

CA-FINAL



AUDIT

Question Bank

For May 2024 & Onwards



CA Final

(For May 2024 Exam & Onwards)

AUDIT QUESTION BANK

CA Shubham Keswani



AUDIT QUESTION BANK

By CA Shubham Keswani

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8-9-10, Hans Bhawan Building, Wing-2,
IP Estate , New delhi 110002

Ph.: +91 9958000380, 9899632870

E- Mail : Contact@makemydelivery.com

Web : makemydelivery.com

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

1. MB & Associates is a partnership firm of Chartered Accountants which was established seven years back. The firm is getting new clients and has also, been offered new engagement services with existing clients. The firm is concerned about obtaining such information as it considers necessary in the circumstances before accepting an engagement with a new client and acceptance of a new engagement with an existing client. The firm is looking to work with only select clients to adhere to the Quality Control Standards. Guide MB & Associates about the matters to be considered with regard to the integrity of a client, as per the requirements of SQC 1.

(Nov-19 New + RTP May 19)

With regard to the integrity of a client, matters that the firm considers include, for example:

- The identity and business reputation of the client's principal owners, key management, related parties and those charged with its governance.
- The nature of the client's operations, including its business practices.
- Information concerning the attitude of the client's principal owners, key management and those charged with its governance towards such matters as aggressive interpretation of accounting standards and the internal control environment.
- Whether the client is aggressively concerned with maintaining the firm's fees as low as possible.
- Indications of an inappropriate limitation in the scope of work.
- Indications that the client might be involved in money laundering or other criminal activities.
- The reasons for the proposed appointment of the firm and non-reappointment of the previous firm.

2. J.A.C.K. & Co., a Chartered Accountant firm was appointed as the statutory auditor of Falcon Ltd. after ensuring the compliance with relevant provisions of the Companies Act, 2013. Mr. Jay was the engagement partner for the aforesaid audit and prior to commencement of the audit, Mr. Jay had called for a meeting of the engagement team in order to direct them and assign them their responsibilities. At the end of meeting, Mr. Jay assigned review responsibilities to two of the engagement team members who were the most experienced amongst all, for reviewing the work performed by the less experienced team members. While reviewing the work performed by the less experienced members of the engagement team, what shall be the considerations of the reviewers?

(Mar-21 MTP)

As per SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements", review responsibilities are determined on the basis that more experienced team members, including the engagement partner, review work performed by less experienced team members.

In the given situation, Mr. Jay, engagement partner assigned review responsibilities to two of the engagement team members who were the most experienced team members. While reviewing the work performed by less experienced members of the engagement team, both the more experienced Reviewers should consider whether:

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

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3. M/s NK & Co., Chartered Accountants were appointed as Statutory Auditors of Fresh Juice Limited for the F.Y 2019-2020. The previous year's audit was conducted by M/s. LP & Associates. After the audit was completed and report submitted, it was found that closing balances of last financial year i.e., 2018-19 were incorrectly brought forward. It was found that M/s NK & Co. did not apply any audit procedures to ensure that correct opening balances have been brought forward to the current period. Accordingly, a complaint was filed against NK & Co. in relation to this matter. You are required to inform what policies are required to be implemented by NK & Co. for dealing with such complaints and allegations as required by Standard on Quality Control (SQC). (Jan-21 New)

Complaints and Allegations in a Firm:

- (i) The firm should establish policies and procedures designed to provide it with reasonable assurance that it deals appropriately with:
- (a) Complaints and allegations that the **work performed by the firm fails to comply with professional standards and regulatory and legal requirements**; and
 - (b) Allegations of **non-compliance with the firm's system of quality control**.
- (ii) Complaints and allegations (which do not include those that are clearly frivolous) **may originate from within or outside the firm**. They may be made by firm personnel, clients or other third parties. They may be received by engagement team members or other firm personnel.
- (iii) As part of this process, the firm establishes **clearly defined channels** for firm personnel to raise any concerns in a manner that enables them to come forward without fear of reprisals.
- (iv) The firm **investigates such complaints and allegations** in accordance with established policies and procedures. The investigation is **supervised by a partner with sufficient and appropriate experience** and authority within the firm but who is not otherwise involved in the engagement, and includes **involving legal counsel** as necessary. Small firms and sole practitioners may use the services of a suitably qualified external person or another firm to carry out the investigation. **Complaints, allegations and the responses to them are documented**.
- (v) Where the results of the investigations indicate **deficiencies in the design or operation of the firm's quality control policies and procedures**, or non-compliance with the firm's system of quality control by an individual or individuals, **the firm takes appropriate action**.

4. HK & Co. Chartered Accountants have been auditors of SAT Ltd (a listed entity) for the last 8 financial years. CA. H, partner of the firm, has been handling the audit assignment very well since the appointment. The audit work of CA. H and her team is reviewed by a senior partner CA. K to assure that audit is performed in accordance with professional standards and regulatory and legal requirements. CA. K was out of India for some personal reasons, so this year CA. G has been asked to review the audit work. In your opinion, what areas CA. G should consider at the time of review. List any four areas and also comment whether firm is complying with Standard on Quality Control or not. (July-21)

Compliance with Standard on Quality Control on review of audit work - As per SQC 1, reviewer should consider following:

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

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(vii) The objectives of the engagement procedures have been achieved.

The firm should establish policies and procedures:

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

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

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

5. PQR & Associates, Chartered Accountants, is a partnership firm having 3 partners CA P, CA Q and CA R. PQR & Associates are appointed as Statutory Auditors of ABC Limited, a listed entity for the financial year 2021-22 and CA P is appointed as Engagement Partner for the audit of ABC Limited. Before issuing the Audit Report of ABC Limited, CA P asked CA R to perform Engagement Quality Control Review and is of the view that his responsibility will be reduced after review by CA R. Whether the contention of CA P is correct? What are the aspects that need to be considered by CA R while performing Engagement Quality Control Review for audit of financial statements of ABC Limited?

