

**MITTAL COMMERCE CLASSES**

**Intermediate Course: Group – II**  
**DATE: 27.08.2024**

**MAXIMUM MARKS: 100**

**(Mock Test Paper : 2)**  
**TIMING: 3¼ Hours**

**AUDITING AND ETHICS**

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

**Case Scenario 1 carries 10 Marks**

**Case Scenario 2 carries 10 Marks**

**General MCQs (10 MCQs x 2 Marks Each = 20 Marks)**

**Total 30 Marks**

**Case Scenario 1 to 5:**

1. Ans. (c)
2. Ans. (d)
3. Ans. (b)
4. Ans. (d)
5. Ans. (b)

**MCQ [5 MCQ of 2 Marks Each : Total 10 Marks]**

**Case Scenario 6 to 10:**

6. Ans. (a)
7. Ans. (b)
8. Ans. (c)
9. Ans. (c)
10. Ans. (a)

**MCQ [5 MCQ of 2 Marks Each : Total 10 Marks]**

11. Ans. (a)
  12. Ans. (c)
  13. Ans. (b)
  14. Ans. (b)
  15. Ans. (d)
- } {2 M Each}

**DIVISION B-DESCRIPTIVE QUESTIONS**

**QUESTION NO. 1 IS COMPULSORY**

**ATTEMPT ANY FOUR QUESTIONS THE REMAINING FIVE QUESTIONS**

**Answer 1:**

**(a)** Judging the significance of a matter requires an objective analysis of the facts and circumstances.

Examples of significant matters include:

Matters that give rise to significant risks.

- Results of audit procedures indicating (a) that the financial statements could be materially misstated, or (b) a need to revise the auditor’s previous assessment of the risks of material misstatement and the auditor’s responses to those risks. } {2 M}
- Circumstances that cause the auditor significant difficulty in applying necessary audit procedures. } {1 M Each}
- Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter Paragraph in the auditor’s report.

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### Answer:

(b) The engagement partner should document following matters pertaining to an audit engagement: -

- (a) Issues identified with respect to compliance with relevant ethical requirements and how they were resolved.
- (b) Conclusions on compliance with independence requirements that apply to the audit engagement, and any relevant discussions with the firm that support these conclusions.
- (c) Conclusions reached regarding the acceptance and continuance of client relationships and audit engagements.
- (d) The nature and scope of, and conclusions resulting from, consultations undertaken during the course of the audit engagement.

{1 M  
Each}

### Answer:

(c) The auditor should, on a test check basis, verify the calculation of interest and ensure that:

- (a) Interest has been provided on all deposits upto the date of the balance sheet;
- (b) Interest rates are in accordance with the bank's internal regulations, the RBI directives and agreements with the respective deposit holder;
- (c) Interest on savings accounts are in accordance with the rules framed by the bank/RBI in this behalf.
- (d) Interest on inter-branch balances has been provided at the rates prescribed by the head office/RBI.

{1 M for  
Any 3  
Points}

### Answer:

(d) Under section 77 of the Multi-State Co-operative Societies Act, 2002, where the Central Government is of the opinion:

- (a) that the affairs of any Multi-State co-operative society are not being managed in accordance with self-help and mutual deed and co-operative principles or prudent commercial practices or with sound business principles; or
- (b) that any Multi-State co-operative society is being managed in a manner likely to cause serious injury or damage to the interests of the trade industry or business to which it pertains; or
- (c) that the financial position of any Multi-State co-operative society is such as to endanger its solvency.

{1 M  
Each}

### Answer 2:

(a) Where the company has any transactions with companies struck off under section 248 of the Companies Act, 2013 or section 560 of Companies Act, 1956, the Company shall disclose the following details:-

Name of struck off Company {1 M}	Nature of transactions with struck off Company {1 M}	Balance outstanding {1 M}	Relationship with the Struck off company, if any, to be disclosed {1 M}
	Investments in securities		
	Receivables		
	Payables		
	Shares held by struck off company		
	Other outstanding balances (to be specified)		

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### Answer:

**(b)** The entity has valid legal ownership rights over the PPE claimed to be held by the entity and recorded in the financial statements-

- In addition to the procedures undertaken for verifying completeness of additions to PPE during the period under audit, the auditor while performing testing of additions should also verify that all PPE purchase invoices are in the name of the entity that entitles legal title of ownership to the respective entity.
- For all additions to land and building in particular, the auditor should check the conveyance deed/ sale deed to verify whether the entity is the legal and valid owner or not.
- The auditor should insist and verify the original title deeds for all immoveable properties held as at the balance sheet date.
- In case the entity has given such immoveable property as security for any borrowings and the original title deeds are not available with the entity, the auditor should request the entity's management for obtaining a confirmation from the respective lenders that they are holding the original title deeds of immoveable property as security.
- In addition, the auditor should also verify the register of charges, available with the entity to assess that any charge has been created against the PPE.

