J.K. SHAH TEST SERIES
Evaluate Learn Succeed

CA FINAL
Test Code – JK-AUD-22
(Date: 29-09-2020)

(Marks - 100)

All MCQs are compulsory Question No. 1 is compulsory.
Attempt any four questions from the Rest.
Division A – Multiple Choice Questions

(30 Marks)

Questions No. (1-10) carry 1 Mark each and Questions no. 11-20 carry 2 Marks each.

1. (IESBA Code) related to an audit of financial statements establishes which of the following as the fundamental principles of professional ethics relevant to the auditor when conducting an audit of financial statements

(a) Integrity
(b) Objectivity
(c) Professional competence and due care
(d) All of the above

2. Completion memorandum means

(a) Summary of significant matters
(b) Notes of concluding discussion
(c) Notes of audit team
(d) Notes of queries

3. Which of the following is not an analytical procedure?

(a) Tracing of purchases recurred in the purchase book to purchase invoices.
(b) Comparing aggregate wages paid to number of employees
(c) Comparing the actual costs with standard costs
(d) All of them are analytical procedures

4. Tests of control are not concerned with_

(a) Existence of controls
(b) Effectiveness of controls
(c) Continuity of controls
(d) Designing of controls

5. In Which of the following situation Emphasis of Matter Para Becomes Mandatory in audit report

(a) Facts that come to his knowledge after date of auditor's report leading to report revision

(b) Changes in accounting policies

(c) Material Uncertainty over going concern

(d) None of these. Emphasis of Matter Para is a voluntary concept and not a mandatory concept.

6. Compliance in order to establish Risk Management committee is applicable to _____________as per Regulation 21.

(a) Top 100 listed entities determined on the basis of market capitalization, as at the end of the immediate previous financial year.

(b) Top 100 listed entities determined on the basis of Book value, as at the end of the immediate previous financial year.

(c) Top 150 listed entities determined on the basis of Book value, as at the end of the immediate previous financial year.

(d) None of these

7. _______means insurance of suppliers against the risk of non-payment of goods or services by their buyers

(a) Trade credit insurance
(b) Bad debts Insurance
(c) Write-off Insurance
(d) Sale Insurance

8. As per the notification issued by The Indian Govt. GSR No.329E dated 13.02.1992, environment audit report is submitted to

(a) Central Pollution Control Board

(b) State Pollution Control Board

(c) Ministry of Environment and Forest

(d) None of these

9. Article 150 of constitution of India states that..

(a) Appointment of C&AG

(b) Rights and duties of CAG

(c) Form of accounts in consultation with CAG.

(d) Audit reporting by CAG

10. Dividend once declared become the liability of the company and must be paid within_________ from the date of declaration. Any failure to do so attract a penalty for the various persons associated with the management.

(a) 15 days (b) 30 days
(c) 20 days (d) 45 days

11. Medivision Industries designs and manufactures spectacles. Medivision's year end was 31 March 2018 and its draft financial statements show a profit before tax of ₹ 60 lakh. The fieldwork stage for this audit has largely been completed but there are few outstanding issues. On 1 January 2018, Medivision began the commercial production of a new range of lightweight frames which have been proven to keep their shape regardless as to how roughly they are treated. Up to 31 December 2017, the company had correctly capitalised development costs of ₹ 45 lakh relating to this project. The directors believe that the new frames will have a product life of three years. The financial statements show development costs at a carrying amount of ₹45 lakh. Medivision's accounting policy states that it amortises intangible assets on a straight-line basis. The auditor's report for Medivision is due to be signed in the next week or so, and you have been unable to resolve a disagreement with the directors concerning the amortisation of the development costs. The directors have refused to include any amortisation on the basis that sales of the product have not yet commenced. Which of the following options correctly summarises the impact on the auditor's report if the issue remains unresolved?

