

**(GI-1, GI-2, GI-3, GI-4, VI-1 & SI-1)**

DATE: 26.08.2019

MAXIMUM MARKS: 100

TIMING: 3¼ Hours

**PAPER : AUDITING****DIVISION – A (MULTIPLE CHOICE QUESTIONS)****Questions (1-20) carry 1 Mark each****Questions (21-25) carry 2 Marks each**

- (1) As per SA 200 "Overall Objectives of the Independent Auditor", in conducting an audit of financial statements, the overall objectives of the auditor are:
- (a) To obtain reasonable assurance
  - (b) To report on the financial statements
  - (c) Both (a) and (b) above
  - (d) None of the above
- (2) (IESBA Code) related to an audit of financial statements establishes which of the following as the fundamental principles of professional ethics relevant to the auditor when conducting an audit of financial statements :
- (a) Integrity;
  - (b) Objectivity;
  - (c) Professional competence and due care;
  - (d) All of the above
- (3) The auditor's \_\_\_\_\_ safeguards the auditor's ability to form an audit opinion without being affected by any influences.
- (a) Objectivity
  - (b) Independence
  - (c) Confidentiality
  - (d) Integrity
- (4) With reference to SA 300, the auditor shall document:
- (a) The overall audit strategy
  - (b) The audit plan
  - (c) Any significant changes made during the audit engagement to the overall audit strategy or the audit plan, and the reasons for such changes.
  - (d) All of the above
- (5) The overall audit strategy and the audit plan remain the \_\_\_\_\_ responsibility.
- (a) Auditor's
  - (b) Management's
  - (c) Those charged with governance
  - (d) All of the above
- (6) Determining a percentage to be applied to a chosen benchmark (in relation to materiality) involves the exercise of \_\_\_\_\_
- (a) Independence
  - (b) Professional Judgment
  - (c) Professional skepticism
  - (d) All of the above

- (7) As per SQC-1 "An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than days after the date of the auditor's report".
- (a) 30
  - (b) 60
  - (c) 90
  - (d) 45
- (8) A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.
- (a) Positive confirmation request
  - (b) Non Response
  - (c) Negative Confirmation request
  - (d) Exception
- (9) Auditor's judgment as to sufficiency may be affected by which factor:
- (a) Materiality
  - (b) Risk of material misstatement
  - (c) Size and characteristics of the population.
  - (d) All of the above
- (10) Controls can be \_\_\_\_\_ related to an assertion.
- (a) Directly
  - (b) Indirectly
  - (c) Directly or indirectly
  - (d) None of the above
- (11) Control activities, whether within IT or manual systems, have various objectives and are applied at various organisational and functional levels. Which of the following is an example of control activities:
- (a) Authorization
  - (b) Performance reviews
  - (c) Information processing
  - (d) All of the above
- (12) When credit purchases of Rs. 5100 is recorded on credit side and credit sales of Rs. 5100 is recorded on debit side, this kind of error is called\_\_\_\_\_.
- (a) Error of omission
  - (b) Compensating error
  - (c) Error of principle
  - (d) Error of commission
- (13) If, as a result of a misstatement resulting from fraud, the auditor encounters exceptional circumstances that bring into question his ability to continue performing the audit, he shall-
- (a) Withdraw from the engagement immediately
  - (b) Report to Audit team regarding withdrawal
  - (c) Determine the professional and legal responsibilities applicable in the circumstances
  - (d) Ask the management for his withdrawal

- (14) Which of the following is an example of inflating cash payments?  
 (a) Making payments against purchase vouchers  
 (b) Teeming and lading  
 (c) Not accounting for cash sales fully  
 (d) Making payments against inflated vouchers
- (15) The type of errors, existence of which becomes apparent in the process of compilation of accounts is known as-  
 (a) Self-revealing errors  
 (b) Intentional errors  
 (c) Concealed errors  
 (d) Unconcealed errors
- (16) While auditing the books of accounts of QHMP Ltd., CA. Ranker, the statutory auditor of the company, came to know that the management of the company has recognized internally generated goodwill as a fixed asset. CA. Ranker discussed with the management that according to accounting standards, internally generated goodwill is not recognized as an asset because it is not an identifiable resource controlled by the enterprise that can be measured reliably at cost. However, the management is quite rigid to the accounting treatment followed for internally generated goodwill and not paying attention to the auditor. Thus, through an example, CA. Ranker explained which type of goodwill may be recognized as a fixed asset for which the management got justified. State which of the following examples the auditor must have given to the management?  
 (a) If an item meeting the definition of an intangible asset is acquired in a business combination, it forms part of the goodwill to be recognized at the date of the amalgamation.  
 (b) Only those goodwill needs to be recognized as a fixed asset which can be touched like physical assets, for example, land and buildings.  
 (c) Goodwill is recognised only when there is a contractual or other legal rights for a physical asset which shall not be amortized over the period.  
 (d) All of the above.
- (17) Eeyore Pvt. Ltd. is incorporated on 1<sup>st</sup> July, 2017. During the Financial Year ending on 31<sup>st</sup> March, 2018, the company did not opt for any borrowing at any point of time and have a total revenue of Rs. 60 Lakh. At the year end, it provides the following information regarding its paid-up capital and reserve & surplus-

