

CA - INTER AUDITING AND ETHICS

SUPER 100



RELEVANT FOR MAY 2024 EXAMS

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CA Inter – Auditing & Ethics

(Super 100 Questions for May 2024 Exams)

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Additional Questions

[Asked in RTP (Nov. 23 & May 24), MTP (Sep. 23 & Oct. 23) & Past Exam (Nov. 23)]

PART I – DESCRIPTIVE QUESTIONS

Chapter 1 – Nature, Objective and Scope of Audit

1.1 – Meaning and Nature of Auditing

- Q.11A** M Motors Ltd is a leading Indian automobile manufacturer with many offerings across commercial, passenger and electric vehicles. The Company is pioneering India's electric vehicle transition and enjoys considerable advantage in one of the fastest growing automotive markets. GR & Associates have been appointed as its statutory auditors for financial year 2023-24. J and K are newly appointed audit assistants in the firm and are part of engagement team constituted for purpose of audit of M Motors Ltd. However, they are confused about what such an audit tends to achieve. They perceive audit as a guarantee against possible errors or frauds in financial statements. Do you agree with perception of both the assistants? In this context, outline objectives of an independent audit conducted in accordance with Standards on Auditing. [RTP - May 24]

Ans: Objectives of an Independent Audit:

In conducting audit of financial statements, objectives of auditor in accordance with SA-200 "Overall Objectives of the Independent auditor and the conduct of an audit in accordance with Standards on Auditing" are:

- (a) 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
- (b) To report on the financial statements, and communicate as required by the SAs, in accordance with the auditor's findings.

An analysis of above brings out following points clearly: -

- (1) Auditor's objective is to obtain a reasonable assurance whether financial statements as a whole are free from material misstatement whether due to fraud or error.

Reasonable assurance is to be distinguished from absolute assurance. Absolute assurance is a complete assurance or a guarantee that financial statements are free from material misstatements. However, reasonable assurance is not a complete guarantee. Although it is a high-level of assurance but it is not complete assurance.

Audit of financial statements is carried out by the auditor with professional competence and skills in accordance with Standards on Auditing. Audit procedures are applied in accordance with SAs, audit evidence is obtained and evaluated. On the basis of that, conclusions are drawn and opinion is formed. It leads to high level of assurance which is called as reasonable assurance but it is not absolute assurance.

- (2) Misstatements in financial statements can occur due to fraud or error or both. The auditor seeks to obtain reasonable assurance whether financial statements as a whole are free from material misstatements caused by fraud or error. He has to see effect of misstatements on financial statements as a whole, in totality.
- (3) Obtaining reasonable assurance that financial statements as a whole are free from material misstatements enables 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.
- (4) The opinion is reported and communicated in accordance with audit findings through a written report as required by Standards on Auditing.

Conclusion: Therefore, perception of both assistants is not proper. Auditor of financial statements does not seek to provide guarantee that financial statements are free from material misstatements caused by frauds or errors. He obtains reasonable assurance.

Chapter 2 – Audit Strategy, Audit Planning and Audit Programme

2.3 – Audit Planning

Q.19A The audit plan includes the nature, timing and extent of audit procedures to be performed by engagement team members. Explain. [RTP - Nov. 23]

Ans: Elements of Audit Plan:

The auditor shall develop an audit plan that shall include a description of

- The nature, timing and extent of planned risk assessment procedures, as determined under SA 315 “Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment”.
- The nature, timing and extent of planned further audit procedures at the assertion level, as determined under SA 330 “The Auditor’s Responses to Assessed Risks”.
- Other planned audit procedures that are required to be carried out so that the engagement complies with SAs.

The audit plan is more detailed than the overall audit strategy that includes the nature, timing and extent of audit procedures to be performed by engagement team members. Planning for these audit procedures takes place over the course of the audit as the audit plan for the engagement develops.

2.4 - Audit Programme

Q.26A The assistant of CA K is assigned responsibility of drafting “audit programme” relating to purchases appearing in financial statements of “Broad Industries”, a partnership firm. The said firm is a GST registered tax payer and is engaged in manufacturing of packing boxes from a special type of paper taxable under GST. Help him by drafting a sample audit programme for purchases. [RTP - May 24]

Ans: Sample audit programme pertaining to purchases

Name of Concern	:	Broad Industries
Financial Year	:	20XX-XX
Prepared by	:	Name of person with date
Reviewed by	:	Name of person with date
Approved by	:	Name of person with date

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

Chapter 3 – Risk Assessment and Internal Control

3.1 – Audit Risk (SA 315)

Q.19A Satranga Foods Private Limited is engaged in manufacturing of pickles. The auditors of the company have planned audit procedures in respect of recognition of revenues of the company. Despite that, there is a possibility that misstatements in revenue recognition are not identified by planned audit procedures. Identify and explain that particular risk in detail. [RTP - May 24]

Ans: Detection Risk:

There is a possibility that planned audit procedures may not achieve desired result and fail to detect misstatements in revenue recognition. Such a risk is referred to as “detection risk”.

SA 200 defines detection risk as the risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

For example, auditor of a company uses certain audit procedures for the purpose of obtaining audit evidence and reducing audit risk, but still there will remain a risk that audit procedures used by the auditor may not be able to detect a misstatement which by nature is material, then that risk is known as detection Risk.

Detection risk comprises sampling and non-sampling risk.

- (a) **Sampling risk** is the risk that the auditor’s conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. It simply means that the sample was not representative of the population from which it was chosen.
- (b) **Non-sampling risk** is the risk that the auditor reaches an erroneous conclusion for any reason not related to sampling risk. Like an auditor may reach an erroneous conclusion due to application to some inappropriate audit procedure.

3.15 – The Auditor’s Responses to Assessed Risks (SA 330)

Q.90A While obtaining audit evidence about the effective operation of internal controls, the auditor considers how they were applied, the consistency with which they were applied during the period and by whom they were applied. The concept of effective operation recognises that some deviations may have occurred. Analyse and Explain. [MTP – Oct. 23]

Ans: Obtaining Audit Evidence about the effective operation of Internal Controls:

- While obtaining audit evidence about the effective operation of internal controls, the auditor considers how they were applied, the consistency with which they were applied during the period and by whom they were applied.
- The concept of effective operation recognises that some deviations may have occurred. Deviations from prescribed controls may be caused by such factors as changes in key personnel, significant seasonal fluctuations in volume of transactions and human error.
- When deviations are detected, the auditor makes specific inquiries regarding these matters, particularly, the timing of staff changes in key internal control functions. The auditor then ensures that the tests of control appropriately cover such a period of change or fluctuation.
- Based on the results of the tests of control, the auditor should evaluate whether the internal controls are designed and operating as contemplated in the preliminary assessment of control risk.
- The evaluation of deviations may result in the auditor concluding that the assessed level of control risk needs to be revised. In such cases, the auditor would modify the nature, timing and extent of planned substantive procedures.
- Before the conclusion of the audit, based on the results of substantive procedures and other audit evidence obtained by the auditor, the auditor should consider whether the assessment of control risk is confirmed.
- In case of deviations from the prescribed accounting and internal control systems, the auditor would make specific inquiries to consider their implications. Where, on the basis of such inquiries, the auditor concludes that the deviations are such that the preliminary assessment of control risk is not supported, he would amend the same unless the audit evidence obtained from other tests of control supports that assessment.
- Where the auditor concludes that the assessed level of control risk needs to be revised, he would modify the nature, timing and extent of his planned substantive procedures.

Chapter 5 – Audit of Items of Financial Statements

5.4 – Audit of Borrowings

Q.13A How is "Short Term Borrowings" disclosed in the Financial Statements as required under Part I of Schedule III to the Companies Act, 2013? [Nov. 23 (4 Marks)]

Ans: Disclosure w.r.t. Short Term Borrowings as per Part I of Schedule III:

- (i) Short-term borrowings shall be classified as:
 - (a) Loans repayable on demand; (A) from banks. (B) from other parties.
 - (b) Loans and advances from related parties;
 - (c) Deposits;
 - (d) Other loans and advances (specify nature).
- (ii) Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.
- (iii) Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed.

- (iv) Period and amount of default as on balance sheet date in repayment of loans and interest, shall be specified separately in each case.
- (v) Current maturities of long-term borrowings shall be disclosed separately.

Q.13B **Droma Shoes Private Limited was established in year 2023-24 for manufacturing of footwear. As funds were needed to carry on its business activities - including for purchase of different raw materials, incurring of regular expenses like power and fuel and payment of wages etc., it had got sanctioned a credit facility amounting to ₹ 2 crores repayable on demand from a bank against primary security of its current assets and collateral security of residential house of one of its directors. Duly signed guarantee documents by directors in favour of bank also form part of bank’s loan documentation. Account statement of above facility downloaded from bank’s website shows debit balance of ₹ 1.85 crores as on 31st March, 2024. The operations in above credit facility are satisfactory. In this regard:**

- (i) Identify nomenclature of such credit facility given by banks. How would above amount of ₹ 1.85 crores be reflected and classified in financial statements of company as on 31.3.24?**
- (ii) Also state specific disclosure requirements of Schedule III of Companies Act, 2013 in relation to above.**

[RTP - May 24]

Ans: Cash Credit/Overdraft Facilities:

- (i) The type of credit facilities referred to in above situation given by banks to meet working capital requirements of business which are repayable on demand are known as “cash credit facilities/overdraft” facilities. The amount of ₹ 1.85 crores outstanding as on 31st March, 2024 reflects borrowings of the company and it would be classified as “short-term borrowings” as loans repayable on demand from banks under current liabilities in balance sheet of the company. Borrowings shall further be subclassified as secured.
- (ii) Specific disclosure requirements of short-term borrowings under Schedule III to Companies Act, 2013 in given situation are as under:
 - Nature of security i.e. primary security of current assets and collateral security of residential house belonging to a director shall be specified.
 - As loans have been guaranteed by directors, the aggregate amount of such loans shall be disclosed.

To be disclosed as Additional Regulatory Information

Since the Company has borrowings from bank on the basis of security of current assets, it shall also disclose the following:

- (a) whether quarterly returns or statements of current assets filed by the Company with banks or financial institutions are in agreement with the books of accounts.
- (b) if not, summary of reconciliation and reasons of material discrepancies, if any to be adequately disclosed.

5.7 – Audit of Inventories

Q.26A **Narrate the audit procedures to be performed by an auditor in order to ascertain that the Raw materials and consumables are valued appropriately and as per generally accepted accounting policies and practices.**

[Nov. 23 (4 Marks)]

Ans: Audit procedures ascertain appropriate Valuation of Raw materials and consumables:

- (a) Ascertain what elements of cost are included e.g. carriage inward, non-refundable duties etc.

- (b) If standard costs are used, enquire into basis of standards; how these are compared with actual costs and how variances are analyzed and accounted for/treated in accounting records.
- (c) Test check cost prices used with purchase invoices received in the month(s) prior to counting.
- (d) Follow up valuation of all damaged or obsolete inventories noted during observance of physical counting with a view to establishing a realistic net realizable value.

5.19 – Other Miscellaneous Provisions

Q.67A Following is extract of notes to accounts of financial statements of STU Private Limited listing some ratios. Discuss, whether disclosure, given in following manner meets requirements of Schedule III of the Companies Act, 2013. Ignore other ratios which are not listed in extract given below:

Name of Ratio	31.03.2024	31.03.2023
Current Ratio	2.50	2.30
Inventory turnover ratio	3.00	6.00
Trade receivables turnover ratio	1.75	5.00
Net profit ratio (in%)	13%	10%

[RTP-May 24]

Ans: Disclosure of Ratios as per Schedule III of the Companies Act, 2013:

The disclosure given in the question does not meet requirements of Schedule III to Companies Act, 2013.

