

MOCK TEST PAPER - 2
INTERMEDIATE (IPC) GROUP – II
PAPER – 6: AUDITING AND ASSURANCE

Time Allowed – 3 Hours

Maximum Marks – 100

Division A- Multiple Choice Questions

Case Scenario 1 carries 10 Marks

Case Scenario 2 carries 10 Marks

Total 30 Marks

General MCQs carry 2 Marks each

Case Scenario 1

Mars Ltd. is a public limited Company incorporated during the previous financial year 2019-20. R S Shah & Associates have been appointed as the Auditors of the Company. CA R and CA S are the partners of the Firm.

Para 1

Its Authorized Capital was ₹ 75 Lacs. Subsequently it increased its Share Capital. They issued Shares at a premium of ₹25/- per share. The Company has transferred the amount received as premium to the Securities Premium Account.

Para 2

CA R recommended his Engagement Team to prepare an Audit Strategy as well as Audit plan for efficient conduct of audit. He advised to the team that they should include a series of verification procedures to be applied to Financial Statements of the Company for accomplishing the Audit objectives. CA R illustrated to his team the relationship between Audit strategy as well as Audit plan.

Para 3

Ten Field Pvt. Ltd approached the firm R S Shah & Associates for undertaking their Audit Assignment. The paid up capital of the Company is ₹150 Crores. The Firm R S Shah & Associates is also desirous of taking up the Assignment. The Firm R S Shah & Associates hitherto is auditing 42 Companies that includes 2 Dormant Companies and 1 Pvt Ltd Company having paid up Capital of ₹75 Crores. They were in a dilemma as whether they would be eligible for appointment or not?

Para 4

R S Shah and Associates have been appointed as Auditors of a large Enterprise namely Search Results Ltd. Considering the overhaul required in the Organization's Risk Management, Directors of the listed companies braced the subject of Internal Financial Control with much seriousness and rigor. The dawn of the Financial Year lays down the daunting task of establishing and implementing Internal Financial Control in an Enterprise.

Para 5

The role of an Auditor, in general, is no walk in the park. Having been regarded as a certified professional, the Auditor has placed himself responsible to various parties and the duties that go with it. Responsibilities as well as duties of Auditor go hand in hand. Provisions of Companies Act 2013, confer rights, responsibilities and duties on an Auditor. The Auditor should comply with Accounting Standards.

1. Sec. 52 of the Companies Act states that Security Premium Account can be applied by the Company for one of the purpose mentioned below. Which of the following is an INCORRECT option?
 - (a) To write off preliminary expenses of the Company

- (b) To pay dividend to equity shareholders
 - (c) To provide premium on redemption of Preference share capital
 - (d) To purchase its own shares or other securities under Sec 68(Buyback)
2. With reference to para 2, which of the following Statement is inappropriate?
- (a) Once the overall audit strategy is established, an audit plan can be developed to address the various matters identified in the overall audit strategy.
 - (b) The establishment of overall audit strategy as well as detailed audit plan is a discrete and sequential process.
 - (c) Audit Strategy and Audit plan are inter-related as changes in one may result in consequential changes to the other.
 - (d) The Audit plan is more detailed than the Audit Strategy that includes the nature, timing and extent of audit procedures to be performed by engagement team members.
3. With reference to information given in para 3, can you please elucidate the Partners of the Firm with regard to their question of whether they can accept the new Audit Assignment of Ten Field Pvt. Ltd.?
- (a) No the Firm cannot accept the Audit assignment as they have exceeded the ceiling on number of Audits to be accepted.
 - (b) Yes, the Firm can accept the Audit assignment as provisions pertaining to ceiling on number of Audit apply only to Public Companies.
 - (c) The provisions of Sec 141(3)(g) apply to individual Auditor and not the Firm as a whole, hence not applicable.
 - (d) Yes, the Firm can accept the Audit assignment as their appointment would be in conformity with the provisions of Sec 141(3)(g) of Companies Act 2013.
4. With reference to para 4, which of the following point ensures implementation of policies and procedures with regard to Internal Financial Control by the Companies?
- (a) Reliability of Financial Reporting
 - (b) Effectiveness and efficiency of operations
 - (c) Compliance with applicable laws and regulations
 - (d) All of the above.
5. With reference to Para 5 above, it is the -----of the Auditor to comply with the Accounting Standards? Which of the following option is appropriate?
- (a) right
 - (b) duty
 - (c) both duty and right
 - (d) moral responsibility

(5 x 2 = 10 Marks)

Case Scenario 2

A Partnership Firm of Chartered Accountants by the name of S K and Associates were appointed as the Auditors of the Company named Big Box Ltd.

Para 1

Big Box Ltd is a Public Listed Company. The CA Firm comprised of 2 partners namely CA S and CA K. Subsequently, a close relative of CA K, acquired security having face value ₹495000/- of Big Box Ltd. As per

the provisions of Section 141 of the Companies Act 2013, an Auditor will be disqualified from appointment, if the Auditor himself or his relative acquires the security exceeding the prescribed limit in the Company.