Particulars	Amount (in Rs.)
Paid-up Capital	
- Consideration received in cash for equity shares (including unpaid calls of Rs. 5,00,000)	40,00,000
- Consideration received in cash for preference shares	25,00,000
- Bonus shares allotted	7,00,000
- Share application money received pending allotment	<u>10,00,000</u>
Sub-Total	82,00,000
Reserve & Surplus	
- Balance in Statement of Profit and Loss	15,00,000
- Capital Reserves	10,00,000
Sub-Total	<u>25,00,000</u>
GRAND TOTAL	1,07,00,000

You are provided with the provisions regarding applicability of Companies (Auditor's Report) Order, 2016, (CARO, 2016) issued under section 143(11) of the Companies Act, 2013 to a private limited company that it specifically exempts a private limited

company having a paid up capital and reserves and surplus not more than Rs. 1 crore as on the Balance Sheet date and which does not have total borrowings exceeding Rs. 1 crore from any bank at any point of time during the financial year and which does not have a total revenue as disclosed in Scheduled III to the Companies Act, 2013 exceeding Rs. 10 crore during the financial year. Considering the information given above, which of the following shall be considered as a reason regarding applicability or non-applicability of CARO, 2016?

- (a) Reporting under CARO, 2016 shall be applicable as the company is having a paid up capital and reserves and surplus of Rs. 1.07 crore i.e. more than Rs. 1 crore as on the Balance Sheet date.
  - (b) Reporting under CARO, 2016 shall be applicable as the company is having a paid up capital and reserves and surplus of Rs. 1.02 crore i.e. more than Rs. 1 crore as on the Balance Sheet date.
  - (c) Reporting under CARO, 2016 shall not be applicable as the company is having a paid up capital and reserves and surplus of Rs. 0.92 crore i.e. not more than Rs. 1 crore as on the Balance Sheet date.
  - (d) Reporting under CARO, 2016 shall not be applicable as the company is having a paid up capital and reserves and surplus of Rs. 0.82 crore i.e. not more than Rs. 1 crore as on the Balance Sheet date.
- (18) CA. Goofy has been appointed as an auditor for audit of a complete set of financial statements of Dippy Ltd., a listed company. The financial statements of the company are prepared by the management in accordance with the Accounting Standards prescribed under section 133 of the Companies Act, 2013. However, the inventories are misstated which is deemed to be material but not pervasive to the financial statements. Based on the audit evidences obtained, CA. Goofy has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with SA 570. Further, CA. Goofy is also aware of the fact that a qualified opinion would be appropriate due to a material misstatement of the Financial Statements. State what phrases should the auditor use while drafting such opinion paragraph?
- (a) In our opinion and to the best of our information and according to the explanations given to us, except for the effects of the matter described in the Basis for Qualified Opinion section of our report, the aforesaid financial statements present fairly, in all material respects, or give a true and fair view in conformity with the applicable financial reporting framework.
  - (b) In our opinion and to the best of our information and according to the explanations given to us, with the foregoing explanation, the aforesaid financial statements present fairly, in all material respects, or give a true and fair view in conformity with the applicable financial reporting framework.
  - (c) In our opinion and to the best of our information and according to the explanations given to us, subject to the misstatement regarding inventories, the aforesaid financial statements present fairly, in all material respects, or give a true and fair view in conformity with the applicable financial reporting framework.
  - (d) In our opinion and to the best of our information and according to the explanations given to us, with the explanation described in the Basis for Qualified Opinion section of our report, the aforesaid financial statements present fairly, in all material respects, or give a true and fair view in conformity with the applicable financial reporting framework.

