

MOCK TEST PAPER -II
FINAL (OLD) 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.

- KB Associates a chartered accountant firm has been appointed as an auditor of the company for the financial year 2020-21. It consists of two partners CA K & CA B. CA K is brother of the father of the finance director of the company. CA B is an old friend of the finance director of the company.
What kind of ethical threat is associated with appointment of KB Associates as an auditor of ABC LTD.?
 (a) Self Interest Threat.
 (b) Advocacy Threat.
 (c) Familiarity Threat.
 (d) Self-Review Threat.
- The audit team has obtained the following results from the trade receivables circularization of Nemi Co for the year ended 31 March 2021.

Customer	Balance as per sales ledger	Balance as per customer confirmation	Comment
	Rs.	Rs.	
AM Co	2,25,000	2,25,000	
AN Co	3,50,000	2,75,000	Invoice raised on 29 March 2021
AO Co	6,20,000	4,80,000	Payment made on 30 March 2021
AP Co	5,35,000	5,35,000	A balance of Rs. 45,000 is currently being disputed by AP Co.
AR Co	1,78,000	No reply	

Which of the following statements in relation to the results of the trade receivables circularisation is TRUE?

- No further audit procedures need to be carried out in relation to the outstanding balances with AM Co. and AP Co.
- The difference in relation to AN Co. represents a timing difference and should be agreed to a pre-year-end invoice.
- The difference in relation to AO Co. represents a timing difference and should be agreed to pre-year-end bank statements.
- Due to the non-reply, the balance with AR Co. cannot be verified and a different customer balance should be selected and circularized.

3. Mr. R, (friend of Mr. P) a CA in practice invited Mr. P to set up a 'Network Firm' along with 2 more friends. All the four auditors agreed to the same and decided to start a network firm by the name M/s RP & Co. However, one of the auditors suggested that they cannot use the term '& Co.' and it needs to be changed. But Mr. R informed that there is no such Regulation regarding the firm's name. Which among the name shall be suitable to the newly started 'Network Firm', in accordance with the provisions of Chartered Accountant Act and Regulation?
 - (a) RP and Co.
 - (b) RP & Associates.
 - (c) RP and Networks.
 - (d) RP & Affiliates.

4. AJ Associates a chartered accountant firm is acting as an auditor of the XYZ Ltd. Provisions of the cost audit are also applicable to the XYZ Ltd. Two years ago, ABC Associates was appointed as cost auditor of the XYZ Ltd. However, this year due to some reason the Cost Auditor firm resigned. The management being of the opinion that AJ Associates being the auditor of the company knows everything about the company so AJ Associates should be appointed as the cost auditor of the XYZ Ltd for the current year. Select the correct statement with respect to the appointment of AJ Associates as the cost auditor of the Company?
 - (i) Practicing CA/CWA/CMA can be appointed as cost auditor of the company, so appointment of AJ Associates as cost auditor being a company auditor is valid.
 - (ii) Only Practicing CWA/CMA can be appointed as cost auditor of the company, but appointment of AJ Associates as cost auditor being a company auditor is invalid.
 - (iii) Company Auditor can be appointed as cost auditor subject to fulfilment of certain conditions as specified under section 148 of the Companies Act 2013.
 - (iv) Company Auditor cannot be appointed as cost auditor of the company.
 - (a) (i) and (ii).
 - (b) (ii) and (iv).
 - (c) (ii) and (iii).
 - (d) (i) and (iv).

5. During the conduct of audit, it was found that the management has intentionally made material misstatements in the several items of the financial statements to deceive the users of the financial statements, to reduce the pressures of meeting market expectations and to increase the reputation of the company. What would be the implications on the auditor's report if no adjustments are made to the financial statements regarding the misstatements made by the management?
 - (a) The auditor would issue a qualified audit opinion stating that 'except for' these matters the financial statements are fairly presented. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.
 - (b) The auditor would issue an adverse audit opinion stating that 'except for' these matters the financial statements are fairly presented. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.
 - (c) The auditor would issue an adverse audit opinion stating that financial statements 'do not give a true and fair view'. The auditor should also include a 'Basis for Adverse Opinion' paragraph below the opinion paragraph.

