MOCK TEST PAPER- 1

FINAL (NEW) GROUP – I

PAPER – 3: ADVANCED AUDITING AND PROFESSIONAL ETHICS

Time Allowed – 3 Hours **Maximum Marks – 100**

Division A- Multiple Choice Questions (30 Marks)

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

1. KJLIC Ltd is a life insurance company. The company is based at Nagpur and has offices across Western India.

KJ & Associates are the statutory auditors of this company. At the time of audit of this company, areas like cash and bank, receipts and payment and fixed assets where the internal controls of the management are similar to the ones adopted by other companies are dealt by the auditors as per the publications on the Internal Control Questionnaire, published by the Institute of Chartered Accountants of India (ICAI). Since various operational cycles are inter-linked, the internal controls operating within the systems of such cycles are reviewed simultaneously by the auditors.

The company avails services of an actuary for computing various liabilities and provisions which are certified by the actuary.

During the audit of the financial statements for the financial year ended 31 March 2020, the auditors of the company would like to have a discussion with the actuary who has given actuarial certificate on the basis of which certain liabilities have been recorded in the financial statements, however, the actuary and the management of the company are not comfortable with this and they have asked the auditor to complete their work on the basis of certificate. Further the management also provides management representation letter in respect of all of these points.

Please suggest if you were the auditors of this company, how would you have handled this matter?

a. The management is correct and as an auditor getting certificate would be a good audit evidence.

b. The management is not correct and the auditor may have discussions with the actuary.

c. The auditor is not correct because the IRDAI Guidelines require the actuary to maintain confidentiality and by having such discussion it would be a non-compliance. Auditors should be aware of such legal requirements.

d. The auditor is not correct because such requirements require approval of the Insurance Regulatory and Development Authority of India (IRDA) and that would unnecessarily delay the completion of audit.

2. KJ Private Ltd has a business of pharmaceuticals and has an annual turnover of INR 1,500 crore. During the last few years, considering the environment in which the company operates, its profit has reduced and are still reducing. Hence, the management has been looking at various ways to cut the costs.

AD & Associates are the statutory auditors of the company and RM & Associates are the internal auditors of the company.

Initially, the company did not want to appoint any internal auditors to save costs, however, at insistence of the statutory auditors, the company appointed the internal auditors.

During the course of the statutory audit for the financial year ended 31 March, 2020, the statutory auditors requested for the detailed working papers of the internal auditors which the internal auditors refused. However, the statutory auditors told the management if the same are not provided then they would qualify their report.

In this situation, please advise which of the following would be correct.

a. The statutory auditors should review the detailed working papers but they cannot qualify their report on this ground.

b. The statutory auditors may review the detailed working papers and even after that they may qualify their report.

c. The statutory auditors are not required to go to the extent of review of detailed working papers of internal auditors.

d. The statutory auditors may review the detailed working papers of internal auditors but for that purpose they would require prior approval of the ICAI.

3. D.M. Ltd. appointed M/s K.K. & Co., Chartered Accountants as Statutory Auditors. The Statutory Auditors found the internal audit function reliable and effective. The Statutory Auditor assigned the task of assessing the inventory levels of a few branches where the Statutory Auditor believed that there might be some risk of material misstatement to one of the internal auditor Mr. Ryan. Since the Internal Auditor had recently done such assessment as a part of their internal audit program, therefore, the Statutory Auditor believed that they could rely on the former's report. Besides this, because of the paucity of time the Statutory Auditors also requested Mr. Ryan to help them in some paperwork including audit documentation.

Before the audit was concluded, Mr. Ryan got promoted and shifted to another city. During the audit discussion stage, the lead Statutory Auditory found out that the documentation delegated to Mr. Ryan was not complete. Accordingly, Statutory Auditor further checked the inventory work delegated to the Internal Auditor, however, it was found to be satisfactory.

In view of the above case scenario, state which of the following statement(s) hold true:

a. The working of Internal Audit function was reliable and satisfactory; therefore, the allocation of inventory level work was within the authority of the Statutory Auditor. This was further confirmed by the satisfactory work of Internal Auditory, as found out later.

b. The documentation would be considered complete as far as the Statutory Auditor's responsibility is concerned as the missing documentation was because of the oversight of the Internal Auditor.

c. Since the Internal Audit had conducted the similar inventory level checking activity recently, therefore, because of familiarity with the audit the Statutory Auditor was right in delegating the same to the Internal Auditor.

d. The Statutory Auditors should not have delegated the inventory level checking to the Internal Auditor, as the risk assessed was material. Further, the audit documents are Statutory Auditor's property and responsibility. Also, the Statutory Auditor should maintain confidentiality during all the stages of the audit. Therefore, it was wrong on the part of the Statutory Auditor to handover the task of audit documentation to the Internal Auditor.

4. SK Private Limited is a medium-sized company having operations inJharkhand. The company manufactures some parts and sells that to various dealers on ex-works basis. The financial statements of the company are prepared as per Ind AS and internal financial controls report is also applicable on the same.

During the course of audit of the financial statements for the year ended 31 March 2020, the management of the company had a detailed discussion with the auditors for audit planning.

Further it was also decided that any observations of the auditors should also be discussed with the management before conclusion by the audit team which was not done in the past years.

Considering this, the auditors started the risk assessment and requested the management to share their documentation for the same on whichthe management said that they don't have any risks and if the auditors come across any such thing they can discuss that with the management.

But the auditors were not convinced with the view of the management and the same thing has happened in the past years as well. You are required to provide your inputs to resolve this matter.

a. The requirement of the audit team is not correct.

b. The view of the management is correct because of the applicability of Ind AS.

c. The view of the management is correct because of the applicability of internal financial controls reporting.

d. The view of the management is not correct.

5. XYZ Private Limited is engaged in trading of parts of machineries used in boiler plants. Company has seen growth of 60% in the sales and management expecting similar growth in next 3 financial years and is planning to onboard new dealers in order to achieve management goal. Purchase department also expect to develop new suppliers in order to meet customer demands.

Internal auditor of the company has identified frequent changes in the bank account and other master details of suppliers. At this expansion planning phase, company has no defined control to provide assurance on said supplier master changes. Management agreed to develop the process of monthly detailed review of supplier master changes done in supplier master by Finance assistant in order to ensure authorized changes in supplier master.

One of the members from the Management would like to know that above controls falls under which category:

a. Automated control.

b. Preventive control.

c. Detective control.

d. Compensating control.

6. M/s Ram Raj & Associates have been appointed as statutory auditors of Venus Ltd. for the FY 2019-20. During the year, the company has entered into some related party transactions. CA Ram, the engagement partner has taken a management representation letter regarding the proper accounting, presentation and disclosure of such related party transactions. Is there any further responsibility of CA Ram with respect to the other procedures to be performed for related party transactions?

a. No, there is no further responsibility of CA Ram as the best audit evidence for the related party transaction is the management representation letter.

b. No, there is no further responsibility of CA Ram as the audit firm is responsible for verifying the balances and disclosure of related party transactions. The identification of related party transactions is the responsibility of the management of Venus Ltd.

c. Yes, the audit firm has the responsibility to perform the audit procedures to identify, assess and respond to the risk of material misstatement arising from the entity's failure to appropriately account for related party relationships, transactions and balances.

d. Yes, the auditor has the responsibility to detect fraud and error with respect to the related party transactions.

7. You are the internal auditor of FCD Bank Limited for the year 2019-20 and the bank maintains all the data on computer. You are instructed by your senior to verify the loan against fixed deposits of the Navi Mumbai branch. As per the scope of audit, you need to ensure that proper lien has been marked on all the fixed deposits against which loan has been issued. Which of the following procedure you will follow for the same:

a. Ensure that all the fixed deposit receipts are attached along with the approved loan documents.

b. Ensure that all the fixed deposit receipts, against which the loan has been sanctioned, are discharged in favour of bank and check that the lien is marked in the computer software.

c. Discuss the process followed for lien marking with the branch manager.

d. Ensure that all the fixed deposit receipts, against which the loan has been sanctioned, are discharged in favour of bank, check that the lien is marked in the computer software and the fixed deposit should be kept separately with the branch manager.

8. AV Ltd is in the business of manufacturing of chemicals and has a net worth of INR 700 crore. The company has been preparing its financial statements as per Ind AS. For the purpose of Form 3CD, management did not identify any items which may require adjustments because of the differences between Ind AS and ICDS. However, the tax auditors during the course of their audit identified few items where adjustments are required to be made and accordingly, should be reported under Clause 13(e) of Form 3CD.