(a) The auditor to provide an 'Unmodified opinion', since the directors are correct not to include any amortisation on the basis that sales of the product have not yet commenced.
(b) The auditor to provide an 'Unmodified opinion' with emphasis of matter paragraph about the amortisation charge on the capitalised development costs.
(c) The auditor to provide a Modified opinion - Adverse opinion since having obtained sufficient appropriate evidence, concludes that the misstatement is both material and pervasive.
(d) The auditor to provide a Modified opinion – Qualified opinion due to material misstatement of not recording the amortization charge on the capitalised development costs, which is material but not pervasive

12. Your audit firm has been appointed as auditors of Red White Limited a manufacturing entity. The year under audit is 31 March 2018. While verifying account heads with high risk areas like revenue and inventory, you identify certain issues for which you are not provided satisfactory replies and documents by the client. At the same time Red White Limited approaches you to change the scope of the engagement. They give you the reason that they have misunderstood the scope of assignment earlier. What course of action would you adopt in this situation?

(a) Accept the revised terms of engagement, as the change is resultant of change in circumstance which affect entity’s requirements or misunderstanding concerning nature of service originally requested and consider aforesaid as reasonable basis for requesting change in the engagement.

(b) Accept the revised terms of engagement and record justification of the change in the engagement letter.

(c) Disagree to the revised terms and withdraw from the engagement where possible under applicable law and regulations and determine whether there is any obligation, either contractual or otherwise, to report the circumstance to other parties such as those charged with governance, owners or regulators.

(d) Disagree to the revised terms of the engagement and have your terms of increased fees since the scope of the engagement has changed.

13. The auditor is required to audit a complete set of annual financial statements for the year ended 31 March 2018 prepared under Ind AS by the management solely for preparation of consolidated financial statements of the holding company. Is the auditor required to include 'Other Legal and Regulatory Requirements' to comment on matters such as maintenance of proper books of accounts, compliance with accounting standards etc. in the audit report.

(a) Since the auditor is required to audit complete set of annual financial statements for the year ended 31 March 2018 prepared under Ind AS, it will be mandatory for the auditor to include 'Other Legal and Regulatory Requirements' in his audit report.

(b) The audit report is not issued pursuant to requirement of section 143 and hence 'Other Legal and Regulatory Requirements' is not required to be included in the audit report.

(c) The audit report is not issued pursuant to requirement of section 143 and hence some of the requirements related to 'Other Legal and Regulatory

Requirements' may be included in the audit report as per the discretion of the management of the Company.

(d) The auditor may include 'Other Legal and Regulatory Requirements' in the audit report but he would need approval of the Board of Directors for doing so.

14. The auditor is required to audit a complete set of annual financial statements for the year ended 31 March 2018 prepared under Ind AS by the management solely for preparation of consolidated financial statements of the holding company. Is the auditor required to include 'Other Legal and Regulatory Requirements' to comment on matters such as maintenance of proper books of accounts, compliance with accounting standards etc. in the audit report?

(a) Since the auditor is required to audit complete set of annual financial statements for the year ended 31 March 2018 prepared under Ind AS, it will be mandatory for the auditor to include 'Other Legal and Regulatory Requirements' in his audit report.

(b) The audit report is not issued pursuant to requirement of section 143 and hence 'Other Legal and Regulatory Requirements' is not required to be included in the audit report.

(c) The audit report is not issued pursuant to requirement of section 143 and hence some of the requirements related to 'Other Legal and Regulatory Requirements' may be included in the audit report as per the discretion of the management of the Company.

(d) The auditor may include 'Other Legal and Regulatory Requirements' in the audit report but he would need approval of the Board of Directors for doing so.

15. BDJ Ltd. is engaged in the business of providing management consultancy services and have been in operation for the last 15 years. The company’s financial reporting process is very good and its statutory auditors always issued clean report on the audit of the financial statements of the company. The auditors were required to be rotated due to mandatory audit rotation requirement of the Companies Act 2013.

RNJ & Associates, a firm of Chartered Accountants, was appointed as the new auditor of the company for a term of 5 years and have to start their first audit for the financial year ended 31 March 2019.

The auditors had a detailed and clear discussion with the management that they will perform their audit procedures in respect of opening balances along with the audit procedures for the financial year ended 31 March 2019.

Management agreed with that and the audit was completed as per the plan.

The auditors did not have any significant observations and hence they communicated to the management that their report will be clean. Management was quite happy with this and also requested the auditors to share draft report before issuing the final report.

In the draft audit report, all the particulars were fine except 'other matters paragraph' wherein the auditors gave a reference that the financial statements for the comparative year ended 31 March 2018 was audited by another auditor. Management asked the audit team to remove this paragraph as the auditors had performed all the audit procedures on opening balances also. But the auditors did not agree with the management.