As per SQC 1, "Quality Control for Firms that Perform Audit and Reviews of Historical Financial Information, and other Assurance and Related Services Engagements", the review does not reduce the responsibilities of the engagement partner. Hence, contention of CA. P that after engagement quality control review by CA. R, his responsibility will be reduced, is not correct.

However, CA. R needs to consider the following aspect while performing Engagement

Quality Control Review for audit of financial statements of a listed entity ABC Ltd.:

1. The engagement team's evaluation of the firm's independence in relation to the specific engagement.
2. Significant risks identified during the engagement and the responses to those risks.
3. Judgments made, particularly with respect to materiality and significant risks.
4. Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations.
5. The significance and disposition of corrected and uncorrected misstatements identified during the engagement.
6. The matters to be communicated to management and those charged with governance and, where applicable, other parties such as regulatory bodies.
7. Whether working papers selected for review reflect the work performed in relation to the significant judgments and support the conclusions reached.
8. The appropriateness of the report to be issued.

Engagement quality control reviews for engagements other than audits of financial statements of listed entities may, depending on the circumstances, include some or all of these considerations

6. AP & Associates, Chartered Accountants, are Statutory Auditors of XP Limited for the last four years. XP Limited is engaged in the manufacture and marketing of FMCG Goods in India. During 2021-22, the Company has diversified and commenced providing software solutions in the area of "e-commerce" in India as well as in certain European countries. AP & Associates, while carrying out the audit for the current financial year, came to know that the

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company has expanded its operations into a new segment as well as new geography. AP & Associates does not possess necessary expertise and infrastructure to carry out the audit of this diversified business activity accordingly wishes to withdraw from the engagement and client relationship. Discuss the issues that need to be addressed before deciding to withdraw. [Nov-22]

Acceptance and Continuance of Client Relationships and Specific Engagements: As per SQC 1, "Quality Control for Firms that Perform Audit and Reviews of Historical Financial Information, and other Assurance and Related Services Engagements", the firm should establish **policies and procedures for the acceptance and continuance of client relationships and specific engagements**, designed to provide it with reasonable assurance that it will undertake engagements only where it is competent to perform the engagement and has the necessary professional capabilities, time and resources to do so.

In the given case, AP & Associates, Chartered Accountants, statutory auditors of XP Limited for the last four years. Recently, AP & Associates came to know that the company has expanded its operations into a new segment as well as new geography. AP & Associates does not possess necessary expertise for the same, therefore, AP & Associates wish to withdraw from the engagement and client relationship.

Policies and procedures on withdrawal from an engagement or from both the engagement and the client relationship should address issues that include the following:

- Discussing with the appropriate level of the client's management and those charged with its governance regarding the **appropriate action that the firm might take based on the relevant facts and circumstances**.
- If the firm determines that it is appropriate to withdraw, discussing with the appropriate level of the client's management and those charged with its governance **withdrawal from the engagement or from both the engagement and the client relationship, and the reasons for the withdrawal.**
- Considering whether there is a **professional, regulatory or legal requirement** for the firm to remain in place for the firm to **report the withdrawal from the engagement, or from both the engagement and the client relationship, together with the reasons for the withdrawal, to regulatory authorities.**
- **Documenting significant issues, consultations, conclusions and the basis for the conclusions.**

AP & Associates should address the above issues before deciding to withdraw.

SA 200: Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing

1. M/s SG & Co. Chartered Accountants were appointed as Statutory Auditors of XYZ Limited for the F.Y 2020-21. The Company implemented internal controls for prevention and early detection of any fraudulent activity. Audit was carried out test of controls and found out no major observations. After the completion of audit, audit report was submitted by the auditors and audited results were issued. Fraud pertaining to the area of inventory came to light subsequently for the period covered by audit and auditors were asked to make submission as to why audit failed to identify such fraud. Auditors submitted that because of inherent limitations of audit, it is not possible to obtain persuasive evidence of certain matters like fraud. Do you think auditor made correct statement? Also discuss certain subject matters or assertions where it is difficult to detect material misstatements due to potential effects of inherent limitations. (July-21 New)

Certain assertions or subject matters where it is difficult to detect material misstatements due to potential effects of inherent limitations -

As per SA 200 - "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing" and as per SQC 1 because of the inherent limitations of an audit, there is an unavoidable risk that some material misstatements may not be detected.

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that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with SAs.

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Accordingly, the subsequent discovery of a material misstatement of the financial statements resulting from fraud or error does not by itself indicate a failure to conduct an audit in accordance with SAs. However, the inherent limitations of an audit are not a justification for the auditor to be satisfied with less-than-persuasive audit evidence.

Whether the auditor has performed an audit in accordance with SAs is determined by the audit procedures performed in the circumstances, the sufficiency and appropriateness of the audit evidence obtained as a result thereof and the suitability of the auditor's report based on an evaluation of that evidence in the light of the overall objectives of the auditor.

In view of above, it can be concluded that auditors did not give correct statement.

In the case of certain assertions or subject matters, the potential effects of the inherent limitations on the auditor's ability to detect material misstatements are particularly significant.

Such assertions or subject matters include:

- (i) Fraud, particularly fraud involving senior management or collusion.
- (ii) The existence and completeness of related party relationships and transactions.
- (iii) The occurrence of non-compliance with laws and regulations.
- (iv) Future events or conditions that may cause an entity to cease to continue as a going concern.

2. Yupee (P) Ltd. got incorporated on 15th May 2021 and Mr. Harsh, the director of Yupee (P) Ltd. proposed to Kamal & Co. on 24th May 2021, for being appointed as its statutory auditor. Mr. Kamal, the sole proprietor of Kamal & Co., after checking the compliance with all the statutory requirements, accepted the said offer and issued an audit engagement letter vide email to Yupee (P) Ltd.

Mr. Harsh found all terms of audit engagement to be proper but in the paragraph relating to auditor's responsibility in the engagement letter, as produced below:-

"We will conduct our audit in accordance with Standards on Auditing (SAs), issued by the Institute of Chartered Accountants of India (ICAI). Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement."

