FINAL CA – NOV 2018

SUB: AUDIT

Topics: Audit & Assurance Standards and Professional Ethics

Test Code – CF9

Branch (MULTIPLE) (Date :)

(50 Marks)

Note: ***All*** *questions are compulsory.*

Question 1 (5 marks)

1. As per SA 710 "Comparative Information—Corresponding Figures and Comparative Financial Statements", in respect of corresponding figures, the auditor shall determine whether the financial statements include the comparative information required by the applicable financial reporting framework and whether such information is appropriately classified.		1
2. For this purpose, the auditor shall evaluate whether: (a) The comparative information agrees with the amounts and other disclosures presented in the prior period; and (b) The accounting policies reflected in the comparative information are consistent with those applied in the current period or, if there have been changes in accounting policies, whether those changes have been properly accounted for and adequately presented and disclosed.		1 1
3. If the auditor becomes aware of a possible material misstatement in the comparative information while performing the current period audit, the auditor shall perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence to determine whether a material misstatement exists. If the auditor had audited the prior period's financial statements, the auditor shall also follow the relevant requirements of SA 560 "Subsequent Events".		1/2 1/2
4. As required by SA 580, "Written Representations", the auditor shall request written representations for all periods referred to in the auditor's opinion. The auditor shall also obtain a specific written representation regarding any prior period item that is separately disclosed in the current year's statement of profit and loss.		1/2 1/2

Question 2 (6 marks)

1. As per SA 560 "Subsequent Events" deals with the events occurring between the dates of balance sheet and audit report and the facts that become known to the auditor after the date of the auditor's report.		1

2. 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.		1
3. The auditor is not, however, expected to perform additional audit procedures on matters to which previously applied audit procedures have provided satisfactory conclusions.		1/2
4. The auditor shall perform the procedures required above so that they cover the period from the date of the financial statements to the date of the auditor's report, or as near as practicable thereto.		1/2
5. The auditor shall take into account the auditor's risk assessment in determining the nature and extent of such audit procedures, which shall include the following: (a) Obtaining an understanding of any procedures management has established to ensure that subsequent events are identified. (b) Inquiring of management and, where appropriate, those charged with governance as to whether any subsequent events have occurred which might affect the financial statements. (c) Reading minutes, if any, of the meetings, of the entity's owners, management and those charged with governance, that have been held after the date of the financial statements and inquiring about matters discussed at any such meetings for which minutes are not yet available. (d) Reading the entity's latest subsequent interim financial statements, if any.		1/2 1/2 1/2 1/2
6. When, as a result of the procedures performed as required the auditor identifies events that require adjustment of, or disclosure in, the financial statements, the auditor shall determine whether each such event is appropriately reflected in those financial statements.		1

Question 3 (5 marks)

As per SA 701, "Communicating Key Audit Matters in the Auditor's Report", the purpose of communicating key audit matters is to enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed. It is applicable w.e.f 1st April 2018 onwards for audit of listed entities.

Communicating key audit matters provides additional information to intended users of the financial statements to assist them in understanding those matters that, in the auditor's professional judgement, were of most significance in the audit of the financial statements of the current period. The auditor shall describe each key audit matter, using an appropriate subheading, in a separate section of the auditor's report under the heading "Key Audit Matters". The introductory language in this section of the auditor's report shall state that:

(a) Key audit matters are those matters that, in the auditor's professional judgement, were of most significance in the audit of the financial statements [of the current period]; and

(b) These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditor's opinion there on, and the auditor does not provide a separate opinion on these matters.

Communicating key audit matters in the auditor's reports in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report is not:

(a) A substitute for disclosure in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;

(b) A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705 (Revised):

(c) A substitute for reporting in accordance with SA 705 when a material uncertainty exists relating to event or conditions that may cast significant doubt on an entity's ability to continue as a going concern; or

(d) A separate opinion on individual matters.

Question 4 (6 marks)

1. As per SA 501 "Audit Evidence – Additional Considerations for Specific Items", the auditor should perform audit procedures, designed to obtain sufficient appropriate audit evidence during his attendance at physical inventory counting. SA 501 is additional guidance to that contained in SA 500, "Audit Evidence", with respect to certain specific financial statement amounts and other disclosures.		1
2. If the auditor is unable to be present at the physical inventory count on the date planned due to unforeseen circumstances, the auditor should take or observe some physical counts on an alternative date and where necessary, perform alternative audit procedures to assess whether the changes in inventory between the date of physical count and the period end date are correctly recorded.		1
3. The auditor would also verify the procedure adopted, treatment given for the discrepancies noticed during the physical count.		1
4. The auditor would also ensure that appropriate cut off procedures were followed by the management.		1
5. He should also get management's written representation on (a) the completeness of information provided regarding the inventory, and (b) assurance with regard to adherence to laid down procedures for physical inventory count.		2
6. By following the above procedure it will be ensured that the physical verification conducted by the management was in order.		