Further tax auditors also are of the view that disclosures in respect of ICDS should be made in Clause 13(f) of Form 3CD which the management has not done. In this case, please suggest which of the following would be the correct option.

a. If the impact of the adjustments related to ICDS identified by the auditors is material then such adjustments need to be reported in Form 3CD. And disclosures in respect of ICDS should in any case be given in Form 3CD.

b. If the impact of the adjustments related to ICDS identified by the auditors is immaterial even then such adjustments need to be reported in Form 3CD. To give disclosures in respect of ICDS is the management choice.

c. Both the impact of the adjustments related to ICDS identified by the auditors, whether material or immaterial, and disclosures need to be mandatorily reported in Form 3CD.

d. ICDS and Ind AS don't have any differences and hence assessment of the auditor doesn't seem to be correct. Hence no reporting would be required under Clause 13(e) of Form 3CD. If there is no reporting under Clause 13(e) then reporting under Clause 13(f) would also not be required in Form 3CD.

9. OSK Ltd was incorporated on 15 February 2020. The company chose to prepare its financial statements for the purposes of Companies Act 2013 for the period from 15 February 2020 to 31 March 2021 as its first reporting period. The company had a turnover of INR 6 crore for the period ended 31 March 2020 which is expected to increase to INR 50 crore for the period from 1 April 2020 to 31 March 2021. The company filed its income tax return for the financial year 31 March 2020 before30 September 2020 i.e. before the due date of filing return of income for the financial year 2019-20 (before considering any extension). The company would prepare its financial statements for the period from 15 February 2020 to 31 March 2021 and would get them audited from its statutory auditors.

In this case, please suggest which of the following would be correct.

a. The company would be exempt from tax audit for FY 2019-20.For 2020-21, the company would need Form 3CB under tax audit.

b. The company would be covered under tax audit for the FY 2019- 20 and 2020-21. It would need Form 3CA for both these years.

c. The company would be covered under tax audit for the FY 2019- 20 and 2020-21. It would need Form 3CB for both these years.

d. The company would be covered under tax audit for the FY 2019- 20 and 2020-21. It would need Form 3CB for FY 2019-20 and Form 3CA for FY 2020-21.

10. RIM Private Ltd is engaged in the business of manufacturing of water bottles and is experiencing significant increase in turnover year on year. It is a subsidiary of RIM Gmbh, based out of Germany.

During the financial year ended 31 March 2019, the company carried out a detailed physical verification of its inventory and property, plant and equipment.

During the year, various other activities were carried out to increase efficiency in operations and reductions of costs.

The statutory auditors of the company started their audit work from April 2019 and requested for a documentation on changes in processes and activities during the year as well as any resultant impact of the same on management controls.

The management of the company told the auditors that all such documentation is maintained by the parent company as this is a closely held private company and even though internal financial controls reporting is applicable on this company, the parent company is taking due care of each and every process.

The auditors did not agree with the views of the management. Please advise both the management and the auditors.

a. The auditors should look for documentation as per Sarbanes Oxley in this case.

b. The auditors are correct in this case and the management should provide the required documentation.

c. The auditors are correct in this case and the management should provide the required documentation. However, in case the parent company is covered by Sarbanes Oxley then it can be ignored by the auditors.

d. The management is correct.

<u>Case Scenario 1</u>

M/s Sudharma & Associates have been appointed as the statutory auditors of Veer Ltd. for the FY 2022-23. Veer Ltd. is a listed company dealing in the manufacture of iron and steel bars and it is among the top 1000 listed entities. FY 2022-23 is the first year after the incorporation of the company. The company has duly complied with the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations 2015.

When the audit was started, the management of Veer Ltd. discussed with Mr. Sudharma (the engagement partner) about the strong internal control system of the company. The management discussed about the whistle blowing policy of the company, the HR policies, company code of conduct and ethics policies. Mr. Sudharma was told that the audit team can rely on the information provided to them and the entity level controls without any second thought. The management advised the auditor not to waste time in checking the direct entity level controls and instead to concentrate on indirect entity level controls during their conduct of audit. Further Veer Ltd. has constituted its qualified Audit Committee and a Risk Management Committee as per the relevant regulations. Since FY 2022-23 was the first year after incorporation of the company, the meetings of both the committees were held twice during the year based on the company's requirement where all the company's important matters were duly discussed.

Further, while conducting the audit, the auditor found that a Management Discussion and Analysi s Report is a part of the Directors Report. With respect to the non-financial information like industry structure and development, opportunities and threats, the auditor was asked by the management to verify those particular facts and to comment on the same.

