

CA-FINAL
GROUP I – PAPER 3
ADVANCED AUDITING AND PROFESSIONAL ETHICS
SERIES - 2 (May 2020)

Roll No.
Time Allowed: - 3 Hours

Date : 14.03.2020
Maximum Marks: 100

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Division "A"
All Questions are compulsory.
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(Q. 1 to 5) Multiple Choice Questions based on Integrated Case Scenarios

RS Ltd was set up by Raj and Shanti in 1992. Initially the name of the company was Rajeev Private Limited. The company is currently into the business of aviation. The company has its head office at Chennai. The company has been in the same business since its incorporation but over the years had to shut down its business 3 times due to operational inefficiencies and resultant losses.

In the year 2012, when the company restarted its operations after shutting that down third time, the company got funding from foreign investors. The management of the company increased its focus on the processes of the company and various checks and controls to improve the efficiency of the operations. This gradually resulted in improving the overall business culture of the company and gradually company started earning profits.

In the year 2016, the company got converted into public company and got its name changed to RS Ltd. After that the company also tried to get listed on the New York Stock Exchange but the market was not favourable and the company instead got listed in India.

The company kept increasing its focus on operational efficiencies which was also extended to all other processes of the company, most importantly, financial reporting which was not focused earlier by the management.

The company also appointed a large firm of Chartered Accountants, KB & Co, as its internal auditors, who have had specialization in the same sector so that they can help the company to fill the gaps in the processes, wherever required.

The company also appointed other consultants to improve on the operations and management functions.

During the financial year ended 31 March 2018, the internal auditors of the company raised some observations which were discussed in detail with the management, primarily because the management was not agreeing to some of the points of the internal auditors.

Subsequently in the financial year ended 31 March 2019, the management decided to set up its in-house internal audit function along with the CA firm, KB & Co. The idea was to do the work in-house and over the period, KB & Co can move out once the management is confident of the in-house internal audit function.

Considering the above mentioned facts, please provide your suggestions in respect of the following:

1. The Standard Operating Procedures (SOP) for logistics process was not defined from the point of vehicle request received from the sales marketing department up to the bills verification. The management explained that part of this process was developed and remaining part was expected within next 3 months. 1
 - (a) This is more of a documentation and hence not relevant for the management.
 - (b) Auditor should highlight and report this matter in his report.
 - (c) The matter which is already under development should not be considered by the auditor.
 - (d) Management needs to demonstrate the development process further and get this issue closed.

2. **It was noted that during a particular period, cash in hand balance was higher than actual cash requirement at some locations. Ratio of cash expenses to closing cash balance during that period ranged from 7 to 84 times. Further the insurance cover was also not taken for the cash in hand kept at some locations. The management explained that this occurred only during a specified period and the insurance coverage plan was in place for the next year.** 1
- (a) Auditor should report this matter in his report.
(b) The management needs to explain the amount involved and if that is low then the auditor should ignore this.
(c) The cash balance should not be looked at by the internal auditor as this is more relevant from financial reporting.
(d) Internal auditor should only report about not availability of the insurance coverage to the management.
3. **On review of procurement process, it was observed that the system was not enabled to show pending delivery of same material while raising a subsequent purchase order and the guidelines were not defined for review of open purchase orders and long pending orders.** 1
- Management explained that this was due to lead time, locking in quantity/price, lead time to shipment, delays in delivery due to rake unavailability, failure of vendors to supply material as per timelines or quality etc and they will explore how system driven reporting can be done.**
- (a) This was an operational challenge and hence out of the purview of internal auditor.
(b) This related to some system constraints and hence may be ignored by the internal auditor.
(c) The internal auditor needs to highlight this in his report.
(d) The management should draw a proper plan to take care of this. In any case there doesn't appear to be any financial impact due to this and hence the same should be ignored.
4. **It was observed that the credit limit assessment was not being performed for all the customers which could result in possibility of credit being given to customers with weak financial credibility leading to bad debts/ financial losses to the company. Management replied that they started the process of updation of credit limit in their ERP package which shall be completed in a month's time for major customers and for customers wherever temporary credit limit was defined. This would cover majority of exposure.** 1
- (a) Since the management has already taken remedial action, the internal audit should drop this point.
(b) Since this matter related to financials, this should be covered by the statutory auditors and not the internal auditors.
(c) The management said that statutory auditors have also raised this point and hence internal auditors should drop this.
(d) Internal auditors should report this irrespective of the fact whether statutory auditors covered this or not.
5. **The management's plan to phase out the CA firm by building up in-house internal audit team has been questioned by the statutory auditors saying this is not acceptable.** 1
- (a) Statutory auditors are correct.
(b) Statutory auditors should observe this for a period and if that is working fine then they should have no concern regarding this.
(c) The management has a discretion regarding this and hence statutory auditors are not correct.
(d) The management should take approval from relevant authority like MCA and then statutory auditors would have to accept this.

