

MOCK TEST PAPER- 2
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

CA Sanjoy is conducting audit of PETA Education Solutions Private Limited for the first time. The company is engaged in providing solutions to students appearing for competitive exams under engineering and medical streams. Company's business is operated from physical centres spread in many states of the country. However, of late, number of aspirants availing company's services are shrinking due to emergence of new competitors and inability of company to switch to new technologies available in market to render its services.

The company had taken bank loans in past years for expansion of its physical centres. However, due to reduction in strength of aspirants opting for services provided by the company, management is always looking for means to meet its financial commitments on time. During the course of audit, CA Sanjoy wants to be sure about revenue and profit assertions reflected in financial statements of the company. Therefore, he is planning to test company's system for booking revenue in its books of accounts.

He notices that during the year under consideration, many experienced teaching faculties have left due to late payment of their contractual payments by the company. These have been replaced by inexperienced faculties having lower contractual costs but leading to poor satisfaction outcomes among aspirants. Besides, employee turnover of regular administrative staff also remains high. The company has not organized any training programmes either for its faculties or administrative staff for considerable period of time.

He has, in his wisdom, decided to increase the area of substantive checking in the company. He does not want to suffer from probable adverse publicity or loss of his professional goodwill.

Based on above case scenario, answer the following MCQs: -

- 1.1 After studying description of the company and its nature of operations, which of following statements is most appropriate?
 - (a) Inherent risk for revenue and profit assertions is likely to be lower.
 - (b) Inherent risk for revenue and profit assertions is likely to be higher.
 - (c) Inherent risk for revenue and profit assertions cannot be assessed from given situation.
 - (d) There does not exist inherent risk for revenue and profit assertions in described situation.
- 1.2. The case scenario describes a situation of leaving of experienced faculties, high employee turnover and absence of training programmes for staff of the company. Such indicators are an example of _____?
 - (a) Unsatisfactory risk assessment process used by the company
 - (b) Unsatisfactory control environment of the company
 - (c) Unsatisfactory performance reviews carried out by the company

- (d) Unsatisfactory system of segregation of duties in the company
- 1.3. The auditor is planning to test company's system for booking revenue in its books of accounts. Identify the correct statement in this regard: -
- (a) He is likely to place greater reliance on controls relating to booking of revenue.
 - (b) He is likely to place lower reliance on controls relating to booking of revenue.
 - (c) Reliance placed by him on controls relating to booking of revenue would be unaffected due to reduction in contractual costs by company.
 - (d) Reliance placed by him on controls relating to booking of revenue would be unaffected due to shrinking number of aspirants.
- 1.4. The auditor has increased area of "substantive checking" in the company. It is due to the reason that _____
- (a) he wants to lower detection risk
 - (b) he wants to lower control risk
 - (c) he wants to raise sample risk
 - (d) he wants to lower inherent risk
- 1.5. The auditor does not want to suffer from probable adverse publicity or loss of professional goodwill. Such a situation is indicative of _____?
- (a) audit risk
 - (b) auditor's business risk
 - (c) auditor's detection risk
 - (d) non-sampling risk
- (5 x 2 = 10 Marks)**

Case Scenario - 2

You are a partner in ABC & Company, a firm of Chartered Accountants based in New Delhi. ABC & Company have been appointed as the statutory auditors of Onetime Limited, a public company which manufactures and sells wall and table clocks and has many branches all over India. Onetime Limited has been exporting the clocks since past two years. However, the domestic sales have contributed towards major source of revenue for the Company.

One of the team members, CA B noticed that one of the suppliers of Onetime Limited, Mr AM had sent some raw material to the Company for storage in their warehouse in March 2023. Due to renovation going on at his warehouse, his stock could be damaged and so he had requested Onetime Limited to keep the same in their warehouse. Onetime Limited contended that since the raw material was anyway billed to the Company the next month, so the same had been included in the valuation of stock, since physically the stock was present in the warehouse of Onetime Limited as on 31.03.2023.