- (19) While auditing the accounts of Thought Co. Ltd., CA. Bliss, the auditor of the company came across certain accounts payable balances for which direct confirmation procedure needs to be applied. Thus, for the year ending 31<sup>st</sup> March, 2018, he sent positive confirmation requests wherein the trade payables are requested to respond whether or not they are in agreement with the balance shown. The auditor received all the confirmation replies from the trade payables on time as correct except from five of them. What other option the auditor is left with regard to trade payables from which no reply for confirmation requests received?
- (a) Perform additional testing which may include agreeing the balance to subsequent cash paid.
  - (b) Accept the balances as it is assuming other replies against received confirmation requests being correct.
  - (c) Accept the balances as it is assuming that the trade payables must have replied in case of any discrepancies.
  - (d) None of the above.
- (20) CA. Daffy is the auditor of xBose Ltd. for the previous 2 years. However, due to certain unavoidable circumstances, no Annual General Meeting (AGM) was held for the current Financial Year ending on 31<sup>st</sup> March, 2018 within every possible time limit and thus, the ratification procedure for her appointment in the AGM could not be performed. Whether she may continue to hold the office of the auditor?
- (a) CA. Daffy may continue to hold the office of the auditor for the current Financial Year only and thereafter shall resign herself as the ratification procedure could not be completed.
  - (b) CA. Daffy shall continue to hold the office of the auditor and ask the Board to re- appoint her in a private meeting.
  - (c) CA. Daffy shall continue to hold the office of the auditor as no such ratification provisions for appointment by members at every AGM exist.
  - (d) CA. Daffy shall not continue to hold office of the auditor as the ratification procedure could not be completed as per proviso to section 139(1) of the Companies Act, 2013.
- (21) Marvin Ltd. is a renowned food chain supplier in a posh area providing restaurant facility along with food delivering. CA. Felix was appointed as an auditor of the company for the Financial Year 2017-18. While examining the books of account of the company, CA. Felix came to know about one of the major expenses of the company i.e. rent expense of Rs. 1,20,000 per month, for which he applied substantive analytical procedure for verification purpose. Explain, how would CA. Felix perform substantive analytical procedure in the given scenario?
- (a) CA. Felix would inspect every single rent invoice per month of Rs. 1,20,000 and verify other elements appropriately.
  - (b) CA. Felix would compare the rental expense of the company with that of another nearby company having corresponding dimensions, for high degree of accuracy.
  - (c) CA. Felix would select the first month rent invoice of Rs. 1,20,000 and appropriately verifying other elements would predict that the rent for the whole year would be Rs. 14,40,000 (i.e. Rs. 1,20,000 \* 12). Thereafter, he would compare the actuals with his prediction and follow-up for any fluctuation.
  - (d) (a) and (b), both.

- (22) Coyote Ltd. is dealing in trading of electronic goods. Huge inventory (60% approximately) of the company is lying on consignment (i.e. under the custody of third party). CA. Star, the auditor of the company, wants to obtain sufficient appropriate audit evidence regarding the existence and condition of the inventory lying on consignment. Thus, he requested & obtained confirmation from the third party as to the quantities and condition of inventory held on behalf of the entity, however, it raised doubts about the integrity and objectivity of the third party. Which of the following other audit procedures may be performed by CA. Star to obtain sufficient appropriate audit evidence regarding the existence and condition of the inventory under the custody of third party?
- (a) Attend third party's physical counting of inventory.
  - (b) Arrange for another auditor to attend third party's physical counting of inventory.
  - (c) Inspect warehouse receipts regarding inventory held by third parties.
  - (d) All of the above.
- (23) In July, 2018, M/s Tom & Co. entered into an agreement with M/s Jerry & Co. under which a machinery would be let on hire and M/s Jerry & Co. would have the option to purchase the machinery in accordance with the terms of the agreement. Thus, M/s Jerry & Co. agreed to pay M/s Tom & Co. a settled amount in periodical instalments. The property in the goods shall be passed to M/s Jerry & Co. on the payment of last of such instalments. While checking such hire-purchase transaction, what would the auditor examine?
- (a) That the periodical instalments paid are charged as an expenditure by M/s Jerry & Co.
  - (b) That the hire purchase agreement specifies clearly the hire-purchase price of the machinery to which the agreement relates.
  - (c) That M/s Tom & Co. charges depreciation throughout the life of the machinery.
  - (d) All of the above.
- (24) The management of Magoo Ltd. has developed a strong internal control in its accounting system in such a way that the work of one person is reviewed by another. Since no individual employee is allowed to handle a task alone from the beginning to the end, the chances of early detection of frauds and errors are high. CA. Olive has been appointed as an auditor of the company for current Financial Year 2017-18. Before starting the audit, she wants to evaluate the internal control system of Magoo Ltd. To facilitate the accumulation of the information necessary for the proper review and evaluation of internal controls, CA. Olive decided to use internal control questionnaire to know and assimilate the system and evaluate the same. Which of the following questions need not be framed under internal control questionnaire relating to purchases?
- (a) Are authorized signatories for purchases limited to elected officials?
  - (b) Are payments approved only on original invoices?
  - (c) Does authorized officials thoroughly review the documents before signing cheques?
  - (d) Are monthly bank reconciliations implemented for each and every bank accounts of the company?
- (25) CA. Bobby is a recently qualified Chartered Accountant. He is appointed as an auditor of Droopy Ltd. for the current Financial Year 2017-18. He is quite conservative in nature which is also replicated in his professional work. CA. Bobby is of the view that he shall record all the matters related to audit, audit procedures

to be performed, audit evidence obtained and conclusions reached. Thus, he maintained a file and recorded each and every of his findings during the audit. His audit file, besides other thing, includes audit programmes, notes reflecting preliminary thinking, letters of confirmation, e-mails concerning significant matters, etc. State which of the following need not be included in the audit documentation?