Schedule III requires that the company shall explain the items included in numerator and denominator for computing the ratios. Further explanation shall be provided for any change in the ratio by more than 25% as compared to the preceding year.

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

Name of Ratio	31.03.24	31.03.23	Variation
Current Ratio	2.50	2.30	8.69%
Inventory turnover ratio	3.00	6.00	50%
Trade receivables turnover ratio	1.75	5.00	65%
Net Profit ratio (in%)	13%	10%	30%

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

Chapter 6 – Audit Documentation

Q.16A Audit Documentation refers to the record of three items. Explain stating clearly the objective and nature of audit documentation. [RTP-Nov. 23]

Ans: Objective and nature of audit documentation

Audit Documentation refers to the record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached.

	<p>The objective of the auditor is to prepare documentation that provides:</p> <p>(i) A sufficient and appropriate record of the basis for the auditor's report; and</p> <p>(ii) Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.</p> <p>Nature of Audit Documentation</p> <p>Audit documentation provides:</p> <p>(a) evidence of the auditor's basis for a conclusion about the achievement of the overall objectives of the auditor; and</p> <p>(b) evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.</p>
Q.16B	<p>IT related risks can have an impact on audit. In what different ways, such risks can have an impact on audit of financial statements? [RTP-May 23]</p> <p>Ans: Impact of IT related risks on audit:</p> <p>Impact on substantive checking:</p> <p>Inability to address IT risks may lead to non-reliance of data obtained from systems. In such a case, all information, data, and reports would have to be tested thoroughly for their completeness and accuracy. It could lead to increased substantive checking i.e. detailed checking.</p> <p>Impact on controls</p> <p>It can lead to non-reliance on automated controls, system calculations and accounting procedures built into applications. It may result in additional audit work.</p> <p>Impact on reporting</p> <p>Due to regulatory requirements in respect of internal financial controls in case of companies, it may lead to modification of auditor's report in some instances.</p>

Chapter 7 – Completion and Review

7.1 – Subsequent Events (SA 560)

Q.6A	<p>CA K is statutory auditor of DEMA Private Limited for the year 2022-23. The company has three plants in India. He is nearing completion of audit procedures relating to financial statements for the year under audit and has yet to sign audit report. Meanwhile, a huge fire had broken out in one of plants of the company located near Nashik on 25th June, 2023 damaging substantial part of machinery and work-in-process resulting in loss of about ₹ 5 crores. Unaware of the incident, he is in process of finalizing his report in first fortnight of July 2023. State few audit procedures to be performed by him to obtain sufficient appropriate evidence for identifying such events. Also explain auditor's responsibilities in this situation. [RTP-May 24]</p> <p>Ans: Audit procedures w.r.t. Subsequent Events:</p> <p>In the given situation, a huge fire had broken out in one of plants of company on 25th June, 2023 destroying substantial part of machinery and work-in-process resulting in loss of ₹ 5 crores. The auditor has yet to sign audit report.</p> <p>Before signing audit report, he should perform following audit procedures to obtain sufficient appropriate audit evidence that all such events have been identified and are appropriately reflected in financial statements: -</p>
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- Inquiry of management whether any subsequent events have occurred
- Reading minutes of the meetings of owners, management that have been held after date of financial statements and inquiring about matters discussed at such meetings for which minutes are not available
- Reading entity's latest subsequent interim financial statements
- Obtaining Written representations from management in accordance with SA 580

The situation is an example of subsequent event occurring between date of financial statements and date of audit report requiring disclosure in financial statements. The auditor has a responsibility to obtain sufficient appropriate audit evidence whether such an event requiring disclosure in financial statements is appropriately reflected in financial statements.

7.2 – Going Concern (SA 570)

Q.14A Kundan, a CA student, is part of an engagement team conducting audit of an entity. The audit procedures are nearing completion. He notices that engagement partner has asked for a cash flow forecast from management for next twelve months from date of financial statements. Keeping in view above, answer the following: -

- Discuss likely purpose of engagement partner in the above situation. Elaborate upon significance of such testing being performed by engagement partner.**
 - State any two audit procedures in relation to cash flow forecast likely to be performed by engagement partner.**
- [RTP-May 24]**

Ans: Evaluating appropriateness of Going Concern basis of accounting:

In the given situation, the engagement partner has asked for a cash flow forecast from management for next twelve months from date of financial statements. The audit procedures are also nearing completion.

Therefore, purpose of engagement partner in requiring a cash flow forecast is to obtain sufficient appropriate audit evidence regarding and to conclude on appropriateness of management's use of going concern basis of accounting in preparation of its financial statements. Further, his purpose is also to conclude on basis of audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast a significant doubt on ability to entity to continue as a going concern, and to report in accordance with SA 570.

The significance of testing going concern assumption is due to its effect on preparation of financial statements. When the use of going concern is considered as appropriate, assets and liabilities are recorded on the basis that entity will be able to realize its assets and discharge liabilities in normal course of business. In case it is not so viewed, financial statements are prepared on liquidation basis. Hence, testing such an assumption provides evidence to auditor whether use of such assumption is appropriate or not.

Two audit procedures in relation to cash flow forecast likely to be performed:

- Evaluate reliability of underlying data generated to prepare the forecast
- Determine whether there is adequate support for assumptions underlying the forecast

Chapter 8 – Audit Report

8.1 - Forming an Opinion & Reporting on F.S. (SA 700)

Q.18A	<p>The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements." Give a brief description about management's responsibilities in the auditor's report as it helps to explain the users the premise on which an audit is conducted.</p> <p>Also state the requirement specified in Standard on Auditing 210 for the auditor to agree management's responsibilities. [Nov. 23 (4 Marks)]</p>
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Ans: Responsibilities of Management for F.S.:

"Responsibilities of Management for F.S." section in Auditor's report shall describe management's responsibility for:

- (a) Preparing the F.S. in accordance with the applicable FRF, and for such internal control as management determines is necessary to enable the preparation of F.S. that are free from material misstatement, whether due to fraud or error; and
- (b) Assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern.

Requirements of SA 210:

Auditor is to **accept or continue** an audit engagement only when the basis upon which it is to be performed has been agreed, through:

- (a) Establishing whether the **preconditions for an audit** are present; and
- (b) Confirming that there is a **common understanding** between the auditor and management and TCWG, of the terms of the audit engagement.

In order to establish whether the preconditions for an audit are present, the auditor shall:

- (a) Determine whether FRF to be applied in preparation of F.S. is acceptable; and
- (b) Obtain agreement of management that it acknowledges and understands its responsibilities for followings:
 - (i) preparation of the F.S. in accordance with the applicable FRF.
 - (ii) exercising necessary internal control to enable the preparation of F.S. that are free from material misstatement, whether due to fraud or error.
 - (iii) to provide the auditor with:
 - (a) Access to all relevant information such as records, documentation and other matters;
 - (b) Additional information that the auditor may request from management for the purpose of the audit; and
 - (c) Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

8.2 - Modifications to the Opinion in the Independent Auditor's Report (SA 705)

Q.34A	<p>CA. S, while conducting audit of an entity is facing the following issues: -</p> <p>(i) He has not been provided with necessary support for attending inventory count process of entity as at year end.</p>
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- (ii) Accounts Manager is not providing him present addresses of customers as well as suppliers for sending external confirmations. Even mail ids have not been provided on the pretext of business confidentiality.
- (iii) He was not able to verify revenues of entity due to lack of complete details.
- (iv) He has been asking for bills on a sample basis for the purpose of verifying expenses, but staff has been making lame excuses.

The matter was brought to knowledge of higher management, but of no avail. The auditor, CA S has come to the conclusion that the possible effects on the financial statements of undetected misstatements would be material and affecting many aspects of financial statements and in such a case, a qualification of the opinion would be inadequate to communicate the gravity of the situation.

How should the auditor proceed in such a situation?

[MTP-May 24]

Ans: Limitation after Auditor has accepted the Engagement:

In the given case, auditor has not been able to obtain sufficient appropriate audit evidence relating to inventories, debtors, creditors, revenues and expenses. The matter was brought to the knowledge of management but no result has been achieved. In such circumstances, auditor should proceed as given here under:

If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall:

- (i) Withdraw from the audit, where practicable and possible under applicable law or regulation; or
- (ii) If withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements.

If auditor withdraws from such an engagement, before withdrawing, auditor shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion.

8.4 - Communicating Key Audit Matters in the Independent Auditor's Report (SA 701)

Q.41A M/s ABC & Associates, statutory auditors of Opaque Ltd., are in the process of finalizing the audit report of the company but in view of their inability to obtain sufficient appropriate audit evidence, they would like to disclaim their opinion on the financial statements.

Explain reporting responsibilities of M/s ABC & Associates pursuant to SA 700(Revised). How they will address key audit matters section in accordance with SA 701 when they are expressing disclaimer of an opinion on the financial statements? [Nov. 23 (4 Marks)]

Ans: Reporting responsibilities:

- (a) The auditor shall express an **unmodified opinion** when he concludes that F.S. are prepared, in all material respects, in accordance with the applicable FRF.
- (b) The auditor shall **modify the opinion** in accordance with SA 705 if:
 - concludes that, based on the audit evidence obtained, the F.S. as a whole are not free from material misstatement; or
 - is unable to obtain SAAE to conclude that the F.S. as a whole are free from material misstatement.

The decision regarding which type of modified opinion is appropriate depends upon:

- (a) Nature of the matter giving rise to the modification, that is, whether the F.S. are materially misstated or, in the case of an inability to obtain SAAE, may be materially misstated; and
- (b) Auditor's judgement about pervasiveness of effects or possible effects of matter on the F.S.

Auditor shall disclaim an opinion when he is unable to obtain SAAE on which to base the opinion, and he concludes that the possible effects on the F.S. of undetected misstatements, if any, could be both material and pervasive.

When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall:

- (a) State that auditor does not express an opinion on accompanying F.S.;
- (b) State that, because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion section, auditor has not been able to obtain SAAE to provide a basis for an audit opinion on the financial statements; and
- (c) Amend statement in Opinion Section, which indicates that the F.S. have been audited, to state that the auditor was engaged to audit the F.S.

Addressing Key Audit matters:

SA 705 prohibits the auditor from communicating Key Audit Matters when the auditor disclaims an opinion on the financial statements.

8.8 - Reporting Requirements under Companies Act, 2013

Q.59A CA E was appointed statutory auditor of XYZ Private Limited in AGM held in the month of August, 2023 for the first time for audit of financial statements of the company from year 2023-24 onwards. Since he is new to the company, he wants to be sure about integrity of accounting records. In this regard, he wants to ensure that software used by company for maintenance of its books of accounts is capable of tracking user activities and changes made to entries in books of accounts, if any, during the course of year.

What CA E is looking for in the given situation? Discuss the reporting requirements for CA E in this matter to be included in audit report to be issued under the Companies Act, 2013. [MTP-Oct. 23]

Or

As per Rule 11(g) of the Companies (Audit and Auditors) Rules, 2014, auditor's report should state whether the accounting software used for maintaining its books of account has a feature of recording audit trail (edit log) facility. What are the reporting requirements under Rule 11(g)?

