

Intermediate Course: Group – II (Mock Test Paper – Series : 1)
DATE: 10.09.2024 MAXIMUM MARKS: 100 TIMING: 3¹/₄ Hours

PAPER 5: AUDITING AND ETHICS

DIVISION - A (MULTIPLE CHOICE QUESTIONS)

Case Scenario 1 carries 10 Marks

Case Scenario 2 carries 08 Marks

Case Scenario 3 carries 06 Marks

General MCQs (3 MCQs x 2 Marks Each = 06 Marks)

Total 30 Marks

Q. 1 to Q. 5: CASE SCENARIO

Sun Group of companies is a retail chain involved in the selling of daily consumer needs directly to the customer. They are in the process of appointing an audit firm for the audit of their accounts for the financial year 2021-22. Sun Group is a South Indian based consumer store having a total of 16 outlets across 4 cities in South India.

Sachin & Co. is appointed as the principal auditor for the entire group. Companies Act 2013 prescribes in detail the terms of this audit engagement. Further, there are many branch auditors appointed for the outlets in the other cities. The company also has an internal audit function conducted on quarterly basis by Shyam & Co. Following are the observations during the course of the statutory audit:

- (a) One of the discounts offered by the store is in the form of payback cards where reward points are accumulated and the customer can redeem the same on subsequent purchase. The management and internal auditors are of the opinion that the points redeemed are to be treated as trade discount. The external auditors are doubtful on the matter.
- (b) One of the outlet in Chennai region is in the verge of getting closed and is only left with low value stock to be cleared before closure. During the year, the sales were only around ₹ 1,40,000/- and the auditor considers this component immaterial. All other outlets are performing well with good revenue share.
- (c) The gratuity valuation of the employees of the retail chain is done by an external valuer. The auditor, considering the quantum involved appoints an external auditor's expert for the verification of the actuarial calculation of gratuity.

From the above facts, answer the following questions by choosing the correct answer:

- 1. As per SA 210 Agreeing the Terms of Audit Engagement, which of the following statement is correct?
 - (a) Though law prescribes in sufficient detail the terms of the audit engagement, the auditor still needs to record them in a written agreement and also seek written agreement from management that it acknowledges and understands that it has responsibility for the preparation of financial statements.
 - (b) Since law prescribes in sufficient detail the terms of the audit engagement, the auditor need not record them in a written agreement except for the fact that law or regulation applies and also seek written agreement from management that it acknowledges and understands that it has responsibility for the preparation of financial statements.
 - (c) The auditor has to take an extract of the law prescribing the details of the terms of the audit engagement and obtain the counter signature of the management in it.
 - (d) Though law prescribes in sufficient detail the terms of the audit engagement, the auditor still needs to record them in a written agreement, however it need not seek written agreement from management that it acknowledges and understands that it has responsibility for the preparation of financial statements.

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- 2. With respect to the treatment of discount on redemption of points in payback card, what should be the action of the external auditor?
 - (a) The auditor can place reliance and go by the opinion of the branch auditor and internal auditor as they have only done a thorough and detailed audit of the accounts
 - (b) The auditor can place reliance on the management's accounting policy as prima facie they are only responsible for preparation of financial statements.
 - (c) The external auditor has sole responsibility for the audit opinion expressed and hence he should perform procedures to satisfy himself on the correct treatment and issue opinion accordingly.
 - (d) The auditor can advise management on correct treatment but cannot qualify his opinion as branch auditor's opinion has higher authority than external auditor's opinion.
- 3. What is the main objective of the external auditor, when he uses the work of the internal audit function of Shyam & Co.?
 - (a) To determine as to which areas, what extent the work can be used and whether that work is adequate for the purposes of the audit.
 - (b) To appropriately direct, supervise and review the work of the internal audit function
 - (c) Review the internal audit report and audit the areas not covered by the internal audit function
 - (d) Enquire from management on the special points that arose during internal audit and follow up on the course of action on those points.
- 4. The external auditor finds that the branch auditor of the outlet in the Chennai region, which is in the verge of closing down, is audited by an auditor who is not a member of the Institute of Chartered accountants of India. What should the external auditor do?
 - (a) Since the professional competence of the auditor is in question, the external auditor should himself visit the premise and audit the accounts.
 - (b) Since the financial statement of the component is immaterial, the provisions of SA 600 do not apply.
 - (c) The auditor can rely on the financial statements of that component by obtaining written representation from management that the branch auditor is otherwise well qualified.
 - (d) Since the professional competence of the auditor is in question, the external auditor should co-ordinate with the branch auditor and call for the books of accounts and other explanations.
- 5. Which of these is not a factor affecting the external auditor's evaluation of the objectivity of the internal audit function?
 - (a) Whether the organizational status of the internal audit function supports the ability of the function to be free from bias, conflict of interest or undue influence of others to override professional judgment.
 - (b) Whether the internal audit function is free of any conflicting responsibilities.
 - (c) Whether the internal auditors have adequate technical training and proficiency in auditing.
 - (d) Whether those charged with governance oversee employment decisions related to internal audit function.

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

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Q. 6 to Q. 9: CASE SCENARIO

M/s MN & Associates have been appointed as auditors of Times Ltd. for the financial year 2019-20. The team consist of Mr. M & Mr. N both Chartered Accountants as also the engagement partners and the audit staff consisting of 2 article assistants. While starting the audit work of Times Ltd, the engagement partners briefed the audit staff about the audit work, areas to be covered and the various auditing concepts and their application in the audit of Times Ltd along with applicable Standard on Auditing.

Various topics like audit planning, overall audit strategy, audit programme were discussed in detail. The team was told about the purpose and implication of various statements and guidance notes issued by the Institute of Chartered Accountants of India (ICAI) from time to time. Mr. N also briefed the team about the concept of materiality to be applied while planning and performing audit. The team was also explained in detail about the area where benchmark materiality can be applied in case of Times Ltd.

Based on the above facts, answer the following:-

- 6. _____sets the scope, timing & direction of the audit and guides the development of the more detailed plan.
 - (a) Audit Programme
 - (b) Overall Audit Strategy
 - (c) Completion Memorandum
 - (d) Audit Plan
- 7. Statement 1: The establishment of the overall audit strategy and the detailed audit plan are not necessarily discrete or sequential process but are closely interrelated.

Statement 2: The auditor shall establish an overall audit strategy that guides the development of audit plan.

- (a) Only Statement 1 is correct
- (b) Only Statement 2 is correct
- (c) Both Statements 1 & 2 are correct
- (d) Both Statements 1 & 2 are incorrect
- 8. means the amount set by the auditor at less than materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatement exceeds materiality for the financial statements as a whole:-
 - (a) Benchmark Materiality
 - (b) Materiality in Planning
 - (c) Performance Materiality
 - (d) Materiality
- 9. (i) Guidance notes issued by ICAI provide guidance to members on matters which may arise in the course of their professional work.
 - (ii) Statements are issued by ICAI with a view to secure compliance by members on some matters.
 - (iii) Guidance notes are recommendatory in nature.
 - (iv) Statements are mandatory in nature.
 - (a) All the above statements are correct.
 - (b) Statements 1 & 2 are correct
 - (c) Statements 1, 2 & 3 are correct
 - (d) Statements 1,2 & 4 are correct

MCQ [4 MCQ of 2 Marks Each: Total 8 Marks]



Q. 10 to Q. 12: CASE SCENARIO

In accordance with requirements of Standards on Auditing, CA Meena (a freshly qualified professional) wants to obtain sufficient appropriate audit evidence in an audit engagement pertaining to financial statements of a partnership firm for year 2022-23. The firm is trading in FMCG goods. Appointed in May, 2023, she needs evidence to obtain information for arriving at her judgment. Clearly remembering fundamentals that an auditor has to obtain sufficient appropriate audit evidence to draw reasonable conclusions on financial statements, she proceeded in accordance with audit plan prepared by her.

During the year 2022-23, firm was maintaining a current account with a branch of a public sector bank. Her audit plan had included procedure of confirming balance of current account directly from bank. As at 28th March, 2023, the firm had an urgent need to pay its utility bill amounting to Rs. 1.00 lacs. However, due to insufficiency of funds, it had requested branch manager to get cheque drawn on utility company cleared. Therefore, balance in current account of firm in books of bank branch stood at Rs. 0.92 lacs (Debit). The firm had also issued cheques in evening of 31st March,2023 in anticipation of funds on next working day i.e.3rd April, 2023. It had also certain cheques dated 27th March, 2023 from its debtors lying with it which were deposited in afternoon of 31st March,2023 in bank branch at request of debtors.

Her plan also included performance of certain procedures pertaining to verification of inventories. Inventories of FMCG goods were material to financial statements. Her assistant, Nisha, had her own notion about understanding of sufficient appropriate audit evidence. She further feels that when audit evidence is obtained from available records of an entity, it is known as internal evidence like purchase bills of FMCG goods, debit notes issued by firm on debtors for GST short charged earlier during the year and credit notes issued by firm during the year on debtors to account for extra price charged in accordance with provisions of GST law. She is also of the view that audit evidence obtained by auditor is final and conclusive.

Based upon above, answer the following questions:-

- 10. As regards matter of balance in current account and related issues is concerned, which of following statements is likely to be most appropriate?
 - (a) Amount of Rs. 0.92 lac is required to be classified under cash & bank balances in financial statements of firm. Procedure of confirming balance directly from the bank alone is likely to constitute sufficient appropriate audit evidence.
 - (b) Amount of Rs. 0.92 lac is required to be classified under cash & bank balances in financial statements of firm. Procedure of confirming balance directly from the bank alone is not likely to constitute sufficient appropriate audit evidence.
 - (c) Amount of Rs. 0.92 lac is required to be classified under current liabilities in financial statements of firm. Procedure of confirming balance directly from the bank alone is likely to constitute sufficient appropriate audit evidence.
 - (d) Amount of Rs. 0.92 lac is required to be classified under current liabilities in financial statements of firm. Procedure of confirming balance directly from the bank alone is not likely to constitute sufficient appropriate audit evidence.
- 11. Considering matter of verification of inventories, which of following statements is based on facts described in the situation and also in essence of Standards on Auditing?
 - (a) She should verify subsequent sale invoices of inventory items lying in stocks as at year end. Besides, she should also review stock records of year 2022-23 and subsequent period. Such evidence may constitute sufficient appropriate audit evidence.



- (b) She should verify subsequent sale invoices of inventory items lying in stocks as at year end. Besides, she should also review stock records of year 2022-23 and subsequent period. She should attend physical inventory count at year end in above situation. Such evidence may constitute sufficient appropriate audit evidence.
- (c) She should verify purchase invoices of inventory items lying in stocks as at year end. Stock records are not required to be verified. Such evidence is likely to constitute sufficient appropriate audit evidence.
- (d) She should verify purchase invoices of inventory items lying in stocks as at year end. She should attend physical inventory count at year end in above situation Such evidence may constitute sufficient appropriate audit evidence.
- 12. Identify correct statement on the basis of description provided in case scenario: -
 - (a) Purchase bills of FMCG goods, debit notes issued by firm on debtors for GST short charged earlier during the year and credit notes issued by firm during the year on debtors to account for extra price charged in accordance with provisions of GST law are all examples of internal evidence. Audit evidence obtained by auditor is final and conclusive.
 - (b) Purchase bills of FMCG goods, debit notes issued by firm on debtors for GST short charged earlier during the year and credit notes issued by firm during the year on debtors to account for extra price charged in accordance with provisions of GST law are all examples of internal evidence. Audit evidence obtained by auditor is persuasive.
 - (c) Only debit notes issued by firm on debtors for GST short charged earlier during the year and credit notes issued by firm during the year on debtors to account for extra price charged in accordance with provisions of GST law are examples of internal evidence. Audit evidence obtained by auditor is persuasive.
 - (d) Only debit notes issued by firm on debtors for GST short charged earlier during the year is an example of internal evidence. Audit evidence obtained by auditor is persuasive.

MCQ [3 MCQ of 2 Marks Each : Total 6 Marks]

- 13. Statement 1: Analytical procedures are more useful while conducting the audit and at the completion phase and are of no use at the planning stage.
 - Statement 2: In the planning stage, audit procedures assist the auditor in understanding the client's business and identifying the areas of potential risks.
 - (a) Statement 1 & 2 are correct
 - (b) Statement 1 & 2 are incorrect
 - (c) Only Statement 1 is correct
 - (d) Only Statement 2 is correct

(2 Marks)

14. In WH Limited every business activity was being carried out manually. The top management of WH Limited decided to change the business environment of WH Limited by using computer systems and computer systems related technology to carry out all the major business activities of WH Limited.

This business environment of WH Limited, where all the major business activities are done using computer systems and computers related technology is an example of:

- (a) Operational Environment.
- (b) Computational Environment.
- (c) Control Environment.
- (d) Automated Environment.

(2 Marks)



- 15. Which of the following is Incorrect:
 - (a) An auditor conducting an audit in accordance with SAs is responsible for obtaining absolute assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error.
 - (b) As described in SA 200, owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements will not be detected, even though the audit is properly planned and performed in accordance with the SAs.
 - (c) The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error.
 - (d) The risk of the auditor not detecting a material misstatement resulting from management fraud is greater than for employee fraud

(2 Marks)

DIVISION B-DESCRIPTIVE QUESTIONS QUESTION NO. 1 IS COMPULSORY. ATTEMPT ANY FOUR QUESTIONS THE REMAINING FIVE QUESTIONS

Question 1:

(a) 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)

(b) External confirmation procedures frequently are relevant when addressing assertions associated with account balances and their elements but need not be restricted to these items. Apart from confirmations for bank balances and accounts receivables, what are the other situations where external confirmation procedures may provide relevant audit evidence in responding to assessed risks of material misstatement?

(4 Marks)

(c) Explain the meaning of Audit Sampling as per the relevant standard on auditing. State the requirements relating to audit sampling, sample design, sample size and selection of items for testing.

(3 Marks)

(d) APQ Ltd. deals in real estate and classifies all of its land holding under current assets as inventory. The same is, therefore valued at cost or market value whichever is less. How would you verify profit or loss arising on sale of plots of land by such a dealer?

(3 Marks)

Question 2:

(a) The engagement partner shall take the responsibility for the overall 'quality on each audit engagement to which that partner is assigned. Discuss with reference to SA 220 "Quality Control for an audit of financial statements".

(4 Marks)

- **(b)** Name the assertions for the following audit procedures:
 - (i) Year end inventory verification.
 - (ii) Depreciation has been properly charged on all assets.
 - (iii) The title deeds of the lands disclosed in the Balance Sheet are held in the name of the company.

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(iv) All liabilities are properly recorded in the financial statements.

(4 Marks)

(c) Describe how risks in IT systems, if not mitigated, could have an impact on audit .

(3 Marks)

(d) In establishing overall audit strategy, the auditor shall ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required. Elucidate those cases by which auditor can ascertain the reporting objectives of the engagement.

(3 Marks)

Question 3:

(a) The senior member of the firm Kaur & Associates, Chartered Accountants, informed to its auditing staff that at the time of audit reporting regarding corresponding figures, when corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in specified circumstances. What are those exceptional circumstances?

(4 Marks)

(b) The auditor has to ensure whether PPE has been valued appropriately and as per generally accepted accounting policies and practices and also the entity has valid legal ownership rights over the PPE claimed to be held by the entity and recorded in the financial statements. Explain how the auditor will verify the same.

(4 Marks)

(c) The auditor has a responsibility to perform audit procedures to identify, assess and respond to the risks of material misstatement arising from the entity's failure to appropriately account for related party relationships, transactions or balances. During the audit, the auditor should maintain alertness for related party information while reviewing records and documents. He may inspect the records or documents that may provide information about related party relationships and transactions. Explain in detail with examples.

(3 Marks)

(d) CA Amar is the statutory auditor of XYZ Ltd. for the FY 2021-22. During the course of audit, CA Amar found that a litigation is going against the company for which the company has hired an external legal team (management expert). CA Amar wanted to use the information as audit evidence which is prepared using the work of the management expert. What should CA Amar consider before using the work of such management expert?

(3 Marks)

Question 4:

(a) CDE Private Limited, a manufacturing company, had made investment in shares of some blue-chip companies. Additionally, it had temporarily deposited some of its extra funds in fixed deposits with a scheduled bank. Dividend from shares amounting to Rs. 1.80 lakhs (net of TDS, TDS = Rs. 0.20 lakhs) and bank interest of Rs. 2.70 lakhs (net of TDS, TDS = Rs. 0.30 lakhs) were credited in bank account of the company. During the year 2023-24, it has also sold some shares resulting in net gain of Rs. 5 lakhs. The company has shown above incomes under head "Other income" for consolidated amount of Rs. 9.50 lakhs in the statement of Profit and Loss. No other information is furnished in the financial statements put up for audit. As the



auditor of the company, discuss whether the above situation constitutes "misstatement" in the financial statements of the company. Also state, few examples of misstatements.

(4 Marks)

(b) The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor to understand significant matters arising during the audit. Explain the above statement and also give examples of significant matters.

(4 Marks)

(c) Explain the matters which should be included for factors relevant to the auditors' judgement about whether a control is relevant to the audit.

(3 Marks)

(d) Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after the completion of the previous audit and continues until the completion of the current audit engagement. Planning includes the need to consider certain matters prior to the auditor's identification and assessment of the risks of material misstatement. Explain clearly stating those matters also.

(3 Marks)

Question 5:

(a) The Chartered Accountant has a responsibility to remain independent by taking into account the context in which they practice, the threats to independence and the safeguards available to eliminate the threats.

In the above context, explain the guiding principles.

(4 Marks)

(b) The external control of municipal expenditure is exercised by the state governments through the appointment of auditors to examine municipal accounts. Explain stating important objectives of audit of such bodies.

(4 Marks)

(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. Explain

(3 Marks)

- (d) While doing audit of ABC Pvt Ltd, on the basis of sufficient and appropriate evidence, auditor comes to a conclusion that use of the Going Concern Basis of Accounting is appropriate, but a material uncertainty exists. Discuss the implications for auditor's report if:
 - (a) Adequate Disclosure of a Material Uncertainty is Made in the Financial Statements
 - (b) Adequate Disclosure of a Material Uncertainty is Not Made in the Financial Statements

(3 Marks)

Question 6:

(a) When is an agricultural advance considered as non performing as per the RBI guidelines?

(4 Marks)



(b) Briefly explain the provisions for qualification and appointment of Auditors under the Multi-State Co-operative Societies Act, 2002.

(4 Marks)

(c) Saburi Textile Ltd is an established player in the textile manufacturing sector. It has developed strong internal controls in almost every area. It has appointed you as an Internal Audit team head. Internal audit has a very strong relation with internal control of the company. Internal Audit analyses the effectiveness with which the internal control of the company is operating and also makes suggestions for improvement in that internal control. Explain stating clearly activities relating to Internal Control.

(3 Marks)

(d) Discuss the reporting requirements under CARO 2020, with respect to the moneys raised by the company by way of initial public offer or further public offer and where the company has made any preferential allotment or private placement of shares.

(3 Marks)

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