Certain queries raised in his mind that what does reasonable assurance meant? Which Standard on Auditing requires the auditor to obtain such reasonable assurance? Is it possible to give absolute assurance on such financial statements?

Assuming that you are Mr. Kamal, the newly appointed statutory auditor of Yupee (P) Ltd. Please address to the queries of Mr. Harsh as stated above. [MTP Apr-22]

As per SA 200, "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing", the auditor is required:- "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."

Reasonable assurance is a high level of assurance and is less than absolute assurance. It is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (i.e., the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level.

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The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit, which result in most of the audit evidence on which the auditor draws conclusions and forms the auditor's opinion being persuasive rather than conclusive. The inherent limitations of an audit arise from:

- The nature of financial reporting;
- The nature of audit procedures, and
- The need for the audit to be conducted within a reasonable period of time and at a reasonable cost.

SA 210: Agreeing the Terms of Audit Engagement

1. T & Co, a firm of Chartered Accountants has not revised the terms of engagements and obtained confirmation from the clients for last 5 years despite changes in business and professional environment. Please elucidate the circumstances that may warrant the revision in terms of engagement. (Nov-19 Old)

Circumstances that may Warrant the Revision in Terms of Engagement : As per SA 210 on "Agreeing the Terms of Audit Engagements", auditor may decide not to send a new audit engagement letter or other written agreement each period. However, the following factors may make it appropriate to revise the terms of the audit engagement or to remind the entity of existing terms:

- (i) Any indication that the entity misunderstands the objective and scope of the audit.
- (ii) Any revised or special terms of the audit engagement.
- (iii) A recent change of senior management.
- (iv) A significant change in ownership.
- (v) A significant change in nature or size of the entity's business.
- (vi) A change in legal or regulatory requirements.
- (vii) A change in the financial reporting framework adopted in the preparation of the financial statements.
- (viii) A change in other reporting requirements.

2. Mr. Ram Kapoor, Chartered Accountant, has been appointed as the statutory auditor by XYZ Private Limited for the audit of their financial statements for the year 2018-19. The company has mentioned in the audit terms that they will not be able to provide internal audit reports to Mr. Ram during the course of audit. Further, company also imposed some limitation on scope of Mr. Ram. What are the preconditions Mr. Ram should ensure before accepting/ refusing the proposal? Also advise, whether Mr. Ram should accept the proposed audit engagement? (RTP Nov-19)

As per SA 210 "Agreeing the Terms of Audit Engagements", in order to establish whether the preconditions for an audit are present, the auditor shall:

- (a) Determine whether the FRF to be applied in the preparation of the financial statements is acceptable; and
- (b) Obtain the agreement of management that it acknowledges and understands its responsibility
 - (i) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation;
 - (ii) For such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
 - (iii) To provide the auditor with:
 - a) Access to all information of which management is aware that is relevant to the preparation of the financial statements 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.

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Further, if management or TCWG impose a limitation on scope of the auditor's work in the terms of a proposed audit engagement such that the auditor believes the limitation will result in the auditor disclaiming an opinion on the financial statements, the auditor shall not accept such a limited engagement as an audit engagement, unless required by law or regulation to do so.

In addition if the preconditions for an audit are not present, the auditor shall discuss the matter with management. Unless required by law or regulation to do so, the auditor shall not accept the proposed audit engagement.

In the instant case, Mr. Ram should not accept the appointment as statutory auditor of XYZ Private Limited due to limitation imposed on his scope of work.

3. AKJ Ltd is a small-sized 30 years old company having business of manufacturing of pipes. Company has a plant based out of Dehradun and have their corporate office in Delhi. Recently the company appointed new firm of Chartered Accountants as their statutory auditors.

The statutory auditors want to enter into an engagement letter with the company in respect of their services but the management has contended that since the statutory audit is mandated by law, engagement letter may not be required. Auditors did not agree to this and have shared a format of engagement letter with the management for their reference before getting that signed. In this respect management would like to understand that as per SA 210 (auditing standard referred to by the auditors), if the agreed terms of the engagement shall be recorded in an engagement letter or other suitable form of written agreement, what should be included in terms of agreed audit engagement letter?

[SM +RTP May-21]

As per SA 210 'Agreeing the Terms of Audit Engagements', the auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate.

The agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include:

- (i) The objective and scope of the audit of the financial statements;
- (ii) The responsibilities of the auditor;
- (iii) The responsibilities of management;
- (iv) Identification of the applicable financial reporting framework for the preparation of the financial statements;
- (v) Reference to the expected form and content of any reports to be issued by the auditor and a statement that the auditor may be circumstances in which a report may differ from its expected form and content.

SA 220: Quality Control for an Audit of Financial Statements

1. Ace Limited (manufacturer of textile goods) got an order of manufacturing of PPE kits in December 2020. There was shortage of machinery and manpower to accomplish the ordered requirement of PPE kits. Ace Limited approached another manufacturing unit Jack Limited for purchase of the unit. Jack Limited was interested in the sale of unit, so the deal went through and Ace Limited acquired ninety five percent shares of Jack Limited. The management of Jack Limited proposed and appointed NKB Associates, Chartered Accountants, (already a member firm of Ace Limited) as new auditors of Jack Limited. NKB Associates accepted the assignment without conducting any due diligence information whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate. Comment with respect to appropriate Standard on Auditing which provides information assists the engagements partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate or not?

[Nov-21 Old + N]

Acceptance and Continuance of Client Relationships and Audit Engagements : As per SA 220, "Quality Control for an Audit of Financial Statements" , SQC 1, "Quality Control for Firms that Perform Audits and Reviews of Financial Information, and Other Assurance and Related Services Engagements", requires the firm to

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Information considered necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client.

Information such as the following assists the engagement partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate:

- The integrity of the principal owners, key management and those charged with governance of the entity;
- Whether the engagement team is **competent** to perform the audit engagement and has the necessary capabilities, including time and resources;
- Whether the firm and the engagement team can comply with relevant **ethical requirements**; and
- **Significant matters** that have arisen during the current or previous audit engagement, and their implications for continuing the relationship.