[Nov. 23 (3 Marks)]

Ans: Reporting requirements under Rule 11(g)

In the given situation, the auditor is looking for a feature of "audit trail" in software used by company for maintenance of books of accounts. Under section 143(3) of Companies Act, 2013, it has to be reported by the auditor as under: -

- Whether the company has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and
- the same has been operated throughout the year for all transactions recorded in the software and
- the audit trail feature has not been tampered with and
- the audit trail has been preserved by the company as per the statutory requirements for record retention.

Chapter 9 – Special Features of Audit of Different Type of Entities

9.2 – Audit of Local Bodies

Q.18A Before commencing the Audit of Local Bodies, a Chartered Accountant employee in firm of XYZ & Co., firm of Chartered Accountants seeks assistance of Mr. X, partner, in preparation of audit programme for local bodies. How Mr. X should advise to him in this connection? [MTP-Sep. 23]

Ans: Audit Programme for local bodies

- (i) The Local Fund Audit Wing of the State Government is generally in-charge of the audit of municipal accounts. Sometimes bigger municipal corporations e.g. Delhi, Mumbai etc have power to appoint their own auditors for regular external audit. So the auditor should ensure his appointment.
- (ii) The auditor while auditing the local bodies should report on the fairness of the contents and presentation of financial statements, the strengths and weaknesses of system of financial control, the adherence to legal and/or administrative requirements; whether value is being fully received on money spent. His objective should be to detect errors and fraud and misuse of resources.
- (iii) The auditor should ensure that the expenditure incurred conforms to the relevant provisions of the law and is in accordance with the financial rules and regulations framed by the competent authority.
- (iv) He should ensure that all types of sanctions, either special or general, accorded by the competent authority.
- (v) He should ensure that there is a provision of funds and the expenditure is incurred from the provision and the same has been authorized by the competent authority.
- (vi) The auditor should check that the different schemes, programmes and projects, where large financial expenditure has been incurred, are running economically and getting the expected results.

9.6 – Audit of Charitable Institution, Educational Institution and Hospital

Q.38A CA Z is appointed as the auditor of Chanakya Open University which offers higher learning educational courses through the Distance Mode of Education. Discuss four steps involved in his audit of other receipts/grants and donations received by the University. [Nov. 23 (4 Marks)]

Ans: Steps involved in his audit of other receipts/grants and donations received by the University:

- (1) Verify rental income from landed property with the rent rolls, etc.
- (2) Vouch income from endowments and legacies, as well as interest and dividends from investment; also inspect the securities in respect of investments held.
- (3) Verify any Government or local authority grant with the memo of grant. If any expense has been disallowed for purposes of grant, ascertain the reasons thereof.

9.8 – Audit of Hire Purchase and Leasing Companies

Q.43A ABC Ltd. wants to buy some equipment on lease and hence is required to sign lease agreement with the supplier of the equipment. What are the important points to be considered in the lease agreement? [MTP-Sep. 23]

Ans: Important points to be examined in the lease agreement:

- (i) Description of the lessor, the lessee, the equipment and the location where the equipment is to be installed. (The stipulation that the equipment shall not be removed from the described location except for repairs. For the sake of identification, the lessor may also require plates or markings to be attached to the equipment).
- (ii) Amount of tenure of lease, dates of payment, late charges, deposits or advances etc. should be noted.
- (iii) Whether the equipment shall be returned to the lessor on termination of the agreement and the cost shall be borne by the lessee.
- (iv) Whether the agreement prohibits the lessee from assigning the subletting the equipment and authorises the lessor to do so.

Q.43B From a lessee's perspective, highlight main differences between an operating lease and finance lease only in relation to accounting treatment and tax benefits. [RTP-May 24]

Ans: Accounting treatment

Operating lease is generally treated like a renting arrangement. Lease payments are treated as operating expenses and asset does not appear as asset in lessee's balance sheet. Finance lease is treated like a loan arrangement Hence, asset ownership is considered of that of lessee and thus appears on the balance sheet of the lessee.

Tax benefits

Operating lease payment is considered like an expense just as in case of renting. However, no depreciation can be claimed by lessee. In case of finance lease, lessee can claim both interest and depreciation as it is treated like a loan.

Chapter 10 – Audit of Banks

10.2 – Auditing Framework

Q.12A CA X is acting as concurrent auditor of a branch of KLT Bank (a nationalized bank) located in Delhi during the year 2023-24. The assignment started from 1st October 2023 and is for a period of one year. By virtue of this assignment, he is required to issue monthly reports on different aspects of the functioning of branch including deposits, advances and housekeeping to controlling authorities of Bank.

At the end of March, 2024, he has got an offer to conduct statutory audit of two branches of KLT Bank located in the State of Rajasthan for the year 2023-24. Can he accept the above offer? Discuss.

[MTP-Oct. 23]

Ans: Initial Considerations in accepting an audit:

In the given situation, CA X has undertaken concurrent audit assignment of KLT Bank which is in the nature of internal assignments.

In accordance with RBI guidelines, statutory audit assignments should not be undertaken by auditors while being associated with internal assignments in bank during the same year like concurrent audits (Internal audits of banks conducted monthly during the year).

As CA X is associated with KLT Bank as concurrent auditor, he should not accept statutory audit assignment of same bank even though it relates to different branches of the bank.

10.3 – Types and Classification of Advances

Q.27A While verifying provisions of advances of a branch of MCO Bank as part of statutory branch audit, CA Z notices that credit facilities consisting of term loan to KRT Enterprises have been classified under doubtful asset (D1) category.

The outstanding balance in above term loan account as on 31.3.2024 is ₹ 50 lakhs. Value of security held in account is ₹ 40 lakhs. The branch has made provision of ₹ 7.50 lakhs. Is provision made by branch proper? Discuss. [MTP-Sep. 23; RTP-May 24]

Ans: Provisioning for Advances:

The provision for advances falling in D1 category is required @ 25% of secured portion and 100% of unsecured portion. Therefore, provision in above case is arrived as under: -

Outstanding balance as on 31.3.24	₹ 50 lakhs
Less: Value of security	<u>₹ 40 lakhs</u>
Unsecured portion	<u>₹ 10 lakhs</u>

Therefore, outstanding balance of ₹ 50 lakhs is secured to the tune of ₹ 40 lakhs and balance ₹ 10 lakhs is unsecured.

Provision calculation

25% of secured part i.e., 25% of ₹ 40 lakhs	₹ 10 lakhs
100% of unsecured part i.e., 100% of ₹ 10 lakhs	<u>₹ 10 lakhs</u>
Required provision	<u>₹ 20 lakhs</u>

Therefore, provision made by branch is not proper. It should have made provision of ₹ 20 lakhs instead of ₹ 7.50 lakhs.

10.6 – Audit of Revenue Items (Income)

Q.39A While conducting statutory audit of branch of a nationalized bank, it is noticed by CA Z that credit facilities granted to a borrower consisting solely of term loan have been classified as “Sub-standard Asset” during the year 2023-24 due to failure of borrower to pay EMIs on time. Such EMIs were outstanding for more than 90 days and account was, therefore, classified as “Sub-Standard Asset”. CA Z has also agreed to above asset classification made by branch management.

What are CA Z’s responsibilities regarding verification of compliance with income recognition norms by branch in respect of above credit facilities? [MTP-Oct. 23/RTP-May 24]

Ans: Income recognition norms in respect of credit facilities classified as NPA:

RBI norms stipulate that if any advance account becomes NPA as at close of any year, the entire interest accrued or credited to income account in past periods should be reversed or provided for, if the same is not realized.

Further, in respect of NPAs, fees, commission and other similar income that have accrued should cease to accrue in the current period and should be reversed or provided for with respect to past periods, if uncollected.

In the given case, account has turned Sub-standard asset which is a type of NPA. Therefore, auditor should make compliance of above norms relating to income recognition.

Chapter 11 – Ethics and Terms of Audit Engagements

11.4 – Agreeing the Terms of Audit Engagement (SA 210)

Q.23A CA X has been offered audit of financial statements of TDK Industries, a partnership firm. Prior to accepting proposed offer, he insists upon obtaining an agreement of management regarding acknowledgment of its responsibility of having a proper process in place to ensure that financial statements prepared are free from material misstatements. However, management is of the view that it is auditor's duty to detect material misstatements in financial statements and such an insistence by auditor is totally uncalled for. Whose view is proper? Also discuss reasons for arriving at your conclusion. What should be likely proper course of action for CA X in above situation?

[RTP-May 24]

Ans: Duty to detect material misstatements in financial statements

SA 210 deals with the auditor's responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance. This includes establishing that certain preconditions for an audit, responsibility for which rests with management and, where appropriate, those with governance, are present.

The objective of the auditor is to accept or continue an audit engagement only when the basis upon which it is to be performed has been agreed, through:

- (A) Establishing whether the preconditions for an audit are present and
- (B) Confirming that there is a common understanding between the auditor and management and, where appropriate, those charged with governance of the terms of the audit engagement.

One of the preconditions for an audit is to obtain the agreement of management that it acknowledges and understands its responsibility for preparation of financial statements and for such internal control as is necessary to enable preparation of financial statements that are free from material misstatements.

In the given situation, CA X is insisting only upon obtaining agreement of management regarding acknowledgment of its responsibility for internal control to enable preparation of financial statements that are free from material misstatements in accordance with SA 210. Design, implementation and maintenance of internal control to ensure preparation of reliable financial statements that are free from material misstatements is management's responsibility. He is insisting on obtaining agreement of management regarding acknowledgment of its responsibility. Therefore, CA X's view is proper.

In case management does not provide such agreement acknowledging its responsibility, the auditor shall not accept proposed audit engagement unless required by law or regulation.

11.5 - SQC 1 "Quality Control for Firms that perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements"

Q.27A An auditing firm should monitor compliance with quality control policies and procedures. Discuss the purpose of this. [Nov. 23 (3 Marks)]

Ans: Purpose of Monitoring Compliance with Quality Control Policies and procedures:

- Firm should establish policies and procedures designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, operating effectively and complied with in practice.

- Such policies and procedures should include an ongoing consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements.
- EP shall consider the results of the firm's monitoring process as evidenced in the latest information circulated by the firm and, if applicable, other network firms and whether deficiencies noted in that information may affect the audit engagement.

11.6 - SA 220 "Quality Control for an Audit of Financial Statements"

Q.30A "SA 220 is premised on the basis that the firm is subject to SQC 1". What do you understand by given statement in context of audit quality? [RTP-May 24]

Ans: SA 220 is premised on the basis that the firm is subject to SQC 1:

Audit quality is essential to maintain confidence in the independent assurance provided by the auditors. It is responsibility of auditor to maintain high audit quality. SQC 1 and SA 220 both deal with quality control. SQC 1 applies to entire firm. However, SA 220 applies to a particular audit engagement. Based upon quality control system of firm established in accordance with requirements of SQC 1, quality control policies pertaining to audit engagements are decided by engagement teams. Engagement partner of a team is responsible for quality control procedures of a particular audit engagement in accordance with SA 220.

Therefore, SA 220 is premised on the basis that the firm is subject to SQC 1. Within the context of the firm's system of quality control, engagement teams have a responsibility to implement quality control procedures that are applicable to the audit engagement.