(Q. 6 to 10) Multiple Choice Questions based on Integrated Case Scenarios

The Chanakya Bank Ltd. was having 150 branches all over India by the year ending 31st March, 2019. Ten branches of the bank were already covered for concurrent audit and the Bank's Audit Committee decided to include the below mentioned branches for concurrent audit from the year 2019-20.

1. Banaras branch which deals in treasury functions like investments and inter bank borrowings but not in bill re-discounting.
2. Allahabad branch which started foreign exchange business from February 2019.
3. Rae Bareilly branch whose aggregate deposits were more than 35% of the aggregate deposits of the bank.

Sista and Chartered Accountants were appointed as the stock auditors by the Bank's audit committee for five branches for year 2019-20. The Bank's management appointed and fixed the remuneration of Sista and Chartered Accountants as the statutory auditors also for the year 2019-20, for the same five branches for which they were given the assignment of stock audit.

At the Kanpur branch of the bank there were high value cash deposits in one of the current account from April 2019. Your firm has been appointed as the concurrent auditors for the Kanpur branch for the year 2019-20. The cash collected by the branch was remitted to currency chest on the very same day but, during the concurrent audit for the month of April 2019 itself the auditor noticed that the branch has not filed the requests sent via e-mail to currency chest for the cash remittance.

Answer the below questions based on the above paragraph:

6. **Whether the decision of audit committee to include the three branches mentioned in above paragraph for concurrent audit is as per RBI Guidelines?** 1

- (a) The decision of audit committee is valid as according to RBI Guidelines, all the three branches fulfil the criteria for compulsory concurrent audit.
- (b) Banaras and Allahabad branch falls under the compulsory audit criteria as per RBI Guidelines, however Rae Bareilly branch whose aggregate deposits are less than 50%.
- (c) As Banaras branch doesn't deal in bill re-discounting, it is not required to be covered under concurrent audit. Allahabad and Rae Bareilly branch are compulsorily required to be covered under concurrent audit as per RBI Guidelines.
- (d) Allahabad branch has started foreign exchange business in February 2019 and as per RBI Guidelines only the branches dealing in Foreign exchange business from more than three years are covered under concurrent audit. Therefore, Allahabad branch is not covered under compulsory concurrent audit criteria as per RBI Guidelines but the Banaras and Rae Bareilly branch are covered under compulsory concurrent audit criteria.

7. **Sista and Chartered Accountants were already appointed for stock audit by the audit committee for the five branches, so whether Sista and Chartered Accountants are authorised to accept the appointment as statutory auditors for the same branches?** 1

- (a) Sista and Chartered Accountants cannot accept the appointment as it was not offered by the audit committee and Bank's management is not authorised to appoint the auditors.
- (b) Sista and Chartered Accountants can accept the appointment as they were already appointed for the stock audit of those branches by the audit committee.
- (c) Sista and Chartered Accountants can accept the appointment as they have been appointed statutory auditors for the same five branches for which they were conducting stock audit.
- (d) Sista and Chartered Accountants cannot accept the appointment as the audit firms should not undertake statutory audit assignment while they are associated with internal assignments in the Bank during the same year.

8. **Whether the Bank's Management is authorise to appoint and fix the remuneration of statutory auditors without consulting the Audit Committee of the Board of Directors or members in Annual General Meeting?** 1
- (a) Bank's Management cannot appoint or fix the remuneration of the statutory auditor unless the same is passed by a resolution in the Annual General Meeting of the Bank.
 - (b) Bank's Management can appoint and fix the remuneration of statutory auditors only in consultation with the Audit Committee of the Board of Directors.
 - (c) Sista and Chartered Accountants were already appointed for stock audit by the audit committee, therefore only audit committee was authorise to appoint or fix their remuneration as statutory auditors.
 - (d) Sista and Chartered Accountants were already appointed for stock audit by the audit committee, so the Bank's Management is authorise to appoint the same firm as the statutory auditors without consulting the audit committee or members in the Annual General Meeting.
9. **You have been asked by your senior to verify the high value cash deposits at the Kanpur branch. What parameters/ documents will you verify as the concurrent auditor of the branch?** 1
- (a) Concurrent auditor has to verify the details of cash remittance to Currency Chest only.
 - (b) You need to verify the KYC documents of the customer/s and the reason for high value cash deposit in the account like nature of business or sale of property etc.
 - (c) Verify the KYC documents of the account in which cash is deposited; verify the reason for high value cash deposit in the account like nature of business/ transaction etc.; verify the discrepancies found in the cash of the customer/s, if any and ensure that the records of Currency Chest remittance is maintained properly.
 - (d) As a concurrent auditor you need to verify the reason of regular cash deposit in the account/s and the nature of discrepancies, if any, found in cash deposited by the customer/s.
10. **How the discrepancy of not filing the details of cash remittances to currency chest by Kanpur branch of the bank should be dealt by the concurrent auditor in his audit report?** 1
- (a) The auditor should report the matter as a major irregularity in his audit report to the management.
 - (b) The auditor should verify the details from e-mail sent to currency chest and close the matter.
 - (c) As it is a minor irregularity the auditor can ignore the same.
 - (d) The auditor should discuss the importance of filing the copy of e-mail sent for cash remittance with the Branch Manager and check for its compliance in the next audit period.