2. During the audit of FMP Ltd, a listed company, Engagement Partner (EP) completed his reviews and also ensured compliance with independence requirements that apply to the audit engagement. The engagement files were also reviewed by the Engagement Quality Control Reviewer (EQCR) except the independence assessment documentation. Engagement Partner was of the view that matters related to independence assessment are the responsibility of the Engagement Partner and not Engagement Quality Control Reviewer. Engagement Quality Control Reviewer objected to this and refused to sign off the documentation. Please advise as per SA 220. (RTP May-19 + MTP Oct-19 + SM)

As per SA 220, Engagement Partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, Engagement Partner shall:

- Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate circumstances and relationships that create threats to independence;
- Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for the audit engagement; and
- Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is permitted by law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action.

Engagement Partner shall take responsibility for reviews being performed in accordance with the firm's review policies and procedures.

As per SA 220, "Quality Control for Audit of Financial Statements", for audits of financial statements of listed entities, Engagement Quality Control Reviewer (EQCR), on performing an engagement quality control review, shall also consider the engagement team's evaluation of the firm's independence in relation to the audit engagement.

In the given case, Engagement Partner is not right. The independence assessment documentation should also be given to Engagement Quality Control Reviewer for his review.

3. Rishikumar & Co. has been appointed as an auditor of PK Ltd. for the financial year 2016 -17. CA. Kumar, one of the partners of M/s Rishikumar & Co., completed entire routine audit work by 29th May, 2017. Unfortunately, on the very next morning, while roving towards office of PK Ltd. to sign final audit report, he met with a road accident and died. CA. Rishi, another partner of M/s Rishikumar & Co., therefore, signed the accounts of PK Ltd., without reviewing the work performed by CA. Kumar. Advise, whether CA. Rishi is right in expressing an opinion on financial statements the audit of which is performed by another auditor. (MTP April-18)

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relying on Work Performed by Another Auditor: As per SA 220 "Quality Control for an Audit of Financial Statements", an engagement partner taking over an audit during the engagement may apply the review procedures such as

- the work has been performed in accordance with professional standards and regulatory and legal requirements;
- significant matters have been raised for further consideration;
- appropriate consultations have taken place and
- the resulting conclusions have been documented and implemented;
- there is a need to revise the nature, timing and extent of work performed;
- the work performed supports the conclusions reached and is appropriately documented;
- the evidence obtained is sufficient and appropriate to support the auditor's report; and
- the objectives of the engagement procedures have been achieved.

Further, one of the basic principles, which govern the auditor's professional responsibilities and which should be complied with wherever an audit is carried, is that when the auditor delegates work to assistants or uses work performed by other auditor and experts, he will continue to be responsible for forming and expressing his opinion on the financial information.

However, he will be entitled to rely on work performed by others, provided he exercises adequate skill and care and is not aware of any reason to believe that he should not have so relied. This is the fundamental principle which is ethically required as per Code of Ethics. However, the auditor should carefully direct, supervise and review work delegated.

He should obtain reasonable assurance that work performed by other auditors/experts and assistants is adequate for his purpose.

In the given case, all the auditing procedures before the moment of signing of final report have been performed by CA. Kumar. However, the report could not be signed by him due to his unfortunate death. Later on, CA. Rishi signed the report relying on the work performed by CA. Kumar. Here, CA. Rishi is allowed to sign the audit report, though, will be responsible for expressing the opinion.

He may rely on the work performed by CA. Kumar provided he further exercises adequate skill and due care and review the work performed by him as required in compliance with SA 220.

4. OP & Associates are the statutory auditors of BB Ltd. BB Ltd is a listed company and started its operations 5 years back. The field work during the audit of the financial statements of the company for the year ended March 31, 2018 got completed on May 1, 2018. The auditor's report was dated May 12, 2018. During the documentation review of the engagement, it was observed that the engagement quality control review was completed on May 15, 2018. Engagement partner had completed his reviews in entirety by May 10, 2018. Comment. (MTP Mar-19)

As per SA 220, the engagement partner shall take responsibility for reviews being performed in accordance with the firm's review policies and procedures. For audits of financial statements of listed entities, the engagement partner shall:

- Determine that an engagement quality control reviewer has been appointed;
- Discuss significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer; and
- Not date the auditor's report until the completion of the engagement quality control review.

SA 700 also requires the auditor's report to be dated no earlier than the date on which the auditor has obtained sufficient appropriate evidence on which to base the auditor's opinion on the financial statements. In cases of

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audit of financial statements of listed entities where the engagement meets the criteria for an engagement quality control review, such a review assists the auditor in determining whether sufficient appropriate evidence has been obtained.

Conducting the engagement quality control review in a timely manner at appropriate stages during the engagement allows significant matters to be promptly resolved to the engagement quality control reviewer's satisfaction on or before the date of the auditor's report.

In the given case, the signing of auditors' report before completion of review of engagement quality control review is not right.

SA 230: Audit Documentation

1. Mr. PM, a practising Chartered Accountant, has been appointed as an auditor of Truth Pvt. Ltd. What factors would influence the amount of working papers required to be maintained for the purpose of his audit? (RTP May-20)

Factors Influencing the amount of Working Papers: As per SA 230 "Audit Documentation", which refers to the record of audit procedures performed, relevant audit evidence obtained and conclusions the auditor reached, the amount of audit working papers depend on factors such as-

- (i) The size and complexity of the entity.
- (ii) The nature of the audit procedures to be performed.
- (iii) The identified risks of material misstatement.
- (iv) The significance of the audit evidence obtained.
- (v) The nature and extent of exceptions identified.
- (vi) The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained.
- (vii) The audit methodology and tools used.
- (viii) Timely preparation of Audit Documentation.