Para 2

Further, the Auditors, S K and Associates also had to bank on the policies and procedures adopted by the Company for ensuring the efficient conduct of its business. They have to state about the adequacy of Internal Financial Controls in the Company. The Company had a turnover of ₹ 60 Crores as per the latest Audited Balance Sheet and its Borrowings during the year were ₹ 20 Crores from Banks.

Para 3

The CFO of the Company, Mrs. Darshana felt dubious in the Accounts department of the Company. She entreated the Auditors to perform a thorough investigation of the Accounts department. Mrs. Darshana was also anticipating a fraud in this situation. Both the Auditor as well as the CFO of the Company analyzed the various risk factors. The Auditors observed that the Head Accountant of the Department has inflated the Sales amount to finish his targets. There was collusion between the Head Accountant & Employees of the Company. Employees were presented incentives on accomplishing their targets. This resulted in a fraud by the Head Accountant of amount aggregating to ₹75 Lacs.

Para 4

Big Box Ltd falls under the class of Companies to constitute Audit Committee. It consisted of Directors including the Independent Directors, CFO, Company Secretary as well as the Internal Auditor. Audit Committee helps in ensuring better standards of Corporate Governance. The Audit Committee executes various functions. Sec 177 of the Companies Act 2013, states various functions of Audit Committee.

Para 5

Big Box Ltd. is expanding its business. Consequently it requires many Computers. Purchasing computers may involve paying a huge upfront cost. Cash flow may get disrupted. Hence the Company came up with an idea of getting the Computers on lease. It will allow the businesses to have access to the latest technology without harming their cash flow.

The Auditors explained to the Directors that leasing Computers shall come under the purview of Operating Lease.

1. With reference to para 1, S K and Associates can take corrective actions within _____ days. The relative may hold security or interest in the company of face value not exceeding _____
 - (a) 45 days, Face Value ₹100000/-
 - (b) 60 days, Market Value ₹500000/-
 - (c) 30 days, Face Value ₹ 500000/-
 - (d) 60 days, Face Value ₹100000/-
2. The Auditors of S K and Associates were doubtful concerning the applicability of Internal Financial Controls in the Company Big Box Ltd. With reference to details provided in Para 2 above, please guide them in this regard.
 - (a) It will be applicable as Turnover exceeds the threshold limit of ₹50 Crores.
 - (b) It is not applicable as the Borrowings are less than 25 Crores during the financial year.
 - (c) It will be applicable as the Company is a Public Listed Company.
 - (d) Reporting on Internal Financial Control is not under the scope of Auditors reporting. Hence, Not Applicable.

3. With reference to para 3, wherein a fraud was observed by the Auditor, what should be the course of action of the Auditor?
- (a) The Auditor should report the fraud details to Central Government.
 - (b) The Auditor shall report the fraud to the audit Committee or to the Board within the prescribed time.
 - (c) The Auditor shall disclose it in the Audit Report and report the fraud details to RBI too.
 - (d) Both a & c above.
4. With regard to information provided in Para 4, which of the following functions the Audit Committee abstains from performing?
- (a) Terms of appointment of the auditor of the Company.
 - (b) Management Compensation
 - (c) Examination of financial statements and auditor's report thereon
 - (d) Monitoring Auditor's independence & effectiveness of audit process.
5. In reference to para 5, which among the following is an INCORRECT trait about the Operating Lease?
- (a) The Lessee does not have the option to buy the asset during the lease period.
 - (b) The Lessee cannot claim Depreciation on the leased asset.
 - (c) The Lessee generally bears the Insurance, Maintenance and Taxes.
 - (d) The Lease term generally extends to less than 75% of the projected useful life of the leased asset.

(5 x 2 = 10 Marks)

General MCQs

1. If the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted by management to continue the original audit engagement, the auditor shall:
- (a) Withdraw from the audit engagement where possible under applicable law or regulation;
 - (b) Determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators.
 - (c) Withdraw from the audit engagement where possible under applicable law or regulation and determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators.
 - (d) Withdraw from the audit engagement where possible under applicable law or regulation or determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators.
2. Audit documentation provides:
- (a) evidence of the auditor's basis for a conclusion about the achievement of the overall objectives of the auditor; or evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.
 - (b) evidence of the auditor's basis for a conclusion about the achievement of the overall objectives of the auditor; and evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.
 - (c) evidence of the auditor's basis for a conclusion about the achievement of the overall objectives of the auditor

- (d) evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements.
3. Audit evidence includes
- (a) information contained in the accounting records underlying the financial statements
 - (b) both information contained in the accounting records underlying the financial statements and other information.
 - (c) other information.
 - (d) information contained in the accounting records underlying the financial statements or other information.
4. Risk of material misstatement may be defined as the risk
- (a) that the financial statements are materially misstated after audit.
 - (b) that the financial statements are materially misstated during audit.
 - (c) that the financial statements are materially misstated prior to audit.
 - (d) All of the above
5. Statement I : A capital reserve cannot be utilised for writing down fictitious assets or losses or (subject to provisions in the Articles) for issuing bonus shares if it is realized.
- Statement II : The amount of securities premium or capital redemption reserve account can be utilised only for the purposes specified in Sections 52 and 55 of the Companies Act, 2013, respectively.
- (a) only Statement I is correct
 - (b) only Statement II is correct
 - (c) both the statements are correct
 - (d) both the statements are incorrect.
- (5 x 2=10 Marks)**

Division B- Descriptive Questions

Question No. 1 is compulsory.