Question 5 (4 marks)

(i) Bank balance from bankers		1/2
(ii) Account receivable balances		1/2
(iii) Inventories held by third parties		1/2
(iv) Property title deeds held by third parties		1/2
(v) Investments purchased but delivery not taken		1/2

(vi) Loan from lenders		1/2
(vii) Account payable balances		1/2
(viii) Long outstanding share application money.		1/2

Question 6 (8 marks)

(a) 'Zenga' a chartered accountant, wrote several letters to Government Department pointing out the seniority of his firm and sending his life sketch and stating that he had rendered glorious service to the country and to the accountancy profession with a view to getting the audit work. Clause (6) of Part I of First Schedule to the Chartered Accountants Act, 1949 prohibits a member not to solicit professional work by means of advertisement, circular, personal communication or interview or by any other means. Since these letters were clearly in the nature of advertising professional attainments, "Zenga" was guilty of professional misconduct under Clause (6) of Part I of First Schedule to the Chartered Accountants Act, 1949.		2
(b) Communication with the Previous Auditor: Clause (8) of Part I of the First Schedule to the Chartered Accountants Act, 1949 requires communication by the incoming auditor with the previous auditor before accepting a position by him. The Council of the Institute has taken the view that a mere posting of a letter "under certificate of posting" is not sufficient to establish communication with the retiring auditor unless there is some evidence to show that the letter has in fact reached the person communicated with. A Chartered Accountant who relies solely upon a letter posted "under certificate of posting" therefore does so at his own risk. Since the letters were sent by "Wadia" to the previous auditor informing him of his appointment as an auditor before the commencement of audit by him under Certificate of Posting is not sufficient to prove communication with the retiring auditor. In the opinion of the Council, communication by a letter sent "Registered Acknowledgement Due" or by hand against a written acknowledgement would in the normal course provide positive evidence. Hence "Wadia" was guilty of professional misconduct under Clause (8) of Part I of First Schedule to the Chartered Accountants Act, 1949.		3

(c) Apparently, as it appears from the facts of the case that the auditor did not exercise proper skill and care and that he performed his work in a desultory and haphazard manner. In this matter, the test for auditor's liability lies in whether he has applied reasonable care, skill and caution called for in the circumstances of the case and whether he reasonably used all the information that he came across in the course of audit. Cash is a very significant item in any situation and the fact that the cashier had left during the year without notice should have placed the auditor on alert as regards the cash book. In fact, the very fact that the cashier was absconding, i.e., left without any notice constituted sufficient circumstances to excite suspicion of the auditor to probe to the bottom. As per SA 240, "The auditor's responsibilities relating to fraud in an audit of financial statements", it can be concluded that the auditor did not plan and perform the audit with an attitude of professional skepticism. Thus, having regard to this and a fraud has actually taken place during the year, committed by the absconding cashier, it is reasonable to think that prima facie there is a case against the auditor for gross negligence. Clause (7) of Part I of Second Schedule to the Chartered Accountants Act, 1949 requires that it is the duty of an auditor to bring to bear in the work he has to perform that skill, care and caution as per the circumstances in an honest and reasonable manner. As it appears from the facts of the case, the auditor has been grossly negligent in performing his duties which constitutes professional misconduct. Thus, such instances require reference to Disciplinary Committee of the Council of the Institute. If a member is found guilty by the Council of any of the acts or omissions stated in the Schedule, its finding with recommendations are to be referred to the High Court for decision.		3

Question 7 (8 marks)