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PART II – Correct/Incorrect QUESTIONS

Chapter 2 – Audit Strategy, Audit Planning and Audit Programme

1	The overall audit strategy is more detailed than the audit plan.	[MTP-Sep. 23]
	<p>Ans.: Statement is incorrect.</p> <p>The audit plan is more detailed than the overall audit strategy that includes the nature, timing and extent of audit procedures to be performed by engagement team members.</p> <p>Once the overall audit strategy has been established, an audit plan can be developed to achieve the audit objectives through the efficient use of the auditor's resources.</p>	

Chapter 3 – Risk Assessment and Internal Control

2	There is direct relationship between detection risks and the combined level of inherent and control risks.	[RTP-Nov. 23]
	<p>Ans.: Statement is incorrect.</p> <p>There is an inverse relationship between detection risks and the combined level of inherent and control risks. For example, when inherent and control risks are high, acceptable detection risks need to be low to reduce audit risk to an acceptably low level.</p> <p>On the other hand, when inherent and control risks are low, an auditor can accept a higher detection risk and still reduce audit risk to an acceptably low level.</p>	

Chapter 4 – Audit Evidence

3	While auditing the books of accounts of XYZ Ltd., the auditor of the company was involved in examining records and documents in paper form, electronic form etc. and was also conducting physical examination of assets. In the present case, audit procedure used by the auditor is known as "Observation".	[MTP-Sep. 23, Oct. 23]
	<p>Ans.: Statement is incorrect.</p> <p>The audit procedure used by the auditor of XYZ Ltd. is known as "Inspection".</p> <p>Whereas Observation consists of looking at a process or procedure being performed by others.</p>	
4	Sales invoice is an example of external evidence.	[Nov. 23 (2 Marks)]
	<p>Ans.: Statement is incorrect.</p> <ul style="list-style-type: none"> • External Evidence is one that originates outside client's organization. • Sales invoice is internal evidence as it originates within the entity. 	
5	Block sampling does not involve judgement, does not even use the random number tables and has no structured approach.	[Nov. 23 (2 Marks)]

Ans.: Statement is incorrect.

Block Sampling method involves selection of a block(s) of contiguous items from within the population. Haphazard sampling has no structured approach, does not involve judgement and does not even use the random number tables

Chapter 5 – Audit of Items of Financial Statements

6 An unexplained decrease in GP Ratio may result due to fictitious sales. [RTP-Nov. 23]

Ans.: Statement is incorrect.

A fictitious sale will increase the GP Ratio, instead of decreasing it. GP ratio normally comes down if there are unrecorded sales or reversal of fictitious sale entries recorded in the previous year or fictitious purchase or decrease in closing stock.

Chapter 9 – Special Features of Audit of Different Type of Entities

7 NGOs registered under the Companies Act, 2013 are not allowed to maintain accounts on cash basis. [Nov. 23 (2 Marks)]

Ans.: Statement is Correct.

NGOs registered under the Companies Act, 2013 must maintain their books of account under the accrual basis as required by the provisions of section 128 of the said Act. If the accounts are not maintained on accrual basis, it would amount to non-compliance of the provision of the Companies Act, 2013.

The NGOs which are not registered under the Companies Act, 2013 are allowed to maintain accounts either an accrual basis or cash basis.

8 Under 'finance lease' lease term generally extends to less than 75% of the projected useful life of the leased asset. [Nov. 23 (2 Marks)]

Ans.: Statement is incorrect.

In case of Operating lease, lease term generally extends to less than 75% of the projected useful life of the leased asset.

In case of Finance lease, lease term is generally more than or equal to estimated economic life of the asset under the lease arrangement.

9 In government expenditure audit, audit against provision of funds aims at ensuring that each item of expenditure is covered by sanction, either general or special, of the competent authority. [Nov. 23 (2 Marks)]

Ans.: Statement is incorrect.

Ensuring that each item of expenditure is covered by sanction, either general or special, of the competent authority is covered by audit of sanctions.

Audit against provision of funds aims that there are provisions or budget of funds out of which expenditure can be met.

PART III - MULTIPLE CHOICE QUESTIONS

Chapter 3 – Risk Assessment and Internal Control

1	<p>To evaluate the Internal Control of Kingsway Limited, a team member of the auditors used a method according to which, number of questions relating to internal control of the company were required to be answered by the employees of the company. After obtaining the answers there was a discussion relating to those answers between team member of the auditor and employees of the company for a clear picture. State the method of evaluation of internal control as discussed above.</p> <p>(a) Narrative record (b) Check List (c) Internal Control questionnaire (d) Flow chart</p> <p style="text-align: right;">[MTP-Sep. 23]</p>
2	<p>The term Internal Financial Controls (IFC) basically refers to the policies and procedures put in place by companies for ensuring:</p> <p>(i) Reliability of financial reporting (ii) Compliance with applicable laws and regulations (iii) Safeguarding of assets. (iv) Effectiveness and efficiency of operations (v) Prevention and detection of frauds</p> <p>Which statement is correct?</p> <p>(a) (i), (ii) and (iv) (b) (i), (iii), (v) and (ii) (c) (i), (ii), (iii) and (iv) (d) (i), (ii), (iii), (iv)and (v)</p> <p style="text-align: right;">[MTP-Sep. 23]</p>
3	<p>Financial statements of a company have been put up for audit before the auditor. On going through financial statements, he wants to verify some major bills debited in “Machinery repair” account. The purpose of it is to ensure that bills are entered correctly and their classification is proper. As regards verification of bills debited in “Machinery repair” account, identify what he intends to perform?</p> <p>(a) Tests of Controls (b) Tests of transactions (c) Tests of balances (d) Risk assessment procedures</p> <p style="text-align: right;">[MTP-Sep. 23]</p>
4	<p>Which of the following is a risk that arises from the use of IT systems?</p> <p>(a) Direct data changes (backend changes). (b) Limited/Monitored access. (c) Adequate segregation of duties. (d) Authorized access to data.</p> <p style="text-align: right;">[RTP-Nov.23]</p>

5	<p>You have been appointed as statutory auditor of a company for the first time. It has become very important for you to understand the company and its environment. Which of the following activities are not expected to be included in your attempts to know about the company and its environment?</p> <p>(a) Gaining a knowledge about debt structure of the company (b) Evaluating whether company's accounting policies are appropriate for its business (c) Understanding business risks faced by the company (d) Gathering evidence about valuation of trade receivables of the company</p>	[RTP-May 24]
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Chapter 4 – Audit Evidence

6	<p>While auditing the books of accounts of Mehra Limited for the financial year 2022-23, the auditor of the company used an audit procedure according to which complete documents and records of the company were checked in detail in order to obtain audit evidence. Explain the audit procedure used by the auditor of company.</p> <p>(a) Recalculation (b) Analytical Procedures (c) Inquiry (d) Inspection</p>	[MTP-Sep. 23]
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Chapter 5 – Audit of Items of Financial Statements

7	<p>ABC Ltd is engaged in manufacturing of fabrics from yarn purchased from different suppliers. Occasionally, it also manufactures fabrics tailor made in accordance with requirements of certain mills from yarn received from these mills. ABC Ltd raises bills of its labour charges only on mills for converting yarn into fabrics. The auditor of ABC Ltd tries to ensure that stocks of the company as at year end do not include stocks pertaining to these mills. Which assertion auditor tries to verify in above situation:</p> <p>(a) completeness (b) Occurrence (c) rights and obligations (d) cut -off</p>	[MTP-Sep. 23]
8	<p>CA Tarini is in process of formulating audit plan for conducting audit of a company engaged in business of dealing in commodity futures. Which of the following is not likely to be an appropriate audit procedure to be included in audit plan for the abovesaid company?</p> <p>(a) Verification of turnover of company (b) Verification of cost of raw material consumed (c) Examination of company's accounting policy for revenue recognition (d) Verification of contract notes with brokers</p>	[MTP-Oct. 23]
9	<p>CA Muskan is auditor of two concerns viz. Well Star Homes and Well Star Stores. The partners in both the firms are common. While auditing financial statements of Well Star Homes, she has noticed that few expenditure bills pertaining to Well Star Stores have been entered in its books. Which assertion of Well Star Homes is disproved in above situation?</p>	

	(a) Completeness (b) Accuracy (c) Occurrence (d) Classification	[RTP – May 24]
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Chapter 6 – Audit Documentation

10	Which of the following is not a likely purpose of audit documentation? (a) It helps to show that audit was conducted in accordance with requirements of SQC 1. (b) It serves as a record of matters of continuing significance to future audits. (c) It assists engagement team to plan and perform the audit. (d) It can directly help auditor in expanding client base.	[MTP-Sep. 23]
11	A company has started its manufacturing operations from a newly constructed building. CA Z is statutory auditor of company. Which of following is not likely to be an example of audit documentation? (a) E-mail correspondence with CFO of company concerning significant matters (b) Audit programme (c) Response to external confirmation requests (d) Structural engineer's report on strength of building	[MTP-Oct. 23]

Chapter 7 – Completion and Review

12	Following are examples of events or conditions that may cast significant doubt on an entity's ability to continue as a going concern. Which of following is an example of operating event/conditions? (a) Adverse key financial ratios (b) Inability to pay creditors on due dates (c) Indications of withdrawal of financial support by creditors (d) Shortages of important supplies	[MTP-Oct. 23]
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Chapter 8 – Audit Report

13	Which of following is not an element of audit report in accordance with SA 700? (a) Title (b) Addressee (c) Audit strategy (d) Auditor's opinion	[MTP-Oct. 23]
14	An auditor disclaims opinion when _____? (a) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be material.	

	<p>(b) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be both material and adverse.</p> <p>(c) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be both material and pervasive.</p> <p>(d) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be both material and perverse. [MTP-Oct. 23]</p>
15	<p>UDIN (Unique Document Identification Number) is required to be stated by practising Chartered Accountant on: -</p> <p>(a) Each audit report only</p> <p>(b) Each audit report and each certificate</p> <p>(c) Each audit report issued under Companies Act, 2013 only</p> <p>(d) Each audit report issued under Companies Act, 2013 only and each certificate [MTP-Oct. 23]</p>
16	<p>For which of following company, provisions of CARO,2020 would be applicable?</p> <p>(a) Boost Up Training (OPC) Private Limited</p> <p>(b) RCI Bank Limited</p> <p>(c) PST Industries Limited</p> <p>(d) Moon Insurance Limited [MTP-Oct. 23]</p>
17	<p>While reporting under CARO, 2020, it is duty of statutory auditor of company to report:</p> <p>(a) Fraud of less than ₹ 1 crore committed by officers or employees of company during the year</p> <p>(b) Fraud of ₹ 1 crore or more committed by officers or employees of company during the year</p> <p>(c) Fraud of ₹ 5 crore or more committed by officers or employees of company during the year</p> <p>(d) Any fraud by the company or on the company noticed or reported during the year [MTP-Oct. 23]</p>

Chapter 10 - Audit of Banks

18	<p>Which of the following statements is true regarding financial statements of a bank?</p> <p>(a) Financial statements of a bank are to be prepared in accordance with Third Schedule to Banking Regulation Act, 1949.</p> <p>(b) Financial statements of a bank are to be prepared in accordance with Schedule III of Companies Act, 2013.</p> <p>(c) Financial statements of a bank are to be prepared in accordance with Schedule II of Reserve Bank of India Act, 1934.</p> <p>(d) Financial statements of a bank are to be prepared in accordance with format prescribed by Comptroller and Auditor General of India. [MTP-Sep. 23]</p>
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Chapter 11 - Ethics and Terms of Audit Engagements