2. You are the team leader of 10 members for an audit of a Multinational company. All the team members are concerned about Audit documentation in order to provide evidence that the audit complies with SAs. Hence, the team members wish to document every matter concerned, In your opinion it is neither necessary nor practicable for the auditor to document every matter considered or professional judgement made in an audit. Further you feel that it is unnecessary for the auditor to document separately compliance with matters for which compliance is demonstrated by documents included within the audit file. Illustrate by giving examples with reference to relevant Standard on Auditing. [May-22]

As per SA 230, "Audit Documentation" it is unnecessary for the auditor to document separately (as in a checklist, for example) compliance with matters for which compliance is demonstrated by documents included within the audit file.

For example:

- ✓ The existence of an adequately documented audit plan demonstrates that the auditor has planned the audit.
- ✓ The existence of a signed engagement letter in the audit file demonstrates that the auditor has agreed the terms of the audit engagement with management, or where appropriate, those charged with governance.
- ✓ An auditor's report containing an appropriately qualified opinion demonstrates that the auditor has complied with the requirement to express a qualified opinion under the circumstances specified in the SAs.
- ✓ In relation to requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file:

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- For example, there may be no single way in which the auditor's professional skepticism is documented. But the audit documentation may nevertheless provide evidence of the auditor's exercise of professional skepticism in accordance with SAs. Such evidence may include specific procedures performed to corroborate management's responses to the auditor's inquiries.
- Similarly, that the engagement partner has taken responsibility for the direction, supervision and performance of the audit in compliance with the SAs may be evidenced in a number of ways within the audit documentation. This may include documentation of the engagement partner's timely involvement in aspects of the audit, such as participation in the team discussion required by SA 315.

SA 240: The Auditor's Responsibilities relating to Fraud in an Audit of Financial Statements

1. Arhant Limited was engaged in the business of owning and managing hotels and resorts, selling tourism packages and performing airline bookings for corporate and individuals. It appointed Upadhyay & Co. as its statutory auditor for the financial year 2021-22.

While planning the audit, the audit team decided that the risk of improper revenue recognition from hotel business should not be treated as a fraud risk. This conclusion was based on the assessment of earlier years, wherein no fraud was identified in revenue recorded from such business. While testing the internal financial controls over the process of revenue recognition, it was identified that the controls are not properly designed to mitigate the risk of fraud and risk of improper revenue recognition. As a result, the audit team decided to perform additional substantive testing. However, the audit team still were to the conclusion that there is no risk of fraud in revenue recognition.

During the course of substantive testing, it was identified that the management did not account for revenue received from corporate hotel bookings amounting to ₹35 crore. These amounts were partially received in the company's bank accounts and partially received in the CFO's personal account. The amounts received in the bank account of the company were disclosed as advances received against the future bookings.

In the light of above scenario, kindly guide the statutory auditors with respect to their responsibility relating to fraud in an audit of a financial statement. [RTP Nov-22]

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

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

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

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

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

Therefore, the auditor while performing the risk assessment procedures should consider the complexity and nature of the revenue for determining the fraud risks in revenue recognition. Also, there were no adequate controls addressing the risk of improper revenue recognition or fraud risk, the audit team rebutted the fraud risk. Moreover, the audit team should have recognised fraud risk by identifying the deficiencies of internal control over the revenue recognition process and should have treated the risk of improper revenue recognition as a significant risk.

Also, as per Section 143(12), the auditor is required to report all the frauds identified during the course of the audit involving amounts above ₹ 1 crore within the prescribed time frame to the Central Government

2. In the course of audit of Quick Ltd, you suspect that the management has made misstatements in the financial statements intentionally to deceive the users and to succumb to pressures to meet market expectations. Elucidate how the fraudulent financial reporting may be accomplished and also discuss the techniques of committing fraud by management overriding controls. (Nov-20 New)

As per SA 240 on "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements"

Fraudulent financial reporting may be accomplished by the following:

- i. Manipulation, falsification (including forgery), or alteration of accounting records or supporting documentation from which the financial statements are prepared.
- ii. Misrepresentation in or intentional omission from, the financial statements of events, transactions or other significant information.
- iii. Intentional misapplication of accounting principles relating to amounts, classification, manner of presentation, or disclosure.

Fraudulent financial reporting often involves management override of controls that otherwise may appear to be operating effectively. Fraud can be committed by management overriding controls using such techniques as:

- i. Recording fictitious journal entries, particularly close to the end of an accounting period, to manipulate operating results or achieve other objectives.
- ii. Inappropriately adjusting assumptions and changing judgments used to estimate account balances.
- iii. Omitting, advancing or delaying recognition in the financial statements of events and transactions that have occurred during the reporting period.
- iv. Concealing, or not disclosing, facts that could affect the amounts recorded in the financial statements.
- v. Engaging in complex transactions that are structured to misrepresent the financial position or financial performance of the entity.
- vi. Altering records and terms related to significant and unusual transactions.

3. M/s Kumar & Co., Chartered Accountants were appointed as statutory auditors of PC limited for the financial year 2020-21. During the course of audit, one of the partners CA. Kumar observed that there is misappropriation of

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assets in the form of theft of entity's inventory and is perpetrated by employees in relatively small and immaterial amounts. CA. Kumar is concerned with the existence of certain circumstances for increasing the susceptibility of assets to misappropriation.

Guide CA. Kumar with respect to Risk factors related to misstatements arising from misappropriation of assets with reference to relevant Standard on Auditing. (Nov-15, Nov-21 5 Marks)

Risk Factors Relating to Misstatements Arising from Misappropriation of Assets:

As per SA 240, "The Auditor's Responsibilities Relating to Fraud in audit of Financial Statements", misappropriation of assets involves the theft of an entity's assets and is often perpetrated by employees in relatively small and immaterial amounts. However, it can also involve management who are usually more able to disguise or conceal misappropriations in ways that are difficult to detect.

Risk factors that relate to misstatements arising from misappropriation of assets are classified according to the three conditions generally present when fraud exists: incentives/pressures, opportunities, and attitudes/rationalization. The following are examples of risk factors related to misstatements arising from misappropriation of assets:

Incentives/Pressures: Personal financial obligations may create pressure on management or employees with access to cash or other assets susceptible to theft to misappropriate those assets.