While verifying the debtors, team member C noticed that there were a few trade receivables pertaining to export sales mainly to England. Mr. C verified the same with respect to the invoices issued and other supporting documents. The amount booked as on 31.03.2023 was based on the exchange rate as on the date of the invoice.

Mr. T, another team member verified the PPE of the Company. Onetime Limited had purchased few cars for its directors during the year of audit. The same were appearing in the PPE schedule of the Company. Mr T verified the same with respect to the invoices as well as physically verified the assets in the Company's premises. Since the cars were for the official use of the Directors, they were purchased in the name of the Directors of the Company. Mr. T verified the amount with the Invoice and checked the registration and

insurance documents. Besides, all items appearing in the PPE schedule were verified and he was satisfied that all PPE items that should have been recorded have, in fact, been recorded.

One of the articled clerks was assigned the work of verification of "Provisions" appearing in the Balance sheet. He wanted to understand from you the circumstances in which a provision is recognised in the books of accounts. You explained him the situations in which an entity recognises Provisions in its books.

Onetime Limited has invested in the shares of other companies. One of the Companies has declared dividend on its shares. Onetime Limited has not recognised the same in the profit & loss account. Team Member R has asked you to look into the matter since she is unable to understand the reasons for the same.

- 2.1 Is the raw material lying in the warehouse of Onetime Limited accounted for correctly in its books of account?
- (a) No, since the same belongs to Mr. AM and should appear in his books.
 - (b) Yes, since the same is in possession of Onetime Limited and was billed to it the following month.
 - (c) It should be shown in the books of both Onetime Limited and Mr. AM.
 - (d) It should not appear in the books of Onetime Limited or Mr. AM and the raw material should be disclosed as a note in the final accounts of both the entities.
- 2.2 Which exchange rate is considered for accounting of foreign debtors at the year end?
- (a) Exchange Rate on the date of the invoice.
 - (b) Exchange Rate on the last day of the financial year.
 - (c) Exchange Rate on the date of shipment of the products to the customer.
 - (d) Exchange Rate on the date of delivery of the products to the customer.
- 2.3 Which of the following management assertions is not satisfied with respect to Cars included in the PPE items by the company :
- (a) Existence
 - (b) Valuation
 - (c) Completeness
 - (d) Rights and Obligations
- 2.4 Which of the following condition is not required to be met for recognizing a provision?
- (a) When a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.
 - (b) When an entity has a present obligation (legal or constructive) as a result of a past event.
 - (c) A reliable estimate can be made of the amount of the obligation.
 - (d) When it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation.
- 2.5 Which of the following conditions is not necessary for recognising dividends in the statement of profit and loss of Onetime Ltd.:
- (a) the entity's right to receive payment of the dividend is established.
 - (b) it is probable that the economic benefits associated with the dividend will flow to the entity.
 - (c) the amount of the dividend can be measured reliably.

(d) payment of income tax on dividends received

(5 x 2 = 10 Marks)

General MCQs

1. The persons with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity are :
 - (a) management
 - (b) those charged with governance
 - (c) audit committee
 - (d) board of directors
2. CA Tarini is in process of formulating audit plan for conducting audit of a company engaged in business of dealing in commodity futures. Which of the following is not likely to be an appropriate audit procedure to be included in audit plan for the abovesaid company?
 - (a) Verification of turnover of company
 - (b) Verification of cost of raw material consumed
 - (c) Examination of company's accounting policy for revenue recognition
 - (d) Verification of contract notes with brokers
3. A company has started its manufacturing operations from a newly constructed building. CA Z is statutory auditor of company. Which of following is not likely to be an example of audit documentation?
 - (a) E-mail correspondence with CFO of company concerning significant matters
 - (b) Audit programme
 - (c) Response to external confirmation requests
 - (d) Structural engineer's report on strength of building
4. Following are examples of events or conditions that may cast significant doubt on an entity's ability to continue as a going concern. Which of following is an example of operating event/conditions?
 - (a) Adverse key financial ratios
 - (b) Inability to pay creditors on due dates
 - (c) Indications of withdrawal of financial support by creditors
 - (d) Shortages of important supplies
5. Which of following is not an element of audit report in accordance with SA 700?
 - (a) Title
 - (b) Addressee
 - (c) Audit strategy
 - (d) Auditor's opinion
6. An auditor disclaims opinion when _____?
 - (a) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be material.
 - (b) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be both material and adverse.