Since FY 2022-23 is the first year after the incorporation of Veer Ltd., the company is in the process of exploring the market and venturing towards its expansion plans. The management will be approaching the banks for the purpose of raising funds for its projects. The management accordingly, requested the auditor to mention in their audit report or the compliance certificate about the entity's future viability. Further, in one of the meetings of Audit Committee conducted during the FY 2022-23, the internal control system and auditor's report of Veer Ltd. were discussed. Mr. Sudharma was also present at the meeting and the Audit Committee called for the comments of Mr. Sudharma, if any. Certain important decisions regarding the changes in the internal control system were duly taken by majority voting.

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

11. What should be Mr. Sudharma's audit plan regarding the checking of direct entity level controls and indirect entity level controls after considering the management's advise?

- **a.** Mr. Sudharma should check the indirect entity level controls in detail and he can skip the checking of direct entity level controls as the company has a strong internal control system.
- **b.** Mr. Sudharma should check the direct entity level controls in detail and he can skip the checking of indirect entity level controls as the company has a strong internal control system.
- **c.** Mr. Sudharma should evaluate and understand both direct entity level controls and indirect entity level controls and should accordingly decide the nature, timing, extent of audit procedures.
- **d.** Mr. Sudharma should check the indirect entity level controls in detail as it relates the business process and account balance and contribute indirectly to the effective operation of direct ELC. Thus, he can skip the checking of direct entity level controls.

12. Is the company justified in holding meeting of its Audit Committee and Risk management Committee twice in the FY 2022-23?

- **a.** Yes, the company is justified as the meetings of both the committees were held as per the company's requirement and the important matters were duly discussed and conducting a meeting involves expense and when all the matters were discussed in two meetings it is wise on the part of the company that they did not hold more meetings.

b. No, the company is not justified in holding two meetings of both the committees as the Audit Committee should meet at least four times in a year and Risk management committee can meet once in a year.

c. The company is not justified in holding two meetings of the Audit Committee as an audit committee should meet at least four times in a year; however, the company is justified in holding two meetings of Risk management committee.

d. The company is justified as it is at the discretion of the Board of Directors to hold the meetings of the various committees of the company as per the company's requirement to discuss the matters.

13. With respect to the meeting of Audit Committee attended by Mr. Sudharma, what all rights can be exercised by Mr. Sudharma?

a. Mr. Sudharma has right to be heard and to vote in the meeting of Audit Committee of Veer Ltd. when it considers the auditor's report.

b. Mr. Sudharma has right to vote in the meeting of Audit Committee of Veer Ltd. when it considers the auditor's report.

c. Mr. Sudharma, being statutory auditor does not have right to be heard and to vote in the meeting of Audit Committee of Veer Ltd. even if it considers the auditor's report. Such rights vest with the internal auditors of the company.

d. Mr. Sudharma has right to be heard in the meeting of Audit Committee of Veer Ltd. when it considers the auditor's report but shall not have right to vote.

14. What is the responsibility of M/s Sudharma & Associates so far as the Management Discussion and analysis report of Veer Ltd. is concerned?

a. M/s Sudharma & Associates should verify and comment on the non financial information reflected in the Management Discussion and analysis report as it forms the part of the Boards Report.

b. M/s Sudharma & Associates should verify the non financial information reflected in the Management Discussion and analysis report as it forms the part of the Boards Report and can take expert opinion for analysing and commenting on the same.

c. M/s Sudharma & Associates is required to review the compliance with the disclosure requirement and need not verify the facts related to the non financial information reflected in the Management Discussion and analysis report.

d. M/s Sudharma & Associates can verify and comment on the non financial information reflected in the Management Discussion and Analysis Report provided additional fees for such work is given by the management.

15. What should M/s Sudharma & Associates do with respect to the management's request to the auditor regarding mentioning about company's future viability?

a. M/s Sudharma & Associates can mention about the company's future viability in its compliance certificate as auditor's report is not an assurance as to future viability of the entity.

b. M/s Sudharma & Associates can mention about the company's future viability in its audit report as compliance certificate is not an assurance as to future viability of the entity.

c. M/s Sudharma & Associates cannot mention about the company's future viability in its compliance certificate or auditor's report as both the documents are not an assurance as to future viability of the entity.

d. M/s Sudharma & Associates can mention about the company's future viability in either its compliance certificate or auditor's report as both the documents act as an assurance as to future viability of the entity.