19	<p>Which of following is not a threat to independence of auditor?</p> <p>(a) Self-interest threats</p> <p>(b) Self- review threats</p> <p>(c) Advocacy threats</p> <p>(d) Peer group threats [MTP-Oct. 23]</p>
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20	<p>CA Piyush is offered appointment as statutory auditor of branch of a bank. He has also taken housing loan of ₹ 75 lakhs from the same bank. Identify threat to independence involved.</p> <p>(a) Advocacy threat (b) Self-interest threat (c) Self-review threat (d) Familiarity threat</p> <p style="text-align: right;">[RTP-May 24]</p>
21	<p>A Chartered Accountant finds during the course of statutory audit of a company that management is not serious about findings of internal audit reports. No action has been taken on findings of internal auditor and reports for last two quarters are gathering dust.</p> <p>He has further found that management has not disclosed information relating to transactions with another company. However, he has assiduously gathered that it is a related party by going through annual reports of past years and searching online database on MCA portal.</p> <p>The described situation most appropriately denotes_____?</p> <p>(a) Objectivity (b) Professional knowledge (c) Independence (d) Professional skepticism</p> <p style="text-align: right;">[RTP-May 24]</p>

Answer Key to MCQ Questions

Q. No.	Answer
1	(c) Internal Control questionnaire
2	(d) (i), (ii),(iii),(iv)and (v)
3	(b) Tests of transactions
4	(a) Direct data changes (backend changes).
5	(d) Gathering evidence about valuation of trade receivables of the company
6	(d) Inspection
7	(c) rights and obligations
8	(b) Verification of cost of raw material consumed
9	(c) Occurrence
10	(d) It can directly help auditor in expanding client base.
11	(d) Structural engineer’s report on strength of building
12	(d) Shortages of important supplies
13	(c) Audit strategy
14	(c) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be both material and pervasive.
15	(b) Each audit report and each certificate
16	(c) PST Industries Limited

17	(d)	Any fraud by the company or on the company noticed or reported during the year
18	(a)	Financial statements of a bank are to be prepared in accordance with Third Schedule to Banking Regulation Act, 1949.
19	(d)	Peer group threats
20	(b)	Self-interest threat
21	(d)	Professional skepticism



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PART IV - INTEGRATED CASE SCENARIO

Chapter 1 – Nature, Objective and Scope of Audit

Integrated Case Scenario - 1

Sookrit, a CA student, has decided to participate in “Mega Conference of CA Students” being organized by Student Skills Enrichment Board, (Board of Studies-Operations), ICAI to be held in a city in South India. He has decided to try his luck for presenting a paper in one of the technical sessions of the conference on the topic of “Nature, Objective and Scope of Audit”. He has to first submit for approval a soft copy of the paper to the competent authority.

While preparing a draft for the presentation, he has included some paragraphs on the topic. Para A requires filling of certain gaps to explain nature of auditing to prospective audience at the conference. Para B and C have certain misleading and false statements which need corrections. Para D needs certain elaborations.

Para A

An audit of financial statements provides _____ assurance to the users of financial statements. It is a _____ level of assurance but it is not _____ assurance. The auditor has to see effect of misstatement(s) _____. Misstatements in financial statements can arise due to frauds or _____ or both.

Para B

Audit of financial statements should be organized adequately to cover all aspects of the entity relevant to the financial statements being audited. The auditor makes a judgment of reliability and sufficiency of financial information by making a study and assessment of accounting systems and internal controls. He also carries out appropriate tests and procedures. Due to professional training and knowledge acquired by auditor, he can authenticate genuineness of documents. However, he is not expected to perform duties which fall outside his domain of competence. Auditor is not an official investigator.

Para C

The process of audit suffers from certain inbuilt limitations. Inherent limitations of audit may arise due to nature of financial reporting, nature of audit procedures and need to strike a balance between reliability of information and cost of obtaining it. The information being relied upon by the auditor cannot lose its reliability due to historical nature of financial information presented in financial statements. However, future events may affect an entity adversely.

Para D

The chief utility of audit lies in reliable financial statements on the basis of which the state of affairs may be easy to understand. Its basic nature lies in providing assurance i.e., confidence to users of financial statements. Apart from this obvious utility, there are other advantages of an audit. Some or all of those are of considerable value even to those enterprises and organizations where audit is not compulsory.

On the basis of the abovementioned facts, you are required to choose the most appropriate answer for the following MCQs: [MTP-Sep. 23]

Q.1	<p>Identify appropriate words to be used in blanks to make the sentences meaningful and relevant in context of theme of the topic.</p> <p>(a) absolute, high, complete, individually, uncertainties</p> <p>(b) reasonable, high, complete, in totality, errors</p> <p>(c) reasonable, moderate, low, in totality, errors</p> <p>(d) moderate, low, complete, individually, judgments</p>
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Q.2	After reading Para B, which of following statements is false as regards scope of an audit of financial statements is concerned?
	<p>(a) Audit of financial statements should be organized adequately to cover all aspects of the entity relevant to the financial statements being audited.</p> <p>(b) The auditor makes a judgment of reliability and sufficiency of financial information by making a study and assessment of accounting systems and internal controls.</p> <p>(c) Due to professional training and knowledge acquired by auditor, he can authenticate genuineness of documents.</p> <p>(d) Auditor is not an official investigator.</p>
Q.3	After reading Para C, which statement needs to be corrected in draft regarding inherent limitations of audit?
	<p>(a) Inherent limitations of audit may arise due to nature of financial reporting, nature of audit procedures and need to strike a balance between reliability of information and cost of obtaining it.</p> <p>(b) The information being relied upon by the auditor cannot lose its reliability due to historical nature of financial information presented in financial statements.</p> <p>(c) Future events may affect an entity adversely.</p> <p>(d) The process of audit suffers from certain inbuilt limitations.</p>
Q.4	Para D states that an audit provides advantages of considerable value to enterprises. Which of following is not one of advantages of an audit of financial statements of a listed company?
	<p>(a) It acts as a moral check on employees.</p> <p>(b) It acts as an appraisal function.</p> <p>(c) Its chief advantage lies in safeguarding financial interest of management.</p> <p>(d) It is useful for settling trade disputes for higher wages or bonus.</p>
Q.5	Para D states that audit can be of considerable value even to those enterprises where it is not compulsory. In context of companies in India, which of following statements is correct in relation to Companies Act, 2013?
	<p>(a) OPC and small companies are exempted from audit.</p> <p>(b) OPC, small companies and section 8 companies are exempted from audit.</p> <p>(c) For all companies in India, except Section 8 companies, audit is legally obligatory.</p> <p>(d) For all companies in India, audit is legally obligatory.</p>

Answer - Integrated Case Study 1

Q. No.	Answer	
1	(b)	reasonable, high, complete, in totality, errors
2	(c)	Due to professional training and knowledge acquired by auditor, he can authenticate genuineness of documents.
3	(b)	The information being relied upon by the auditor cannot lose its reliability due to historical nature of financial information presented in financial statements.
4	(c)	Its chief advantage lies in safeguarding financial interest of management.
5	(d)	For all companies in India, audit is legally obligatory.

Chapter 3 – Risk Assessment and Internal Control

Integrated Case Scenario – 2

CA Sanjoy is conducting audit of PETA Education Solutions Private Limited for the first time. The company is engaged in providing solutions to students appearing for competitive exams under engineering and medical streams. Company's business is operated from physical centres spread in many states of the country. However, of late, number of aspirants availing company's services are shrinking due to emergence of new competitors and inability of company to switch to new technologies available in market to render its services.

The company had taken bank loans in past years for expansion of its physical centres. However, due to reduction in strength of aspirants opting for services provided by the company, management is always looking for means to meet its financial commitments on time. During the course of audit, CA Sanjoy wants to be sure about revenue and profit assertions reflected in financial statements of the company. Therefore, he is planning to test company's system for booking revenue in its books of accounts.

He notices that during the year under consideration, many experienced teaching faculties have left due to late payment of their contractual payments by the company. These have been replaced by inexperienced faculties having lower contractual costs but leading to poor satisfaction outcomes among aspirants. Besides, employee turnover of regular administrative staff also remains high. The company has not organized any training programmes either for its faculties or administrative staff for considerable period of time.

He has, in his wisdom, decided to increase the area of substantive checking in the company. He does not want to suffer from probable adverse publicity or loss of his professional goodwill.

On the basis of the abovementioned facts, you are required to answer the following MCQs: [MTP-Oct. 23]

Q.1	<p>After studying description of the company and its nature of operations, which of following statements is most appropriate?</p> <p>(a) Inherent risk for revenue and profit assertions is likely to be lower. (b) Inherent risk for revenue and profit assertions is likely to be higher. (c) Inherent risk for revenue and profit assertions cannot be assessed from given situation. (d) There does not exist inherent risk for revenue and profit assertions in described situation.</p>
Q.2	<p>The case scenario describes a situation of leaving of experienced faculties, high employee turnover and absence of training programmes for staff of the company. Such indicators are an example of _____?</p> <p>(a) Unsatisfactory risk assessment process used by the company (b) Unsatisfactory control environment of the company (c) Unsatisfactory performance reviews carried out by the company (d) Unsatisfactory system of segregation of duties in the company</p>
Q.3	<p>The auditor is planning to test company's system for booking revenue in its books of accounts. Identify the correct statement in this regard: -</p> <p>(a) He is likely to place greater reliance on controls relating to booking of revenue. (b) He is likely to place lower reliance on controls relating to booking of revenue. (c) Reliance placed by him on controls relating to booking of revenue would be unaffected due to reduction in contractual costs by company. (d) Reliance placed by him on controls relating to booking of revenue would be unaffected due to shrinking number of aspirants.</p>

Q.4	The auditor has increased area of “substantive checking” in the company. It is due to the reason that _____
	<p>(a) he wants to lower detection risk</p> <p>(b) he wants to lower control risk</p> <p>(c) he wants to raise sample risk</p> <p>(d) he wants to lower inherent risk</p>
Q.5	The auditor does not want to suffer from probable adverse publicity or loss of professional goodwill. Such a situation is indicative of _____?
	<p>(a) audit risk</p> <p>(b) auditor’s business risk</p> <p>(c) auditor’s detection risk</p> <p>(d) non-sampling risk</p>

Answer – Integrated Case Study 2

Q. No.	Answer	
1	(b)	Inherent risk for revenue and profit assertions is likely to be higher.
2	(b)	Unsatisfactory control environment of the company
3	(b)	He is likely to place lower reliance on controls relating to booking of revenue.
4	(a)	he wants to lower detection risk
5	(b)	auditor’s business risk

Integrated Case Study - 3

Roop & Co. are the auditors of Onda group of Hotels. This is the first time the firm is auditing an industry in food and beverage and it is day one of the audit. The engagement partner along with his team wants to make a thorough understanding of the entity and its environment in order to identify and assess the risks of material misstatements, whether due to fraud or error. The following are some of the points identified by them on Day 1.