{1 M for  
Any 4  
Points}

### Answer:

**(c)** Given below are some such risks that should be considered:

- Inaccurate processing of data, processing inaccurate data, or both.
- Unauthorized access to data.
- Direct data changes (backend changes).
- Excessive access / Privileged access (super users).
- Lack of adequate segregation of duties.
- Unauthorized changes to systems or programs.
- Failure to make necessary changes to systems or programs.
- Loss of data.

{1 M for  
Any 3  
Points}

### Answer:

**(d)** The auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work. The nature, timing and extent of the direction and supervision of engagement team members and review of their work vary depending on many factors, including: -

1. The size and complexity of the entity.
2. The area of the audit.
3. The assessed risks of material misstatement
4. The capabilities and competence of the individual team members performing the audit work.

{1 M for  
Any 3  
Points}

### Answer 3:

**(a)** As per SA-610 "using the work of external auditor" the external auditor shall not use internal auditors to provide direct assistance to perform procedures that:

- (a) Involve making significant judgments in the audit;
- (b) Relate to higher assessed risks of material misstatement where the judgment required in performing the relevant audit procedures or evaluating the audit evidence gathered is more than limited;
- (c) Relate to work with which the internal auditors have been involved and which has already been, or will be, reported to management or those charged with governance by the internal audit function; or

{1 M  
Each}

- (d) Relate to decisions the external auditor makes in accordance with this SA regarding the internal audit function and the use of its work or direct assistance.
- Ramprakash & Co. cannot use work of internal auditor to provide direct assistant for significant matter in the light of above provision.

**Answer:**

- (b) While performing audit, auditor has to see that financial statements would not mislead anybody by ensuring that: -
- o the accounts have been drawn up with reference to entries in the books of account;
  - o the entries in the books of account are adequately supported by sufficient and appropriate evidence;
  - o none of the entries in the books of account has been omitted in the process of compilation;
  - o the information conveyed by the statements is clear and unambiguous;
  - o the financial statement amounts are properly classified, described and disclosed in conformity with accounting standards; and
  - o the statement of accounts presents a true and fair picture of the operational results and of the assets and liabilities.

{1 M for  
Any 4  
Points}

**Answer:**

- (c) When the auditor disclaims an opinion on the financial statements due to an inability to obtain sufficient appropriate audit evidence, the auditor shall amend the description of the auditor's responsibilities required by SA 700 (Revised) to include only the following:
- (a) A statement that the auditor's responsibility is to conduct an audit of the entity's financial statements in accordance with Standards on Auditing and to issue an auditor's report;
  - (b) A statement that, however, because of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and
  - (c) The statement about auditor independence and other ethical responsibilities required by SA 700 (Revised).

{1 M  
Each}

**Answer:**

- (d) All sales are accurately measured as per applicable accounting standards and correctly journalized, summarized, and posted
- Trace a few transactions from inception to completion. (Examination in depth)  
E.g: Take few sales transaction, and check from the receipt of sales order to the payment of receivable balance, every underlying document to ensure if it is properly recorded at every stage and measured accurately taking into consideration all the incentives, discounts, if any. The recognition shall be according to the revenue recognition policy of the entity.
  - if the client is engaged in export sales, then compliance with AS 11 shall be ensured.
  - Auditor must understand client's operations and related GAAP issues e.g. point of sale revenue recognition vs. percentage of completion, wherever applicable.

{1 M for  
Any 3  
Points}

- Compare the rate of sales affected with related parties and review them for collectability, as well as whether they were properly authorized and the value of such transactions were reasonable and at arm’s length.

**Answer 4:**

**(a)** Examples of indicators of significant deficiencies in internal control

- 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.
- Absence of a risk assessment process within the entity where such a process would ordinarily be expected to have been established.
- 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.
- Evidence of an ineffective response to identified significant risks (e.g., absence of controls over such a risk).
- Misstatements detected by the auditor’s procedures that were not prevented, or detected and corrected, by the entity’s internal control.
- Disclosure of a material misstatement due to error or fraud as prior period items in the current year’s Statement of Profit and Loss.
- Evidence of management’s inability to oversee the preparation of the financial statements.

**{1 M for Any 4 Points}**

**Answer:**

**(b)** Matters such as-

- Integrity of principal owners and key management,
- Competence of engagement team to perform the audit engagement,
- Implications of matters that have arisen during current and previous audit engagement may need to be considered,
- Besides, in case of initial engagements, communication with predecessor auditor should be made, where there has been a change of auditors.

**{1 M Each}**

**Answer:**

**(c)** The audit documentation shall include: -

- (a) The amount below which misstatements would be regarded as clearly trivial;
- (b) All misstatements accumulated during the audit and whether they have been corrected; and
- (c) The auditor’s conclusion as to whether uncorrected misstatements are material, individually or in aggregate, and the basis for that conclusion.

**{1 M Each}**

**Answer:**

**(d)** Ethical guidance may follow principles-based approach or rules-based approach. The essence of principles-based approach to ethics is that it requires compliance with spirit of ethics. It requires accountants to exercise professional judgment in every situation based upon their professional knowledge, skill and expertise. It requires that accountants should use professional judgment to evaluate every situation to arrive at conclusions.

**{1 M}**

However, rules-based approach to ethics strictly follows clearly established rules. It may lead to a narrow outlook and spirit of ethics may be overlooked while strictly adhering to rules. Further, rules-based approach is somewhat rigid as it may not be possible to deal with every practical situation relying upon rules. } {1 M}  
Therefore, it is necessary that spirit of code is followed. } {1 M}

**Answer 5:**

- (a)
1. Verify that the Provident Fund money of the staff has been invested in appropriate securities.
  2. Vouch donations, if any with the list published with the annual report. If some donations were meant for any specific purpose, see that the money was utilised for the purpose.
  3. Vouch, all capital expenditure in the usual way and verify the same with the sanction for the Committee as contained in the minute book.
  4. Vouch, in the usual manner, all establishment expenses and enquire into any unduly heavy expenditure under any head. If there was any annual budget prepared, see that any excess under any head over the budgeted amount was duly sanctioned by the Managing Committee. If not, bring it to the Committee's notice in your report.
  5. See that increase in the salaries of the staff have been sanctioned and minuted by the Committee.
- } {1 M for Any 4 Points}

**Answer:**

- (b) Whether during the year the company has made investments in, provided any guarantee or security or granted any loans or advances in the nature of loans, secured or unsecured, to companies, firms, Limited Liability Partnerships or any other parties, if so,-
- (a) whether during the year the company has provided loans or provided advances in the nature of loans, or stood guarantee, or provided security to any other entity [not applicable to companies whose principal business is to give loans], if so, indicate-
- (A) the aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to subsidiaries, joint ventures and associates;
  - (B) the aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to parties other than subsidiaries, joint ventures and associates;
- (b) whether the investments made, guarantees provided, security given and the terms and conditions of the grant of all loans and advances in the nature of loans and guarantees provided are not prejudicial to the company's interest;
- (c) in respect of loans and advances in the nature of loans, whether the schedule of repayment of principal and payment of interest has been stipulated and whether the repayments or receipts are regular;
- (d) if the amount is overdue, state the total amount overdue for more than ninety days, and whether reasonable steps have been taken by the company for recovery of the principal and interest;
- (e) whether any loan or advance in the nature of loan granted which has fallen due during the year, has been renewed or extended or fresh loans granted to settle the overdues of existing loans given to the same parties, if so, specify the aggregate amount of such dues renewed or extended or settled by fresh loans and the percentage of the aggregate to the total loans or advances in
- } {1 M for Any 4 Points}

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- the nature of loans granted during the year [not applicable to companies whose principal business is to give loans];
- (f) whether the company has granted any loans or advances in the nature of loans either repayable on demand or without specifying any terms or period of repayment, if so, specify the aggregate amount, percentage thereof to the total loans granted, aggregate amount of loans granted to Promoters, related parties as defined in clause (76) of section 2 of the Companies Act, 2013.

### Answer:

- (c) The auditor of Nitesh India Ltd should express modify opinion in following circumstances.
- (a) Management refuses to give the auditor permission to communicate or meet with the entity's external legal counsel,  
**Or** the entity's external legal counsel refuses to respond appropriately to the letter of inquiry, or is prohibited from responding; and {2 M}
- (b) the auditor is unable to obtain sufficient appropriate audit evidence by performing alternative audit procedures,  
 the auditor shall modify the opinion in the auditor's report in accordance with SA 705. {1 M}

### Answer:

- (d) Much of the information obtained by the auditor's inquiries is obtained from management and those responsible for financial reporting. However, the auditor may also obtain information, or a different perspective in identifying risks of material misstatement, through inquiries of others within the entity and other employees with different levels of authority.
- Inquiries directed toward internal audit personnel may provide information about internal audit procedures performed during the year relating to the design and effectiveness of the entity's internal control and whether management has satisfactorily responded to findings from those procedures.
  - Inquiries of employees involved in initiating, processing or recording complex or unusual transactions may help the auditor to evaluate the appropriateness of the selection and application of certain accounting policies.
  - Inquiries directed toward in-house legal counsel may provide information about such matters as litigation, compliance with laws and regulations, knowledge of fraud or suspected fraud affecting the entity, warranties, post-sales obligations, arrangements (such as joint ventures) with business partners and the meaning of contract {1 M for Any 3 Points}
  - Inquiries directed towards marketing or sales personnel may provide information about changes in the entity's marketing strategies, sales trends, or contractual arrangements with its customers.
  - Inquiries directed to the risk management function (or those performing such roles) may provide information about operational and regulatory risks that may affect financial reporting.
  - Inquiries directed to information systems personnel may provide information about system changes, system or control failures, or other information system- related risks.

### Answer 6:

- (a) Communication from auditor is important with those charged with governance. An effective two-way communication is important in assisting: -
- (a) The auditor and those charged with governance in understanding matters related to the audit in context, and in developing a constructive working {1 M}

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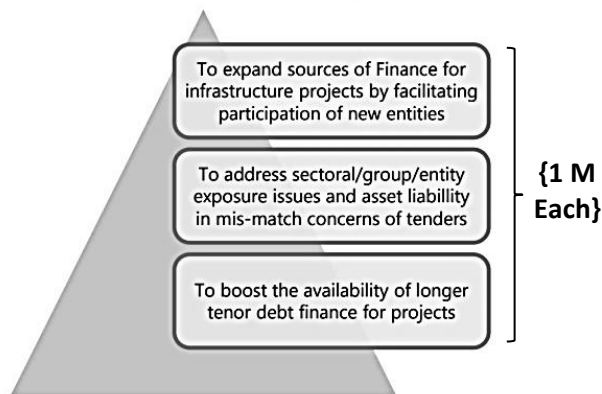
- relationship. This relationship is developed while maintaining the auditor's independence and objectivity.
- (b) The auditor in obtaining from those charged with governance information relevant to the audit. For example, those charged with governance may assist the auditor in understanding the entity and its environment, in identifying appropriate sources of audit evidence, and in providing information about specific transactions or events; and {2 M}
- (c) Those charged with governance in fulfilling their responsibility to oversee the financial reporting process, thereby reducing the risks of material misstatement of the financial statements. {1 M}

### Answer:

- (b) To address the issue, the following guiding principles are to be applied: -
- For the public to have confidence in the quality of audit, it is essential that auditors should always be and appears to be independent of the entities that they are auditing.
  - Before taking on any work, an auditor must conscientiously consider whether it involves threats to his independence.
  - When such threats exist, the auditor should either desist from the task or eliminate the threat or at the very least, put in place safeguards which reduce the threats to an acceptable level. All such safeguards measures need to be recorded in a form that can serve as evidence of compliance with due process.
  - If the auditor is unable to fully implement credible and adequate safeguards, then he must not accept the work.
- {1 M Each}

### Answer:

- (c) **OBJECTIVE OF TAKEOUT FINANCE**



### Answer:

- (d) Manual elements in internal control may be more suitable where judgment and discretion are required such as for the following circumstances:
- Large, unusual or non-recurring transactions.
  - Circumstances where errors are difficult to define, anticipate or predict.
  - In changing circumstances that require a control response outside the scope of an existing automated control.
  - In monitoring the effectiveness of automated controls.
- {1 M Each for Any 3 Points}

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