<u>Case Scenario 2</u>

POSH Bank of India is a Public Sector Bank founded in the year 1967. The bank has 179 branches all over India as on 31.03.2022. Total Deposits of the bank on 31.03.2021 was ` 50,000 crore. The Motto of the Bank is "Royalty lies in Loyalty". The Statutory Auditors for FY 2021-22 are SAHU & Associates, Chartered Accountants. The audit manager of the firm while reviewing advances has noticed the following:

a. The Advance granted to Mr. Ram has been guaranteed by State Government. However, said advance is overdue since November 2021.

b. As on 20.04.2022, the ad hoc limit of account of Mr. Shyam has not been reviewed even though 120 days of date of ad hoc sanction were over.

The above advances have been granted by Meerut Branch. However, this branch is not subject to Concurrent Audit.

The Bank has also granted Term Loan of ` 20 crore to Sumati Ltd (An Unlisted Company) on 01.02.2022. The sanction letter read as follows:

"The Facility shall be used for Repayment of Unsecured Loans of Promoters – ` 10 crore and towards development & construction expenses (Other than Land Cost) of the company's new office to be situated in Faridabad, Haryana – ` 10 crore".

The company has utilized the facility as follows as on 31st March 2022-

(i) Land Purchased for New Office: ` 4 crore;

(ii) Development and construction Expenses of New Office: ` 11 crore;

(iii) Repayment of Unsecured Loans of Promoters: ` 3 crore;

(iv) Investment in Fixed Deposit: ` 2 crore (Temporarily);

Company's Total Borrowings from all Banks as on 31st March 2022 is ` 60 crore.

POSH Bank of India is the parent organization (100% Holding) of POSH General Insurance Co. Ltd. The Statutory auditors of POSH General Insurance are AK & Co., Chartered Accountants (Firm based in Mumbai). Brief Financial Information is as under as on 31st March 2022:

• Value of Assets: ` 700 crore.

• Amount of Liabilities: ` 415 crore.

• Capital: ` 200 crore.

The POSH General Insurance has entered into reinsurance contract with Fair Reinsurance Co. Ltd. against the risk of fire only. Fair Reinsurance Co. Ltd. is one of the largest reinsurers in India.

Mr. Shri (Partner in SAHU & Associates) also acts as Surveyors and Loss Assessors under Insurance Act, 1938. However, he has not intimated or taken permission from the Council of Institute of Chartered Accountants of India.

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

16. As Statutory Auditor of Sumati Ltd, identify the aggregate amount which shall be reported under clause (ix) of Para 3 of CARO, 2020 on account of utilisation of term loans for the purpose other than for which they were obtained?

a. ` 4 crore.

b. ` 5 crore.

c. ` 7 crore.

d. ` 2 crore.

17. As an audit manager of the firm, advice which advance(s) shall be classified as Non-Performing Asset?

a. Mr. Ram.

b. Mr. Shyam.

c. Both Mr. Ram and Mr. Shyam.

d. Neither Mr. Ram nor Mr. Shyam.

18. Based on above data, state whether POSH General Insurance has maintained adequate solvency margin u/s 64VA of Insurance Act, 1938? If no, then state what further action will be done?

a. Yes, solvency margin has been maintained therefore no action is required.

b. No, It shall deemed to be insolvent.

c. No, It shall submit a financial plan to the authority.

d. The requirement of Solvency Margin is not applicable in case of general insurance companies.

19. Whether the acting of Mr. Shri as a Surveyor and Loss Assessor is in the violation of Clause 11 of Part 1 of First Schedule of Chartered Accountants Act, 1949?

a. Yes, as specific permission from the council shall be required.

b. No, as general permission from the council has been granted.

c. No, as specific permission from the council can be obtained at any point of time.

d. Yes, as general permission is not granted for above occupation.

20. Identify the type of reinsurance contract between POSH General Insurance and Fair Reinsurance Co. Ltd.

a. Treaty Reinsurance.

b. Proportional Treaty Reinsurance.

c. Non-Proportional Treaty Reinsurance.

d. Facultative Reinsurance.

Division B- Descriptive Questions

*Question No. **1** is compulsory.*

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

Total 70 Marks

1. **(a)** Jinchandra & Co., Chartered Accountants, have been appointed Statutory Auditors of Gurudeva Ltd. for the F.Y. 2020-21. The audit team has completed the audit and is in the process of preparing audit report Management of the company has also prepared draft annual report.

Audit in-charge was going through the draft annual report and observed that the company has included an item in its Annual Report indicating downward trend in market prices of key commodities/raw material as compared to previous year. However, the actual profit margin of the company as reported in financial statements has gone in the reverse direction. Audit Manager discussed this issue with partner of the firm who in reply said that auditors are not covered with such disclosures made by the management in its annual report, it being the responsibility of the management.