Adverse relationships between the entity and employees with access to cash or other assets susceptible to theft may motivate those employees to misappropriate those assets. For example, adverse relationships may be created by the following:

1. Known or anticipated future employee layoffs.
2. Recent or anticipated changes to employee compensation or benefit plans.
3. Promotions, compensation or other rewards inconsistent with expectations.

Opportunities: Certain characteristics or circumstances may increase the susceptibility of assets to misappropriation. For example, opportunities to misappropriate assets increase when there are the following:

- Inventory items that are small in size, of high value, or in high demand.
- Fixed assets which are small in size, marketable, or lacking observable identification of ownership.
- Inadequate internal control over assets may increase the susceptibility of misappropriation of those assets.
- Inadequate segregation of duties or independent checks.

Attitudes/Rationalizations

- Disregard for the need for monitoring or reducing risks related to misappropriations of assets.
- Disregard for internal control over misappropriation of assets by overriding existing controls or by failing to take appropriate remedial action on known deficiencies in internal control.
- Behaviour indicating displeasure or dissatisfaction with the entity or its treatment of the employee.
- Changes in behaviour or lifestyle that may indicate assets have been misappropriated.

4. Explain briefly duties and responsibilities of an auditor in case of material misstatement resulting from Management Fraud. (May-17 6 Marks)

Misstatement in the financial statements can arise from fraud or error. The term **fraud** refers to an 'Intentional Act' by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.

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As per SA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", the responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management. The auditor, conducting an audit, is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. However, to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the Standards on Auditing (SAs).

As described in SA 200, the potential effects of inherent limitations are particularly significant in the case of misstatement resulting from fraud. The risk of not detecting a material misstatement resulting from fraud is generally greater than the risk of not detecting one resulting from error. This is because fraud may involve sophisticated and organized schemes designed to conceal it, such as forgery, deliberate failure to record transactions, or intentional misrepresentations being made to the auditor. Such attempts at concealment may be even more difficult to detect when accompanied by collusion. Collusion may cause the auditor to believe that audit evidence is persuasive when it is, in fact, false. While the auditor may be able to identify potential opportunities for fraud to be perpetrated, it is difficult for the auditor to determine whether misstatements in judgment areas such as accounting estimates are caused by fraud or error.

Furthermore, the risk of the auditor not detecting a material misstatement resulting from management fraud is generally greater than for employee fraud, because management is frequently in a position to directly or indirectly manipulate accounting records, present fraudulent financial information or override control procedures designed to prevent or detect similar frauds by other employees.

When obtaining reasonable assurance, the auditor is responsible for maintaining professional skepticism throughout the audit, considering the potential for management override of controls and recognizing the fact that control procedures that are effective for detecting error may not be effective in detecting fraud.

Further, as per section 143(12) of the Companies Act, 2013, if an auditor of a company, in the course of performance of his duties as auditor, has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company, he shall immediately report the matter to the Central Government (in case amount of fraud is ₹ 1 crore or above) or Audit Committee or Board in other cases (in case the amount of fraud involved is less than ₹ 1 crore) within such time and in such manner as may be prescribed.

The auditor is also required to report as per Clause (xi) of Paragraph 3 of CARO, 2020, Whether any fraud by or on the company or any fraud on the company has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated.

5. You notice a misstatement resulting from fraud or suspected fraud during the audit and conclude that it is not possible to continue the performance of audit. As a Statutory Auditor, how would you deal? (PM)

Impossibility to continue the performance of audit: According to SA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", if, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit, the auditor shall:

- Determine the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities;

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- b. Consider whether it is appropriate to withdraw from the engagement, where withdrawal from the engagement is legally permitted; and
- c. If the auditor withdraws:
- Discuss with the appropriate level of management and those charged with governance, the auditor's withdrawal from the engagement and the reasons for the withdrawal; and
 - Determine whether there is a professional or legal requirement to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities; the auditor's withdrawal from the engagement and the reasons for the withdrawal.

Further, as per section 143(12) of the Companies Act, 2013, if an auditor of a company, in the course of the performance of his duties as auditor, has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company, he shall immediately report the matter to the Central Government (in case amount of fraud is ₹ 1 crore or above) or Audit Committee or Board in other cases (in case the amount of fraud involved is less than ₹ 1 crore) within such time and in such manner as may be prescribed.

6. The Managing Director of the Company has committed a "Teeming and Lading" Fraud. The amount involved has been however subsequently after the year end deposited in the company. As a Statutory Auditor, how would you deal? (PM + Mar'18 MTP + CA Inter SM)

The Managing Director of the company has committed a "Teeming and Lading" fraud. The fact that the amount involved has been subsequently deposited after the year end is not important because the auditor is required to perform his responsibilities as laid down in SA 240.

First of all, as per SA 240, the auditor needs to perform procedures whether the financial statements are materially misstated. Because an instance of fraud cannot be considered as an isolated occurrence and it becomes important for the auditor to perform audit procedures and revise the audit risk assessment.

Secondly, the auditor needs to consider the impact of fraud on financial statements and its disclosure in the audit report.

Thirdly, the auditor should communicate the matter to the Chairman and Board of Directors.

Finally, in view of the fact that the fraud has been committed at the highest level of management, it affects the reliability of audit evidence previously obtained since there is a genuine doubt about representations of management.

+Sec 143(12) + CARO 2020

7. On 15th March, 2020, the directors of Phony Ltd. instructed their accountant to enter purchases amounting Rs. 1.02 crores from a company incorporated dated 11th March, 2020. However, no amount was actually paid and Rs. 1.02 crore was provided in the books of account as purchases for the year ending on 31st March, 2020.

On inspection, no documentary or other evidence of such purchases was found. As the auditor of Phony Ltd., what would be your approach regarding reporting of such bogus purchases? (July 20 MTP, RTP Nov-18, Nov-13)

Reporting of Fraud Committed by Management/Directors of the Company: As per SA 240 on "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", fraud can be committed by management overriding controls using such techniques as recording fictitious journal entries, particularly close to the end of an accounting period, to manipulate operating results or achieve other objectives. In the given case, Phony Ltd. has made purchases amounting Rs. 1.02 crores, at year-end. It also debited the sum in the books of account, however, no documentary or other evidence of such purchases was found, on investigation. It is clear that company has passed fictitious journal entries, near year-end, to manipulate the operating results.

