

MOCK TEST PAPER -I
FINAL COURSE: GROUP – I
PAPER – 3: ADVANCED AUDITING AND PROFESSIONAL ETHICS

All MCQs are compulsory

Question No. 1 is compulsory.

*Attempt any **four** questions from the Rest.*

Time Allowed – 3 Hours

Maximum Marks – 100

DIVISION A – MCQs (30 Marks)

Questions no. (1-10) carry 1 Mark each and Questions no. 11-20 carry 2 Marks each.

1. Mr. Kartik a practicing Chartered Accountant was engaged in conducting statutory audits, data privacy assessments and other trade compliance risk assessments for his clients. As a result, he had good knowledge of the laws and regulations applicable to an entity operating digital space. In 2022, some of his clients approached him and asked him to share his knowledge and guide them in which Technology Company they should invest in. Mr. Kartik considered their request and started providing paid advisory regarding investment in Technology and Fintech Sector stock. By the end of FY 2022, Mr. Kartik's clients made a good amount of profit based on the advice provided by Mr. Kartik.

The overall income (gross) earned by Mr. Kartik is mentioned below:

Client Name	Statutory Audit Service Fee	Other Advisory Service Fee	Investment Advisory Service Fee
Fondue Forte Pvt Ltd	-	6,57,000	2,36,200
Home Made Pvt Ltd	7,50,000	-	6,75,000
Home Fresh Pvt Ltd (Fully owned subsidiary of Home Made Pvt Ltd.)	3,45,000	-	12,50,000

Whether Mr. Kartik can do so?

- (a) Mr. Kartik is allowed to provide investment advisory services to its clients under section 144 of the Companies Act 2013. Hence, Mr. Kartik is not liable for professional misconduct.
 - (b) Mr. Kartik cannot provide investment advisory services directly or indirectly to the company or its holding company or subsidiary company as per section 144 of the Companies Act 2013. Moreover, a Chartered Accountant in Practice is not permitted to render any service which is out of the scope of the approved Management Consultancy Service.
 - (c) Mr. Kartik can provide investment advisory services directly or indirectly to the company or its holding company or subsidiary company as per section 144 of the Companies Act 2013 up to ₹ 50,00,000 in each calendar year. Hence, Mr. Kartik is not liable for professional misconduct.
 - (d) Mr. Kartik can provide investment advisory services directly or indirectly to the company or its holding company or subsidiary company as per section 144 of the Companies Act 2013 up to ₹ 5,00,000 in each calendar year. Hence, Mr. Kartik is liable for professional misconduct.
2. A branch of ABC Bank was having three staff i.e., one cashier, one officer and one manager. The cashier was responsible for the signing of cash slips, passing entries for cash withdrawals and providing cash to customers. You as a Bank's branch Auditor decided to verify the cash withdrawal transactions and after testing you decided to pass the control over the cash process. Also, there were no observations identified during the testing. Moreover, as the process is present in the branch, work performed by the cashier is not monitored on daily basis. However, on a quarterly basis, certain test checks are performed

by an officer of the branch. Internal Audit team reported the said controls over process as operating. You are required to guide whether reporting of the said controls by Internal Audit Team is correct or not

- (a) The controls over the cash process should be reported as operating because no issues were identified during the testing of controls.
 - (b) The controls over the cash process should be reported operating as test checks are being performed by officers on a quarterly basis.
 - (c) This control should be reported as non-operating because segregation of duties was not present with respect to the processing of payment transactions by the cashier.
 - (d) This control should be reported as non-operating as the manager of the branch should have at least 2 officers for test checks of cash transactions and for cash process.
3. KFintech Pvt Ltd was having paid-up share capital and reserves of ₹ 150 lakh including paid-up share capital of ₹ 90 lakh at the end of FY 20-21. During FY 21-22, KFintech borrowed ₹ 80 Lakh from Bank A and ₹ 140 Lakh from Bank B. The amount borrowed from Bank B was repaid during the same FY. For FY 20-21 the turnover of the company was ₹ 1,850 lakh. Select the appropriate option with respect to the applicability of CARO 2020:
- (a) CARO 2020 will be applicable as the paid-up capital and reserves exceeding the limit specified in the Order i.e., one crore rupees.
 - (b) CARO 2020 will be applicable as the company has paid-up capital and reserves exceeding the limit specified in the Order i.e., one crore rupees and have total borrowings exceeding one crore rupees from any bank or financial institution at any point of time during the financial year.
 - (c) CARO 2020 will not be applicable as the company repaid the amount borrowed from bank B before the end of the financial year and hence, the borrowings do not exceed the limit specified in the Order.
 - (d) CARO 2020 will not be applicable as the company will fall under the exemption provided in the Order for Small Company as per section 2(85) of the Companies Act 2013.
4. ABC & Co were appointed to conduct a forensic audit of XYZ Limited. After successfully conducting the forensic audit, ABC & Co prepared its report for the appointing authority. A copy of the report was also shared with the Board of Directors of the company. In the report, Forensic Auditors enumerated the findings of the investigation, including a summary of the evidence, a conclusion as to the amount of loss suffered as a result of the fraud and identification of those involved in fraud. The report also covered sections on the nature of the assignment, scope of the investigation, approach utilized, limitations of scope and opinions. Upon receiving the report, the Board of Directors raised objections as to how forensic auditors can mention the names of those who are involved in fraud.
- You as a Forensic Expert guide whether is it appropriate to mention the details of the person who are involved in fraud in the final report.
- (a) Report can include a section to identify those involved in fraud. This is recommendatory and in line with the appropriate practice of reporting.
 - (b) Report should not contain such details till the time it is proved in a court of law.
 - (c) Report can include a section to identify those involved in fraud but subject to prior approval of the Board of Directors of the company.
 - (d) Report should not include a section to identify those involved in fraud as it is not permitted under SA 700.
5. Which of the following statements is INCORRECT?
- (a) Inoperative saving and current accounts are a fraud prone area.