Do you think that the partner is correct in his approach on this issue?

Discuss with reference to relevant Standard on Auditing the Auditor's duties with regard to reporting.

[5 Marks]

(b) Abhinandan Limited a chemical manufacturing company, having its factory located at Nanded Village, for the year 2021-22 appointed Subahu & Co. as their statutory auditors. During the course of the audit, Subahu & Co. identified that Abhinandan Limited received a show cause notice from National Green Tribunal based on the investigation performed by the regional forest department for violating environmental laws. Upon gathering a further understanding of the said matter, it was identified that Abhinandan Limited was dumping toxic solid waste, without treating it, on the nearby grounds, and because of this, the nearby water bodies were getting polluted. Based on the preliminary investigation performed by the regional forest department under the directions of the National Green Tribunal, it was identified that these practices were carried out since 2009 and a lot of damage has been done to the environment by Abhinandan Limited. A show cause notice was already issued to Abhinandan Limited by the National Green Tribunal for levying the penalty of an amount of ` 500 crore. The unaudited profit for the financial year 2021 -22 of Abhinandan Limited was ` 35 crore and the unaudited turnover was ` 100 crore. Upon inquiry it was identified that Abhinandan Limited has disclosed this matter in the financial statements by way of footnote, the extract of which is provided below:

“The company has received a show cause notice from the National Green Tribunal for some potential violation of environmental laws and the company’s legal department has assessed and found that the judgment would be in favour of the company. Accordingly, no provision has been created for such notices.”

In the light of the above scenario kindly provide what should be the appropriate opti on for the statutory auditor of the company to report this matter.

[5 Marks]

(c) Chintamani Ltd appoints Chintan & Mani as statutory auditors for the financial year 2021 - 2022. Chintan & Mani seem to have different opinions on Audit approach to be adopted for audit of Chintamani Ltd. Mani is of the opinion that 100% checking is not required and they can rely on Audit Sampling techniques in order to provide them a reasonable basis on which they can draw conclusions about the entire population.

Chintan is concerned that whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

You are required to guide Chintan about his role if audit sampling has not provided a reasonable basis for conclusions about the population that has been tested in accordance with SA 530,

[4 Marks]

2. **(a)** Comptroller & Auditor General appointed Sambhav & Associates, a chartered accountant firm, to conduct Performance audit of MAP Ltd., a public sector undertaking of Government of India. The firm conducted the audit with a view to check all the expenses of the unit are in conformity with the public interest and publicly accepted customs. The audit report submitted by audit firm was rejected by C&AG. Give your opinion on the action of C&AG.

[4 Marks]

(b) Secretarial staff of the Quality Review Board (QRB) is in the process of preparing a panel for submission to Board to enable it to initiate reviews of the quality of audit services provided by members of ICAI. The draft panel has been prepared by Mr. Paras, a junior staff in QRB secretariat and it has moved up in hierarchy for vetting by a senior staff, Mr. Suparas, before being put up in the upcoming meeting of Quality review board for its consideration.

The draft panel contains details of following entities audited by different audit firms: -

Name of entity	Listing status	Sector	Paid up capital*	Annual turnover*	O/s loans & deposits*	Name of audit firm
PQR Ltd.	Listed in BSE, NSE and NYSE	Manufacturing	1000	5000	750	GPR & Co.
X Insurance Ltd.	Unlisted	Health insurance	250	1500	400	DS & Co.
AB Banking Co.	Unlisted	Banking	400	900	300	PS & Co.
AAZ Ltd.	Unlisted	Manufacturing	200	800	200	CT & Co.

* Figures are of immediately preceding year and are in ` Crore.

Is the inclusion of names of audit firms of corresponding entities in the draft panel to be put up before QRB appropriate? Guide Mr. Suparas.

[5 Marks]

(c) Give your comments with reference to the Chartered Accountants Act, and schedules thereto: Mrs. M is a Director of XYZ Private Limited, having 15% share-holdings in the company. During 2017, the company appointed C.A. Mr. N, Mrs. M spouse, as its statutory auditor. On Mr. N's advice, the company issued fresh equity shares in 2017-18, in the ratio of one share for every two shares held by the shareholders of the company. Mr. N used to deliver audit report for subsequent years without any comments or disclosures, thereupon.