- (a) Audit programmes.
- (b) Notes reflecting preliminary thinking.
- (c) Letters of confirmation.
- (d) E-mails concerning significant matters.

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**Division B-Descriptive Questions****Question No. 1 is compulsory****Attempt any four questions from the Rest.**

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**Question 1:**

**Examine with reasons (in short) whether the following statements are correct or incorrect : (Attempt any 7 out of 8)**

- (i) Audit procedures used to gather audit evidence may be effective for detecting an intentional misstatement.
- (ii) An audit is an official investigation into alleged wrongdoing.
- (iii) The matter of difficulty, time, or cost involved is in itself a valid basis for the auditor to omit an audit procedure for which there is no alternative.
- (iv) There is no relation between Audit Plans and knowledge of the client's business.
- (v) Planning is not a discrete phase of an audit, but rather a continual and iterative process.
- (vi) Audit documentation is a substitute for the entity's accounting records.
- (vii) An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 30 days after the date of the auditor's report.
- (viii) When the auditor has determined that an assessed risk of material misstatement at the assertion level is a significant risk, the auditor shall not perform substantive procedures that are specifically responsive to that risk.

**(2 x 7 = 14 Marks)****Question 2:**

- (a)** Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. Explain

**(3 Marks)**

- (b)** The chief utility of audit lies in reliable financial statements on the basis of which the state of affairs may be easy to understand. Apart from this obvious utility, there are other advantages of audit. Some or all of these are of considerable value even to those enterprises and organisations where audit is not compulsory. Explain.

**(4 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)**

- (d) Explain the benefits of planning in the audit of financial statements. **(3 Marks)**

**Question 3:**

- (a) Mr. A, a chartered accountant, has been appointed as an auditor of Laxman Ltd. in the Annual General Meeting of the company held in September, 2016, which assignment he accepted. Subsequently in January, 2017 he joined Mr. B, another chartered accountant, who is the Manager Finance of Laxman Ltd., as partner. Analyse and explain. **(4 Marks)**
- (b) CA. Donald was appointed as the auditor of PS Ltd. at the remuneration of Rs. 30,000. However, after 4 months of continuing his services, he could not continue to hold his office of the auditor as his wife got a government job at a distant place and he needs to shift along with her to the new place. Thus, he resigned from the company and did not perform his responsibilities relating to filing of statement to the company and the registrar indicating the reasons and other facts as may be relevant with regard to his resignation. How much fine may he be punishable with under section 140(3) for non-compliance of section 140(2) of the Companies Act, 2013? **(4 Marks)**
- (c) The first auditor of Bhartiya Petrol Ltd., a Government company, was appointed by the Board of Directors. Analyse and Explain **(3 Marks)**
- (d) Why Central Government permission is required, when the auditors are to be removed before expiry of their term, but the same is not needed when the auditors are changed after expiry of their term? **(3 Marks)**

**Question 4:**

- (a) Explain the duties of Auditor to inquire under Section 143(1) of the Companies Act, 2013. **(4 Marks)**
- (b) The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error. Explain **(3 Marks)**
- (c) Define Emphasis of Matter paragraph. When the auditor shall include an Emphasis of Matter paragraph in the auditor's report? Also explain how the auditor would include an Emphasis of Matter in the auditor's report? **(4 Marks)**
- (d) Discuss the different ways in which defalcation of cash may take place. **(3 Marks)**

**Question 5:**

- (a) On the basis of which assumption the financial statements of a company are prepared. Explain. Also describe the objectives of the auditor regarding going concern. **(3 Marks)**



- (b) 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. Explain.  
**(4 Marks)**
- (c) Explain the meaning, objectives and scope of internal audit functions as per SA 610. Also discuss who can be appointed as Internal Auditor?  
**(4 Marks)**
- (d) What do you mean by Audit Documentation? Also explain the nature and purpose of audit documentation.  
**(3 Marks)**

**Question 6:**

- (a) Explain how would you deal as an auditor if, as a result of a misstatement resulting from fraud or suspected fraud, you encounter exceptional circumstances that bring into question your ability to continue performing the audit.  
**(3 Marks)**
- (b) Explain techniques available as substantive analytical procedures.  
**(4 Marks)**
- (c) Explain clearly the purpose of communicating key audit matters.  
**(3 Marks)**
- (d) You have been appointed as an auditor of an NGO, briefly state the points on which you would concentrate while planning the audit of such an organisation?  
**(4 Marks)**

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