Accordingly, the auditor would adopt the approach which will be based on the result of misstatement on the basis of such fictitious journal entry, i.e. if, as a result of a misstatement resulting from fraud or suspected fraud, the auditor

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encounters exceptional circumstances that bring into question the auditor's ability to continue performance of the audit, the auditor shall determine the professional and legal responsibilities applicable in the circumstances. If, in some cases, there is a requirement for the auditor to report to the person or persons who made the audit appointment, or, in some cases, to regulatory authorities; or the auditor may consider for appropriateness of withdrawal from the engagement, where withdrawal from the engagement is legally permitted.

In addition, the auditor is required to report according to section 143(12) of the Companies Act, 2013. As per section 143(12), if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of Rs. 1 crore or more, or being or has been committed in the company by its officers or employees, he shall report the matter to the Government in prescribed manner.

The auditor is also required to report under clause (xi) of paragraph 3 of Companies (Auditor's Report) Order, 2016, whether any fraud by the company or any fraud on the Company by its officers or employees has been reported during the year. If yes, the nature and the amount involved is to be indicated.

8. Is it appropriate for the auditor to make inquiries of management regarding management's own assessment of the risk of fraud and the controls in place to prevent and detect it? Discuss. (Nov-16 5 Marks)

Appropriateness of making inquiries of management regarding assessment of fraud: SA 240 "Responsibilities relating to Fraud in an Audit of Financial Statements" requires the auditor to make inquiries of management regarding:

- Management's assessment of risk of material misstatement due to fraud;
- Management's process for identifying & responding to the risks of fraud in the entity, including any special controls designed to reduce the risks of fraud;
- Management's communication, if any, to TCWG; and
- Management's communication, if any, to employees regarding its views on business practices and behaviour.

Management is responsible for the entity's internal control and for the preparation of the financial statements. Accordingly, it is appropriate for the auditor to make inquiries of management regarding management's assessment of the risk of fraud and the controls in place to prevent and detect it.

The nature, extent and frequency of management's assessment of such risk and controls may vary from entity to entity. In some entities, management may make detailed assessments on an annual basis or as part of ongoing monitoring. In other entities, management's assessment may be less structured and less frequent.

The nature, extent and frequency of management's assessment are relevant to the auditor's understanding of the entity's control environment. For example, the fact that management has not made an assessment of the risk of fraud may in some circumstances be indicative of the lack of importance that management places on internal control.

SA 250 (Revised) "Consideration of Laws and Regulations in an Audit of Financial Statements"

PQ Limited, a listed entity, is in the business of manufacturing of specialty chemicals. The company has CA Jazz as CFO of the company. CA Jazz is concerned about compliance with the provisions of laws and regulations that determine the reported amounts and disclosure in financial statements of PQ Limited. According

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wants to implement such policies and procedures that can assist him in the prevention and detection of non-compliance with laws and regulations. Help CA Jazz by citing examples of such policies and procedures. (Nov-20)

As per SA 250, "Consideration of Laws and Regulations in an Audit of Financial Statements",

The following are examples of the types of policies and procedures PQ Ltd. may implement to assist in the prevention and detection of non-compliance with laws and regulations:

- (i) **Monitoring** legal requirements and ensuring that operating procedures are designed to meet these requirements.
- (ii) Instituting and operating appropriate systems of **internal control**.
- (iii) Developing, publicizing and following a **code of conduct**.
- (iv) Ensuring **employees are properly trained** and understand the code of conduct.
- (v) **Monitoring compliance with the code of conduct** and acting appropriately to discipline employees who fail to comply with it.
- (vi) Engaging **legal advisors** to assist in monitoring legal requirements.
- (vii) Maintaining a **register of significant laws and regulations** with which the entity has to comply within its particular industry and a record of complaints.

2. While verifying the employee records in a company, it was found that a major portion of the labour employed was child labour. On questioning the management, the auditor was told that it was outside his scope of the financial audit to look into the compliance with other laws. Comment in accordance with relevant Standards on Auditing.

(MTP May 20)

As per SA 250, "Consideration of Laws and Regulations in an Audit of Financial Statements", the auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements including tax and labour laws.

Further, non-compliance with other laws and regulations may result in fines, litigation or other consequences for the entity, the costs of which may need to be provided for in the financial statements, but are not considered to have a direct effect on the financial statements.

In the instant case, major portion of the labour employed in the company was child labour. While questioning by auditor, reply of the management that it was outside his scope of financial audit to look into the compliance with other laws is not acceptable as it may have a material effect on financial statements.

Thus, auditor should ensure the disclosure of above fact and provision for the cost of fines, litigation or other consequences for the entity. In case if the auditor concludes that noncompliance has a material effect on the financial statements and has not been adequately reflected in the financial statements, the auditor shall express a qualified or adverse opinion on the financial statement as per SA 705 "Modifications to the Opinion in the Independent Auditor's Report".

3. As an Auditor of TRP Ltd., you are suspicious that there might be non-compliance with laws and regulations to which the Company is subject to. Indicate the possible areas or aspects where you may have to look out for forming an opinion as to whether your suspicion has some basis to further inquire. (May-18 New, May 16, Nov-21 Old)

OR

You are appointed as an auditor of Moksh Ltd., a company engaged in export of agricultural equipment. During the course of audit, your audit team informed you regarding non-deduction of TDS on huge payments made to legal counsel of Moksh Ltd. You want to alert your team on the possibility of non-compliance with Laws and Regulations by Moksh Ltd. Help your audit team in identifying any other indications of non-compliance with Laws and Regulations particularly related to payments made by the company. [MTP May-23]

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Indications of Non-Compliance with Laws and Regulations: When the auditor becomes aware of the existence of information about the following matters, it may be an indication of non-compliance with laws and regulations. The possible areas or aspects to look out for forming an opinion are:

- Investigations by regulatory organisations and government departments or payment of fines or penalties to employees.
- Sales commissions or agent's fees that appear excessive in relation to those ordinarily paid by the company in its industry or to the services actually received.
- Purchasing at prices significantly above or below market price.
- Unusual payments in cash, purchases in the form of cashiers' cheques payable to bearer or transferable numbered bank accounts.
- Unusual payments towards legal and retainership fees.
- Unusual transactions with companies registered in tax havens.
- Payments for goods or services made other than to the country from which the goods or services originate.
- Payments without proper exchange control documentation.
- Existence of an information system which fails, whether by design or by accident, to provide an adequate audit trail or sufficient evidence.
- Unauthorised transactions or improperly recorded transactions.
- Adverse media comment.