[5 Marks]

3. **(a)** Billimoria & Billimoria, a partnership firm, is engaged in providing engineering consultancy services to insurance corporates in automobile sector. The firm conducts risk inspection of vehicles and submit their reports to insurance companies. Both the partners are Chartered Engineers. The Firm is one of your regular tax audit clients. The following information is culled out from the account books of the company for financial year 2021 -22 by the firm:

Particulars	Rupees in Crore
Turnover	8.50
Receipt on account of sales/debtors	6.00
Cash receipt from debtors	0.10
Expenditure during year	7.00
Cash expenditure	0.21
Cash loan repayment	0.05

The partner of said firm informs you that due to changes in income-tax laws, their firm is not liable for audit under section 44 AB of Income tax Act (commonly called as tax audit). How would you deal with the matter? Is contention of partner in accordance with law?

[4 Marks]

(b) RAO & Co., a Chartered Accountant Firm, is appointed as the principal auditor of a listed company, Triumph Ltd.

Figures of income and net-worth of five out of seven components of Triumph Ltd., which are its unlisted subsidiaries, is tabulated below for the immediate preceding financial year along with the consolidated amount:-

(Rs. in crores)

Particulars	Consolidated	A	B	C	D	E
Income	300	35	10	70	65	20
Net Worth	800	40	20	140	180	50

The remaining two components i.e., Component 'F' & Component 'G' of Triumph Ltd. were unaudited. According to Mr. RAO, the engagement partner, Component 'F' is material to the consolidated financial statements whereas Component 'G' is not material to consolidated financial statements and this fact has also been discussed in writing with those charged with governance of Triumph Ltd. and it will also form part of report as a 'Key audit matter' in accordance with SA 701.

(i) Which of the components of Triumph Ltd. can be termed as "material subsidiary" and in the board of which of the unlisted subsidiaries at least one independent director of Triumph Ltd. needs to be appointed or would be appointed?

(ii) What shall be the audit consideration in relation to reporting in case of unaudited components of Triumph Ltd. by RAO & Co. and how RAO & Co. as a principal auditor shall report in case of Component 'F' & Component 'G', respectively?

[6 Marks]

(c) CA M has been appointed as an auditor of Life Secure Insurance Ltd. He observed that few insurance policies have been sold by the company in the last month of the financial year ending 31st March, 2021. While recognizing income in the income statement of the company, it is the responsibility of CA M to make an assessment of the reasonability of the risk pattern managed by the management.

Also, it is to be ensured by him that Life Secure Insurance Ltd. should not issue policies, if the risk is not established before the closure of the F.Y.2020 -21.

Indicate the circumstances when the company should not issue the policy documents.

[4 Marks]

4. **(a)** The Director (Discipline) of the ICAI received information of alleged misconduct against Mr. Jayprakash, the proprietor of JP & Associates, as follows:-

   i. Audit of a college was accepted by JP & Associates in which Mr. Jayprakash is working as a part-time lecturer and also, he had not taken permission of the ICAI for working as a part-time lecturer in the college.

   ii. An event relating to Corporate Social Responsibility was sponsored by JP & Associates, whereby in the sponsorship banner, name of Mr. Jayprakash as 'CA Jayprakash, Proprietor, JP & Associates' was mentioned.

   On the basis of above information and along with certain evidence against Mr. Jayprakash, he was found guilty and so he was reprimanded and a fine of ₹ 1 lakh was imposed by an order passed against him dated 12th July, 2020.

   Against the said order, Mr. Jayprakash preferred an appeal with the Appellate Authority on 17th August, 2020 by submitting a statement of appeal along with the application form of appeal. During such appellate proceedings, it was discovered that the said statement of appeal contained some facts which were false to which Mr. Jayprakash admitted it to be false and apologized for it.

   (i) Mr. Jayprakash has violated which of the provisions of the Chartered Accountants Act, 1949?

   (ii) Before which authority, the matter of Mr. Jayprakash would have been placed and what maximum punishment could have been imposed on him by the said authority in accordance with the Chartered Accountant Act, 1949?

[6 Marks]

(b) Prabhu & Co LLP is a large firm of Chartered Accountants based out of Mumbai. Prabhu & Co. LLP is subject to peer review which was last conducted 3 years back. For the peer review of the financial year ended 31st March 2021, the firm got an intimation on 29th May 2021. The process of peer review got started and was completed on 27th September 2021. In view of peer reviewer, the systems and procedures of Prabhu & Co. LLP are deficient / non-compliant. The peer reviewer did not share any of his observations with Prabhu & Co LLP as draft and final report was submitted to the Board. Comment.

[4 Marks]

(c) The volatility, unpredictability and pace of fast changes that exists in the automated environment today is far greater than in the past and consequently it throws more risk to business which requires them to have a need to continuously manage such risks. State various risks which an enterprise may have to face and manage.