- (b) Debit balances in current account are reduced from aggregate demand deposits in balance sheet of a bank.
 - (c) Interest accrued but not due on deposits is shown separately under head "Other Liabilities and provisions."
 - (d) FCNR deposits are in designated foreign currencies only.
6. ADI Ltd. is engaged in the business of providing management consultancy services and have been in operation for the last 15 years. The company's financial reporting process is very good and its statutory auditors always issued clean report on the audit of the financial statements of the company. The auditors were required to be rotated due to mandatory audit rotation requirement of the Companies Act 2013.
- RNJ & Associates, a firm of Chartered Accountants, was appointed as the new auditor of the company for a term of 5 years and have to start their first audit for the financial year ended 31 March 2022.
- The auditors had a detailed and clear discussion with the management that they will perform their audit procedures in respect of opening balances along with the audit procedures for the financial year ended 31 March 2022.
- Management agreed with that and the audit was completed as per the plan.
- The auditors did not have any significant observations and hence they communicated to the management that their report will be clean. Management was quite happy with this and also requested the auditors to share draft report before issuing the final report.
- In the draft audit report, all the particulars were fine except 'other matters paragraph' wherein the auditors gave a reference that the financial statements for the comparative year ended 31 March 2021 was audited by another auditor. Management asked the audit team to remove this paragraph as the auditors had performed all the audit procedures on opening balances also. But the auditors did not agree with the management.
- Please advise the auditor or the management whoever is incorrect with the right guidance.
- (a) The contention of the management is valid. After performing all the audit procedures, an auditor should not pass on the responsibility to another auditor by including such references in his audit report.
 - (b) Any auditor has two options, either to perform audit procedures on opening balances or given such reference of another auditor in his report. An auditor can not mix up the things like this auditor has done. It is completely unprofessional.
 - (c) In the given situation even if the auditor wants to give such reference, the management and the auditor should have taken approval from the previous auditor at the time of appointment of new auditor. In this case, it cannot be done.
 - (d) The report of the auditor is absolutely correct and is in line with the auditing standards. An auditor is required to include such reference in his report as per the requirements of the auditing standard.
7. The following inherent limitations in an audit affect the auditor's ability to detect material misstatements except:
- (a) Test and sampling.
 - (b) Audit process permeated by judgement.
 - (c) Poor corporate governance.
 - (d) Audit evidence.
8. Vishudh & Co. is the auditor of JIN Insurance Company. The insurance company is also involved in re-insurance business and necessary provision for re-insurance premium has been made in the books of accounts. The insurance company is into a re-insurance whereby their contract relates to one particular risk and is expressed in the re-insurance policy. Each transaction is negotiated individually, and each

party has a free choice i.e. for the insurance company to offer and the re-insurer to accept. What kind of a re-insurance business is the insurance company into?