- 1. The hotel has two banquet halls. The documentation available for verification of banquet hall revenue is only the invoice raised by the hotel and some mail conversations on customer enquiry and finalization of price. On audit trial, it is found that finance approval of the transaction is only after invoice is sent to them for accounting at final settlement. Advance paid by the clients are not vetted through finance team. The auditor suspects a weakness in this system.**
- 2. The auditor also finds a control deficiency in the process of procurement of stores. A goods receipt note is not prepared at the time of receipt of goods. On enquiry with management, the auditor finds that there exists a system control where in goods receipt note is automatically prepared and approved in the system once the quantity and price of goods is entered against specific vendor. This entry is on real-time basis and system does not allow back dated entries.**
- 3. The auditor enquires of the management as to what is risk assessment process followed by the entity for prevention and detection of risk of material misstatement due to fraud and error. The auditor finds there is no documented risk assessment process.**

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

[BOS Knowledge Portal]

Q.1	<p>What kind of a risk is portrayed in the booking of revenue with respect to Banquet halls?</p> <p>(a) Inherent risk in the class of transaction (b) Control risk in the class of transaction (c) Detection risk in the audit procedures (d) Audit risk in the opinion on the financial statements.</p>
Q.2	<p>Which among the following statement is incorrect in the context of Audit Risk?</p> <p>(a) The more extensive the audit procedures performed, the lower is the detection risk (b) Greater the risk of material misstatement the auditor believes exist, less is the detection risk that can be accepted and accordingly more persuasive evidence is required by the auditor. (c) Audit risk also includes the risk that the auditor may express an opinion that the financial statements are materially misstated when they are actually not. (d) Risk of material misstatement at the assertion level is of two kinds – control risk and inherent risk.</p>
Q.3	<p>In the case of procurement of stores, the auditor has tested more than one control for the same assertion. In that given case, what should be his reliance on the control?</p> <p>(a) Since compensating controls are identified, if tested and evaluated to be effective, the auditor can rely on the control. (b) Even though compensating controls are there, since one control is ineffective, the auditor should not rely on control for this assertion and should perform extensive procedures. (c) Documentation in electronic medium cannot be accepted, hence, he cannot rely only on system control. (d) Even though compensating controls are there, since one control is ineffective, the auditor should not rely on control for this assertion as well as associated assertions.</p>
Q.4	<p>In the context of SA 315, which among the following is not a risk assessment procedure?</p> <p>(a) Inquiries of management, of appropriate individuals within internal audit function and of others within the entity (b) Analytical Procedures (c) Observation and Inspection (d) External Confirmation</p>
Q.5	<p>What should be the course of action of the auditor for the entity not having a documented risk assessment process?</p> <p>(a) The auditor should obtain management written representations on how risks are identified (b) The auditor shall discuss with management on how risks are identified, addressed and determine whether the absence is appropriate in the circumstances or whether it represents a significant deficiency in internal control. (c) The auditor should advise the management to document the same immediately and accordingly opine on the same in his audit report too. (d) The auditor shall discuss with management on how risks are identified by system and place reliance on the same as documentation in this context is immaterial.</p>

Answer – Integrated Case Study 3

Q. No.	Answer	
1	(b)	Control risk in the class of transaction
2	(c)	Audit risk also includes the risk that the auditor may express an opinion that the financial statements are materially misstated when they are actually not.
3	(a)	Since compensating controls are identified, if tested and evaluated to be effective, the auditor can rely on the control.
4	(d)	External Confirmation
5	(b)	The auditor shall discuss with management on how risks are identified, addressed and determine whether the absence is appropriate in the circumstances or whether it represents a significant deficiency in internal control.

Chapter 4 – Audit Evidence

Integrated Case Study - 4

CA X has accepted offer of conducting statutory audit of financial statements of DOS Solutions Private Limited. Keeping in mind requirements of Standards on Auditing including those relating to SA 300, he plans audit so that it is conducted in an effective manner. He knows that because of inherent limitations of an audit, there is audit risk in audit of financial statements even though audit is properly planned and performed in accordance with Standards on Auditing.

Considering nature of operations of the company, he has decided to use audit sampling in performing audit procedures. The various areas of his testing include testing controls over revenues, expenditures, assets and liabilities of the company. Besides, he has decided to perform tests of details in respect of all these areas of financial statements.

While verifying tests of controls over purchase orders placed by the company based on selected audit samples, he has erroneously concluded that Standard operating procedures (SOP) for placing purchase orders are not being followed strictly and controls are less effective than they actually are. Further, while testing controls over wage payments, he has tested 20 sample wage sheets of different sections of company and finds that one wage sheet has not been signed by authorized officer of the company. The rate of deviation was earlier set by him at 3%.

During the course of designing procedures for selecting samples for verification of trade receivables, he has decided to divide trade receivable balances into groups viz. balances in excess of ₹ 10 lakh, balances in range of ₹ 7,50,001 to ₹ 10,00,000, balances in range of ₹ 5,00,001 to ₹ 7,50,000, balances in range of ₹ 2,50,001 to ₹ 5,00,000 and balances of ₹ 2,50,000 and below. He has planned to pick up different percentage of items from each of above groups. Random sample is chosen from each group using random number tables.

Some of the trade payables of the company were outstanding since long. He has decided to merely verify arithmetical accuracy of ageing schedule and its reconciliation with books of accounts.

Therefore, nature of audit procedures, nature of financial reporting itself and need for audit to be conducted within a reasonable period of time and at a reasonable period of cost all lead to inherent limitations of audit.

On the basis of the abovementioned facts, you are required to answer the following MCQs: [RTP-Nov. 23]

1	<p>The auditor has erroneously concluded that Standard operating procedures (SOP) for placing purchase order are not being followed strictly and controls are less effective than they actually are. Which of the following statements is likely to be true in this regard?</p> <p>(a) It is a sampling risk and might lead to auditor expressing inappropriate audit opinion. (b) It is a sampling risk and affects audit effectiveness. (c) It is a sampling risk and affects audit efficiency. (d) It is a control risk and affects audit effectiveness.</p>
2	<p>The auditor has tested 20 sample wage sheets in different sections of the company and finds that one wage sheet has not been signed by authorized officer of the company. It represents_____?</p> <p>(a) Tolerable misstatement (b) Misstatement (c) Tolerable rate of deviation (d) Actual rate of deviation</p>
3	<p>Which method of selecting samples for verification of trade receivables has been planned by auditor?</p> <p>(a) Simple random sampling (b) Systematic sampling (c) Block sampling (d) Stratified sampling</p>
4	<p>The auditor has decided to merely verify arithmetical accuracy and reconciliation of ageing schedule relating to trade payables. The use of above audit procedure can lead to _____?</p> <p>(a) Sampling risk (b) Non-sampling risk (c) Inherent risk (d) Control risk</p>
5	<p>Keeping in view inherent limitations of audit of financial statements, which of following statements is likely to be most appropriate?</p> <p>(a) Due to inherent limitations of audit, auditor obtains conclusive audit evidence. (b) Due to inherent limitations of audit, auditor can be satisfied with less than persuasive evidence. (c) Due to inherent limitations of audit, subsequent discovery of material misstatement in financial statements after audit, which was conducted in accordance with SAs, does not indicate a failure of audit. (d) Due to inherent limitations of audit, auditor can skip a difficult, time-consuming and costly procedure.</p>

Answer - Integrated Case Study 4		
Q. No.	Answer	
1	(c)	It is a sampling risk and affects audit efficiency.
2	(d)	Actual rate of deviation
3	(d)	Stratified sampling
4	(b)	Non-sampling risk
5	(c)	Due to inherent limitations of audit, subsequent discovery of material misstatement in financial statements after audit, which was conducted in accordance with SAs, does not indicate a failure of audit.

Integrated Case Study - 5

M/s JJ & associates having office in Chennai are statutory auditors under Companies Act, 2013 of a company viz. Sweet Aroma Private Limited engaged in business of obtaining and manufacturing rice from paddy catering to both domestic as well as international market mainly in Gulf nations. The company has a huge plant capacity for rice extraction in one of the states in Northern India. Needless to state that inventories are in huge quantity in such type of business consisting of raw material, work in progress and finished goods. The auditors want to obtain sufficient appropriate audit evidence regarding inventories.

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

[BOS Knowledge Portal]

1	<p>Which of the following is most likely correct in relation to obtaining of sufficient appropriate audit evidence regarding existence and condition of inventory?</p> <p>(a) It is mandatory for the auditor to attend physical inventory counting on the date of financial statements in all circumstances.</p> <p>(b) Physical inventory counting may be attended by auditor on the date of financial statement or at a date other than date of financial statements in his discretion mandatorily in all circumstances.</p> <p>(c) The attendance of auditors at physical inventory counting is impracticable due to time and costs involved because of auditor's office location vis-à-vis company's plant location. Hence, attendance at physical inventory counting may be skipped and alternative audit procedures may be performed to obtain sufficient appropriate evidence.</p> <p>(d) The auditor shall attend at physical inventory counting unless impracticable. However, issue of time and costs involved because of auditor's office location vis-à-vis company's plant location is not a valid basis for skipping physical inventory counting</p>
2	<p>Below are given certain cluster of matters which are relevant in planning attendance of auditor at physical inventory counting. Which of the following clusters consists of a likely inappropriate combination?</p> <p>(a) Nature of inventory, timing of physical inventory counting and stages of completion of work in progress</p> <p>(b) Nature of inventory, timing of physical inventory counting and valuation method of inventory</p> <p>(c) Nature of inventory, timing of physical inventory counting, considerations regarding maintenance of a perpetual inventory system</p> <p>(d) Risks of material misstatements related to inventory, nature of internal control pertaining to inventory, considerations regarding maintenance of a perpetual inventory system</p>
3	<p>Which of the following is the most likely logical sequence of steps in relation to attendance at physical inventory counting by auditor?</p> <p>(a) Observance of performance of management's count procedures, inspection of inventory, performing test counts and evaluation of management's procedures for recording and controlling results of physical inventory counting</p> <p>(b) Observance of performance of management's count procedures, performing test counts, inspection of inventory and evaluation of management's procedures for recording and controlling results of physical inventory counting</p> <p>(c) Performing test counts, inspection of inventory, Observance of performance of management's count procedures and evaluation of management's procedures for recording and controlling results of physical inventory counting</p>

	(d) Evaluation of management's procedures for recording and controlling results of physical inventory counting, Observance of performance of management's count procedures, inspection of inventory and performing test counts
4	<p>During attendance at physical inventory counting, the auditor inspects inventory. Following outcomes stated as I, II & III are given below of this inspection procedure: -</p> <p>Outcome I --- Existence of inventory Outcome II ---- Ownership of inventory Outcome III ----- Condition of inventory</p> <p>Which of following statements is most likely true?</p> <p>(a) Outcomes I, II and III are all necessarily established after inspection. (b) Only Outcomes I and III are established after inspection and Outcome II is never established. ☒ (c) Outcomes I and III are established after inspection. However, outcome II may not be necessarily established. (d) Outcome II and III are established after inspection. However, outcome I may not be necessarily established.</p>
5	<p>It was observed by auditors that, out of total rice physically counted on 31 March, 2022 about 67 quintals of rice belonged to M/s PQR, a proprietary concern which had sent paddy to this company's plant for extraction of rice. What would be treatment of this item in financial statements of company?</p> <p>(a) The value of 67 quintals rice would be reflected in company's financial statements as per method of valuation adopted by the company. (b) The value of 67 quintals rice would be reflected in company's financial statements as per method of valuation adopted by the proprietary concern. (c) The value of 67 quintals rice would not be reflected in company's financial statements. (d) The value of 67 quintals rice would be reflected in proprietary concern's financial statements as per method of valuation adopted by the company.</p>

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Answer – Integrated Case Study 5	
Q. No.	Answer
1	(d) The auditor shall attend at physical inventory counting unless impracticable. However, issue of time and costs involved because of auditor's office location vis-à-vis company's plant location is not a valid basis for skipping physical inventory counting
2	(b) Nature of inventory, timing of physical inventory counting and valuation method of inventory
3	(d) Evaluation of management's procedures for recording and controlling results of physical inventory counting, Observance of performance of management's count procedures, inspection of inventory and performing test counts
4	(c) Outcomes I and III are established after inspection. However, outcome II may not be necessarily established.
5	(c) The value of 67 quintals rice would not be reflected in company's financial statements.

Chapter 5 – Audit of Items of Financial Statements

Integrated Case Study - 6

You are a partner in ABC & Company, a firm of Chartered Accountants based in New Delhi. ABC & Company have been appointed as the statutory auditors of Onetime Limited, a public company which manufactures and sells wall and table clocks and has many branches all over India. Onetime Limited has been exporting the clocks since past two years. However, the domestic sales have contributed towards major source of revenue for the Company.