11. **AB Ltd. is a company in which public are not substantially interested. During the previous year 2018-19, the company issued shares to residents of India and provides you the following data related to such issue:** 2
- | | |
|--------------------------------|----------------------|
| No. of shares | 1,00,000 |
| Face Value | ₹10 per share |
| Fair Market Value (FMV) | ₹60 per share |
| Consideration received | ₹80 per share |
- The management of the company contends that, it is normal issue of shares, thus, need not to be reported. As the tax auditor of AB Ltd., how would you deal with the matter in your tax audit report?**
- (a) Excess of issue priced over fair market value of shares issued, is taxable as per section 56(2) (viiia) of the Income Tax Act, 1961. Therefore, the tax auditor is required to furnish the details of shares issued under clause 28 of Form 3CD.
- (b) Excess of issue price over fair market value of shares issued, is taxable as per section 56(2) (viib) of the Income Tax Act, 1961. Therefore, the tax auditor is required to furnish the details of shares issued under clause 29 of Form 3CD.
- (c) Excess of issue price over fair market value of shares issued, is taxable as per section 56(2) (ix) of the Income Tax Act, 1961. Therefore, the tax auditor is required to furnish the details of shares issued under clause 29A of Form 3CD.
- (d) Excess of issue price over fair market value of shares issued, is taxable as per section 56(2) (x) of the Income Tax Act, 1961. Therefore, the tax auditor is required to furnish the details of shares issued under clause 29B of Form 3CD.
12. **Bank are required to cover _____ under concurrent audit.** 2
- (a) 60 per cent of total deposits and 40 per cent of total advances.
 (b) 40 per cent of total deposits and 60 per cent of total advances.
 (c) 50 percent of total deposits and 50 per cent of total advances.
 (d) 75 per cent of total deposits and 75 per cent of total advances.
13. **Every NBF shall maintain a capital ratio consisting of Tier I and Tier II capital of its aggregate risk weighted assets on-balance sheet and of risk adjusted value of off-balance sheet items, which shall not be less than ____%.** 2
- (a) 10% (b) 12%
 (c) 15% (d) 16%
14. **Facultative reinsurance is not available in case of:** 2
- (a) Existence of treaty reinsurance. (b) Treaty reinsurance exhausted.
 (c) When insurer has automatic cover (d) None of the above
15. **Which of the following functions is not covered within the scope of Estimates Committee:** 2
- (a) To suggest alternative policies in order to bring about efficiency and economy in administration;
 (b) To examine whether the money is well laid out within the limits of the policy implied in the estimates;
 (c) To suggest the form in which the estimates shall be presented to parliament.
 (d) To examine that the moneys (shown in the accounts) were disbursed for the purpose to which they were applied.
16. **As per Rule 24 of LLP Rules, 2009, Statement of Account and Solvency shall be filed in _____ with the _____, within a period of _____.** 2
- (a) Form 5, SEBI, 30 days from the end of 3 months of the financial year to which the Statement of Account and Solvency relates.

- (b) Form 5, Register, 30 days from the end of 6 months of the financial year to which the statement of Account and Solvency relates.
- (c) Form 8, SEBI, 30 days from the end of 3 months of the financial year to which the Statements of Accounts and Solvency relates.
- (d) Form 8, Register, 30 days from the end of 6 months of the financial year to which the Statement of Account and Solvency relates.
- 17. In case of Quality Review assignments, Technical Reviewers are required to submit final report along with a copy of Annual report of the company/entity for the year, as specified, to the Board within _____.** **2**
- (a) 45 days from the date of acceptance of the assignment.
- (b) 90 days from the date of acceptance of the assignment.
- (c) 45 days from the date of commencement of work
- (d) 90 days from the date of commencement of work.
- 18. Identify the stages involved in Forensic audit in sequence-** **2**
- (a) Initialisation, planning, Collection of Evidences, Perform Analysis, Reporting and Court proceedings.
- (b) Court Proceedings, Planning, Collection of Evidences, Perform Analysis, Reporting and Initialisation.
- (c) Planning, Collection of Evidences, Perform Analysis, Reporting, Initialisation and Court proceedings.
- (d) Planning, Collection of Evidences, Perform Analysis, Reporting, Court proceedings and Initialisation.
- 19. Effects of a lapsed policy are -** **2**
- (a) It ceases to provide insurance protection to the insured.
- (b) It forfeits the benefits under the policy and cost of new policy is higher.
- (c) Agents do not get renewal premium commission if the policy is lapsed.
- (d) All of the above.
- 20. COSO framework defines five areas, which when implemented, can help support the requirements as set forth in the Sarbanes-Oxley legislation. These five areas are.** **2**
- (a) Risk Assessment, Control Environment, Internal Check, Monitoring, Information and Commission.
- (b) Risk Assessment, Control Environment, Control Activities, Monitoring, Information and Communication.
- (c) Risk Assessment, Control Environment, Control Activities, Documentation, Information and Communication.
- (d) Risk Assessment, Control Environment, Control Activities, Monitoring and Documentation.