Please advise the auditor or the management whoever is incorrect with the right guidance.

(a) The contention of the management is valid. After performing all the audit procedures, an auditor should not pass on the responsibility to another auditor by including such references in his audit report.

(b) Any auditor has two options, either to perform audit procedures on opening balances or given such reference of another auditor in his report. An auditor can not mix up the things like this auditor has done. It is completely unprofessional.

(c) In the given situation even if the auditor wants to give such reference, the management and the auditor should have taken approval from the previous auditor at the time of appointment of new auditor. In this case, it cannot be done.

(d) The report of the auditor is absolutely correct and is in line with the auditing standards. An auditor is required to include such reference in his report as per the requirements of the auditing standard.

Integrated Case Scenario

QRP Lifecare Private Limited, (the 'Company' or 'QRP'), is engaged in the pharmaceuticals. The Company
is based in Hyderabad and has an annual turnover of INR 400 crores.

One of the directors of the Company did not give declaration to the Company under section 164(2) of the Companies Act 2013 as at 31 March 2018. The auditors of the Company have completed their audit of the financial statements for the year ended 31 March 2018 and are awaiting this declaration. But the management is of the view that they will not be able to receive this declaration. All other directors have given the required declarations and the auditors have also verified that.

QRP had given an advance amounting to INR 50 crores to its subsidiary, RPS Ltd (RPS), on 12 January 2014 for carrying out certain projects. The net worth of the subsidiary has eroded substantially as on 31 March 2018 and looking at the future projections there is no certainty in terms of the profitability of the subsidiary.

QRP has a subsidiary, SPS Ltd (SPS), in UK. The company has outstanding trade receivables amounting to INR 10 crores from SPS. QRP has observed that there have been some FEMA (Foreign Exchange Management Act) non-compliances on the part of QRP but the management has an action plan which they have initiated and on the basis of which management is sure that the non-compliance would be done good and there would be no penalty on the company. In case the penalty arises, the impact would be significant for QRP. The auditors of QRP have evaluated this matter by involving a regulatory matters expert and also agree with the management's view.

QRP was using a customized ERP package upto 31 March 2018. However, with effect from 1 April 2018, QRP moved on SAP (ERP package) considering the increase in size of the operations of QRP. The auditors of QRP are of the view that for the financial year ended 31 March 2019, being the first year of SAP implementation, no work on IT controls would be required and they are also evaluating to qualify report on IFC because on the basis of their experience on other clients in the past where the IT controls in the first year of ERP implementation were very weak.

On the basis of the abovementioned facts, you are required to answer the following MCQs:

16. How should the auditors of QRP deal with the matter related to non-receipt of declaration under 164(2) of the Companies Act?

(a) Auditors may perform some alternate procedures in respect of non-receipt of declaration under 164(2) of the Companies Act.

(b) If the auditors have been able to verify that all directors except one have given the required declarations as per the Companies Act then it should be ignored by the auditors on the basis of materiality.

(c) There is no reporting implication due to non-receipt of declaration under 164(2) of the Companies Act from just one director. Accordingly, the auditors should issue clean report in respect of this matter, however, the auditors should insist the management to provide this declaration later on.

(d) Auditors would need to report this matter in their main report.

17. How should the auditors of QRP deal with the matter related to erosion of net worth of RPS? Is there any reporting implication for the same?

(a) In respect of QRP, there is no reporting implication on the part of auditors of QRP due to erosion in net worth of RPS. This matter would be relevant for the auditors of RPS.

(b) In respect of QRP, auditors of QRP would need to give an emphasis of matter in their report considering the uncertainty involved related to profitability of RPS.

(c) In respect of QRP, auditors of QRP would need to give qualification in respect of non-recovery of advances from RPS if the adjustment entry is not recorded in the books.

(d) In respect of QRP, auditors of QRP would need the management to include a note in the financial statements of QRP explaining about the recoverability of advances from RPS.

18. Please suggest the way auditors have handled the matter related to FEMA non-compliances is appropriate or not.

(a) Auditors didn't handle this matter appropriately. Auditors should have informed about this matter to the RBI (Reserve Bank of India) within a period of 30 days from date this matter came to their knowledge.