(a) Certification of Financial Forecast: Under Clause (3) of Part I of Second Schedule to The Chartered Accountants Act, 1949, a CA in practice is deemed to be guilty of professional misconduct if he permits his name or the name of his firm to be used in connection with an estimate of earnings contingent upon future transactions in a manner which may lead to the belief that he vouches for the accuracy of the forecast. Further, SAE 3400 "The Examination of Prospective Financial Information", provides that the management is responsible for the preparation and presentation of the prospective financial information, including the identification and disclosure of the sources of information, the basis of forecasts and the underlying assumptions. The auditor may be asked to examine and report on the prospective financial information to enhance its credibility, whether it is intended for use by third parties or for internal purposes. Thus, while making report on projection, the auditor need to mention that his responsibility is to examine the evidence supporting the assumptions and other information in the prospective financial information, his responsibility does not include verification of the accuracy of the projections, therefore, he does not vouch for the accuracy of the same. Hence, the offer can be accepted if the above requirements are complied with.		2
(b) Bringing Disrepute to the Profession: A Chartered Accountant is expected to maintain the highest standard of integrity even in his personal affairs and any deviation from these standards, even in his non-professional work would expose him to disciplinary action. A member is liable to disciplinary action under Section 21 of the Chartered Accountants Act, if he is found guilty of any professional or "Other Misconduct". As per Clause (2) of Part IV of the First Schedule to the Chartered Accountants Act, 1949, a member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he in the opinion of the Council, brings disrepute to the profession or the Institute as a result of his action whether or not related to his professional work. The question whether a particular act or omission constitutes "other misconduct" should be based on fact and circumstances of each case. Under Negotiable Instruments Act 1881, where any cheque drawn by a person for the discharge of any liability is returned by the bank unpaid, either for insufficiency of funds or the cheque amount exceeds the arrangements made by the drawer of the cheque, the drawer of such cheque shall be deemed to have committed an offence. In the given case the cheque was dishonoured with the remark "refer to drawer". However, such dishonour need not necessarily be only due to insufficiency of funds. If it is proved that the cheques were dishonoured due to insufficiency of funds, the CA would be held guilty of "other misconduct".		2

(c) Failure to Communicate with the Previous Auditor: As per Clause (8) of Part I of First Schedule to the CA Act 1949, a chartered accountant in practice is deemed to be guilty of professional misconduct if he accepts a position as auditor previously held by another chartered accountant or a certified auditor who has been issued certificate under the Restricted Certificates Rules 1932, without first communicating with him in writing. In the instant case, PQ & Co. accepted VAT – audit under State Level Act, carried out by another firm of chartered accountants in the previous year, without prior communication with the previous auditor. A communication is mandatory requirement for all types of audit, if the previous auditor is a chartered accountant. Hence, the firm is guilty of professional misconduct.		2
(d) In terms of Clause (11) of Part I of the First Schedule to the CA Act, 1949, a CA in practice cannot engage (unless permitted by the council) in any business or occupation other than the profession of Chartered accountant, but he can be a director of a company wherein he or any of his partners is not interested in such company as auditor. However, public conscience is expected to be ahead of law and the requirement of independence should be interpreted much more strictly. Members should thus not place themselves in position which would either compromise or jeopardise their independence. In view of the above, an auditor of a subsidiary cannot be a director of a holding company as it will affect his independence.		2

Question 8 (8 marks)

(b) Under Clause (11) of Part I of First Schedule to the Chartered Accountants Act, a chartered accountant in practice is deemed to be guilty of professional misconduct, if he engages in any business or occupation other than the profession of chartered accountants, unless permitted by the council so to engage. However, nothing contained in Clause (11) shall disentitle a chartered accountant from being a director of a company, unless he or any of his partners is interested in such company as an auditor. Regulation 190A, states a member in practice cannot engage himself in any business or occupation other than that of a chartered accountant except when permitted by the council. As per Appendix 10 of Chartered Accountants Regulations, 1988, a Chartered Accountant in practice may hold the office of a Managing Director a Whole-time Director of a body corporate, provided that the member and/or his relatives do not hold substantial interest in such concern, after obtaining the specific and prior approval of the Council. He should seek prior approval of the council otherwise he would be held guilty of misconduct.		2

(c) Under Clause (12) of Part I of First Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice is deemed to be guilty of professional misconduct if he allows a person not being a member of the Institute in practice or a member not being his partner to sign on his behalf or on behalf of his firm, any balance sheet, profit and loss account, report or financial statements. This clause read in conjunction with Section 26 of the Chartered Accountants Act, 1949 stipulates that no person other than the member of the institute shall sign any document on behalf of a Chartered Accountant in practice or a firm of Chartered Accountants in his or its professional capacity. The term 'Financial Statement' for this purpose would cover an examination of the accounts or financial statements given under a statutory enactment or otherwise. Accordingly, Sapna is guilty of professional misconduct under Clause (12) of Part I of First Schedule and also under Clause (1) of Part II of Second Schedule for contravening Section 26.		2
(d) As per the Council General Guidelines 2008, under Chapter IX on appointment as statutory auditor a member of the Institute in practice shall not accepts the appointment as a statutory auditor of a PSUs'/Govt company(ies)/Listed company(ies) and other public company(ies) having a turnover of Rs. 50 crores or more in a year and where he accepts any other work(s) or assignment(s) or service(s) in regard to same undertaking(s) on a remuneration which in total exceeds the fee payable for carrying out the statutory audit of the same undertaking. For this purpose the other work/services includes Management Consultancy and all other professional services permitted by Council excluding audit under any other statute, Certification work required to be done by the statutory auditor and any representation before an authority. In view of the above position it would be a misconduct on Aamir's part if he accepts the management consultancy assignment for a fee of Rs. 1 crore.		2

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