4. XYZ Pvt. Ltd. has submitted the financial statements for the year ended 31-3-18 for audit. The auditor observes and brings to your notice that the company's records show following dues:
Income Tax relating to Assessment Year 2014-15 Rs. 125 lacs - Appeal is pending before Hon'ble ITAT since 30-9-17.
Customs duty Rs. 25 lakhs - Demand notice received on 15-9-17 but no action has been taken to pay or appeal.
Comment. (MTP Oct-18)

As per SA 250 "Consideration of Laws and Regulations in an Audit of Financial Statement", it is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial statements.

The auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether caused by fraud or error. In conducting an audit of financial statements, the auditor takes into account the applicable legal and regulatory framework. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements in the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the SAs.

If the auditor concludes that the non-compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements, the auditor shall express a qualified or adverse opinion on the financial statements.

Further, the auditor is required to report on certain matters specified in Para 3 of CARO, 2020 under section 143 of the Companies Act, 2013.

One of such matter is non-payment of dues to Government, on account of any dispute. As per clause (vii)(a) of Para 3 of CARO, 2020, in case dues of income tax or sales tax or service tax or duty of customs or duty of excise or value

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added tax have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned.

In the present case, there is Income Tax demand of Rs. 125 Lacs and the company has gone for an appeal, it needs considerations as to whether the entire demand is disputed, because it is difficult to presume that the demand by Income Tax authority is without any basis.

Therefore, as per AS 29 "Provisions, Contingent Liabilities and Contingent Assets", partly to the extent the company considers that the demand is based on some logical basis, that amount may be provided for and the remaining may be disclosed as the contingent liability. Further, it should be brought to notice of the members by reporting.

Additionally, the demand notice has been received for Customs duty of Rs. 85 lakhs and is outstanding on the closure of financial year, for which no action has been taken by the management. Therefore, it should also be brought to notice of the members by reporting.

5. During the course of audit of CT Ltd. for the financial year 2017-18, it is noticed that Rs. 3.00 lakhs of employee contribution and Rs. 7.50 lakhs of employer contribution towards employee state insurance contribution have been accounted in the books of accounts in respective heads. Whereas, it was found that Rs. 5.00 lakhs only has been deposited with ESIC department during the year ended 31st March, 2018. The Finance Manager informed the auditor that due to financial crunch they have not deposited the amount due, but will deposit the amount overdue along with interest as and when financial position improves. Comment as a statutory auditor. (MTP Aug-18)

Non-Compliance of Laws and Regulations & Reporting Requirements: As per SA 250 "Consideration of Laws and Regulations in an Audit of Financial Statement", it is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial statements. The auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether caused by fraud or error. In conducting an audit of financial statements, the auditor takes into account the applicable legal and regulatory framework. If the auditor concludes that the non-compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements, the auditor shall express a qualified or adverse opinion on the financial statements.

Further, the auditor is required to report under clause (vii)(a) of Para 3 of CARO, 2020 whether the company is regular in depositing undisputed statutory dues including employees' state insurance with the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as at the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated by the auditor.

In the instant case, even though accrual principles have been followed, disclosure of non-payment is necessary. The auditor should disclose the fact of non-payment of rupees 5.50 lakhs in his report.

6. CA Abhinadan is an auditor of KM Private Limited. During the course of audit, CA Abhinadan becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws and regulations. Being a senior partner of CA. Abhinadan, guide him regarding audit procedures to be followed when non-compliance is identified or suspected. [RTP May-22]

As per SA 250, "Consideration of Laws and Regulations in an Audit of Financial Statements", if the auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws and regulations, the auditor shall obtain:

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- (i) An understanding of the nature of the act and the circumstances in which it has occurred; and
- (ii) Further information to evaluate the possible effect on the financial statements.

If the auditor suspects there may be non-compliance, the auditor shall discuss the matter with management or, where appropriate, those charged with governance. If management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgment, the effect of the suspected non-compliance may be material to the financial statements, the auditor shall consider the need to obtain legal advice.

If sufficient information about suspected non-compliance cannot be obtained, the auditor shall evaluate the effect of the lack of sufficient appropriate audit evidence on the auditor's opinion.

The auditor shall evaluate the implications of non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations, and take appropriate action.

SA 260 "Communication with those Charged with Governance"

1. "The auditors should communicate audit matters of governance interest arising from the audit of financial statements with those charged with the governance of an entity". Briefly state the matters to be included in the communication. (PM)

As per SA 260 "Communication with those Charged with Governance", the auditor shall communicate with those charged with governance, the responsibilities of the auditor in relation to the financial statement audit, including the following:

- (a) The auditor is responsible for forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance; and
- (b) The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.

The auditor shall communicate with those charged with governance the following:

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

2. M/s Manidhari & Associates have been appointed as an auditor of JIN Limited, a multinational company dealing in spare parts. During the course of audit, CA Manidhari is facing many problems including the problem of not getting the desired information from the management. Accordingly, he decided to communicate with those charged with the governance about significant difficulties encountered during the audit. CA Manidhari seeks your guidance on matters which can be considered as significant difficulties as per SA 260. [RTP May-22]

As per SA 260, "Communication with Those Charged with Governance", significant difficulties encountered during the audit may include such matters as: