

**Mock Test Paper - Series II: April 2025**

**Date of Paper: 5<sup>th</sup> April 2025**

**Time of Paper: 10 A.M. – 1 P.M.**

**INTERMEDIATE GROUP – II**

**PAPER – 5: AUDITING AND ETHICS**

**Time Allowed – 3 Hours**

**Maximum Marks – 100**

**PART I - Case Scenario based MCQs (30 Marks)**

***Write the most appropriate answer to each of the following multiple-choice questions by choosing one of the four options given. All MCQs are compulsory and carries 2 Marks each.***

**Case Scenario 1**

Star Ltd., a leading manufacturer of windmills in India, appointed M/s Shahi & Co., LLP of Chartered Accountants, as its statutory auditors for F.Y. 2023-24. During the audit, one of the audit team members, CA Ritik, was asked by the engagement partner to verify the ownership assertion of the company's inventories. To accomplish this, CA Ritik requested the concerned official of company to arrange for the audit team to attend the physical inventory count being conducted by the company. CA Ritik believed that attending the inventory count was the only way to check the ownership assertion related to the company's inventory. He discussed the matter with another audit team member, CA Pari. She had a different perspective. According to CA Pari, the correct course of action would be CA Ritik verifying the purchase requisition, purchase order, receiving reports, vendor invoices, inventory records, and payment files etc. as ownership assertion could not be verified simply by attending the physical inventory count.

While verifying the creditors and purchases balances, CA Pari, have been satisfied with the internal control procedures related to purchases and creditors, and decides to check the creditors balance on a sample basis. She requested the management to provide a list of all the creditors, which included a total of 550 creditors. To determine the sample, CA Pari chose a sampling interval of every 11<sup>th</sup> creditor's balance, which results in a sample size of 50 creditors balances for the audit.

During the audit, while verifying the share capital balance of the company, CA Ritik and CA Pari observed that there has been no change in the share capital raised by the company. CA Pari

was of the view that since there has been no change in the share capital of the company, the audit team is not required to obtain any evidence with respect to the share capital balance. However, CA Ritik is of the opinion that they should obtain audit evidence even if there is no change in the company's capital structure during the year. According to him, such evidence can be a written confirmation from the accounts manager.

Before finalising the audit report, the engagement partner asked CA Ritik to coordinate with the client company to request a written representation from management regarding their responsibilities and the information provided. However, CA Ritik refused to accept the representation, as it contained a qualifying language to the effect that representations are made to the best of its knowledge and belief, which according to him was not reasonable to accept.

Based on the above facts, answer the following:

1. What is the best course of action for CA Ritik for verification of the assertion with respect to the inventory of the company, as asked by the engagement partner?
  - (a) CA Ritik should ask the management to provide a written representation in this regard as it is in itself a sufficient and appropriate audit evidence.
  - (b) CA Ritik should perform test count and inspection while attending the physical inventory count in order to verify the assertion as asked by the engagement partner.
  - (c) CA Ritik should attend the physical inventory count as the only audit procedure.
  - (d) CA Ritik should agree to CA Pari and follow the course of action as suggested by her.
2. While verifying the inventory as asked by the engagement partner, which specific assertion can be best verified by following the specific audit procedure considered appropriate by CA Ritik?
  - (a) Existence and Condition.
  - (b) Rights and Obligations.
  - (c) Presentation & Disclosure.
  - (d) Valuation.
3. Which method of sampling has CA Pari applied while selecting the sample for verification of creditors?
  - (a) Simple random sampling.

- (b) Systematic sampling.
  - (c) Haphazard sampling.
  - (d) Stratified sampling.
4. Which of the following is the most appropriate, with respect to verification of share capital balance of the company?
- (a) The point of view of CA Pari is correct.
  - (b) The point of view of CA Ritik is correct.
  - (c) The point of view of CA Pari is partly correct as no evidence is required to be obtained if the same audit firm has conducted the audit of the previous year thereby verifying the closing balance of share capital in the previous year which becomes the opening balance of the share capital for the year under audit.
  - (d) The point of view of CA Ritik is partly correct as written confirmation should be obtained from the Company Secretary.
5. Whether non-acceptance of the written representation by CA Ritik is correct?
- (a) The non-acceptance of written representation by CA Ritik is not correct as management of the company has the sole discretion to decide as to what language is used or what limitations are imposed in the written representation provided to the auditor.
  - (b) The non-acceptance of written representation by CA Ritik is correct as it is not reasonable for the auditor to accept any qualifying language in the written representations given by the management.
  - (c) The non-acceptance of written representation by CA Ritik is not correct as it is reasonable for the auditor to accept such qualifying language if the auditor is satisfied that the representations are being made by those with appropriate responsibilities and knowledge of the matters included in the representations.
  - (d) The non-acceptance of written representation by CA Ritik is correct as SA 580 requires the auditor to accept the written representation only if it is in the language as used in the letter of audit engagement.

## Case Scenario 2

Raavi & Co., a Chartered Accountants firm, has been appointed as auditor of XYZ Ltd., a prospective new client. CA Sukanya, one of the firm's partner, is handling the potential client. During a meeting with the company's officers, she discovers that Sushant, the company's CFO, is a former classmate. They had both started their Chartered Accountancy (CA) journey together, but Sushant left the program halfway due to repeated failures and later pursued an MBA in finance from a prestigious institution.

During initial discussions, the company reveals plans to launch a new service in the "weather-forecasting" sector. These services will be available on website of company, and users can access micro weather information for a fee. The company requests that the audit firm be visibly associated with their marketing efforts.

Assuming the firm accepts the offer, they send a letter to the previous auditor, Royal & Co., requesting any professional reasons that might prevent them from taking on the assignment. However, Royal & Co. does not respond to the inquiry.

While planning the audit, Raavi & Co. also learn that the company has acquired all shares of another company, which requires the financial statements of both companies to be consolidated and audited, according to applicable laws. Despite this information, Raavi & Co. fails to advise the client on the necessity of auditing the consolidated financial statements.

Firm is also reviewing internal controls of XYZ Ltd. He verifies following things:

- Are tenders called before placing orders?
- Are the purchases made on the basis of a written order?
- Is the purchase order form standardised?
- Are purchase order forms pre-numbered?

Based on the above facts, answer the following:

6. Keeping in view request of the company to be visibly associated with company's new services, identify which type of threat is being faced by audit firm.
  - (a) Self-interest threat.
  - (b) Familiarity threat.
  - (c) Self-review threat.
  - (d) Advocacy threat.

7. The previous auditors, Royal & Co., have not replied to communication of Raavi & Co. Which fundamental principle of professional ethics is not followed by them?
- (a) Objectivity.
  - (b) Professional behaviour.
  - (c) Professional competence and due care.
  - (d) Integrity.
8. Raavi & Co. have failed to advise the company regarding audit of consolidated financial statements. Which fundamental principle of professional ethics is being violated by Raavi & Co.?
- (a) Professional behaviour.
  - (b) Integrity.
  - (c) Objectivity.
  - (d) Professional competence and due care.
9. Which method is Raavi & Co. using to facilitate the accumulation of the information necessary for the proper review and evaluation of internal controls?
- (a) Narrative record.
  - (b) Flow chart.
  - (c) Check List.
  - (d) Internal Control questionnaire.

### **Case Scenario 3**

CA Misha is appointed as the statutory audit of a branch of FDH Bank. During the audit, the following issues were observed:

The bank provides "Kisan Credit Card" loans to farmers to meet their short-term credit needs for crop cultivation. One such loan, with an outstanding balance of ₹ 20 lakh at the year end, had no transactions for the past 90 days. The loan was granted for paddy cultivation, which typically takes 3-4 months from sowing to harvest. The branch has classified the loan as a "Standard Asset".

It was also noted that the account of a borrower with a cash credit limit of ₹ 50 lakh, which was taken over from another bank, was sanctioned by the branch manager instead of the immediate higher authority, as required in bank's "Manual of Delegation of Powers".

CA Misha also served as the statutory auditor for a multiplex cinema. During the audit, CA Misha observed that the revenue of company has fallen from ₹ 50 crore in last year to ₹ 5 crore in current year (for which financial statements have been received for audit) due to lack of demand in the market for company's products.

Based on the above facts, answer the following:

10. As regards description of agricultural advance, which of the following statements is most appropriate in this regard?
  - (a) The branch has erred in making classification as per RBI norms. It is a "Sub-standard" asset.
  - (b) The classification made by branch is proper. However, there are no transactions in account since last 90 days, it is SMA.
  - (c) The classification made by branch is proper.
  - (d) The branch has erred in making classification as per RBI norms. It is a "doubtful" asset.
11. Regarding taken over account from another bank, which of the following statements is most appropriate?
  - (a) It is a serious violation of laid down procedures of bank for sanction of advances and should be reported by auditor without fail.
  - (b) It is an internal issue of Bank. However, the auditor may, at his discretion, report it.
  - (c) It is an internal issue of Bank and auditor is not concerned with it.
  - (d) There is no issue involved as credit facility was properly sanctioned.
12. Regarding drastic fall in revenue of the company, which of the following is an audit risk?
  - (a) Fall in revenue would result in fall of profits for the company.
  - (b) Drastic fall in revenue may imply that company is not able to carry out its operations in foreseeable future due to lack of demand in the market for company's products. There is a risk that going concern disclosure is omitted to be made in financial statements.
  - (c) The company can explore some new line of activity, if demand of its products is falling.
  - (d) Fall in revenue would mean lower tax liabilities for the company.

### MCQs

13. CA Radha is appointed as an auditor of a PVC Ltd. for the first time. A detailed set of instructions has been prepared by her office and handed over to assistants in engagement team. During the course of audit, she noticed that company is also producing substantial quantities of scrap generated during manufacturing process. However, no instructions have been given to engagement team in this regard. What should be proper course of action by CA Radha?
- (a) She should ignore this information as audit has already begun.
  - (b) She should modify earlier set of instructions.
  - (c) She should leave the matter to wisdom of engagement team.
  - (d) She should put the ball in court of management as she was not provided with complete information earlier.
14. The management of a company has approached its bankers and requested for enhancement in working capital credit facilities. The bank manager requested for financial statements of the company for half year along with report providing assurance in this respect duly signed by CA. It also requires projected financial statements for coming years along with a report from CA providing assurance regarding these projections to consider request of management. Which of the following standards issued by ICAI are relevant for CA P in such a situation, if any?
- (a) Standards on Review Engagements.
  - (b) There are no standards for issuing such type of reports.
  - (c) Standards on Related Services.
  - (d) Standards on Assurance Engagements.
15. While conducting the audit of receipts of Government Company, which of the following area is to be covered as part of Audit of Receipts?
- 1. Whether all revenues or other debts due to government have been correctly assessed, realised and credited to government account by the designated authorities of Government Company.
  - 2. Whether adequate checks are imposed to ensure the prompt detection and investigation of irregularities, double refunds, fraudulent or forged refund vouchers or other loss of revenue through fraud or wilful omission or negligence to levy or collect taxes or to issue refunds.

3. Whether the expenditure incurred has been on the purpose for which the grant and appropriation had been provided and that the amount of such expenditure does not exceed the appropriation made.
  4. Whether the various schemes/projects are executed and their operations conducted economically and whether they are yielding the results expected of them.
- (a) Only statement 1 is correct.
  - (b) Statements 1 & 2 are correct.
  - (c) Statements 1, 2, 3, 4 are correct.
  - (d) Statements 1, 2, 3 are correct.

## **PART II - Descriptive Questions (70 Marks)**

*Question No. 1 is compulsory.*

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

1. (a) Identify and briefly explain the component of risks of material misstatement involved in the following situations:
  - (i) GHK Private Limited is a start-up engaged in providing comprehensive solutions to the issue of paddy stubble burning, mainly catering to the needs of farmers of North-western India. Due to the importance given by governments to this issue, companies have entered the market in the past few years. Many of these companies have not been successful and have gone bust.
  - (ii) A company has devised a control that its inventory of perishable goods is stored in appropriate conditions in a controlled environment to prevent any damage to inventory. Responsibility is fixed on two people to monitor the environment using sensors and to report on deviations.
  - (iii) Shree Foods Private Limited is engaged in the manufacturing of garlic bread. The auditors of the company have planned audit procedures in respect of recognition of revenues of the company. Despite that, there is a possibility that the misstatements in revenue recognition are not identified by planned audit procedures. **(5 Marks)**



- (b) The assistant of CA Bhavik is assigned responsibility of drafting “audit programme” relating to purchases appearing in financial statements of Arya Industries, a partnership firm for F.Y. 2023-24. The said firm is a GST registered taxpayer and is engaged in manufacturing of packing boxes from a special type of paper taxable under GST. Draft a sample audit programme for purchases.

**(5 Marks)**

- (c) Identify and explain briefly the audit procedure used by the auditor to obtain audit evidence in following situations:

- (i) While auditing the books of accounts of ANT Limited for the financial year 2023-24, the auditor checked the complete documents and records of the company in detail to obtain audit evidence.
- (ii) Mr. M, auditor of company, looks at the process of inventory counting by the entity’s personnel and of the performance of control activities.
- (iii) XYZ Ltd. is engaged in export of goods to Europe. The sales invoices raised in Euros are converted into Indian rupees as per applicable norms. The auditor wants to verify whether conversion of foreign currency into Indian rupees is proper or not.
- (iv) CA Isha is appointed as auditor of TUV Ltd., during the initial stage of audit, she reviewed the Gross Profit Ratio of the company. She also compared GP ratio of TUV Ltd. with the other companies operating in similar industry.

**(4 Marks)**

2. (a) Identify and explain the assertions that the auditor will check by performing the following audit procedures-

- (i) Inventory recognised in the balance sheet actually existed as at the period end.
- (ii) All the items of inventory pertaining to the relevant year shall be included regardless of the location.
- (iii) All goods dispatched prior to the period/ year-end have been invoiced and included in debtors on a test check basis.
- (iv) Examine client correspondence, sales and receivables records, purchase documents.
- (v) Verifying that the entity has charged depreciation on all items of PPE unless any item of PPE is non-depreciable like freehold land. **(5 Marks)**

- (b) While planning the audit of an NGO, the auditor may focus on knowledge of the NGO's work, its mission and vision, updating knowledge of relevant statutes especially with regard to recent amendments, circulars etc. Explain the other relevant points the auditor needs to focus while planning the audit of NGO. **(5 Marks)**
- (c) CA Tina, the auditor of SKY Ltd., asks its finance and audit head to prepare audit strategy for conducting audit of SKY Ltd. CA Tina also insists him to draw detailed audit procedures. In response to the auditor's request, the finance head of the company completes the audit strategy as well as audit procedures. Subsequently, the auditor realises that the effectiveness of the audit is compromised and it was his responsibility to prepare the overall audit strategy. Comment. **(4 Marks)**
3. (a) While auditing a renowned four-star hotel in Pune, CA Shrey observes a gift shop operating within the hotel premises. On further enquiries, he comes to know that stocks in gift shop belong to gift shop owner and hotel receives rent for letting out this space. Discuss, how, auditor can verify payment of common amenities used by gift shop owner to the hotel. **(5 Marks)**
- (b) Auditors are required to obtain an understanding of internal control relevant to the audit when identifying and assessing its effectiveness and risk of material misstatement. PDC Ltd. appointed CA Nikhil as auditor for the F.Y. 2023-24. During the audit, he observed that significant deficiency exists in the internal control system and he wants to ascertain the same. Elucidate the various indicators of significant deficiencies which will help you in assessing the efficiency of internal control system of the organisation. **(5 Marks)**
- (c) Wire Limited, a company engaged in manufacturing of electric equipment, gets some part of its production processes outsourced from third parties. During the audit, the company had sent raw material to third parties for carrying out certain processes on these raw materials and such inventories worth ₹ 1.50 crores (material to financial statements) were lying with different third parties as at year end. How can auditor obtain sufficient appropriate audit evidence in respect of existence and condition of inventories lying with third parties? **(4 Marks)**
4. (a) The senior member of the firm Soni & Associates, Chartered Accountants, informed to its auditing staff that at the time of audit reporting regarding corresponding figures, when corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in specified circumstances. What are those exceptional circumstances? **(5 Marks)**

- (b) The auditor shall plan and perform an audit with professional skepticism recognising that circumstances may exist that cause the financial statements to be materially misstated. Discuss any five examples of professional skepticism.  
**(5 Marks)**
- (c) During the audit of Jimjam Ltd., CA Arjun, the auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report, that requires adjustment of, or disclosure in, the financial statements have been identified. With reference to Standards on Auditing, what specific audit procedures should CA Arjun include in his risk assessment to address subsequent events effectively?  
**(4 Marks)**
5. (a) As per Multi-state Co-operative Societies Act, 2002, the auditor shall make a report to the members of the multi-state co-operative society on the accounts examined by him and on every balance sheet and profit and loss account and on every other document required to be part of or annexed to the balance sheet or profit and loss account. Explain.  
**(5 Marks)**
- (b) During the audit of Grace Pvt. Ltd., CA Tanu notices that significant amount of depreciation and amortisation charges are reflected in financial statements of the company. Which attributes need to be considered by him while verifying such depreciation and amortisation charges?  
**(5 Marks)**
- (c) The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit. Explain.  
**(4 Marks)**
6. (a) The auditor has a responsibility to perform audit procedures to identify, assess and respond to the risks of material misstatement arising from the entity's failure to appropriately account for related party relationships, transactions or balances.  
During the audit, the auditor should maintain alertness for related party information while reviewing records and documents. He may inspect the records or documents that may provide information about related party relationships and transactions. Explain in detail with examples.  
**(5 Marks)**
- (b) While it is true that companies can benefit immensely from the use of data analysis in terms of increased profitability, better customer service, etc. Analyse various functions that an auditor can perform using Data Analytics tools and techniques to obtain good results.  
**(5 Marks)**

- (c) Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report is not considered as a substitute or alternative for a number of important items. What are those items in view of above?

**(4 Marks)**

**OR**

CAR Ltd., an automotive parts manufacturer, appointed Amit & Associates as auditors for F.Y. 2023-24. During the audit, CA Amit noticed a significant rise in raw material consumption (steel and aluminium) despite a decrease in production. This discrepancy led to detailed reviews of vendors supplying these raw materials. While verifying the existence of vendors and the actual receipt of goods or raw materials by the company, which assertion is being verified by CA Amit. Explain the procedure for the same.

**(4 Marks)**

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**INTERMEDIATE: GROUP – II**  
**PAPER – 5: AUDITING AND ETHICS**  
**SUGGESTED ANSWERS / HINTS**  
**Part I - Multiple Choice Questions**

1. (d)
2. (a)
3. (b)
4. (d)
5. (c)
6. (d)
7. (b)
8. (d)
9. (c)
10. (c)
11. (a)
12. (b)
13. (b)
14. (d)
15. (b)

**Part II - Descriptive Answers**

1. (a) (i) It has been stated that many companies engaged in providing holistic solutions to problem of stubble burning have not been successful. It shows that line of activity is inherently risky. Therefore, there is a greater possibility of misstatements. The component of risks of material misstatement involved in given situation is “inherent risk.”

- (ii) The company has devised a control that its inventory of perishable goods is stored in appropriate conditions and responsibility is fixed on two persons to monitor environment using sensors and to report on deviations. There is a possibility that persons given responsibility do not perform their work and report deviations. The component of risks of material misstatement involved in given situation is “control risk”.
- (iii) There is a possibility that planned audit procedures may not achieve desired result and fail to detect misstatements in revenue recognition. The risk alluded to it is “detection risk”.

**(b) Sample audit programme pertaining to purchases**

Name of Concern : Arya Industries  
 Financial Year : 2023-24  
 Prepared by : Name of person with date  
 Reviewed by : Name of person with date  
 Approved by : Name of person with date

S.no.	Nature of Procedure	Extent of Check	Basis of Sample	Done by
(i)	Vouch few purchase invoices of paper from purchase records of concern.			
(ii)	Trace these invoices into account books of concern.			
(iii)	Verify few purchase invoices of paper on GST portal.			
(iv)	Trace few purchase invoices of paper in stock records to ensure that these have been added to stocks of raw material.			

- (c)** (i) The audit procedure used by auditor of ANT Limited is known as Inspection because inspection is an audit procedure in which complete documents and records of a company are checked in detail for the purpose of obtaining audit evidence.
- (ii) Mr. M is using Observation as audit procedure as Observation consists of looking at a process or procedure being performed by others.

- (iii) The audit procedure used by auditor is Recalculation. Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.
  - (iv) CA Isha is using Analytical Procedure to obtain audit evidence. Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial and non-financial data.  
  
Analytical procedures also encompass the investigation of identified fluctuations and relationships that are inconsistent with other relevant information or deviate significantly from predicted amounts.
2. (a)
- (i) The auditor will check the Existence Assertion to ensure Assets, liabilities and equity balances exist as at the period end.
  - (ii) The auditor will check the Cut-off assertion to ensure that all assets and liabilities are reported in the appropriate period.
  - (iii) The auditor will check Completeness Assertion to ensure all Trade receivable balances that were supposed to be recorded have been recognized in the financial statements.
  - (iv) The auditor will check Rights & Obligations assertion to ensure that the entity has valid legal ownership rights over the inventories claimed to be held by the entity and recorded in the financial statements.
  - (v) The auditor will check Valuation assertion to ensure PPE have been valued appropriately and as per generally accepted accounting policies and practices
- (b) **While planning the audit, the auditor may concentrate on the following:**
- (i) Knowledge of the NGO's work, its mission and vision, areas of operations and environment in which it operate.
  - (ii) Updating knowledge of relevant statutes especially with regard to recent amendments, circulars, judicial decisions viz. The Foreign Contribution (Regulation) Act 1976, The Societies Registration Act, 1860, The Income-tax Act 1961 etc. and the Rules related to the statutes.
  - (iii) Reviewing the legal form of the Organisation and its Memorandum of Association, Articles of Association, Rules and Regulations.
  - (iv) Reviewing the NGO's Organisation chart, then Financial and Administrative Manuals, Project and Programme Guidelines, Funding Agencies Requirements and formats, budgetary policies if any.

- (v) Examination of minutes of the Board/Managing Committee/Governing Body/ Management and Committees thereof to ascertain the impact of any decisions on the financial records.
  - (vi) Study the accounting system, procedures, internal controls and internal checks existing for the NGO and verify their applicability.
  - (vii) Setting of materiality levels for audit purposes.
  - (viii) The nature and timing of reports or other communications.
  - (ix) The involvement of experts and their reports.
  - (x) Review the previous year's Audit Report.
- (c) The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. The auditor plans what type of audit procedures are to be performed, their timing and how much work should be done taking into account sample size etc.

The overall audit strategy and the audit plan remain the auditor's responsibility. It is the auditor who is responsible for establishing overall audit strategy and developing audit plan. However, auditor may discuss elements of planning with entity's management without compromising effectiveness of audit.

In the given case, CA Tina, auditor of SKY Ltd. asks its finance and audit head to prepare audit strategy and to draw detailed audit procedures. On Auditor's request, finance head completes the audit strategy as well as audit procedures.

In view of above, CA Tina should prepare overall audit strategy and detailed audit procedures. Therefore, approach of CA Tina was wrong.

3. (a) While auditing a renowned four-star hotel in Pune, CA Shrey observes that a gift shop is operating within the hotel premises. Upon further enquiry, he finds that the stock in the gift shop belongs to gift shop owner and the hotel receives rental income for letting out the space. In this context, to verify the payment of common amenities used by the gift shop owner to hotel, the auditor may adopt the following audit procedures:
- The auditor should obtain and examine the rental/lease agreement entered into between the hotel and the gift shop owner.
  - The auditor should verify rent receipts. This would enable the auditor to ensure that controls regarding revenue cycle are in order.



- The auditor should satisfy himself that all taxes collected from gift shop have been paid over to the proper authorities.
  - Evaluate internal controls related to monitoring of utility consumption and collection of recoveries from tenants or concessionaires (like gift shops).
  - Verify the hotel's utility bills (electricity bill, water bill etc.) and assess whether cost sharing with the gift shop is proportionate and reasonable.
  - The auditor should verify that amounts charged for such amenities have been appropriately recorded in the hotel's books and that collections are reconciled with receipts.
  - The auditor should see that costs of repairs and minor renovation and redecoration are treated as revenue expenditure, where as costs of major alterations and additions to the hotel building and facilities capitalised.
- (b) As per SA 265, "Communicating Deficiencies in Internal Control to Those Charged with Governance and Management", Indicators of significant deficiencies in internal control include, for example:
- (i) Evidence of ineffective aspects of the control environment, such as: -
    - Indications that significant transactions in which management is financially interested are not being appropriately scrutinised by those charged with governance.
    - Identification of management fraud, whether or not material, that was not prevented by the entity's internal control.
    - Management's failure to implement appropriate remedial action on significant deficiencies previously communicated.
  - (ii) Absence of a risk assessment process within the entity where such a process would ordinarily be expected to have been established.
  - (iii) Evidence of an ineffective entity risk assessment process, such as management's failure to identify a risk of material misstatement that the auditor would expect the entity's risk assessment process to have identified.
  - (iv) Evidence of an ineffective response to identified significant risks (e.g., absence of controls over such a risk).
  - (v) Misstatements detected by the auditor's procedures that were not prevented, or detected and corrected, by the entity's internal control.

- (vi) Disclosure of a material misstatement due to error or fraud as prior period items in the current year's Statement of Profit and Loss.
  - (vii) Evidence of management's inability to oversee the preparation of the financial statements.
- (c) When inventory under the custody and control of a third party is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of that inventory by performing one or both of the following: -
- (i) Request confirmation from the third party as to the quantities and condition of inventory held on behalf of the entity.
  - (ii) Perform inspection or other audit procedures appropriate in the circumstances.

Other audit procedure may include –

For example,

- Inspecting documentation regarding inventory held by third parties, example, warehouse receipts.
- Requesting confirmation from other parties when inventory has been pledged as collateral.
- Attending, or arranging for another auditor to attend, the third party's physical counting of inventory, if practicable.
- Obtaining another auditor's report, or a service auditor's report, on the adequacy of the third party's internal control for ensuring that inventory is properly counted and adequately safeguarded.

4. When corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in the following circumstances:
1. If the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which gave rise to the modification is unresolved, the auditor shall modify the auditor's opinion on the current period's financial statements. In the Basis for Modification paragraph in the auditor's report, the auditor shall either:
    - (a) Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or

- (b) In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.
2. If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements on which an unmodified opinion has been previously issued, the auditor shall verify whether the misstatement has been dealt with as required under the applicable financial reporting framework and, if that is not the case, the auditor shall express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, modified with respect to the corresponding figures included therein.
3. Prior Period Financial Statements Not Audited - If the prior period financial statements were not audited, the auditor shall state in an Other Matter paragraph in the auditor's report that the corresponding figures are unaudited. Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements.
- (b) Professional skepticism includes being alert to, for example:
- (i) Audit evidence that contradicts other audit evidence obtained.
  - (ii) Information that brings into question the reliability of documents and responses to inquiries to be used as audit evidence.
  - (iii) Conditions that may indicate possible fraud.
  - (iv) Circumstances that suggest the need for audit procedures in addition to those required by the SAs.
  - (v) Maintaining professional skepticism throughout the audit is necessary if the auditor is to reduce the risks of:
    - Overlooking unusual circumstances.
    - Over generalising when drawing conclusions from audit observations.
    - Using inappropriate assumptions in determining the nature, timing, and extent of the audit procedures and evaluating the results thereof.
- (c) The auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the

financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements have been identified.

The auditor is not, however, expected to perform additional audit procedures on matters to which previously applied audit procedures have provided satisfactory conclusions.

The auditor shall perform the procedures required above so that they cover the period from the date of the financial statements to the date of the auditor's report, or as near as practicable thereto. The auditor shall take into account the auditor's risk assessment which shall include the following:

- (i) Obtaining an understanding of any procedures management has established to ensure that subsequent events are identified.
- (ii) Inquiring of management and, where appropriate, those charged with governance as to whether any subsequent events have occurred which might affect the financial statements.
- (iii) Reading minutes, if any, of the meetings, of the entity's owners, management and those charged with governance, that have been held after the date of the financial statements and inquiring about matters discussed at any such meetings for which minutes are not yet available.
- (iv) Reading the entity's latest subsequent interim financial statements, if any.

5. (a) As per sub-section (3) & (4) of section 73 of the Multi-state Co-operative Societies Act, 2002, the auditor shall make a report to the members of the Multi-State Co-operative society on the accounts examined by him and on every balance-sheet and profit and loss account and on every other document required to be part of or annexed to the balance-sheet or profit and loss account, which are laid before the Multi-State co-operative society in general meeting during his tenure of office, and the report shall state whether, in his opinion and to the best of his information and according to the explanation given to him, the said account give the information required by this act in the manner so required, and give a true and fair view:

- (i) In the case of the balance-sheet, of the state of the Multi-State co-operative society's affairs as at the end of its financial year; and
- (ii) In the case of the profit and loss account, of the profit or loss for its financial year.

The auditor's report shall also state:

- (i) Whether he has obtained all the information and explanation which to the best of his knowledge and belief were necessary for the purpose of his audit.

- (ii) Whether, in his opinion, proper books of account have been kept by the Multi - State co-operative society so far as appears from his examination of these books and proper returns adequate for the purpose of his audit have been received from branches or offices of the Multi-State co-operative society not visited by him.
- (iii) Whether the report on the accounts of any branch office audited by a person other than the Multi - State co-operative society's auditor has been forwarded to him and how he has dealt with the same in preparing the auditor's report.
- (iv) Whether the Multi - State co-operative society's balance sheet and profit and loss account dealt with by the report are in agreement with the books of account and return.

Where any of the matters referred to in sub-section (3) or (4) is answered in the negative or with a qualification, the auditor's report shall state the reason for the answer.

**(b) Auditor needs to consider the following attributes while verifying for depreciation and amortisation expenses: -**

- Obtain the understanding of entity's accounting policy related to depreciation and amortisation.
- Ensure the Company policy for charging depreciation and amortisation is as per the relevant provisions of Companies Act/ applicable accounting standards.
- The accounting policy has been applied consistently year on year. Any change in the accounting policy has been adequately disclosed.
- Whether the depreciation has been calculated after making adjustment of residual value from the cost of the assets.
- Whether depreciation and amortisation charges are valid.
- Whether depreciation and amortisation charges are accurately calculated and recorded.
- Whether all depreciation and amortisation charges are recorded in the appropriate period.
- Whether each part of an item of PPE with a cost that is significant in relation to the total cost of the item have been depreciated separately.

Example: It may be appropriate to depreciate separately the airframe and engines of an aircraft, whether owned or subject to a finance lease.

- Whether the most appropriate depreciation method for each separately depreciable component has been used.
- (c) The process of audit suffers from certain inbuilt limitations due to which an auditor cannot obtain an absolute assurance that financial statements are free from misstatement due to fraud or error. These fundamental limitations arise due to the following factors: -
- (i) **The Nature of Financial Reporting:** The preparation of financial statements involves judgment by management. These judgments may involve subjective decisions or a degree of uncertainty. Therefore, auditor may not be able to obtain absolute assurance that financial statements are free from material misstatements due to frauds or errors.
  - (ii) **The Nature of Audit Procedures:** There are practical and legal limitations on the auditor's ability to obtain audit evidence such as:
    - Possibility that management or others may not provide, intentionally or unintentionally, the complete information relevant for preparation and presentation of FS.
    - Fraud may involve sophisticated and carefully organised schemes.
  - (iii) **Not in the nature of Investigation:** An audit is not an official investigation into alleged wrongdoing. Hence, auditor cannot obtain absolute assurance that financial statements are free from material misstatements due to frauds or errors.
  - (iv) **Timeliness of financial reporting and decrease in relevance of information over time:** Relevance of information, and thereby its value, tends to diminish over time, and there is a balance to be struck between the reliability of information and its cost.
  - (v) **Future events:** Future events or conditions may affect an entity adversely. Adverse events may seriously affect ability of an entity to continue its business.
6. (a) During the audit, the auditor should maintain alertness for related party information while reviewing records and documents. He may inspect the following records or documents that may provide information about related party relationships and transactions, for example:
1. Entity income tax returns.
  2. Information supplied by the entity to regulatory authorities.

3. Shareholder registers to identify the entity's principal shareholders.
4. Statements of conflicts of interest from management and those charged with governance.
5. Records of the entity's investments and those of its pension plans.
6. Contracts and agreements with key management or those charged with governance.
7. Significant contracts and agreements not in the entity's ordinary course of business.
8. Specific invoices and correspondence from the entity's professional advisors.
9. Life insurance policies acquired by the entity.
10. Significant contracts re-negotiated by the entity during the period.
11. Internal auditors' reports.
12. Documents associated with the entity's filings with a securities regulator e.g, prospectuses).

**(b)** In today's digital age when companies rely on more and more on IT systems and networks to operate business, the amount of data and information that exists in these systems is enormous. The combination of processes, tools and techniques that are used to tap vast amounts of electronic data to obtain meaningful information is called data analytics. While it is true that companies can benefit immensely from the use of data analytics in terms of increased profitability, better customer service, gaining competitive advantage, more efficient operations, etc., even auditors can make use of similar tools and techniques in the audit process and obtain good results.

The tools and techniques that auditors use in applying the principles of data analytics are known as Computer Assisted Auditing Techniques or CAATs in short. Data analytics can be used in testing of electronic records and data residing in IT systems using spreadsheets and specialised audit tools viz., IDEA and ACL to perform the following:

- Check completeness of data and population that is used in either test of controls or substantive audit tests.
- Selection of audit samples – random sampling, systematic sampling.
- Re-computation of balances – reconstruction of trial balance from transaction data.

- Reperformance of mathematical calculations – depreciation, bank interest calculation.
  - Analysis of journal entries
  - Fraud investigation.
  - Evaluating impact of control deficiencies.
- (c) As per SA 701, “Communicating Key Audit Matters in the Auditor’s Report”, communicating key audit matters in the auditor’s report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor’s report is not:
- (i) A substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;
  - (ii) A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705, “Modifications to the Opinion in the Independent Auditor’s Report”;
  - (iii) A substitute for reporting in accordance with SA 570 when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity’s ability to continue as a going concern; or
  - (iv) A separate opinion on individual matters.

**OR**

- (c) CA Amit is verifying Occurrence Assertion while verifying the existence of vendors and the actual receipt of goods or raw materials by the company.
- The audit procedures generally required to be undertaken while verifying Occurrence Assertion:
- Ensure purchases are not understated/ overstated by performing following audit procedures:
- Whether any fictitious vendors have been booked or purchases have been recorded by reviewing the vendor selection process followed by the entity and also performing procedures to ensure existence of the vendors.
  - Whether the goods were received at the factory gate and whether there exists an entry in the security gate inward register.
  - Whether quality inspection of goods was done.



- Whether a goods receipt note was prepared and signed by an appropriate client personnel.
- Whether the purchase invoice was approved as per delegation of authority and whether a 3 or 2-way match was done.
- Whether stock record has been updated by the stores personnel.

Special considerations during audit of purchases:

- The purchase invoice received should be the "Original" copy (and not photocopy/ carbon copy) against which the entity has recorded the purchase in its books of account.
- Purchase invoice should have been booked only once risk and reward incidental to ownership has been transferred to the entity. Specific consideration for cases where the terms of delivery as agreed with vendor are F.O.B., C.I.F. etc.
- Purchase invoice should be in the name of entity. However, in case of different branches, it should be addressed to the appropriate branch.
- Input tax component should have been booked in the input tax ledger. The auditor should obtain tax returns filed with the authorities and tally the input tax as reflected in the books to the amount disclosed in the returns.
- In case of purchases made from related parties or allied and associated concerns, the auditor needs to verify if requisite approval from Board of Directors (appropriate authority) has been obtained and should verify the selected samples and perform analytical procedures in relation to price of goods to confirm that the price charged is at arm's length.
- The auditor should review whether purchases should be capitalized or expensed off in Statement of Profit and loss according to his professional judgement.
- Review journal entries for unusual transactions.