

DATE: 10.04.2023

(GI-8, FMT)  
MAXIMUM MARKS: 100

TIMING: 3¼ Hours

**PAPER : AUDITING**

**DIVISION – A (MULTIPLE CHOICE QUESTIONS)**

**QUESTIONS (1-20) CARRY 1 MARK EACH**

1. Statement I : A firm whereof majority of partners practising in India are qualified for appointment may be appointed by its firm name to be auditor of a company.  
Statement II : Where a firm including a limited liability partnership is appointed as an auditor of a company, all the partners shall be authorised to act and sign on behalf of the firm.
  - (a) Only Statement I is correct
  - (b) Only Statement II is correct
  - (c) Both statements are correct
  - (d) Both Statements are incorrect
2. If the auditor is unable to obtain sufficient appropriate audit evidence regarding the opening balances, the auditor shall express:
  - (a) a disclaimer opinion
  - (b) a qualified opinion
  - (c) a qualified opinion or a disclaimer of opinion, as appropriate, in accordance with SA 705.
  - (d) unmodified opinion
3. 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.
4. Which of the following is not an example of an event or condition that may cast significant doubt on entity's ability to continue as a going concern:
  - (a) Loss of key management without replacement
  - (b) Adverse key financial ratios
  - (c) Inability to pay creditors on due date
  - (d) Current year profit turns to loss after providing depreciation

5. A failure of the confirming party to respond, or fully respond, to a positive confirmation request, or a confirmation request returned undelivered is called-
- Negative confirmation request
  - Non-response
  - Exception
  - Positive confirmation request
6. Which of the following is not correct:
- SA 700- Forming an Opinion and Reporting on Financial Statements
  - SA 705- Modified Opinion
  - SA 701- Communicating Key Audit Matters
  - SA 706- Comparative Information
7. The concept of materiality is applied by the auditor :
- in planning and performing the audit
  - in evaluating the effect of identified misstatements on the audit
  - both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit
  - none of the above is correct
8. Statement 1: Audit procedures consist of Risk Assessments Procedures and other procedures.  
Statement 2: Substantive procedures consist of test of details and analytical procedures.
- Only Statement 1 is correct
  - Only Statement 2 is correct
  - Both 1 & 2 are correct
  - Both 1 & 2 are incorrect
9. With respect to the forms specified by companies (Cost Records & Audit) Rule 2014, which of the following is incorrect combination:
- Form CRA 1- Maintenance of cost records by the Company.
  - Form CRA 2- Intimation of appointment of another cost auditor to Central Government.
  - Form CRA 3- Submission of Cost Audit Report to the Board of Directors of the company.
  - Form CRA 4- Submission of Cost Audit Report by the company to the Registrar.
10. 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?
- Attend third party's physical counting of inventory.
  - Arrange for another auditor to attend third party's physical counting of inventory.
  - Inspect warehouse receipts regarding inventory held by third parties.
  - All of the above.

11. 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?
12. Statement I As per the Standard on Auditing (SA) 520 "Analytical Procedures", the term "analytical procedures" means evaluations of financial information through analysis of plausible relationships among financial data.  
Statement II Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.
- (a) Only Statement I is correct
  - (b) Only Statement II is correct
  - (c) Both statements are correct
  - (d) Both Statements are incorrect
13. Judging the significance of a matter requires of the facts and circumstances.
- (a) objective analysis
  - (b) subjective analysis
  - (c) Both subjective and objective analysis
  - (d) qualitative analysis
14. \_\_\_\_\_ refer to the audit procedures performed to obtain an understanding of the entity and its environment, including the entity's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.
- (a) Audit assessment procedures
  - (b) substantive procedures
  - (c) test of control
  - (d) Risk assessment procedures
15. 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.
16. When more persuasive audit evidence is needed regarding the effectiveness of a control,
- (a) it may be appropriate to increase the extent of testing of the control and reduce the extent of the degree of reliance on controls.
  - (b) it may be appropriate to decrease the extent of testing of the control as well as the degree of reliance on controls.
  - (c) it may be appropriate to decrease the extent of testing of the control and increase the extent of the degree of reliance on controls.
  - (d) it may be appropriate to increase the extent of testing of the control as well as the degree of reliance on controls.
17. An important factor in determining the form, content and extent of audit documentation of significant matters is the extent of evaluating the results.
- (a) professional skepticism
  - (b) professional integrity
  - (c) professional judgment
  - (d) Professional sincerity
18. 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.
19. Which of the following is not an example of Analytical Procedures having consideration of comparisons of the entity's financial information:
- (a) Comparable information for prior periods.
  - (b) Anticipated results of the entity, such as budgets or forecasts, or expectations of the auditor, such as an estimation of depreciation.
  - (c) Similar industry information, such as a comparison of the entity's ratio of sales to accounts receivable with industry averages or with other entities of comparable size in the same industry.
  - (d) Among elements of financial information that would be expected to conform to a predictable pattern based on the entity's experience, such as gross margin percentages.