- (a) Facultative Re-insurance.
 - (b) Stop loss treaty re-insurance.
 - (c) Auto-fac re-insurance.
 - (d) Proportional treaty re-insurance.
9. SIDH Private Limited uses in-house developed application system for Accounting. The auditor observed that user ID and password is mandatory to access the application system and felt that this is a good control. What type of control is this?
- (a) IT General Control.
 - (b) Application Control.
 - (c) Detective Control.
 - (d) Preventive Control.
10. Below is an extract from the list of supplier statements as at 31st March 2022 held by the Company and corresponding payables ledger balances at the same date along with some commentary on the noted differences:

Supplier	Statement balance ₹'000	Payables ledger balance ₹'000
Shubh Company	78	66
Labh Company	235	205

The difference in the balance of **Shubh Company** is due to an invoice which is under dispute due to defective goods which were returned on 30th March 2022. **Which of the following audit procedures should be carried out to confirm the balance owing to Shubh Company?**

- (I) Review post year-end credit notes for evidence of acceptance of return.
 - (II) Inspect pre year-end goods returned note in respect of the items sent back to the supplier.
 - (III) Inspect post year-end cash book for evidence that the amount has been settled.
- (a) 1, 2 and 3.
 - (b) 1 and 3 only.
 - (c) 1 and 2 only.
 - (d) 2 and 3 only.

(10 x 1 = 10 Marks)

Questions (11-20) carry 2 Marks each

MCQ 11. -15.

Integrated Case Scenario 1

Mr. Paras has been appointed statutory auditor under Companies Act, 2013 of DEMA Limited., a company engaged in manufacturing of range of products. DEMA Limited was also listed on NSE. Besides, he was also appointed to conduct audit u/s 44AB of Income Tax Act. Mr. Chandra, relative of Mr. Paras was involved in the business of trading stocks listed on NSE. During the year FY 21-22 Mr. Chandra performed the following trades.

Name of Stock	Date of Transaction	Purchase / Sale	Quantity	FV per Share	Market Value per Share
DEMA Limited	1-4-2021	Purchase	10	10	3500
DMEA Limited	1-4-2021	Purchase	90	10	3300
DEMA Limited	30-04-2021	Sale	50	10	3600
DEMA Limited	10-05-2021	Purchase	60	10	3450
DEMA Limited	10-05-2021	Purchase	50	10	5000
DEMA Limited	11-05-2021	Purchase	10	10	5050
DEMA Limited	30-06-2021	Sale	30	10	3750

Thereafter no transaction in the shares of DEMA limited was performed by Mr. Chandra during the year.

Moreover, Mr. Paras identified a fraud related to misappropriation of cash amounting to ₹ 3 Crore in the books of the company. In this fraud, Procurement Manager and Payment Managers were together involved. As per provision of Section 143(12) Mr. Paras, reported fraud to Audit Committee within 7 days from date of identification and asked audit committee to submit their response. Audit Committee did not respond as they wanted to investigate further on this.

In the absence of any reply, audit committee and, understanding the nature of issue, Mr. Paras did not report this issue to anyone as it could impact negatively to the image of the company. Further, Mr. Paras made necessary change in their audit procedures to extent their coverage of Procurement and Payments area. After performing additional procedures over Procurement and Payment business process, Mr. Paras identified that the internal controls over the said area are significantly deficient. Mr. Paras did not communicate this finding with those Charged with Governance as he already reported about the fraud and the Audit Committee was investigating the same.

Mr. Paras also identified that the internal audit function reports directly to the management and they do not have any direct communication with those charged with governance or an officer with the appropriate authority. Also, all the findings of internal audit function are first reported to the management and then the management decides what to report to those charged with governance from the findings of internal audit function.

At the end, Mr. Paras issued a qualified opinion, and, in his report, he mentioned the following paragraph under the head "Basis of Qualified Opinion":

- a. Company has not disclosed the impact of pending litigations on its financial position in its financial statement. The impact assessed for the pending litigation is ₹ 4.5 Crore (Best Estimate).
- b. During the audit, a fraud related to misappropriation of cash amounting to ₹ 3 Crore was identified in the books of the company.
- c. Company has not made any provision, as required under any law or accounting standards, for material foreseeable losses on long term contracts including derivative contracts. During the year, as per assessment performed by an expert, the amount of provision for material foreseeable loss on long term contracts was estimated at ₹ 7 Crore for which no provision was made."

No other reference or reporting was made of these qualifications in audit report.

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

Multiple Choice Questions (5 questions of 2 Marks each):

11. Kindly guide whether Mr. Paras is eligible to be appointed as a Tax Auditor of DEMA Limited u/s 288 of the Income Tax Act, by selecting the appropriate option from below:

- (a) As per 288(2)(viii)(a) of Income Tax Act read with Section 141(3) of Companies Act, relative of Mr. Paras is holding securities of market value of ₹ 1,00,000 or more and hence Mr. Paras is not eligible to be appointed as Tax Auditor.
 - (b) As per 288(2)(viii)(a) of Income Tax Act read with Section 141(3) of Companies Act, relative of Mr. Paras is not holding securities of face value having ₹ 1,00,000 or more and hence Mr. Paras is eligible to be appointed as Tax Auditor.
 - (c) As per Section 288(2)(viii)(b) relative of Mr. Paras is indebted to the company or its subsidiary or its holding or associate company or a subsidiary of such holding company and hence Mr. Paras is not eligible to get appointed as a Tax Auditor.
 - (d) Relative of Mr. Paras is the person who is competent to verify the return under section 139 in accordance with the provisions of section 140 and hence Mr. Paras is eligible to get appointed as a Tax Auditor.
12. With respect to the qualifications (a) and (c) specified in the Audit Report, kindly guide with respect to the additional reporting requirement of these matters in audit report.
- (a) As per the Companies (Auditor's Report) Order, 2020, Auditor is required to report these matters under reporting done for Para 3(ix) of the Order.
 - (b) As per section 143(3)(j) read with Rule 11(a) & 11(b) of The Companies (Audit and Auditors) Rules, 2014, Auditor is required to report or give reference of these matters.
 - (c) Company is not required to report these matters anywhere else except for qualification under the head "Basis for Qualification"
 - (d) Company should report this matter under the head "Management Responsibilities".
13. With respect to identification of Fraud in the books of account of the company, Kindly guide Mr. Paras with respect to the appropriate reporting requirements under section 143(12) of Companies Act.
- (a) Mr. Paras should have reported the matter to Audit Committee within 2 days of identification of the fraud. However, Mr. Paras is valid in not reporting this issue further as it could negatively to the image of company.
 - (b) Mr. Paras should have reported the matter to Audit Committee and Board of Directors within 7 days of identification of the fraud. Hence, Mr. Paras did not report to Board of Director which is inappropriate.
 - (c) Mr. Paras should have reported the matter to Audit Committee within 2 days of identification of the fraud. Over and above Mr. Paras should have reported this matter to the Central Government as per prescribed rules.
 - (d) Mr. Paras should not have reported this matter to Audit Committee. Mr. Paras should have reported matter first to central government within 2 days of identification of fraud.
14. With respect to the reporting of significant deficiencies to those charged with governance, kindly guide Mr. Paras with respect to appropriate provisions in this regard.
- (a) As per SA 315, the engagement partner shall determine which matters are to be communicated to management and those charged with governance involved in the discussion.
 - (b) As per SA 265, the auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis.
 - (c) As per SA 315, the auditor should understand the communications between management and those charged with governance before communicating anything to those charged with governance.
 - (d) As per SA 450, the auditor shall communicate on a timely basis critical misstatements accumulated during the audit with the appropriate level of management, unless they are already communicated with management earlier in any form.

15. The external audit team decided to rely on and to use the work of internal audit function in the areas where more judgment was involved or where the risk of material misstatement was assessed at a higher level. Based on the above information, kindly guide the audit team regarding use of the work of internal audit function as per SA 610 by selecting the appropriate option from below:
- (a) The external auditor shall not use the work of an internal audit function if the external auditor determines that the internal audit function's organizational status and the relevant policies and procedures do not adequately support the objectivity of the internal auditors.
 - (b) The external auditors shall not use the work of an internal audit function if the external auditor determines that the internal audit function's organizational structure and relevant policies and procedures do adequately support the objectivity of internal auditors.
 - (c) The external auditor shall use the work of the internal audit function if the external auditor determines that the internal audit function applies a systematic and discipline approach including quality control while discharging their duties.
 - (d) The external auditor shall not use the work of the internal audit function is the external auditor determines that the internal audit function does not lack sufficient competence to discharge their duties.

MCQ 16. -20.

Integrated Case Scenario 2

During the planning stage of audit of Mobile & Cell Limited, the statutory auditor of the company, ABC & Co, decided:

- 1. To evaluate whether to use the work of internal audit function to gather sufficient and appropriate audit evidence for the purpose of expressing opinion on the financial statement of the company.
- 2. To perform test counts on a sample basis for Inventory Balance which was material. Also, the audit team will inquire management to provide copies of management's completed physical inventory count which will assist them in performing subsequent procedures required to determine whether inventory records accurately reflect actual inventory count results.
- 3. To perform substantive analytical procedures to gather sufficient and appropriate audit evidence for payroll cost. Audit team decided to recalculate the payroll cost by multiplying the total employees of the company with the average pay-out per employee.
- 4. To perform substantive procedures over the direct expenses which were assessed as a material with respect to the financial statement as a whole. Moreover, the number of items/transactions in direct expense were huge and of were of non-homogenous nature. As a result, audit team decided to select some samples from each identified strata disaggregated to the lowest level based on their characteristics.
- 5. The performance materiality for assessing any misstatement was fixed at ₹ 10,00,000/-.