One of the team members, CA B noticed that one of the suppliers of Onetime Limited, Mr. AM had sent some raw material to the Company for storage in their warehouse in March 2024. Due to renovation going on at his warehouse, his stock could be damaged and so he had requested Onetime Limited to keep the same in their warehouse. Onetime Limited contended that since the raw material was anyway billed to the Company the next month, so the same had been included in the valuation of stock, since physically the stock was present in the warehouse of Onetime Limited as on 31.03.2024.

While verifying the debtors, team member C noticed that there were a few trade receivables pertaining to export sales mainly to England. Mr. C verified the same with respect to the invoices issued and other supporting documents. The amount booked as on 31.03.2024 was based on the exchange rate as on the date of the invoice.

Mr. T, another team member verified the PPE of the Company. Onetime Limited had purchased few cars for its directors during the year of audit. The same were appearing in the PPE schedule of the Company. Mr. T verified the same with respect to the invoices as well as physically verified the assets in the Company's premises. Since the cars were for the official use of the Directors, they were purchased in the name of the Directors of the Company. Mr. T verified the amount with the Invoice and checked the registration and insurance documents. Besides, all items appearing in the PPE schedule were verified and he was satisfied that all PPE items that should have been recorded have, in fact, been recorded.

One of the articled clerks was assigned the work of verification of "Provisions" appearing in the Balance sheet. He wanted to understand from you the circumstances in which a provision is recognised in the books of accounts. You explained him the situations in which an entity recognises Provisions in its books.

Onetime Limited has invested in the shares of other companies. One of the Companies has declared dividend on its shares. Onetime Limited has not recognised the same in the profit & loss account. Team Member R has asked you to look into the matter since she is unable to understand the reasons for the same.

On the basis of the abovementioned facts, you are required to choose the most appropriate answer for the following MCQs: [MTP-Oct. 23]

1	<p>Is the raw material lying in the warehouse of Onetime Limited accounted for correctly in its books of account?</p> <p>(a) No, since the same belongs to Mr. AM and should appear in his books.</p> <p>(b) Yes, since the same is in possession of Onetime Limited and was billed to it the following month.</p> <p>(c) It should be shown in the books of both Onetime Limited and Mr. AM.</p> <p>(d) It should not appear in the books of Onetime Limited or Mr. AM and the raw material should be disclosed as a note in the final accounts of both the entities.</p>
2	<p>Which exchange rate is considered for accounting of foreign debtors at the year end?</p> <p>(a) Exchange Rate on the date of the invoice.</p> <p>(b) Exchange Rate on the last day of the financial year.</p>

	(c) Exchange Rate on the date of shipment of the products to the customer. (d) Exchange Rate on the date of delivery of the products to the customer.
3	Which of the following management assertions is not satisfied with respect to Cars included in the PPE items by the company: (a) Existence (b) Valuation (c) Completeness (d) Rights and Obligations
4	Which of the following condition is not required to be met for recognizing a provision? (a) When a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity. (b) When an entity has a present obligation (legal or constructive) as a result of a past event. (c) A reliable estimate can be made of the amount of the obligation. (d) When it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation.
5	Which of the following conditions is not necessary for recognising dividends in the statement of profit and loss of Onetime Ltd.: (a) the entity's right to receive payment of the dividend is established. (b) it is probable that the economic benefits associated with the dividend will flow to the entity. (c) the amount of the dividend can be measured reliably. (d) payment of income tax on dividends received

Answer – Integrated Case Study 6

Q. No.	Answer	
1	(a)	No, since the same belongs to Mr. AM and should appear in his books.
2	(b)	Exchange Rate on the last day of the financial year.
3	(d)	Rights and Obligations
4	(a)	When a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.
5	(d)	payment of income tax on dividends received

Integrated Case Study - 7

Kartik, a CA student undergoing his articled training, is part of an engagement team conducting statutory audit of MSE Auto Private Limited, a company engaged in manufacturing of automobile spare parts. The company has its manufacturing facilities located in Pimpri- Chinchwad industrial belt near Pune. It is a profit making company and one of the most sought after by banks in the area due to its good track record. The following is extract of financial information taken from its pre-audit financial statements for year 2023-24. Figures have been rounded off in ₹ 000's.

Particulars	Year 2023-24	Year 2022-23
Share Capitals	2500.00	2500.00
Long term borrowings	0.00	15000.00
Short term borrowings	55000.00	15000.00
Inventories	35000.00	27000.00
Trade receivables	60000.00	25000.00
Revenue from Operations	300000.00	100000.00
Profit before tax	60000.00	18000.00

While going through schedule of long-term borrowings and books of accounts, he finds that reduction of long term borrowings of the company is on account of full payment of a term loan in month of April 2023 taken from a bank in past. However, he finds that charge in respect of above term loan in favour of bank is still subsisting on MCA portal beyond statutory period due to non-registration of charge satisfaction.

He had read about assertions pertaining to balance sheet and income statement. However, he was not sure about nomenclatures assigned to assertions pertaining to balance sheet and income statement.

The team had also attended physical inventory count of the company as at year end in accordance with SA 501.

Besides, company's trade receivables have increased from ₹ 25000 in year 2022-23 to ₹ 60000 in year 2023-24 (both figs in Rs. 000s). His understanding is that increase in company's trade receivables as compared to last year signifies longer time taken by company's customers to make their payments.

Considering substantial rise in revenue from operations of the company in the year under audit, team wants to ensure that revenues of company are not overstated.

On the basis of the abovementioned facts, you are required to choose the most appropriate answer for the following MCQs: [RTP-Nov. 23]

1	<p>Keeping in view description regarding full payment of term loan in April 23 taken from a bank in past and non-registration of satisfaction of charge, which of following statements is correct?</p> <p>(a) The above fact may be disclosed by the company's management in its financial statements at its discretion along with reasons as such disclosure would bring transparency.</p> <p>(b) The above fact along with reasons is required to be disclosed by the company in its financial statements in accordance with requirements of Standards on Auditing.</p> <p>(c) The above fact along with reasons is required to be disclosed by the company in its financial statements in accordance with requirements of Schedule III of Companies Act, 2013.</p> <p>(d) The above fact is not required to be disclosed as term loan has already been repaid in full and there are no outstanding long term borrowings.</p>
2	<p>The company's short-term borrowings have increased during the year 2023-24 as compared to last year. One of following assertions is not relevant to verification of short-term borrowings. Which odd one you would suggest to Kartik in this regard?</p> <p>(a) Existence</p> <p>(b) Occurrence</p> <p>(c) Completeness</p> <p>(d) Valuation</p>

3	<p>As regards team's attendance at physical inventory count process of company's inventories in accordance with SA 501 is concerned, which of following is not a relevant audit procedure?</p> <p>(a) Inspection of inventories (b) Checking appropriateness of method employed for valuation of inventories (c) Evaluating management's instructions for recording results of physical inventory count (d) Performing test counts</p>
4	<p>The company's trade receivables have increased during year 2023-24 as compared to last year. Which of following statements is most appropriate regarding understanding of Kartik on this issue?</p> <p>(a) The view of Kartik is correct and it has led to increased audit risk pertaining to valuation of trade receivables. Therefore, team needs to go through trade receivables ageing schedule to confirm it. (b) The view of Kartik is incorrect. (c) The view of Kartik is correct and it has led to increased audit risk pertaining to valuation of trade receivables. Therefore, team needs to perform direct confirmation procedures to confirm it. (d) The view of Kartik is correct and it has led to increased audit risk pertaining to valuation of trade receivables. Therefore, team needs to perform cut-off procedures to confirm it.</p>
5	<p>The team wants to ensure that revenues of company are not overstated. Which of following is not likely to be a relevant audit procedure in this regard?</p> <p>(a) Obtaining confirmations from customers (b) Reviewing GST returns and their reconciliation with revenue stated in statement of profit & loss (c) Reviewing credit notes issued by company post year end (d) Reviewing debit notes issued by company post year end</p>

Answer – Integrated Case Study 7

Q. No.	Answer
1	(c) The above fact along with reasons is required to be disclosed by company in its financial statements in accordance with requirements of Schedule III of Companies Act, 2013.
2	(b) Occurrence
3	(b) Checking appropriateness of method employed for valuation of inventories
4	(b) The view of Kartik is incorrect.
5	(d) Reviewing debit notes issued by company post year end

Integrated Case Study - 8

A partnership firm of Chartered Accountants, YZ and Associates were appointed as auditors of company UV Private Limited. The financial year for which YZ and Associates were to audit books of accounts of UV Private Limited began on 1 April, 2023 and ended on 31 March, 2024.

YZ and Associates consisted of four partners namely Mr. Y, Mr. Z, Mr. G and Mr. H. While auditing books of accounts of UV Private Limited for the period ending on 31 March, 2024, one of the assistant of YZ and Associates namely Mr. A took up the expenditure part for the purpose of audit.

The management of UV Private Limited had adopted various accounting policies and principles related to expenses which Mr. A was unable to understand. Some of the issues which Mr. A did not understand are mentioned as follows:

- (1) Machinery Insurance expense paid for one year ending on 31.05.2024 has been included in the Insurance Expense for the financial year 2023-24.
- (2) Personal Rent Expense of the son of one of the directors, Mr. T of UV Private Limited has been shown as Rent Expense of business of UV Private Limited.
- (3) Repair and Maintenance Expenses for the months of February 2024 and March 2024 were still outstanding and were not shown in Balance Sheet of UV Private Limited.
- (4) Repair and Maintenance Expenses for the financial year 1 April, 2023 to 31 March, 2024 were very high as compared to financial year 1 April, 2022 to 31 March, 2023. Mr. A asked the appropriate authority about the reasons for such huge differences in amounts of two financial years.

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

[BOS Knowledge Portal]

1	<p>As per point number (1) mentioned in the above case, the Machinery Insurance Expense paid for the months of April 2024 and May, 2024 must be shown in the balance sheet of UV Private Limited as on 31st March, 2024 as:</p> <ol style="list-style-type: none"> (a) Outstanding Insurance Expense (b) Prepaid Insurance Expense (c) Insurance Expense (d) Insurance Expense Payable
2	<p>As per point number (2) mentioned above in the case, the Personal Rent Expense of the son of one of the directors Mr. T was added to Rent Expense of business of UV Private Limited. The amount of personal rent expense of the son of the director Mr. T must:</p> <ol style="list-style-type: none"> (a) be subtracted from Rent Expense of business of UV Private Limited (b) remain added to Rent Expense of business of UV Private Limited (c) be added to Rent Expense of business of UV Private Limited (d) Subtracted twice from Rent Expense of business of UV Private Limited
3	<p>As per point number (3) mentioned above in the case, the Repair and Maintenance Expenses outstanding for the months of February 2024 and March 2024 must be shown in the balance sheet of UV Private Limited as on 31 March, 2024 as:</p> <ol style="list-style-type: none"> (a) Prepaid Repair and Maintenance Expenses (b) Repair and Maintenance Expenses (c) Repair and Maintenance Expenses paid in advance (d) Repair and Maintenance Expenses Payable
4	<p>As per point number (4) mentioned in the case above, Mr. A asked the appropriate authority for reasons of huge differences in the amount of two financial years of repair and maintenance expenses. By appropriate authority Mr. A was referring to:</p> <ol style="list-style-type: none"> (a) All employees of UV Private Limited (b) Management of UV Private Limited (c) Members of UV Private Limited (d) Any one director of UV Private Limited

Answer – Integrated Case Study 8

Q. No.	Answer	
1	(b)	Prepaid Insurance Expense
2	(a)	be subtracted from Rent Expense of business of UV Private Limited
3	(d)	Repair and Maintenance Expenses Payable
4	(b)	Management of UV Private Limited

Chapter 8 – Audit Report

Integrated Case Study - 9

Following is the extract of information taken from financial statements of AAF Private Limited for the financial year 2023-24:

(All Figs in tables are in Rs. 000s)		
Particulars	31.03.24	31.03.23
Paid up share capital	75000	75000
Long term borrowings	24500	30000
Short term borrowings	55000	50000
Other current liabilities	350	550
Property, Plant and Equipment	48500	56000
Depreciation	7500	9500
Profit/(Loss) after tax	(5000)	(6000)

Assume that there are no taxation adjustments.

The schedule of short-term borrowings reflects as under: -

Particulars	31.03.24	31.03.23
Loans repayable on demand from MMT Bank (secured) (Cash credit limit against hypothecation of stocks guaranteed by all directors)	55000	50000

It has been further noticed during the course of audit that quarterly statements filed by company with its bank for availing cash credit facilities of ₹ 5.50 crores during the year vis-à-vis books of accounts reflect following details: -

Period Ending	Value of stocks as per quarterly statements	Value of stocks per Books of accounts
30.6.23	80000	70000
30.9.23	70000	65000
31.12.23	85000	70000
31.3.24	80000	80000

It has also been noticed that long term borrowings consist of a term loan from MMT Bank. Term loan outstanding has reduced in comparison to last year. However, during the year 2023-24, company has not paid one instalment of ₹ 5 lakhs on time which is overdue for 65 days as on balance sheet date. The credit facilities have been classified as Standard assets by the Bank in accordance with prudential guidelines of RBI. Other current liabilities as on 31.3.24 include TDS payable of ₹ 1.00 lac (out of which ₹ 0.60 lac for month of Feb 24 was due for deposit on 7.3.24). The balance ₹ 0.40 lac pertains to month of March 2024.

You are part of engagement team conducting audit of AAF Private Limited. As part of assigned work, you are also responsible for providing information/input to your senior for reporting under CARO, 2020 for financial year 2023-24.

On the basis of the abovementioned facts, you are required to answer the following MCQs: [MTP-Sep. 23]

1	<p>Considering description about short-term borrowings in the case study, which of following statements is in accordance with CARO, 2020?</p> <p>(a) The statutory auditor is required to provide details of differences in quarterly statements filed with bankers with its books of accounts.</p> <p>(b) The statutory auditor is required to provide details of differences only in respect of those quarterly statements where there is discrepancy of more than 10% as compared to its books of accounts.</p> <p>(c) The statutory auditor is not required to provide details of differences as reporting requirement is triggered only when working capital limits have been sanctioned in excess of ` 10 crore during any point of time of the year.</p> <p>(d) The statutory auditor is not required to provide details of differences, as at end of year, books of accounts are in agreement with quarterly statement filed.</p>
2	<p>The company has not paid one instalment of ₹ 5 lakhs on time which is overdue for more than 65 days as on balance sheet date. Identify likely correct statement in this regard in relation to reporting under CARO, 2020: -</p> <p>(a) The account has not become NPA as on 31.3.24. Hence, there is no reporting requirement.</p> <p>(b) The reporting requirement is necessary only when company is declared a wilful defaulter by Bank. In the given situation, there is no reporting requirement.</p> <p>(c) Amount of default along with period of default is required to be reported.</p> <p>(d) The reporting requirement is necessary only when company has diverted amount of term loan for some other purpose. In the given situation, there is no reporting requirement.</p>
3	<p>As regards TDS payable of ₹ 1.00 lakh included in other current liabilities, what input would be provided by you to your senior for reporting under CARO, 2020?</p> <p>(a) TDS payable of ₹ 1.00 lac in financial statements shall not be reported as it does not meet necessary reporting requirements.</p> <p>(b) It is in nature of undisputed statutory dues. Hence, outstanding amount of ₹ 1.00 lac not deposited is to be reported.</p> <p>(c) It is in nature of undisputed statutory dues. However, only outstanding amount of ₹ 0.60 lac not deposited is to be reported.</p> <p>(d) TDS payable of ₹ 1.00 lac does not fall under meaning of “undisputed statutory dues”. Hence there is no question of reporting.</p>
4	<p>Which of following is not a reporting duty of statutory auditor regarding Property, Plant and Equipment reflected in company’s financial statements under CARO, 2020?</p>

	<p>(a) whether the company is maintaining proper records showing full particulars, including quantitative details and situation of Property, Plant and Equipment</p> <p>(b) whether Property, Plant and Equipment have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account</p> <p>(c) whether Property, Plant and Equipment have been physically verified by the auditor during the year; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account</p> <p>(d) whether title deeds of all immovable properties (other than properties where company is lessee and lease agreements are duly executed in favour of the lessee) disclosed in the financial statements are held in the name of the company</p>
5	<p>The company has reflected losses in its financial statements for year 2023-24 and 2022-23. Which of following statements is likely to be correct in this regard while reporting under CARO, 2020 for year 2023-24?</p> <p>(a) Losses reflected in statement of profit and loss for year 2023-24 and 2022-23 are required to be reported under CARO, 2020.</p> <p>(b) Loss reflected in statement of profit and loss for year 2023-24 is alone required to be reported under CARO, 2020.</p> <p>(c) There is no requirement to report losses reflected in statement of profit and loss under CARO, 2020.</p> <p>(d) The company's losses reflected in statement of profit and loss in financial year 2023-24 and 2022-23 are less than prescribed percentage threshold limit of paid- up capital. Hence, these are not required to be reported.</p>

Answer – Integrated Case Study 9

Q. No.	Answer	
1	(a)	The statutory auditor is required to provide details of differences in quarterly statements filed with bankers with its books of accounts.
2	(c)	Amount of default along with period of default is required to be reported.
3	(a)	TDS payable of ₹ 1.00 lac in financial statements shall not be reported as it does not meet necessary reporting requirements.
4	(c)	whether Property, Plant and Equipment have been physically verified by the auditor during the year; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account
5	(c)	There is no requirement to report losses reflected in statement of profit and loss under CARO, 2020.

MISCELLANEOUS

Integrated Case Study - 10

Moon Group of companies is a retail chain involved in the selling of daily consumer needs directly to the customer. They are in the process of appointing an audit firm for the audit of their accounts for the financial year 2023-24. Moon Group is a South Indian based consumer store having a total of 16 outlets across 4 cities in South India.

Sumant & Co. is appointed as the principal auditor for the entire group. Companies Act, 2013 prescribes in detail the terms of this audit engagement. Further, there are many branch auditors appointed for the outlets in the other cities. The company also has an internal audit function conducted on quarterly basis by Ram & Co. Following are the observations during the course of the statutory audit:

- (a) One of the discounts offered by the store is in the form of payback cards where reward points are accumulated and the customer can redeem the same on subsequent purchase. The management and internal auditors are of the opinion that the points redeemed are to be treated as trade discount. The external auditors are doubtful on the matter.
- (b) One of the outlet in Chennai region is in the verge of getting closed and is only left with low value stock to be cleared before closure. During the year, the sales were only around ₹ 1,40,000/- and the auditor considers this component immaterial. All other outlets are performing well with good revenue share.
- (c) The gratuity valuation of the employees of the retail chain is done by an external valuer. The auditor, considering the quantum involved appoints an external auditor's expert for the verification of the actuarial calculation of gratuity.

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

[BOS Knowledge Portal]

1	<p>As per SA 210 – Agreeing the Terms of Audit Engagement, which of the following statement is correct?</p> <p>(a) Though law prescribes in sufficient detail the terms of the audit engagement, the auditor still needs to record them in a written agreement and also seek written agreement from management that it acknowledges and understands that it has responsibility for the preparation of financial statements.</p> <p>(b) Since law prescribes in sufficient detail the terms of the audit engagement, the auditor need not record them in a written agreement except for the fact that law or regulation applies and also seek written agreement from management that it acknowledges and understands that it has responsibility for the preparation of financial statements.</p> <p>(c) The auditor has to take an extract of the law prescribing the details of the terms of the audit engagement and obtain the counter signature of the management in it.</p> <p>(d) Though law prescribes in sufficient detail the terms of the audit engagement, the auditor still needs to record them in a written agreement, however it need not seek written agreement from management that it acknowledges and understands that it has responsibility for the preparation of financial statements.</p>
2	<p>With respect to the treatment of discount on redemption of points in payback card, what should be the action of the external auditor?</p> <p>(a) The auditor can place reliance and go by the opinion of the branch auditor and internal auditor as they have only done a thorough and detailed audit of the accounts</p>

	<p>(b) The auditor can place reliance on the management’s accounting policy as prima facie they are only responsible for preparation of financial statements.</p> <p>(c) The external auditor has sole responsibility for the audit opinion expressed and hence he should perform procedures to satisfy himself on the correct treatment and issue opinion accordingly.</p> <p>(d) The auditor can advise management on correct treatment but cannot qualify his opinion as branch auditor’s opinion has higher authority than external auditor’s opinion.</p>
3	<p>What is the main objective of the external auditor, when he uses the work of the internal audit function of Ram & Co.?</p> <p>(a) To determine as to which areas, what extent the work can be used and whether that work is adequate for the purposes of the audit.</p> <p>(b) To appropriately direct, supervise and review the work of the internal audit function</p> <p>(c) Review the internal audit report and audit the areas not covered by the internal audit function</p> <p>(d) Enquire from management on the special points that arose during internal audit and follow up on the course of action on those points.</p>
4	<p>The external auditor finds that the branch auditor of the outlet in the Chennai region, which is in the verge of closing down, is audited by an auditor who is not a member of the Institute of Chartered accountants of India. What should the external auditor do?</p> <p>(a) Since the professional competence of the auditor is in question, the external auditor should himself visit the premise and audit the accounts.</p> <p>(b) Since the financial statement of the component is immaterial, the provisions of SA 600 do not apply.</p> <p>(c) The auditor can rely on the financial statements of that component by obtaining written representation from management that the branch auditor is otherwise well qualified.</p> <p>(d) Since the professional competence of the auditor is in question, the external auditor should co-ordinate with the branch auditor and call for the books of accounts and other explanations.</p>
5	<p>Which of these is not a factor affecting the external auditor’s evaluation of the objectivity of the internal audit function?</p> <p>(a) Whether the organizational status of the internal audit function supports the ability of the function to be free from bias, conflict of interest or undue influence of others to override professional judgment.</p> <p>(b) Whether the internal audit function is free of any conflicting responsibilities.</p> <p>(c) Whether the internal auditors have adequate technical training and proficiency in auditing.</p> <p>(d) Whether those charged with governance oversee employment decisions related to internal audit function.</p>

Answer - Integrated Case Study 10

Q. No.	Answer	
1	(b)	Since law prescribes in sufficient detail the terms of the audit engagement, the auditor need not record them in a written agreement except for the fact that law or regulation applies and also seek written agreement from management that it acknowledges and understands that it has responsibility for the preparation of financial statements.

2	(c)	The external auditor has sole responsibility for the audit opinion expressed and hence he should perform procedures to satisfy himself on the correct treatment and issue opinion accordingly.
3	(a)	To determine as to which areas, what extent the work can be used and whether that work is adequate for the purposes of the audit.
4	(b)	Since the financial statement of the component is immaterial, the provisions of SA 600 do not apply.
5	(c)	Whether the internal auditors have adequate technical training and proficiency in auditing.



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