- (d) The auditor would issue an adverse audit opinion stating that financial statements 'do not give a true and fair view'. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.
6. While verifying the salary expense of employees, the auditor has been asked to rely on the values as per SAP software and some hard copy reports and documents as the HRMS package (source software) has become corrupt during the year and the management is not having any data backup. How should the auditor deal with this issue?
- The auditor should issue a disclaimer of opinion as records are destroyed and he is unable to obtain sufficient appropriate audit evidence.
 - The auditor should perform alternative procedures to obtain sufficient and appropriate audit evidence before disclaiming the opinion.
 - The auditor should issue an adverse opinion stating that it is deficiency in internal controls.
 - The auditor can rely on the SAP data and there is no need for qualification of report.
7. You are the audit manager of Ranker & Co are responsible for the audit work to be managed for the fixed assets of the company. Ranker & Co has 5 properties amounting to Rs.11.5 crore. One of the important tasks ahead for you is to confirm the ownership of these properties.
- Which of the following would provide the most persuasive evidence of the ownership?
- To conduct a physical inspection of all the properties located at different areas.
 - To ask the management registration documents of these properties and inspect and verify them.
 - To check whether all the properties are recorded properly in the fixed asset register and depreciation has been calculated correctly.
 - Enquire with the management if these properties are insured and review the insurance documentation.
8. ABC 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?
- IT General Control.
 - Application Control.
 - Detective Control.
 - Preventive Control.
9. While examining the computation of Demand and Time liabilities which of the following is to be included in liabilities:
- Part amounts of recoveries from the borrowers in respect of debts considered bad and doubtful of recovery.
 - Amounts received in Indian Currency against import bills and held in sundry deposits pending receipts of final rates.
 - Net credit balance in branch adjustment accounts including these relating to foreign branches.
 - Margins held and kept in sundry deposits for funded facilities.
10. In Case of PSU, Direct Reporting Engagement does not include
- Performance audits.
 - Compliance audits.

- (c) Financial audits.
- (d) Comprehensive Audit.

(10 x 1 = 10 Marks)

Questions (11-20) carry 2 Marks each

MCQ 11. -15.

Integrated Case Scenario 1

Arogya Pradhan Limited is a public company incorporated in September 2011 with a registered office in Chennai. The company is in business of Healthcare services. The company has 151 Ayurvedic clinics and 303 Ayurvedic pharmacies throughout the country.

In the previous year, company achieved turnover of Rs. 3,000 crore and had earned the Net Profit of Rs. 25 crore. The company had borrowed a term loan of Rs. 100 crore from State Bank of India.

M/s Bright Moon LLP are appointed as statutory Auditors of the company for the year 2019-20. After completing the initial engagement procedures and audit planning, the audit team started with the verification of Internal Financial Controls of the company.

While understanding the controls established by the management in the 'Revenue Process', the audit team observed that there is only one Review Control wherein 20 executives had to prepare the sales invoice and Mr. Darshan - Sales Manager, had to review and authorise all the invoices. It was observed that on many occasions, Mr. Darshan had more than 1000 invoices to authorise in a single day. Further, he has frequently asked 2 senior most executive to review pending invoices and he has relied on them by directly giving his authorization on the invoice. It was observed that Mr. Darshan did not take any leave during the entire year. It was observed that Mr. Darshan's performance bonus was linked with number of invoices authorised by him. In addition, Mr. Darshan was the sole authority to approve the sales commission and sales discount which was to be applied by the customers.

The audit team has set Rs. 30 crore as materiality based on 1% of Turnover. For selecting the samples, Mr. Santosh – Audit Executive, used the below mentioned formula:-

$$\frac{\text{Ledger Balance} * 100}{\text{Materiality} * 365 \text{ days}}$$

Mr. Santosh selected 30 samples for the verification of above mentioned "Review Control". It was observed that out of 30 samples, 20 samples had irregularities in invoices which was clearly due to improper functioning of review control. The amount of irregularity in 20 invoices amounted to Rs. 4 crore. The auditor still issued the clean audit report and took the written representation letter from the management for efficient implementation of Internal Financial Controls.

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. Is the Control "Designed" appropriately?
 - (a) No, because there are irregularities amounting to Rs. 4 crore in the samples selected by Auditors.
 - (b) No, because Mr. Darshan's performance bonus is linked with number of invoices authorised.
 - (c) No, because there are no leave taken by Mr. Darshan during the entire year.
 - (d) Yes. 'Review Control' is designed appropriately.
12. Is the Control "Implemented" effectively?
 - (a) No, because Mr. Darshan delegates his work of review to other executives who are senior in experience.
 - (b) No, because Mr. Darshan is heavily burdened with excessive work.

- (c) No, because Mr. Darshan is authorized to finalize sales commission and sales discount.
 - (d) Yes. 'Review Control' is implemented appropriately.
13. In the above case, to whom should M/s Bright Moon LLP report first?
- (a) To ROC.
 - (b) To Central Government u/s 143(12) of Companies Act, 2013 as the impact in above case is more than Rs. 1 crore.
 - (c) To Those Charged with Governance.
 - (d) To Shareholders as they are the appointing authority.
14. How samples are to be selected for the purpose of verification of Internal Financial Control?
- (a) Monetary Unit Sampling.
 - (b) Sampling based on Materiality.
 - (c) Sampling based on probability of default of the control.
 - (d) Sampling based on frequency of functioning of control.
15. In the current scenario, how should M/s Bright Moon LLP report?
- (a) Clean Report with Other Matter paragraph.
 - (b) Clean Report with Emphasis of Matter paragraph.
 - (c) Clean Report with reporting in Key Audit Matter.
 - (d) Qualified Report (both main report and ICFR report).

MCQ 16. -20.

Integrated Case Scenario 2

Andy & Co; a reputed Chartered Accountants firm is appointed as a statutory auditor of Manava Swaroopam Limited. The Company is into manufacturing of copper products. The company has advanced in all its endeavours by supplying million Copper units. The company has incorporated another company "Daiva Swaroopam Private Limited" by investing 45% in the share capital of the company and at the same time having 100% control over the Board of Directors as per the agreement with the majority shareholder. The company is listed in the US Stock Exchange but in the process of listing in the Indian Stock Exchanges, having a net worth of INR 245 crore. The product is promoted by Ali Baba, as its product Brand Ambassador. You are the audit manager in-charge of the audit team this year and your 1st year trainee asks you the following questions listed down. He has also noted down some of the questions for you to answer to discuss the impact on the planning stage after understanding the entity and its environment:

- The company is required to appoint the Internal Auditor as per provisions of the Companies Act, 2013 and the company complied with the same by delegating the duties to an employee, who joined the company as 1st year Architect. The audit team is planning to use the work performed by the Internal Audit function as the reports given by him are designed in a marvellous fashion. Even the Board of Directors are astonished by the design of the Internal Audit report.
- The company is planning to use the working papers of the previous auditor by demanding the audit working papers from him citing the confidentiality clause. The auditor also plans to use the same for testing the opening balances during the year. The previous year auditor having been appointed as the auditor of subsidiary; the company plans to use his work for verifying the investment balance during the year.

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. The engagement partner has requested you to comment upon the usage of work of Internal auditor by the engagement team in accordance with relevant Standard on Auditing:
- (a) As the work done by the internal auditor is marvellously designed and presented the same can be considered to the extent the statutory auditor can use it. As the work is highly appreciated even by the Board of Directors, the same should be definitely used by Andy & Co.
 - (b) The work done by the Internal Auditor need to be assessed for the sufficiency and should be used to avoid the double work. The audit team of Andy & Co need to reduce the unnecessary work as the same has been performed by the other auditor.
 - (c) The auditor is required to assess the competence and professional care of the work performed by the Internal Auditor. Thus, the auditor Andy & Co needs to reconsider the audit strategy and cannot use the work of the Internal Auditor.
 - (d) The work performed by the internal auditor can be used by the External Auditor in this case if the architect is not an employee of the company but is in private practice.
17. The Trainee asked whether the audit team is to perform any procedures over the investment in Daiva Swaroopam Private Limited:
- (a) The company need to prepare the consolidated financial statements and the same need to be audited by the auditor and the auditor needs to consider the financial information and also assess regarding the need to use of the work of the component auditor.
 - (b) The auditor needs to perform audit procedures over the balances in investments and transactions with its related party.
 - (c) The auditor need not perform any procedures as the investment in Daiva Swaroopam Private Limited has already been made in the previous year.
 - (d) Both (a) & (b).
18. The trainee asked about role of auditor in case the investment in Daiva Swaroopam Private Limited is increased to 60% in the next year:
- (a) The auditor need not do any additional procedures compared to this year except for audit procedures over the increase in Investment value and its disclosures in the Financial Statements.
 - (b) The auditor should also audit the group consolidated financial statements as the consolidation becomes applicable for the company being the investment is raised from 45% to 60%.
 - (c) The auditor needs to audit the subsidiary's books of accounts to get comfort over the balances in the material subsidiary. Thus, the audit strategy will change for verifying the investment.
 - (d) The auditor can either on its own, audit the subsidiary or use the work of another auditor to get comfort over the balances in the subsidiary from the next year.
19. The company has requested its previous auditor to give back its audit documentation ("*working papers*") and warned the previous auditor with legal notice to submit them back to the company showing the confidentiality clause:
- (a) The previous auditor is bound to return the workpapers as the company has raised the confidentiality clause over the audit firm. Thus, the SA – 230 is not applicable in such scenario as the original owner itself is requesting to return the working papers.
 - (b) The auditor has a right over its working paper, and he is the owner of the workpapers but he cannot give the workpapers to any person even at the request of the company.

- (c) The auditor has a right over its working paper, and he is the owner of the workpapers and he may give at his discretion make available the workpapers to the company.
 - (d) The auditor has a right over its working papers but the owner of them is the company. He should make available the workpapers to the company at its request and SQC-1 mandates the auditor to make copies made available to its clients.
20. The trainee asked you whether the IND AS is applicable to the group or not?
- (a) Yes, but only Manava Swaroopam Limited need to prepare its financial statements as per the Companies (Indian Accounting Standards Rules), 2015.
 - (b) Yes, the Company Manava Swaroopam Limited and its subsidiaries (including associates) need to prepare its financial statements as per the Companies (Indian Accounting Standards Rules), 2015.
 - (c) The Company is not required to prepare financial statements as per Companies (Indian Accounting Standards Rules), 2015 as the company's net worth is below 250 crore and is not listed in any recognised stock exchange in India.
 - (d) The Company is required to prepare books of accounts as per US GAAP as it is listed in US Stock Exchange and get the books audited by the CPA but not the Indian Chartered Accountant.

(10 x 2 = 20 Marks)

Division B- Descriptive Questions-70 Marks

Question No. 1 is compulsory.

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

1. Comment on the following:
- (a) ANUSHA Associates, Chartered Accountants, conducting the audit of Rishabh Ltd., a listed company for the year ended 31st March 2021 is concerned with the auditor's responsibilities relating to other information, both financial and non-financial, included in the Company's annual report. While reading other information, ANUSHA Associates considers whether there is a material inconsistency between other information and the financial statements. As a basis for the consideration the auditor shall evaluate their consistency, compare selected amounts or other items in the other information with such amounts or other items in the financial statements. Guide ANUSHA Associates with examples of "Amounts" or "other items" that may be included in the "other information" with reference to SA 720. **(5 Marks)**
 - (b) AMRO Limited is availing the services of ABN Private Limited for its payroll operations. Payroll cost accounts for 67% of total cost for AMRO Limited. ABN Limited has provided the type 2 report as specified under SA 402 for its description, design and operating effectiveness of control.