(b) Auditors handled this matter appropriately. The management would need to include this matter in the notes to accounts to the financial statements.

(c) Auditors handled this matter appropriately. But they would also need to include modification in their report because the impact of penalty, if levied, can be material.

(d) Auditors could have handled this matter in a better manner by also involving a tax expert because this might result in a penalty and that may have some taxation impact for the Company.

19. QRP has been preparing consolidated financial statements but they do not consolidate financial statements of SPS every year. This is because the financial year followed by SPS is January to December as against April to March followed by QRP. The auditors have also been fine with this position of the management of QRP year on year. Please suggest.

(a) QRP needs to prepare consolidated financial statements by also consolidating SPS. In case this is not done, the auditors need to qualify their report on consolidated financial statements.

(b) QRP needs to prepare consolidated financial statements by also consolidating SPS. In case this is not done, the auditors need to give emphasis of matter in their report on consolidated financial statements.

(c) QRP's management's view is right because SPS is a foreign company and hence no consolidation may be done while preparing consolidated financial statements in India.

(d) Auditors of QRP should have done materiality assessment in respect of non-consolidation of SPS in the consolidated financial statements. The auditors should ask the management to include a note in the consolidated financial statements and also take management representation letter for the same.

20. As an expert what will be your advice about the view of the auditors of QRP regarding not testing IT controls in the first year of SAP implementation and evaluating qualification in IFC report.

(a) The auditors have precedence on the basis of which they have formed a view and that is completely acceptable. However, the auditors would need to document this properly in their audit files.

(b) The auditors need to perform procedures before forming any view. Any such precedence of other client cannot be taken for QRP without performing any procedure by the auditors.

(c) The auditors have precedence on the basis of which they have formed a view and that is fine as far as they don't want to test IT controls. However, to qualify the IFC report on the basis of precedence of other clients only may not be appropriate. Management should include a note in their financial statements in respect of first year of SAP implementation.

(d) The auditors have precedence on the basis of which they have formed a view and that is fine as far as they don’t want to test IT controls. However, instead of qualification, disclaimer would be appropriate in the IFC report because there is no work for making any conclusion by the auditors. Management should also include a note in their financial statements in respect of first year of SAP implementation.

Division B - Descriptive Questions

Question No. **1** is compulsory.

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

(70 Marks)

Q.1 (a) It was observed from the modified audit report of the financial statements of Ram Ltd. for the year ended 31st March, 2019 that depreciation of ₹ 2.50 crore for the year 2018-19 had been charged off to the statement of Profit and Loss instead of including it in "Carrying value of asset under construction". State in relation to the audit for the year ended 31st March 2020, whether such modification in the previous year's audit report would have any audit implication for the current year and if yes, how would you deal with it in your audit report?

(5 Marks)

(b) The auditor of Laxman & Co. Ltd. has intimated the management that certain misstatements identified during the course of audit need to be corrected. As an auditor, discuss the impact of such misstatements in case the management does not carry out the said corrections

(5 Marks)

(c) Sita & Co., a firm of Chartered Accountants have not revised the terms of engagements and obtained confirmation from the clients, for last 5 years despite changes in business and professional development. Please elucidate the circumstances that may warrant the revision in terms of engagement.

(4 Marks)

Q.2 (a) "Generating and preparing meaningful information from raw system data using processes, tools, and techniques is known as Data Analytics and the data analytics methods used in an audit are known as Computer Assisted Auditing Techniques or CAATs." You are required to give a suggested approach to get the benefit from the use of CAATs.

(4 Marks)

(b) As auditor of Arjun., you would like to limit your examination of account balance tests. What are the control objectives you would like the accounting control system achieve to suit your purpose?

(5 Marks)

(c) Duryodhan Ltd. is a private company. Its balance sheet shows paid up share capital of ₹ 5 crore and public borrowings of ₹ 100 crore. The company appointed M/s Karna & Co., a chartered accountant firm, as the statutory auditor in its annual general meeting held at the end of September, 2017 for 11 years.

You are required to state the provisions related to - rotation of auditors and cooling off period as per the section 139(2) of the Companies Act, 2013 in case of an individual auditor or an audit firm, both, and comment upon the facts of the case provided above with respect to aforesaid provisions.