[4 Marks]

5. **(a)** CA Prachi was conducting statutory audit of branch of a nationalized bank for the year

2021-22. While reviewing operations and documents/papers of a borrower enjoying overdraft credit facilities of ` 50 crore (availed against security of stocks and book debts), following observations were jotted down by her: -

- The balance in overdraft credit facility as on 31st March,2022 was ` 55.65 crore. The balance in account exceeded sanctioned limit during the whole month of March 2022.
- As per terms of sanction letter, stock/book debt statements were required to be submitted monthly. Latest available stock/book debt statement for the month of February, 2022 showed drawing power of ` 48.50 crore only. However, stock/book debt statements of previous months showed adequate drawing power.
- Stock audit of borrower was also conducted during the year by one of empanelled stock auditors of the bank. Stock audit report dated 31st December,2021 placed on the record showed adequate drawing power in the account. However, it has commented adversely on the declining turnover of borrower in year 2021 -22(till the date of stock audit report) as compared to proportionate turnover in preceding year.
- The renewal of overdraft facilities was due on 20th October,2021. The account was short renewed by competent authority for a period of 3 months pending submission of complete papers.

However, borrower has not submitted complete renewal papers till 31 st March,2022. There is a request letter from borrower on record stating that valuation report of a property located at a faraway location was taking time.

The branch has classified the account as 'Standard Asset'. Considering above, CA Prachi is in dilemma relating to proper classification of above advance. Guide her.

[4 Marks]

(b) Sudarshan Ltd. is a company registered under the Companies Act, 2013. The company is engaged in the business of loans and advances, acquisition of shares / stocks / bonds / debentures/securities issued by Government or local authorities. For the year ended 31st March, 2022 following are some extracts from the financial statements:

(i)	Paid-up share capital	` 40.53 Cr.
(ii)	Non-Current Assets - Loans & Advances	` 75.50 Cr.
(iii)	Current Assets - Loans and advances	` 294.33 Cr.
(iv)	Total assets of the company	` 618.55 Cr.
(v)	Intangible assets	` 6.35 Cr.
(vi)	Profit for the Year	` 8.15 Cr.
(vii)	Income from interest and dividends	` 62.31 Cr.
(viii)	Gross income	` 111.23 Cr.

Directors intend to apply for registration as Non-Banking Financial Company (NBFC) under Section 45-IA of the Reserve Bank of India (Amendment) Act, 1997. Advise.

[4 Marks]

(c) It was observed from the modified audit report of the financial statements of Shravasti Ltd. for the year ended 31st March, 2021 that depreciation of ` 3.95 crore for the year 2020-2021 had been charged off to the Statement of Profit and Loss instead of including it in "carrying value of asset under construction". State in relation to the audit for the year ended 31 st March 2022, whether such modification in the previous year's audit report would have any audit implication for the current year i.e. FY 2021-22 and if yes, how the auditor is required to deal with the same in his audit report for the current year?

[6 Marks]

6. (a) Comment on the validity of the appointments of Mr. A as an auditor of ABC Ltd. in the following situations: (Important)

(i) Mr. B, a partner of Mr. A held shares of face value of Rs. 1,00,000 in DEF Ltd., the holding company of ABC Ltd. Mr. B has sold the securities after a period of 45 days from the date of appointment of Mr. A as an auditor of ABC Ltd.

(ii) Mrs. A, wife of Mr. A had given a Financial guarantee for the principal amount of a debt owed by Mr. X to ABC Ltd. for Rs. 6 lakhs. Mr. X has repaid Rs. 5 lakhs to ABC Ltd. 2 days before the date of appointment of Mr. A as an auditor of the company.

[5 Marks]

(b) Evaluating the professional judgment exercised by the auditor is one of the important aspect under Quality Review, please explain the situation with reference to applicable Standard on Auditing.

[5 Marks]

(c) The management of MANIPRABH Limited, a manufacturing unit does not accept the recommendations for improvements made by the Operational Auditor. Suggest an alternative way to tackle the hostile management.

[4 Marks]

OR

(d) Indicate the precise nature of auditor's duties in the following situation: Based upon the legal opinion of a leading advocate, X Ltd. made a provision of Rs. 5 crores towards Income Tax liability. The assessing authority has worked out the liability at Rs. 15 crores. It is observed that the opinion of the advocate was inconsistent with legal position with regard to certain revenue items.

[4 Marks]