20. Audit evidence is necessary to support the auditor's opinion and report. It is in nature and is primarily obtained from audit procedures performed during the course of the audit.
- cumulative
  - regressive
  - selective
  - objective

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**QUESTIONS (21-25) CARRY 2 MARKS EACH**

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21. Which of the following is required documentation in an audit in accordance with generally accepted auditing standards?
- A flowchart or narrative of the information system relevant to financial reporting describing the recording and classification of transactions for financial reporting.
  - An audit plan setting forth in detail the procedures necessary to accomplish the engagement's objectives.
  - A planning memorandum establishing the timing of the audit procedures and coordinating the assistance of entity personnel.
  - An internal control questionnaire identifying controls that assure specific objectives will be achieved.
22. Which of the following statement is not true
- The auditor shall express an opinion on financial statements
  - Auditor's opinion is not guarantee to future viability of business
  - Auditor is responsible for prevention and detection of fraud and error in financial statements
  - Auditor should examine whether recognized accounting principles have been followed
23. 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.)
<b>Paid-up Capital</b>	
- 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	10,00,000
<b>Sub-Total</b>	<b>82,00,000</b>
<b>Reserve &amp; Surplus</b>	
- Balance in Statement of Profit and Loss	15,00,000
- Capital Reserves	10,00,000
<b>Sub-Total</b>	<b>25,00,000</b>
<b>GRAND TOTAL</b>	<b>1,07,00,000</b>

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.
24. 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 31st 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.
25. 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.

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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) Tangible assets are depreciated when the asset is actually put to active use.
- (ii) SA 210 does not require the auditor to agree management's responsibilities in an engagement letter or other suitable form of written agreement.
- (iii) Government audit does not serve as a mechanism or process for public accounting of government funds.
- (iv) A detailed Audit Programme once prepared for a business can be used for all business under all circumstances.
- (v) The audit engagement letter is sent by the client to auditor.
- (vi) The auditor has to report under section 143 of companies act, 2013 whether company has adequate internal controls in place and overall effectiveness of such internal controls.
- (vii) An account should be treated as 'out of order' if the outstanding balance remains continuously in excess of the sanctioned limit/drawing power. In cases where the outstanding balance in the principal operating account is less than the sanctioned limit/drawing power, but there are no credits continuously for 180 days as on the date of Balance Sheet or credits are not enough to cover the interest debited during the same period, these accounts should be treated as 'out of order'.
- (viii) Statistical sampling has narrower application where a population to be tested consists of a large number of similar items.

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

**Question 2:**

**(a)** Engagement partner of Audit Firm MKC AND COMPANY thinks that Planning an audit would involve establishing the overall audit strategy for the engagement and developing an audit plan. Also, Adequate planning would benefit the audit of financial statements in several ways. Analyse explaining the benefits of adequate planning.

**(4 Marks)**

**(b)** The auditor of FAST CARS Ltd obtains an understanding of the control environment. As part of obtaining this understanding, the auditor evaluates whether management has created and maintained a culture of honesty and ethical behaviour and the strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control.

Advise what is included in control environment. Also explain the elements of control environment.

**(4 Marks)**

**(c)** The practice of appointing Chartered Accountants as joint auditors is quite widespread in big companies and corporations. Explain stating the advantages of the joint audit.

**(6 Marks)**

**Question 3:**

**(a)** Having obtained an understanding of the IT systems and the automated environment of a company, the auditor should understand the risks that arise from the use of IT systems. Explain those risks.

**(4 Marks)**

(b) There is a growing realisation that the traditional approach to audit is economically wasteful because all efforts are directed to check all transactions without exception. Explain.

**(4 Marks)**

(c) Explain with examples the audit procedure to establish the existence of intangible fixed assets as at the period- end.

**(6 Marks)**

**Question 4:**

(a) Audit evidence is all the information used by the auditor in arriving at the conclusions on which the audit opinion is based. Written representations are necessary information that the auditor requires in connection with the audit of the entity's financial statements. Accordingly, similar to responses to inquiries, written representations are audit evidence. Explain stating clearly objectives of the auditor regarding written representation.

**(4 Marks)**

(b) In considering the qualitative aspects of the entity's accounting practices, the auditor may become aware of possible bias in management's judgments. The auditor may conclude that lack of neutrality together with uncorrected misstatements causes the financial statements to be materially misstated. Explain and analyse the indicators of lack of neutrality with examples, wherever required.

**(6 Marks)**

(c) Explain in detail the duties of Comptroller and Auditor General of India.

**(4 Marks)**

**Question 5:**

(a) Advances generally constitute the major part of the assets of the bank. There are large number of borrowers to whom variety of advances are granted. The audit of advances requires the major attention from the auditors. In carrying out audit of advances, the auditor is primarily concerned with obtaining evidence about, among other points, the amounts included in balance sheet in respect of advances are outstanding at the date of the balance sheet. Explain

**(6 Marks)**

(b) The nature of related party relationships and transactions may, in some circumstances, give rise to higher risks of material misstatement of the financial statements than transactions with unrelated parties. Explain with the help of at least three examples.

**(4 Marks)**

(c) Give some of the points that an auditor should consider to obtain an understanding of the company's automated environment.

**(4 Marks)**

**Question 6:**

(a) Explain some of the commonly used methods for testing in an automated environment.

**(4 Marks)**

- (b)** Auditor of A Ltd while conducting audit in the course of the performance of his duties as auditor, believes with reasons that "an offence of fraud involving such amount or amounts as may be prescribed, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as may be prescribed". Analyse and also explain the manner of reporting the matter to the Central Government.  
**(6 Marks)**
- (c)** The auditor can obtain sufficient appropriate audit evidence about advances by study and evaluation of internal controls relating to advances. Explain in the context of Audit of Banks.  
**(4 Marks)**

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Mittal Commerce Classes Pvt. Ltd.