During the audit phase the audit team identified that

- I. The internal audit function reports directly to the management and they do not have any direct communication with the those charged with governance or an officer with the appropriate authority. Also, all the findings of internal audit function are first reported to the management and then the management decides what to report to those charged with governance from the findings of internal audit function.
- II. Since last three years the company is making cash losses and is facing liquidity crisis. Moreover, there was a huge loan instalment due for repayment in next three months. Considering the company's liquidity profile, it was evident that company will default the upcoming loan instalment and the payment of interest there on. When inquired with the management as to how they will deal with this situation and how they will consider the impact of these events on management's assumption of going concern, the

management contended that the company would raise more funds through issue of fresh equity in the primary market to manage the liquidity requirements.

- III. Moreover, there was an ongoing litigation on Company and its Officers for misappropriation of loan funds. As a result, after analysing the SEBI Listing Requirements, it was evident that company was not in position to issue fresh equity in the primary market.
- IV. In one of the direct tax litigations, the adjudicating authority issued an unfavourable order against the company because of which the company was now required to pay huge fines and interest to the Tax Authority. The amount of fine and interest there on was material.
- V. The engagement manager identified that the total payroll costs booked for the period was ₹ 30,00,000/- for total 150 employees employed throughout the year from the payroll records & register. Engagement manager was able to identify that the average pay-out per employee was ₹ 20,500/-. Also, the independent expectation developed for the payroll cost was between ₹ 30,00,000/- to ₹ 32,00,000/- for the year.
- VI. The Audit team performed the testing of direct expense and following is the outcome:

Strata Name	Balance as per books	Total of sample value	No of Samples	Exception amount in samples	Reason for exception
Freight Expense	₹ 5,00,000	₹ 1,00,000	10	₹ 25,000	one invoice was incorrectly booked
Loading Charges	₹ 4,00,000	₹ 80,000	15	₹ 0	NA
Shipping Charges	₹ 9,00,000	₹ 2,70,000	10	₹ 0	NA
Packaging Expense	₹ 8,00,000	₹ 2,40,000	5	₹ 3,000	No documents were available for the said samples
Storing Expense	₹ 12,00,000	₹ 1,20,000	10	₹ 8,000	Warehouse charges were booked as storing expense. Wrong classification.
Total	₹ 38,00,000	₹ 8,10,000	50	₹ 36,000	Projected misstatement was ₹ 1,68,889/-(36,000 / 8,10,000 x 38,00,000).

- VII. Management allowed auditor to attend the physical inventory count, however, management did not allow audit team to perform any other procedure during the physical count. When inquired from management regarding the denial to the auditor from performing additional audit procedures along with attending the inventory count, the management explained that the inventory consists of very unstable chemicals and inflammable gases which require handling with skill and care. Any carelessness in handling the inventory can result in catastrophe. As a result, due to safety standards and policies, the management cannot allow the auditor to perform additional audit procedures.

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

Multiple Choice Questions (5 questions of 2 Marks each):

16. Auditor of the company decided to draw attention of the users of the audit report on the existence of the material uncertainty related to events that have casted significant doubts on the entity's ability to continue as going concern by disclosing the same in other matter paragraph. As an Engagement Quality Control Reviewer, guide the Auditor about the correct way of disclosing the existence of the material uncertainty related to events that have casted significant doubts on the entity's ability to continue as going concern when the management has not made appropriate disclosure of a material uncertainty in the financial statement.

