

MOCK TEST PAPER- 1
INTERMEDIATE GROUP – II
PAPER – 6: AUDITING AND ASSURANCE

Time Allowed – 3 Hours

Maximum Marks – 100

Division A- Multiple Choice Questions

Case Scenario 1 carries 10 Marks

Case Scenario 2 carries 10 Marks

Total: 30 Marks

General MCQs carry 1 Mark each

Case Scenario 1

Honest Limited is a listed Company engaged in the construction business. The Company constructs residential buildings after purchasing vacant land and then sells ready flats to customers. The Company has not been earning good profits and so no dividend was declared in the last financial year for which the statutory audit is to be conducted.

XYZ & Company has been appointed as the statutory auditor of Honest Limited. The audit firm has seven partners and is a reputed firm with the partners having expert knowledge in various areas.

While conducting the audit, the engagement partner, CA Z suspects some fraudulent activities undertaken by the officers and employees of the Company. CA Z is aware that for the purpose of SAs, the auditor is concerned with fraud that causes a material misstatement in the financial statements. He understands that misstatements in the financial statements can arise from either fraud or error.

On detailed verification by the audit team, it was observed that accounts were manipulated with a view to presenting a false state of affairs. The fraud was committed to avoid incidence of income-tax and withhold declaration of dividend. There was also an incidence of cash receipts being suppressed which came to the notice of the audit team.

CA Z had enough reasons to believe that the offence of fraud, involved individually an amount of Rs.1 crore, and had been committed against the company by its officers or employees. The audit team discussed the reporting requirements of the fraud committed.

One of the audit team members puts forward his recommendations on reporting which includes disclosure in the Board's Report. He states that sub-section (12) of section 143 of the Companies Act, 2013 prescribes that the companies, whose auditors have reported frauds under this sub-section (12) to the audit committee or the Board, but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as may be prescribed.

CA Z discusses the reporting under Companies (Auditor's Report) Order, 2020 [CARO, 2020] wherein the auditor is required to report under clause (xi) of paragraph 3 of Companies (Auditor's Report) Order, 2020, about fraud by the company or any fraud on the Company.

Based on the above information, answer the following questions:

1. Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is:
 - (a) Fraud causes a material misstatement in the financial statements.
 - (b) Fraud is an intentional act.
 - (c) Fraud is easier to detect than error.

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- (d) Fraud can be committed by only the management, those charged with governance, and the employees.
2. Which of the following is not a technique of suppressing cash receipts?
- (a) Writing down asset values in entirety, selling them subsequently and misappropriating the proceeds.
- (b) Adjusting unauthorized or fictitious rebates, allowances, discounts, etc. to customer' accounts and misappropriating amount paid by them.
- (c) Manipulating totals of wage rolls either by including therein names of dummy workers or by inflating them in any other manner.
- (d) Writing off as debts in respect of such balances against which cash has already been received but has been misappropriated.
3. To whom should XYZ & Company report the fraud committed in Honest Limited?
- (a) Report the matter only to the Audit Committee constituted under section 177 since the amount of fraud has not exceeded 1 crore.
- (b) Report the matter to the Board or the Audit Committee, as the case may be, immediately but not later than 2 days of his knowledge of the fraud, seeking their reply or observations within 45 days and on receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government within 15 days from the date of receipt of such reply or observations.
- (c) Report the matter only to the Board since the amount of fraud is not less than 1 crore.
- (d) Report the matter either to the audit committee constituted under section 177 or the Central Government since the amount of fraud is neither less nor more than 1 crore.
4. Sub-rule (4) of Rule 13 of the Companies (Audit and Auditors) Rules, 2014 states that the auditor is required to disclose in the Board's Report details of each of the fraud reported to the Audit Committee or the Board under sub-rule (3) during the year. Which of the following details is not required to be disclosed in the Board's Report?
- (a) Nature of Fraud with description.
- (b) Parties involved, if remedial action taken.
- (c) Approximate Amount involved
- (d) Remedial actions taken.
5. For reporting under clause (xi) of paragraph 3 of Companies (Auditor's Report) Order, 2020, which of the following points the auditor may consider?
- (a) Fraud by the company or on the company by its officers, employees or third parties to be reported.
- (b) Only suspected frauds shall be included here and not the noticed frauds.
- (c) Principles of materiality outlined in Standards on Auditing.
- (d) The auditor's withdrawal from the engagement and the reasons for the withdrawal.