- (c) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be both material and pervasive.
- (d) He is unable to obtain audit evidence and concludes that possible effects on financial statements of undetected misstatements could be both material and perverse.
7. UDIN (Unique Document Identification Number) is required to be stated by practising Chartered Accountant on: -
- (a) Each audit report only
- (b) Each audit report and each certificate
- (c) Each audit report issued under Companies Act, 2013 only
- (d) Each audit report issued under Companies Act, 2013 only and each certificate
8. For which of following company, provisions of CARO,2020 would be applicable?
- (a) Boost Up Training (OPC) Private Limited
- (b) RCI Bank Limited
- (c) PST Industries Limited
- (d) Moon Insurance Limited
9. While reporting under CARO, 2020, it is duty of statutory auditor of company to report: -
- (a) Fraud of less than ₹ 1 crore committed by officers or employees of company during the year
- (b) Fraud of ₹1 crore or more committed by officers or employees of company during the year
- (c) Fraud of ₹5 crore or more committed by officers or employees of company during the year
- (d) Any fraud by the company or on the company noticed or reported during the year
10. Which of following is not a threat to independence of auditor?
- (a) Self-interest threats
- (b) Self- review threats
- (c) Advocacy threats
- (d) Peer group threats

(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) Negative assertions, encountered in the financial statements, may be expressed or implied.
- (ii) While auditing the books of accounts of XYZ Ltd., the auditor of the company was involved in examining records and documents in paper form, electronic form etc. and was also conducting physical examination of assets. In the present case, audit procedure used by the auditor is known as "Observation".
- (iii) Statistical sampling being more scientific and without personal bias will always be appropriate to use under all circumstances.

- (iv) According to 'propriety audit', the auditors try to bring out cases of improper, avoidable, or infructuous expenditure.
 - (v) Collateral security refers to the security offered by the borrower for bank finance or the one against which credit has been extended by the bank.
 - (vi) PPE is/are depreciated when the asset is actually put to active use.
 - (vii) Historical financial information relates to financial information based on assumptions about the occurrence of future events and possible actions by an entity.
 - (viii) Control risk is the susceptibility of an account balance or class of transactions to misstatement that could be material either individually or, when aggregated with misstatements in other balances or classes, assuming that there were no related internal controls. **(7 x 2 = 14 Marks)**
2. Discuss the following:
- (a) An audit does not provide absolute assurance. Discuss how nature of audit procedures itself is one of the reasons due to which audit cannot provide absolute assurance. **(3 Marks)**
 - (b) While obtaining audit evidence about the effective operation of internal controls, the auditor considers how they were applied, the consistency with which they were applied during the period and by whom they were applied. The concept of effective operation recognises that some deviations may have occurred. Analyse and Explain. **(3 Marks)**
 - (c) 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. **(4 Marks)**
 - (d) With respect to audit in an automated environment, explain the following:
 - (i) Applications
 - (ii) Automated
 - (iii) CAATs
 - (iv) Data Processing **(4 Marks)**
3. (a) Risks of material misstatement may be greater for significant non-routine transactions arising from matters such as complex calculations. Also, risks of material misstatement may be greater for significant judgmental matters that require the development of accounting estimates, arising from matters such as accounting principles for accounting estimates may be subject to differing interpretation etc. Explain in detail. **(3 Marks)**
- (b) CXW Private Limited is having paid-up share capital of ₹25 crores. Its borrowings from banks are to the tune of ₹50 crores. Mr. X, an individual practising Chartered Accountant, is nearing completion of five- year tenure as statutory auditor of company. Discuss, citing relevant provisions under Companies Act, 2013 whether he can be reappointed for another term of five years just after completion of his present tenure. **(4 Marks)**
 - (c) Auditing is a logical process. An auditor is called upon to assess the actualities of the situation, review the statements of account and give an expert opinion about the truth and fairness of such accounts. This he cannot do unless he has examined the financial statements objectively. He needs evidence to obtain information for arriving at his judgment. Discuss explaining clearly the meaning of audit evidence in detail. **(4 Marks)**
 - (d) CA E was appointed statutory auditor of XYZ Private Limited in AGM held in the month of August, 2023 for the first time for audit of financial statements of the company from year 2023-24 onwards. Since he is new to the company, he wants to be sure about integrity of accounting records. In this regard, he wants to ensure that software used by company for maintenance of its books of accounts