- (a) When the management has not made appropriate disclosure of a material uncertainty in the financial statement and there exists a material uncertainty related to events that have casted significant doubts on the entity's ability to continue as going concern then the auditor should disclose the same in "Key Audit Matter" section in Audit Report only. No other disclosure is required.
 - (b) Disclosure of the material uncertainty in the financial statement is the responsibility of the management and the auditor should not comment on the same.
 - (c) When the management has not made appropriate disclosure of a material uncertainty in the financial statement and there exists a material uncertainty related to events that have casted significant doubts on the entity's ability to continue as going concern then the auditor should express a qualified or adverse opinion and should mention in the Basis of Qualified / Adverse Opinion section of the Audit Report about existence of the material uncertainty.
 - (d) When the management has not made appropriate disclosure of a material uncertainty in the financial statement and there exists a material uncertainty related to events that have casted significant doubts on the entity's ability to continue as going concern then the auditor should express an unmodified opinion and should obtain the written representation about existence of the material uncertainty from management.
17. In view of current scenario, which of the following requirements as per SA 610 are required to be fulfilled by Statutory Auditors of the Company, prior to using the direct assistance of the Internal Audit Team?
- (a) Statutory Auditors should obtain written agreement from the management of the Company, that the internal audit team will be allowed to follow the statutory auditors' instructions.
 - (b) Statutory auditors should obtain written agreement from internal audit team that his team will keep the matters confidential.
 - (c) Both a & b.
 - (d) Statutory Auditors can use the direct assistance of the internal audit team after discussing the same with the management. No prior written agreement is required.
18. Considering the inherent limitation with respect to the inventory count, the audit team decided not to perform any other procedure or not to obtain any documentary evidence from management with respect to inventory. Guide the audit team in the current scenario by selecting the appropriate option from below:
- (a) If the auditor has not obtained sufficient appropriate audit evidence as to a material financial statement assertion, the auditor shall not attempt to obtain further audit evidence.
 - (b) If the auditor has not obtained sufficient appropriate audit evidence as to a material financial statement assertion, the auditor shall attempt to obtain further audit evidence. If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall express a qualified opinion or a disclaimer of opinion.
 - (c) In case where audit team is not able to obtain sufficient and appropriate audit evidence as to a material financial statement assertion, then the auditor should appoint management's expert and should try to obtain required evidence from such expert.
 - (d) In case where audit team is not able to obtain sufficient and appropriate audit evidence as to a material financial statement assertion, then the auditor should communicate to management and should obtain written representation from them.
19. Based on the recalculation performed by the audit team, the total payroll cost arrived for the period was ₹ 30,75,000/. Analyse and guide the audit team with respect to the results obtained from the substantive analytical procedure by selecting the appropriate option from below:

- (a) The difference identified between the payroll costs derived through substantive analytical procedure and the expectation developed is material based on the materiality fixed by the audit team and hence it requires further investigation.
 - (b) The amount derived through substantive analytical procedure is not in congruence with the total amount of the payroll cost booked for the period. Hence the audit team should investigate the reasons for the difference between the amount derived and the actual cost booked.
 - (c) The total payroll cost arrived is well within the expectation developed and the difference between the amount recorded and the amount derived through substantive analytical procedure is not material. Hence, it does not require any further investigation.
 - (d) The difference identified between the amount derived through substantive analytical procedure and amount developed as an expectation is significant and the audit team should obtain appropriate written representation from management with respect to the completeness and accuracy of the amount derived through substantive analytical procedure.
20. Based on the above outcome of the direct expense testing the audit team decided to project the total misstatement on the entire balance considered for testing. As per the calculation performed, the projected misstatement was ₹ 1,68,889/-. Kindly analyse and guide the audit team with respect to the results obtained from the substantive testing by selecting the appropriate option from below:
- (a) The projected misstatement calculated is appropriate. Moreover, Based on the performance materiality and projected misstatement the auditor should modify his opinion.
 - (b) When a class of transactions or account balance has been divided into strata, then the misstatement is required to be projected for each stratum separately. Hence, the audit team's approach is incorrect with respect to the calculation of projected misstatement. The Audit team should recalculate the projected misstatement and then they should consider its impact on overall audit opinion based on the materiality.
 - (c) The audit team should have considered the exception of ₹ 8,000/- twice while calculating the projected misstatement, as the error is regarding wrong classification and the same will affect two class of transactions or balances. Hence audit team should consider revising the projected misstatement and then they should consider its impact on overall audit opinion based on the materiality.
 - (d) Audit team has appropriately calculated the projected misstatement. However, before modifying the audit opinion the audit team should obtain written representation with respect to the completeness and accuracy of the direct expense balance which could serve as a sufficient and appropriate.

(10 x 2 = 20 Marks)

Division B- Descriptive Questions-70 Marks

Question No. 1 is compulsory.

Attempt any **four** questions from the Rest.

1. (a) NEMI Limited (manufacturer of textile goods) got an order of manufacturing of PPE kits in December 2021. But there was shortage of machinery and manpower to accomplish the ordered requirement of PPE kits. NEMI Limited approached another manufacturing unit Rathnemi Limited for purchase of the unit. Rathnemi Limited was interested in the sale of unit, so the deal went through, and NEMI Limited acquired ninety five percent shares of Rathnemi Limited. The new management of Rathnemi Limited proposed and appointed Mani Associates, Chartered Accountants, (already auditors of NEMI Limited) as new auditors of Rathnemi Limited. Mani Associates accepted the assignment without considering information whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate. Comment with respect to appropriate Standard on Auditing what type of information assists the engagements partner in determining whether the conclusions reached

regarding the acceptance and continuance of client relationships and audit engagements are appropriate or not? **(5 Marks)**

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

The Company, however, filed an appeal with higher tax authorities against the demand and the matter is undecided as on 31.03.2022. Legal team of the Company anticipated that tax liability might mature. The Company has not made a provision of anticipated tax liability. Considering the provisions of Companies Act, 2013, how an auditor of RST Ltd. should see this matter and report in audit report, if required? **(5 Marks)**

- (c) OM Limited is availing the services of APP Private Limited for its payroll operations. Payroll cost accounts for 65% of total cost for OM Limited. APP Limited has provided the type 2 report as specified under SA 402 for its description, design and operating effectiveness of control.