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

CA Param 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 Param hence asked his assistant to remove such reference and modify report accordingly.

Comment whether CA Param is correct in removing the reference of the work done by service auditor? **(5 Marks)**
 - (c) 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. **(4 Marks)**

2. (a) BN Limited is a listed entity having two subsidiaries namely BUS Limited and ROBUS Limited. Both the subsidiaries are unlisted and are incorporated in Australia. The consolidated net worth of BN Limited and its subsidiaries is Rs. 350 crore (including net worth of BUS Limited and ROBUS Limited Rs. 36 crore & Rs. 80 crore respectively) in the immediately preceding year 2019-20. On observing this fact, your senior manager advises you to inform the management of BN limited to make certain changes in the board of directors of both the subsidiaries, in accordance with the LODR regulation 24(1). Comment. **(5 Marks)**
- (b) The Property, Plant and Equipment of Peer Ltd. included Rs.39.61 crore of earth removing machines of outdated technology which had been retired from active use and had been kept for disposal after knock down. These assets appeared at residual value and had been last inspected seven years back. As an Auditor, what may be your reporting concern in view of CARO, 2016 on matters specified above? **(4 Marks)**
- (c) Mr. Sudhir, a Chartered Accountant in practice, delivered a speech in the national conference organized by the Ministry of Textiles. While delivering the speech, he told to the audience that he is a management expert and his firm provides services of taxation and audit at reasonable rates. He also requested the audience to approach his firm of chartered accountants for these services and at the request of audience he also distributed his business cards and telephone number of his firm to those in the audience. Comment with reference to the Chartered Accountants Act, 1949, and Schedules thereto. **(5 Marks)**
3. (a) You have been appointed to carry out the audit of Blue Insurance Company Ltd. for the year 2020-21. In the course of your audit, you observed that the commission paid to agents constituted a major expense in operating expenses of the Company. Enumerate the audit concerns that address to the assertions required for the Auditor to ensure the continued existence of internal control as well as fairness of the amounts in accounting of commission paid to agents. **(4 Marks)**
- (b) (i) Mr. Shantinath was appointed as an auditor of RST Co. During the course of audit he finds that the company has availed an excess ITC of Rs. 40 lakh. Accordingly, he made recommendations in Part V of GSTR-9C. The management of the company refused to pay the excess ITC and argued that auditors recommendations are not binding. Comment.
- (ii) Mr. Bahubali, made an outward supply of Rs. 4.00 lakh to M/s. S.S. Enterprises on 30th April, 2020 on a credit period of 15 days. However, M/s. S.S. Enterprises made the payment to Mr. Bahubali after 45 days along with interest for 30 days delayed payment @ 12%. As such, Mr. Bahubali received total payment of Rs. 4,04,000/- along with interest. However, while filing Form GSTR-3B/ Form GSTR-1, Mr. Bahubali declared his outward supplies at Rs. 4.00 lakh. Even while filing Form GSTR-9, Mr. Bahubali did not discharge his tax liability. As a GST auditor in Form GSTR-9C, what action is recommended by the auditors. Comment. **(6 Marks)**
- (c) Mr. Dhawal, a practicing CA, is appointed as a Director Simplicitor in Gautam Pvt. Ltd. After three year of appointment, Mr. Dhawal resigned as the Director and accepted the Statutory Auditor position of the Company. Is Mr. Dhawal right in accepting the auditor position? Comment with reference to the Chartered Accountants Act, 1949, and Schedules thereto. **(4 Marks)**
4. (a) Mr. Shripal has been appointed as an auditor of ASG Ltd., a NBFC company registered with RBI. Mr. Shripal is concerned about whether the format of financial statements prepared by ASG Ltd. is as per notification issued by the Ministry of Corporate Affairs (MCA) dated October 11, 2018. The notification prescribed the format in Division III under Schedule III of the Companies Act, 2013 applicable to NBFCs complying with Ind-AS. Mr. Shripal wants to know the differences in the presentation requirements between Division II and Division III of Schedule III of the Companies Act, 2013. Help Mr. Shripal. **(6 Marks)**

- (b) Mr. Sheetal is appointed as a statutory auditor of Mahi Ltd. Mahi Ltd is required to appoint an internal auditor as per statutory provisions given in the Companies Act, 2013 and appointed Mr. Kunthu as its internal auditor. The external auditor Mr. Sheetal asked internal auditor to provide direct assistance to him regarding evaluating the sufficiency of tests performed and the adequacy of disclosures in the financial statements and other matters affecting the auditor's report. Discuss whether Mr. Sheetal, statutory auditor, can ask direct assistance from Mr. Kunthu, internal auditor as stated above in view of relevant Standard on Auditing. **(4 Marks)**
- (c) CA. Rani is practicing since 2007 in the field of tax audit. Due to her good practical knowledge, she was offered editorship of a 'Tax Audit' Journal which she accepted. However, she did not take any permission from the Council regarding such editorship. Comment with reference to the Chartered Accountants Act, 1949, and Schedules thereto. **(4 Marks)**
5. (a) SSP Bank was engaged in the business of providing Portfolio Management Services to its customers, for which it took prior approval from RBI. Your firm has been appointed as the statutory auditors of the Bank's financial statements for the year 2019-20. Your senior has instructed you to verify the transactions of Portfolio Management Services (PMS). While verifying the transactions you noticed that the bank has not maintained separate record for PMS transactions from the Bank's own investments. As a statutory auditor what methodology will be adopted by you for verification of PMS transactions? **(4 Marks)**
- (b) During the process of extracting the exception reports, the auditors noted numerous purchase entries without valid purchase orders. In terms of percentage, about 40% of purchases were made without valid purchase orders whereas few purchase orders were validated after the actual purchase. Also, there was no reconciliation between the goods received and the goods ordered. You are required to briefly explain the audit procedures to address the validity of account balance level. **(4 Marks)**
- (c) RAJUL & Co." is an Audit Firm having partners "Mr. R", "Mr. A", "Mr. J", "Mr. U" and "Mr. L", Chartered Accountants. "Mr. R", "Mr. A", "Mr. J", "Mr. U" and "Mr. L" are holding appointment as an Auditor in 4, 5, 6, 10 and 15 Companies respectively.
- (i) Provide the maximum number of Audits remaining in the name of "RAJUL & Co."
- (ii) Provide the maximum number of Audits remaining in the name of individual partner i.e. "Mr. R", "Mr. A", "Mr. J", "Mr. U" and "Mr. L".
- (iii) Can RAJUL & Co. accept the appointment as an auditor in 80 private companies having paid-up share capital less than Rs. 100 crore which has not committed default in filing its financial statements under section 137 or annual return under section 92 of the Companies Act with the Registrar, 2 small companies and 1 dormant company?
- (iv) Would your answer be different, if out of those 80 private companies, 65 companies are having paid-up share capital of Rs. 115 crore each? **(6 Marks)**
6. (a) Sunshine Limited is a public sector undertaking engaged in production of electricity from solar power. It had commissioned a new project near Puducherry with a new technology for a cost of Rs. 4,926 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) Atishaya Ltd. holds the ownership of 10% of voting power and control over the composition of Board of Directors of Neenu Ltd. While planning the statutory audit of Atishaya Ltd., what factors would be considered by you as the statutory auditors of Atishaya Ltd for the audit of its consolidated financial statements prepared under Ind AS? **(5 Marks)**
- (c) While auditing REAL Ltd., you observe certain material financial statement assertions have been based on estimates made by the management. As the auditor how do you minimize the risk of material misstatements? **(4 Marks)**

OR

Briefly explain the difference between Peer Review and Quality Review. **(4 Marks)**