is capable of tracking user activities and changes made to entries in books of accounts, if any, during the course of year.

What CA E is looking for in the given situation? Discuss the reporting requirements for CA E in this matter to be included in audit report to be issued under the Companies Act, 2013. **(3 Marks)**

4. (a) The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion". Explain what is included in this "Basis for Opinion" section. **(3 Marks)**
- (b) Misappropriation of assets involves the theft of an entity's assets and is often perpetrated by employees in relatively small and immaterial amounts. However, it can also involve management who are usually more able to disguise or conceal misappropriations in ways that are difficult to detect.

Misappropriation of assets can be accomplished in a variety of ways. Explain those particular ways. **(3 Marks)**

- (c) Depreciation and amortisation expense generally constitute an entity's significant part of overall expenses and have direct impact on the profit/loss of the entity. What are the attributes, the Auditor needs to consider while verifying Depreciation and amortisation expense. **(4 Marks)**
- (d) 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.
 - (iv) All liabilities are properly recorded in the financial statements. **(4 Marks)**
5. (a) It is imperative for the auditor to project misstatements for the population while performing audit procedures through sampling. Comment. **(3 Marks)**
- (b) Distinguish between an adverse opinion and a qualified opinion. Also draft an opinion paragraph for both types of opinion. **(4 Marks)**
- (c) The auditor of Saturn Ltd. wants to verify whether the company has valid legal ownership rights over the inventories recorded in the balance sheet as on 31.03.2023. What audit procedures should the statutory auditor of the company perform? **(4 Marks)**
- (d) If analytical procedures performed in accordance with SA 520 identify fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount, how would the auditor investigate such differences. **(3 Marks)**
6. (a) CA X is acting as concurrent auditor of a branch of KLT Bank (a nationalized bank) located in Delhi during the year 2022-23. The assignment started from 1st October 2022 and is for a period of one year. By virtue of this assignment, he is required to issue monthly reports on different aspects of the functioning of branch including deposits, advances and housekeeping to controlling authorities of Bank.
- At the end of March, 2023, he has got an offer to conduct statutory audit of two branches of KLT Bank located in the State of Rajasthan for the year 2022-23. Can he accept the above offer? Discuss. **(3 Marks)**
- (b) Pilfering is one of the greatest problems in any hotel and the importance of internal control cannot be undermined. Explain. **(4 Marks)**

OR

- (c) You have been appointed as an auditor of ABC Hotel, a three-star hotel, for Financial Year 2022-23. As an auditor, what are the special points that need to be considered in verifying the Inventories in the nature of food and beverages? **(4 Marks)**
- (d) The Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971 provides certain powers to the C & AG in connection with performance of his duties. Discuss. **(4 Marks)**
- (e) While conducting statutory audit of branch of a nationalized bank, it is noticed by CA Z that credit facilities granted to a borrower consisting solely of term loan have been classified as "Sub-standard Asset" during the year 2022-23 due to failure of borrower to pay EMIs on time. Such EMIs were outstanding for more than 90 days and account was, therefore, classified as "Sub-Standard Asset". CA Z has also agreed to above asset classification made by branch management.
- What are CA Z's responsibilities regarding verification of compliance with income recognition norms by branch in respect of above credit facilities? **(3 Marks)**