APP Private Limited has also outsourced a material part of payroll operation M/s PMS & Associates in such a way that M/s PMS & Associates is sub-service organization to OM Limited. The Type 2 report which was provided by APP Private Limited was based on carve-out method as specified under SA 402.

CA Sheetal while reviewing the unmodified audit report drafted by his assistant found that, a reference has been made to the work done by the service auditor. CA Sheetal hence asked his assistant to remove such reference and modify report accordingly.

Comment whether CA Sheetal is correct in removing the reference of the work done by service auditor? **(4 Marks)**

2. (a) While auditing the complete set of consolidated financial statements of Moksh Ltd., a listed company, using a fair presentation framework, XYZ & Co., a Chartered Accountant firm, discovered that the consolidated financial statements are materially misstated due to the non-consolidation of one of the subsidiary. The material misstatement is deemed to be pervasive to the consolidated financial statements. The effects of the misstatement on the consolidated financial statements could not be determined because it was not practicable to do so. Thus, XYZ & Co. decided to provide an adverse opinion for the same and further determined that, there are no key audit matters other than the matter to be described in the Basis for Adverse Opinion section. Comment whether XYZ & Co. needs to report under SA 701 'Communicating Key Audit Matters in the Independent Auditor's Report'? **(5 Marks)**

- (b) While conducting the tax audit of Rajul Ltd. you observed that company has timely filed ETDS return for TDS deducted on salary under section 192 of the Income Tax Act, 1961 in form 24Q in respect of fourth quarter period from 1st January 2022 to 31st March 2022. The company has not furnished list of details which are not reported in the statement of tax deducted at source under the pretext that TDS statements are furnished within the prescribed time. As a Tax Auditor of Rajul Ltd. how you would deal and report? **(5 Marks)**

- (c) CA Rani has been appointed as Forensic Auditor by ATM Bank Limited for one of its borrowal accounts FAR Ltd. CA Rani started the audit by first reviewing the transactions of the borrower in Bank statement as per Bank records to identify any hidden patterns in that information. She had to review huge volume of data, as the number of transactions per day were in hundreds and the data was to be reviewed for the last three years. So, she was stuck up as to how to proceed further to identify any hidden patterns in information, if any. Guide CA Rani, suggesting which technique to be used for identifying any hidden patterns in the information. **(4 Marks)**

3. (a) You are an auditor of Fair Insurance Company Ltd. which offers variety of risk management products to business entities wishing to protect their business activities against losses due to various probable risks. Fair Insurance Company Ltd. is in the process of offering to Guru Ltd., a multinational group having worldwide market, "Trade Credit Insurance Policy" to cover domestic risk export risk and political risk. You as an auditor of Insurance Company have been requested to ensure that all the requirements have been met by Fair Insurance Company Ltd. before Trade Credit Insurance Product is offered to Guru Ltd. List down those requirements. **(5 Marks)**
 - (b) "What constitutes a 'true and fair view' is the matter of an auditor's judgement in particular circumstances of a case." Do you agree? Enlist the requirements you as an auditor will observe to ensure true and fair view. **(5 Marks)**
 - (c) AJ & Associates and PK & Co., chartered accountant firms have joined the Network firm A to Z & Affiliates registered with Institute. AJ & Associates was statutory auditor of B Ltd. for last 10 years. Due to rotation of auditor as per section 139 (2) of Companies Act, 2013, B Ltd. retires AJ & Associates and appoints PK & Co., as auditor for the year 2020-21. Comment as per Chartered Accountant Act, 1949 - Guidelines for Networking. **(4 Marks)**
 4. (a) Shreyansh & Co LLP, a firm of Chartered Accountants, was appointed as auditor of an NBFC. The audit work has been completed. The audit team which was involved in the fieldwork came across various observations during the course of audit of this NBFC and have also limited understanding about the exceptions which are required to be reported in the audit report. They would like to understand in detail regarding the obligations on the part of an auditor in respect of exceptions in his report so that they can conclude their work. Briefly explain. **(6 Marks)**
 - (b) Employees of BIG Ltd. have to travel frequently for business purposes, so the company entered into a contract with a Chinmay Travels Ltd. for managing booking, cancellation and other services required by their employees. As per contract terms, Chinmay travels has to raise its monthly bills for the tickets booked or cancelled during the period and the same are paid by BIG Ltd. within 15 days of the bill date. The bills raised by Chinmay travels were of huge amount, so the management of BIG Ltd. decided to get an audit conducted of the process followed for booking/ cancellation of tickets and verify the accuracy of bills raised by the travel agency. Which audit do you feel the management should opt for? Also briefly discuss the qualities the auditor should possess for such audit. **(4 Marks)**
 - (c) Mr. Gautam & Mr. Mahaveer, partners of a Chartered Accountant Firm, one in-charge of Head Office and another in-charge of Branch at a distance of 80 km. from the municipal limits, puts up a name-board of the firm in both premises and also in their respective residences. Comment with reference to the Chartered Accountants Act, 1949, and Schedules thereto. **(4 Marks)**
 5. (a) Mr. Bharat was appointed as statutory auditor of N Limited and O Limited. Both the Companies were having their base in Mumbai they had recently listed their shares on the Stock Exchange. For the financial year 2021-22, Mr. Bharat had signed limited review reports for each quarter, till the quarter ended 31st December 2021 for both the companies. Owing to his personal commitments and increased workload, he tendered his resignation to N Limited on 30th January 2022 and asked the Company to appoint another auditor to issue audit report for the remaining quarter and the FY 2021-22 as a whole. But the management of the Company did not accept the same.
- Mr. Bharat continued to as act as auditor for O limited. During the 1st week of March 2022, Mrs. D (wife of Mr. Bharat) had borrowed a sum of ₹ 5.15 lakh from the Company for her personal use. Having come to know about this, Mr. Bharat immediately informed the management that he had been disqualified to act as auditor and told them that he won 't issue audit report for last quarter. But management of the Company argued that it's the legal responsibility of Mr. Bharat to do the same.