(5 Marks)

Q.3 (a) Mr. G. has been appointed as an auditor of LMP Ltd., a NBFC company registered with RBI. Mr. G is concerned about whether the format of financial statements prepared by LMP Ltd. is as per notification issued by the Ministry of Corporate Affairs (MCA) dated October 11, 2018. The notification prescribed the• format in Division III under Schedule III of the Companies Act, 2013 applicable to NBFCs complying with Ind-AS. Mr. G wants to know the differences in the presentation requirements between Division II and Division III of Schedule III of the Companies Act, 2013. Help Mr. G.

(5 Marks)

(b) CA Kumar who is contesting Central Council Elections of Institute, engages his Articled Assistant for his election campaigning promising him that he will come in contact with influential people which will help to enhance his career after completion of his training period.

(5 Marks)

(d) How as a statutory auditor would you comment on the following: X Pvt. Ltd. Is a subsidiary of a listed entity. The management of the company believes that since X Pvt. Ltd. is a private company and satisfies all condition under CARO 2016, reporting under CARO is not applicable.

(4 Marks)

Q.4 (a) In the course of audit of No Bank Ltd., you found that the bank had sold certain of its non-performing assets. Draft the points of audit check that are very relevant to this area of checking

(5 Marks)

(b) A film artist who was going abroad for long shooting, deposited a sum of ₹ 20 lakhs with his tax consultant Mr. Guru, a practising Chartered Accountant for payment of Goods and Service Tax monthly when they were due, Mr. Guru duly remitted all but one instalments. He utilised the amount of instalment which he did not pay, to remit his own advance income tax. However, while filing return of GST of the film artist, he duly remitted on her behalf the tax payable with interest due for late payment of GST out of money lying with him. He also bore for himself the interest due to short fall in remittance of tax of his client. Comment on the above in the light of Code of Conduct.

(5 Marks)

(c) Draft an Audit programme for conducting the audit of a Public Trust registered under section 12A of the Income tax Act, 1961.

(4 Marks)

Q.5 (a) Jethalal Ltd. is anticipating taking over a manufacturing concern and appoints you for due diligence review. While reviewing, it requests you to look specifically for any hidden liabilities and overvalued assets. State in brief the major areas you would examine for hidden liabilities and overvalued assets.

(5 Marks)

(b) H Co. Ltd., is a holding company with two subsidiaries R Co. Ltd., and S Co. Ltd. The H Co. Ltd., adopts straight line method of depreciation for its assets whereas S Co. Ltd., follows written down value or diminishing value method. Though R Co. Ltd., follows straight line method of depreciation, it does not give effect to component accounting of depreciation in respect of high value assets. While consolidating the financials of the R Co. Ltd., and S Co. Ltd., with those of H Co. Ltd., determine the possible issues that you have to ensure for compliance in the light of above facts.

(5 Marks)

(c) Mr. Lehri while conducting the audit of ABC Ltd., observed that a substantial amount is recognized in respect of obsolescence of inventory and warranty obligation in the financial statements. Mr. Lehri wants to obtain written representation from the management to determine whether the assumptions and estimates used are reasonable. Guide Mr. Lehri with reference to the relevant Standard on Auditing.

(4 Marks)

Q. 6 (a) Mr. Bindesh, a Chartered Accountant in practice was invited to deliver a seminar on GST which was attended by professionals as well as by representatives of various Industries. One section of audience raised a particular issue unique to the industry to which it pertains. Mr. Bindes enthusiastically explained the issue and elaborated how he actually solved this, for his client facing the same issue with worked out examples from the computer storage device using the actual data of one of his clients with full identification of client details being displayed to the group for the sake giving clarity on a topic in a real life situation. Comment his acts in the light of Code of Conduct

(5 Marks)

(b) The elements of skill experience and independence of reviews are ensured before initiating them in Peer Review process. In the above light, state few eligibility criteria fixed for a person to be em-panelled and also for being appointed as a peer Reviewer.

(5 Marks)

(c) Kamal & Co. Chartered Accountants have been appointed by C & AG for performance of a audit of a sugar industry. What factors should be considered by Kamal & Co., while planning a performance audit of a sugar industry?

(4 Marks)