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

Total 70 Marks

1. Examine with reasons (in short) whether the following statements are correct or incorrect : (Attempt any **7 out of 8**)
- (i) The preparation of financial statements involves judgment by management.
 - (ii) Evolving one audit programme applicable to all business under all circumstances is not practicable
 - (iii) Inquiry alone ordinarily does not provide sufficient audit evidence.
 - (iv) The SAs do not ordinarily refer to inherent risk and control risk separately.
 - (v) Intentional errors are most difficult to detect and auditors generally devote greater attention to this type
 - (vi) All automated environments are not complex.
 - (vii) Dividends are recognized in the statement of profit and loss only when the amount of dividend can be measured reliably.

- (viii) When auditing in an automated environment, inquiry is often the most efficient and effective audit testing method. **(7 x 2 = 14 Marks)**
2. Discuss the following:
- The Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971 provides certain powers to the C & AG in connection with performance of his duties. Discuss. **(4 Marks)**
 - Fraud in the form of misappropriation of goods is still more difficult to detect. Explain. **(4 Marks)**
 - Section 71 of the Companies Act, 2013 lays down the requirement of appointment of debenture trustee by the company to protect the interest of debenture holders. Mention the duties of debenture trustee in this regard. **(3 Marks)**
 - CA X is not sure about the kind of Sampling method to be used for audit of a company. Advise him about the choice of methods (name of methods only) of Sampling to be used in various circumstances. Also explain briefly the advantages of the Sampling to be used by him in auditing. **(3 Marks)**
3.
 - As per SA 220, "Quality Control for an Audit of Financial Statements" the auditor should obtain information considered necessary in the circumstances before accepting an engagement with a new client. Explain stating clearly the information that would assist the auditor in accepting and continuing of relationship with the client. **(4 Marks)**
 - In establishing overall audit strategy, the auditor shall ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required. Elucidate those cases by which auditor can ascertain the reporting objectives of the engagement. **(4 Marks)**
 - The auditor has no obligation to perform any audit procedures regarding the financial statements after the date of the auditor's report. However, when, after the date of the auditor's report but before the date the financial statements are issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of the auditor's report, may have caused the auditor to amend the auditor's report. Explain the auditor's obligation in the above situation. **(3 Marks)**
 - Explain how a statutory auditor of a company can apply analytical procedures at the planning phase of audit. **(3 Marks)**
4.
 - Explain the meaning of internal financial controls as per the Companies Act, 2013. Also explain its objectives. **(4 Marks)**
 - The auditor may choose to analyse the monthly trend for Power & Fuel expense. Explain how this analysis will be performed by the auditor. **(4 Marks)**
 - Write the audit Procedure for verification of existence of Trade Receivables. **(6 Marks)**
5.
 - Management of Z Ltd. wants to include all the cost incurred by the Company in valuing the cost of its inventories. The Accountant is, however, of the view that certain costs should be excluded from the cost of inventories and should be recognised as expenses for the period in which they are incurred. What are such costs that should be excluded while determining the cost of inventories? **(4 Marks)**
 - Enumerate the circumstances under which the retiring auditor can be re-appointed. **(4 Marks)**
 - State the matters to be included in auditor's report as per CARO, 2016 regarding:
 - Default in repayment of loan or borrowing to a financial institution, bank etc.
 - Fraud by the company or on the company by its officers or employees. **(3 Marks)**

- (d) Mention the examples of circumstances where the auditor may consider it necessary to include an Emphasis of Matter paragraph. **(3 Marks)**
6. (a) Mention any eight financial events or conditions that, individually or collectively, may cast significant doubt on the Going Concern assumption of an entity. **(4 Marks)**
- (b) What is the function of audit while examining various rules, regulations and orders with regard to Audit against Rules & Orders by C&AG? **(4 Marks)**

OR

- (c) (i) List out the types of Revenue Grants received by local bodies from the State administration. **(2 Marks)**
- (ii) PQR Ltd., a government company, constructed a building in conformity with rules and regulations for installing a telephone exchange but not used for the same purpose resulting in the infructuous expenditure.
- Considering the above case, explain the type of expenditure audit to be performed to curb the situation. **(2 Marks)**
- (d) In the course of audit of SMP Limited for the financial year ended 31st March, 2020 you have observed as an auditor that the company has provided a sum of ₹ 20 Lakhs in the books of account as Gratuity payable to employees based on certificate obtained from an actuary. Give your comments with reference to the Standard on Auditing. **(3 Marks)**
- (e) Explain the objectives of the auditor regarding written representations. **(3 Marks)**