(5 x 2 = 10 Marks)

Case Scenario 2

SAM & Company, a Chartered Accountant firm, is in the process of finalising the audit of Health is Wealth Limited which is a Company listed on the Bombay Stock Exchange. Since the past decade, Health is Wealth Limited has made its presence felt in over 10 countries, including India, making it a leader in the global fitness industry. It runs a chain of fitness centres that offers energetic group workouts and multiple workout formats

to choose from. It also offers the best equipment, knowledgeable staff and personal advice in a welcoming environment.

SAM & Company being a very reputed firm, was appointed for the statutory audit of Health is Wealth Limited. The Engagement Partner CA A and her team of 8 members have conducted the audit in an efficient and effective manner. The senior manager in the team, CA K is of the opinion that they have obtained sufficient appropriate audit evidence, which concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements. One of the article clerks, Mr N, is a fresher and this audit is his first experience as an auditor in a limited company. He is a sharp boy and has grasped all the concepts and techniques very well. However, the term "pervasive" confused him so CA K patiently explained to Mr N the pervasive effects on the financial statements as per the auditor's judgement. Mr. N understood the term well and thanked CA K for clearing all his doubts.

CA A disagreed with CA K that they have obtained sufficient appropriate audit evidence, which concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements. So, the entire team held various meetings and discussions, and finally reached to a conclusion. They concluded that they have obtained reasonable assurance that the financial statements as a whole are free from material misstatement, whether due to fraud or error. That conclusion took into account:

- (a) Whether sufficient appropriate audit evidence had been obtained;
- (b) Whether uncorrected misstatements were material, individually or in aggregate;
- (c) The evaluations.

The Auditor's Report was prepared in writing and it was decided that an unmodified opinion would be expressed. The first section of the auditor's report included the auditor's opinion, and had the heading "Opinion". Following the Opinion section, was a section with the heading "Basis for Opinion". When expressing an unmodified opinion on financial statements, the auditor's opinion used the following phrase,

"In our opinion, the accompanying financial statements give a true and fair view of [...] in accordance with [the applicable financial reporting framework]."

During the audit, the audit team had observed that there was uncertainty in Health is Wealth Limited relating to the future outcome of a regulatory action. So, a paragraph was included in the auditor's report that referred to this matter which was appropriately disclosed in the financial statements and that, in the auditor's judgment, was of such importance that it was fundamental to users' understanding of the financial statements.

CA A also determined whether the financial statements included the comparative information required by the applicable financial reporting framework and whether such information was appropriately classified. One team member, Mr R was curious to know whether the auditor's opinion referred to the corresponding figures or not, whenever the corresponding figures are presented. CA A explained the circumstances to Mr R in which, when the corresponding figures are presented, auditor's opinion referred to the corresponding figures.

Based on the above information, answer the following questions:

1. CA K explained to Mr. N the pervasive effects on the financial statements in the auditor's judgement. Pervasive effects on the financial statements are those that, in the auditor's judgement:
 - (i) Are not confined to specific elements, accounts or items of the financial statements;
 - (ii) If so confined, represent or could represent a substantial proportion of the financial statements; or
 - (iii) In relation to disclosures, are fundamental to users' understanding of the financial statements.

Which of the following is correct?

- (a) (i), (iii)
- (b) (ii), (iii)
- (c) (i), (ii)

- (d) (i), (ii) and (iii)
2. When expressing an unmodified opinion on financial statements, SAM & Company used the following phrase:
“In our opinion, the accompanying financial statements **give a true and fair view of** [...] in accordance with [the applicable financial reporting framework].”
Which is the other phrase which is regarded as being equivalent to the above phrase and could also be used by SAM & Company?
- (a) In our opinion, the accompanying financial statements **give a true and correct view of** [...] in accordance with [the applicable financial reporting framework];
(b) In our opinion, the accompanying financial statements **present correctly, in all material respects,** [...] in accordance with [the applicable financial reporting framework];
(c) In our opinion, the accompanying financial statements **present fairly, in all material respects,** [...] in accordance with [the applicable financial reporting framework];
(d) In our opinion, the accompanying financial statements **give a correct and fair view of** [...] in accordance with [the applicable financial reporting framework].
3. Which of the following statements is not included in the section with the heading “Basis for Opinion” in the Auditor’s Report?
- (a) Audit was conducted in accordance with the Accounting Standards.
(b) Auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit and has fulfilled the auditor’s other ethical responsibilities in accordance with these requirements.
(c) Description of the auditor’s responsibilities under the SAs.
(d) States whether the auditor believes that the audit evidence the auditor has obtained, is sufficient and appropriate to provide a basis for the auditor’s opinion.
4. A paragraph was included in the Auditor’s Report of Health is Wealth Limited that referred to a matter which was appropriately disclosed in the financial statements that, in the auditor’s judgment, was of such importance that it was fundamental to users’ understanding of the financial statements. What is this section of the Auditor’s Report called?
- (a) Other Matters.
(b) Emphasis of Matters.
(c) Key Audit Matters.
(d) Auditor’s Responsibilities for the Audit of the Financial Statements.
5. CA A explained the circumstances to Mr. R in which, when the corresponding figures are presented, auditor’s opinion referred to the corresponding figures. Which of these circumstances did he mention to Mr. R?
- (a) If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements on which a modified opinion has been previously issued.
(b) If the auditor’s report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which gave rise to the modification is resolved.
(c) Prior Period Financial Statements are audited by another auditor.
(d) Prior Period Financial Statements not audited.

(5 x 2=10 Marks)

General MCQs

1. In designing and performing test of controls, the auditor shall perform other audit procedures in combination with inquiry to obtain audit evidence about the operating effectiveness of the controls, including:
- (i) How the controls were applied at relevant times during the period under audit.
 - (ii) The consistency with which they were applied.
 - (iii) By whom or by what means they were applied.

Which of the following is correct?

- (a) (i) and (ii)
 - (b) (ii) and (iii)
 - (c) (i),(ii) and (iii)
 - (d) (i) and (iii)
2. 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
3. _____ implies analysing account fluctuations by comparing current year to prior year information and, also, to information derived over several years.

- (a) Trend analysis
- (b) Ratio analysis
- (c) Structural modelling
- (d) Account fluctuations analysis

4. The agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include:
- (i) The objective and scope of the audit of the financial statements;
 - (ii) The responsibilities of the auditor;
 - (iii) The responsibilities of management;
 - (iv) Identification of the applicable financial reporting framework for the preparation of the financial statements; and
 - (v) Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

Which of the following is correct?

- (a) (i),(ii),(iii)
- (b) (i),(ii),(iii), (iv), (v)
- (c) (i),(ii), (iv), (v)
- (d) (i),(ii),(iii), (iv)

5. Obtaining trade receivables ageing report and analysis and identification of doubtful debts is performed during audit of accounts receivable balances to address the following balance sheet assertion:
- (a) Valuation
 - (b) Rights and obligations
 - (c) Existence
 - (d) Completeness
6. The auditors should classify Credit card accounts as NPA, if _____ amount due, as mentioned in the credit card statement is not paid fully within _____ days from next statement date.
- (a) Total, 90
 - (b) Minimum, 90
 - (c) Minimum, 30
 - (d) Minimum, 60
7. The auditor finds that there is something unusual about the balances outstanding in the receivables. Date wise verification of the bank reconciliation performed by the auditor has resulted in mismatch in dates in most of the receivable ledger. The auditor has identified a pattern in the mismatches. He suspects that there might be a misappropriation of cash and the detection of this misappropriation is being prevented by crediting the amount received subsequently to the account of customer who paid earlier.
- What is the kind of fraud that the auditor has faced in the above case?
- (a) Teeming and Lading
 - (b) Cash skimming
 - (c) Defalcation of cash by inflating cash payment
 - (d) Misappropriation of receivables
8. A Ltd. has been assigned a Cash Credit limit of INR 20 lacs as against its Book Debts furnished as security. What kind of Security creation is it?
- (a) Pledge
 - (b) Mortgage
 - (c) Assignment
 - (d) Set-off
9. Owing to the _____ limitations of an audit, there is _____ 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.
- (a) Inherent, unavoidable
 - (b) Inherent, complete
 - (c) Management, unavoidable
 - (d) Regulatory, control
10. Consider the following statements pertaining to nature and meaning of “assertions”:-
- Statement I—Assertions are representations by the management which are present in financial statements.
- Statement II —The assertions have to be necessarily explicit.

Which of the following is correct?

- (a) Only Statement I is true.
- (b) Only Statement II is true.
- (c) Both statements I and II are true.
- (d) Both statements I and II are false.

(10 x 1=10 Marks)

Division B- Descriptive Questions

Question No. 1 is compulsory.