Whether contention of management of N Limited and O Limited is justified in asking Mr. Bharat to issue audit report for the last quarter and the FY 2021-22 as a whole, despite his resignation? Please comment on the above. **(5 Marks)**

- (b) CA Ram have been doing audit of branch of RICH Bank Ltd. The principal business of the branch is lending advances to large corporates. Since last one year, many large accounts have become Non-Performing Asset (NPA) as per guidelines. The Management of the Bank decided to sell one of the NPA account and consequently one NPA namely Shiva Ltd. amounting to ₹ 11.00 Crore was sold to Asset Reconstruction Company. What audit points CA Ram should keep in mind while doing audit of this transaction? **(4 Marks)**
- (c) CA. Bahubali is Special Executive Magistrate. He also took over as the executive chairman of Software Company on 1.4.2022. He is also a leading income tax practitioner and consultant for derivative products. He resides in Chennai near to the ION commodity stock exchange and does trading in commodity derivatives. Every day, he invests nearly 36% of his time to settle the commodity transactions. He has not taken any permission for becoming Special Executive Magistrate. However, he has got special permission of Council of ICAI for becoming executive chairman and for trading in commodity derivatives. Is CA. Bahubali liable for professional misconduct? Comment with reference to the Chartered Accountants Act, 1949, and Schedules thereto. **(5 Marks)**
6. (a) Shravasti Limited is a public sector undertaking engaged in production of electricity from solar power. It had commissioned a new project near Mumbai with a new technology for a cost of ₹ 9,580 crore. The project had seen delay in commencement and cost overrun. State the matters that a Comprehensive Audit by C&AG may cover in reporting on the performance and efficiency of this project. **(5 Marks)**
- (b) In assessment procedure of M/s Dim Ltd., Income Tax Officer observed some irregularities. Therefore, he started investigation of Books of Accounts audited and signed by Mr. O, a practicing Chartered Accountant. While going through books he found that M/s Dim Ltd. used to maintain two sets of Books of Accounts, one is the official set and other is covering all the transactions. Income Tax Department filed a complaint with the Institute of Chartered Accountants of India saying Mr. O had negligently performed his duties. Comment. **(5 Marks)**
- (c) NEW Limited is a listed company having its operation across India. NEW Limited appointed Mr. N, Mr. E and Mr. W, as its joint auditors for the year 2021-22. After making sure that all of them are qualified to be appointed as statutory auditor, NEW Limited issued engagement letter to all of them. But Mr. N was not clear on some points, so he requested NEW Limited to slightly change the terms of his engagement. This change will not impact the ultimate opinion on the financial statement. The engagement letter contains the details on objective and scope of audit, responsibilities of auditor and identification of framework applicable. It also contains the reference to expected form and content of report from all three joint auditors. In your opinion what was the discrepancy in the Audit engagement letter issued by NEW Limited? **(4 Marks)**

OR

Evaluating the professional judgment exercised by the auditor is one of the important aspects under Quality review, please explain the situation with reference to applicable SA.