Division "B"
Question No. 1 is compulsory.
Attempt any Four questions from the rest.

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- 1A.** Mr. X was appointed as the auditor of M/s Easygo Ltd. and intends to apply the concept of materiality for the financial statements as a whole. Please guide him as to the factors that may affect the identification of an appropriate benchmark for this purpose. **5**
- B.** Discuss the impact of uncorrected misstatements identified during the audit and the auditor's response to the same. **5**
- C.** G Ltd. is a mobile phone operating company. Barring the marketing function it had outsourced the entire operations like maintenance of mobile infrastructure, customer billing, payroll, accounting functions, etc. Assist the auditor of G Ltd. as to how he can obtain an understanding of how G Ltd. uses the services of the outsourced agency in its operations. **4**
- 2A.** You have been appointed to investigate a suspected embezzlement of cash receipts in a departmental store. What are the steps you would take in this regard? **5**
- B.** Explain the difference between the Proportional Treaties and Non Proportional Treaties? **5**
- C.** ABC Limited, an Indian insurance company carrying on general insurance business, is facing liquidity problems and, therefore, it has decided to maintain deposits under section 7 of the Insurance Act, 1938 at one percent of total gross premium written in India. The company thinks that it is sufficient, as the company has a Paid-up Capital of ₹150 Crores. As an Auditor of ABC Limited what would be your suggestion to the company for compliance of Insurance Act and rules and regulations made there under? **4**
- 3A.** What are the main phases in the conduct of Risk Based Audit. **5**
- B.** As an auditor of a Non Banking Financial Company registered with the Reserve Bank of India (RBI), what are the prudential norms of RBI, whose compliance is to be verified? **5**
- C.** What are the professional obligations of the auditor who has resigned from the audit before completion of his term due to non co-operation of the Management in completing certain audit procedures? **4**
- 4A.** Kalmani & Co. Chartered Accountants have been appointed by C & AG for performance audit of a sugar industry. What factors should be considered by Kalmani & Co., while planning a performance audit of a sugar industry? **5**
- B.** ABC & Associates, a firm with 5 partners developed a website www.abcassociates.com. The website also contained a link to "All India Chartered Accountants Association", a voluntary association where X, a partner of the firm is currently the Vice-president. **5**
- C.** XYZ Ltd. pays ₹ 90000 for its 6 employees to a Hotel as boarding and lodging expenses of such employees for a conference. The Company pays the amount in cash to the Hotel. The Hotel gives 6 bills each amounting to ₹ 15000. The Company contends that each bill is within the limit, so there is no violation of the provisions of the Income Tax Act, 1961. As the tax auditor, how would you deal with the matter in your tax audit report for the Assessment Year 2014-15? **4**
- 5A.** Areas to be reviewed in the assessment of independence of the practicing unit, while conducting peer review. **5**

- B.** Priya Co. Ltd. has applied to a bank for loan facilities. The bank on studying the financial statements of the company notices that you are the auditor and requests you to call at the bank for a discussion. In the course of discussions, the bank asks for your opinion regarding the company and also asks for detailed information regarding a few items in the financial statements. The information is available in your working paper file. What should be your response and why? **5**
- C.** M/s IT Limited has prepared the financial statements for the year 2014-15 and mentioned in the significant accounting policies that depreciation on tangible fixed assets is provided on the straight line method over the useful lives of the assets as estimated by the management. The company has ignored the useful lives of assets mentioned in Schedule II of the Companies Act, 2013. As statutory auditor of the company how would you deal with this? **4**
- 6A.** “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. **5**
- B.** Enumerate the steps to be undertaken in case of forensic audit process. **5**
- C.** Mr. X, a young chartered accountant, wants to start practice and he requires your advice, among other things, on criminal liabilities of an auditor under the Companies Act, 2013. Kindly guide him. **4**