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

Total 70 Marks

1. Examine with reasons (in short) whether the following statements are correct or incorrect : (Attempt any 7 out of 8)
 - (i) The preparation of financial statements involves judgment by management.
 - (ii) Evolving one audit programme applicable to all business under all circumstances is not practicable
 - (iii) Inquiry alone ordinarily does not provide sufficient audit evidence.
 - (iv) The SAs do not ordinarily refer to inherent risk and control risk separately.
 - (v) Intentional errors are most difficult to detect and auditors generally devote greater attention to this type
 - (vi) All automated environments are not complex.
 - (vii) A combination of processes, tools and techniques that are used to tap vast amounts of electronic data to obtain meaningful information is known as meaningful data.
 - (viii) An auditor has to report on the matters specified in section 143(1) of the Companies Act, 2013.

(7 x 2 = 14 Marks)
2. Discuss the following:
 - (a) As an auditor of XYZ Ltd, how would you consider the acceptance of a change in audit engagement? **(4 Marks)**
 - (b) CA Vikas Jain discussed with his audit team about advantages and disadvantages of audit programme. He explained to his team that –“work may become mechanical” as disadvantage of the audit programme. Discuss explaining the disadvantages of an audit programme **(4 Marks)**
 - (c) The reliability of information to be used as audit evidence, and therefore of the audit evidence itself, is influenced by its source, its nature and the circumstances under which it is obtained. Explain and elucidate the guiding principles which are useful in assessing the reliability of audit evidence. **(3 Marks)**
 - (d) Factors relevant to the auditor’s judgment about whether a control, individually or in combination with others, is relevant to the audit may include such matters as materiality, size of the entity etc. Explain the other relevant considerations in the above context. **(3 Marks)**
3.
 - (a) Inadequate internal control over assets may increase the susceptibility of misappropriation of those assets. Explain giving examples. **(4 Marks)**
 - (b) Explain some of the points that an auditor should consider to obtain an understanding of the company’s automated environment. **(4 Marks)**

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- (c) ABC Ltd is a Large Company with huge purchase and sales transactions. Which sampling approach is recommended in such a company? Explain giving features of such sampling approach along with example **(3 Marks)**
- (d) While conducting audit of Air Space Ltd, the auditor observes that it has issued shares at discount to its creditors when its debt is converted into shares in pursuance of debt restructuring scheme in accordance with any guidelines specified by the Reserve Bank of India. Discuss explaining clearly the provisions relating to discount on issue of shares and its verification by the auditor. **(3 Marks)**
4. (a) Discuss the provisions regarding appointment of First auditors of a Government company and a Non-Government company. **(4 Marks)**
- (b) While applying the Substantive Analytical Procedures what techniques can be used by the statutory auditor of a company to obtain sufficient and appropriate audit evidence? **(4 Marks)**
- (c) XYZ Ltd made huge additions to Intangible assets during the period 01-04-2021 to 31-03-2022 i.e period under audit. You have been appointed as an auditor and you want to verify the additions made to intangible assets during the period. Suggest the audit procedure to verify the additions to intangible assets. **(6 Marks)**
5. (a) State the matters to be included in auditor's report as per CARO, 2020 regarding "Default in repayment of loan or borrowing to a financial institution, bank etc." **(3 Marks)**
- (b) Under provisions of Section 143(2), the auditor shall make a report to the members of the company on the accounts examined by him. Explain along with relevant rule of The Companies (Audit and Auditors) Rules, 2014 **(4 Marks)**
- (c) While conducting audit of VED Ltd., you as an auditor are not only prevented in completing certain audit procedures but also are not able to obtain audit evidence even by performing alternative procedures. How you will deal with this situation? **(4 Marks)**
- (d) What are the circumstances in which auditors are required to qualify their reports of companies for matters related to AS-I 'Disclosure of Accounting Policies'? **(3 Marks)**
6. (a) The auditor should examine the efficacy of various internal controls over advances to determine the nature, timing and extent of his substantive procedures. Explain this statement. **(4 Marks)**
- (b) Audit of government expenditure is one of the major components of government audit conducted by the office of C & AG. The basic standards set for audit of expenditure are to ensure that there is provision of funds authorised by competent authority fixing the limits within which expenditure can be incurred. Explain those standards. **(4 Marks)**

OR

- (c) Explain the categories of Agricultural Advances in case of Banks and related NPA norms. **(4 Marks)**
- (d) You have been appointed auditor of M/s. BLK Hospital. Discuss important points that would attract your attention while audit. **(6 Marks)**