ICAI are relevant for CA P in such a situation, if any?

- (a) Standards on Review Engagements
- (b) There are no standards for issuing such type of reports.

	(c) Standards on Related Services (d) Standards on Assurance Engagements
Q.5	<p>Suppose CA P also accepts work of issuing projected financial statements with a report to be signed by him. The management has projected turnover of ₹ 100 crore for the next year, ₹ 150 crore & ₹ 200 crore for following years respectively as compared to present turnover of ₹ 25 crore in current half year. Identify the MOST APPROPRIATE statement in this situation: -</p> <p>(a) CA P has to satisfy himself regarding arithmetical accuracy of projected data.</p> <p>(b) CA P has to satisfy himself regarding reasonableness of assumptions underlying projected turnover and its consistency with actuals.</p> <p>(c) CA P has to satisfy himself regarding arithmetical accuracy of data along with its proper presentation to banker.</p> <p>(d) CA P has to satisfy himself regarding reasonableness of assumptions underlying projected turnover, its consistency with actuals, disclosure and presentation.</p>

Answer - Case Study 2	
Q. No.	Answer
1	(c) Standards on Related Services
2	(c) CA P can assist management in preparation of financial statements of the company and he can issue a compilation report in this respect.
3	(c) Standard on Quality Control (SQC 1) is applicable in such type of engagement.
4	(d) Standards on Assurance Engagements
5	(d) CA P has to satisfy himself regarding reasonableness of assumptions underlying projected turnover, its consistency with actuals, disclosure and presentation.

PART I - DESCRIPTIVE QUESTIONS

2.1 - Auditor's Responsibility to Plan an Audit of F.S.

Q.1 MG & Co, a firm of auditors, having a standing of 30 years is appointed as a statutory auditor of company engaged in manufacturing of defence equipment. Due to opening of defence sector by government to private players in recent times, many new companies have entered the fray to manufacture sophisticated defence equipment. Considering technical and complex nature of operations, the auditors recognize that involvement of experts in the audit is required. Does consideration for involvement of experts by auditors fall in the domain of planning audit?

Ans.: Involvement of Experts in Planning:

- Planning in auditing encompasses developing an overall plan for the expected scope and conduct of the audit and developing an audit programme showing the nature, timing and extent (NTE) of audit procedures.
- While planning an audit, auditor would have to consider whether involvement of experts is necessary.
- In the stated case, company is involved in technical and complex operations. Therefore, while planning an audit, auditors would have to consider whether involvement of expert is necessary.

Conclusion: Consideration for involvement of experts by auditors falls within domain of planning.

Q.2 CA Kartik is planning for audit of a company engaged in manufacturing of cosmetics. Considering nature of operations of the company, he had planned to include testing of controls of the company over purchases, sales and inventories. One fine day, he reaches the corporate office and asks for manuals and required documentation to ensure surprise element in testing. He had never shared with management his intention to carry out above procedures. Is approach of CA Kartik proper?

Ans.: Discussion of elements of planning with management:

- Auditor may decide to discuss elements of planning with the entity's management to facilitate the conduct and management of the audit engagement without compromising effectiveness of audit.
- In the case, CA Kartik has reached office of the company without sharing with management his intention to test the controls. Sharing details of visit to test controls does not compromise effectiveness of audit. It is for the better facilitation and conduct of audit.

Conclusion: Approach of CA Kartik is not proper.

Q.3 Discuss how performing preliminary engagement activities as part of planning an audit assists auditor.

Ans.: Preliminary Engagement Activities:

As per SA 300 "Planning an Audit of F.S.", preliminary engagement activities include the following:

- (a) Performing procedures regarding the continuance of the client relationship.