

Gurukripa's Guideline Answers to Nov 2014 Exam Questions CA Final ADVANCED AUDITING AND PROFESSIONAL ETHICS

Question 1 is compulsory (4 × 5 = 20 Marks)

Answer **any five** questions from the **remaining six** questions (16 × 5 = 80 Marks). [Answer any 4 out of 5 in Q.7]

Notes:

1. **Applicable Law:**

- Answers are given here, under Provisions of Companies Act, 2013, as applicable for May 2015 Exams.
- Also see Notes below for modifications of certain answers as applicable for Nov 2014 Exams.

2. **Page Number References:** Page Number References are given with the following abbreviations –

- **SA Book** means – “Padhuka’s Students’ Referencer on Standards on Auditing – For CA Final”
- **AS Book** means – “Padhuka’s Students’ Referencer on Accounting Standards – For CA Final”
- **This Book** means – “Padhuka’s Students Handbook on Advanced Auditing – For CA Final”

Qn	Questions	Reference/Hint Answer	Marks
1	(a) In the Notes to Accounts of Z Co. Ltd as on 31-03-2015, Note No. 10 states that certain machinery items are lying at customs warehouses and that the Company has paid ₹ 500 lakhs up to 30-06-2014 as Detention Charges, out of which a sum of ₹ 220 Lakhs is written back during the year 2014-2015 based on settlement with the concerned authorities in respect of a major spares of machinery. For the remaining machinery items, negotiations are pending and a provision of ₹ 48 Lakhs has been made. As such a total amount of ₹ 328 Lakhs paid / provided on account of Detention Charges have been capitalized and included in the Fixed Assets / Capital Work in Progress. The Management is of the view that these expenses are directly attributable to the acquisition of the related Fixed Assets. As the Auditor, how would you respond to this?	<p style="text-align: center;">Refer:Q.No.25, Page 10.7 of AS Book. Same as N 10</p> <p>Hint:</p> <ol style="list-style-type: none"> 1. Detention Charges are not Cost incurred directly or indirectly on the Asset. Such costs should not be capitalized. 2. Auditor should report non-compliance with AS-10 principles, in this case. 	5
	(b) The Auditor of PQR Pvt. Ltd having Turnover of ₹ 12 Crores, was not able to get the confirmation about the existence and value of certain Stock. However, a certificate from the Management has been obtained regarding the existence and value of the Stock at the year end. The Auditor relied on the same and without any further procedure, signed the Audit Report. Is he right in his approach?	<p style="text-align: center;">Refer: Q.No.10, Page 133 SA- 580, and Q.6, Page 89 SA-501 of SA Book. Same as F-N 03, P-N 07</p> <p>Hint:</p> <ol style="list-style-type: none"> 1. SA-501 requires the Auditor to obtain audit evidence on Inventory by attendance at physical inventory counting, under it is impracticable. Also alternative audit procedures are to be done. 2. Auditor cannot issue a Clean Opinion based on the Management’s Certificate only without performing any further Audit Procedures. 	5
	(c) Discuss the impact of Uncorrected Misstatements identified during the audit and the Auditor’s response to the same.	<p style="text-align: center;">Refer: Q.No.5, Page 81 of SA Book. Same as M 97, M 02</p> <p>Hint: Under SA-450, Auditor should consider materiality of uncorrected misstatement by assessing their size and nature, circumstances, prior period effects, etc. He should document his conclusion and basis thereof.</p>	5
	(d) What are the roles and responsibilities of the Statutory Auditors in relation to compliance with the Laws and Regulations by the Entity?	<p style="text-align: center;">Refer: Q. No. 3, Page 40 of SA Book.</p> <p>Hint: Under SA- 250 Auditors’ response-bilities include- (a) Identification of material non-compliance with laws &</p>	5

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		regulations, (b) reporting to Those charged with Governance, Regulatory & Enforcement Authorities, (c) considering impact in Auditors' Report, & reporting of frauds.	
2	(a) While commencing the Statutory Audit of ABC Company Limited, what should be the considerations of the auditor to assess Risk of Material Misstatement, and his response to such risks?	Refer: Q.No.3, Page 72 of SA Book. Hints: Auditors should perform Risk Assessment Procedures. For this purpose, proper understanding of the Entity and its Environment is to be done.	4
	(b) How would the method of collecting audit evidence relating to effectiveness of controls and evaluating the same change under a Computerized Environment.	Refer: Q.No.13, Page 14.8 of This Book. Same as N 97, N 07	4
	(c) Describe the principal methods of selection of samples.	Refer: Q.No.10, Page 104 of SA Book. Hints: Principal Methods are–(1) Random sampling – simple or stratified (2) Internal sampling– Block & Cluster, (3) Monitory unit sampling, (4) Haphazard Selection, and (5) Block Selection.	4
	(d) Describe how you would identify the inherent risk at the Account Balance and Class of Transaction Level in the planning process of the audit of a large multi-locational company.	Refer:Q.No.28, Page 63 of SA Book. Same as N 09 Hint: 1. Account Balances: Auditor to assess risk affecting assertions of (a) Existence, (b) Rights & Obligations, (c) Completeness, and (d) Valuation & Allocation. 2. Classes of Transaction: Auditor to assess risk affecting assertions of – (a)Occurrence, (b) Completeness, (c) Accuracy, (d) Cut-off and (e) Classification.	4
3	(a) Big and Small Ltd received a show cause notice in December 2014 from the Central Excise department intending to levy a sum of ₹ 25 Lakhs. The Company replied to the above Notice in January 2015 contending that it is not liable for the proposed levy. No further action was initiated by the Central Excise Department up to the finalization of the audit for the year ended on 31 st March 2015. As the Auditor of the Company, how would you deal with this matter in your Report?	Refer Q.No. 82 Page 5.32 of This Book Refer Q.No.5 Page 29.2 of AS Book Same as M 11 Hint: Conditions relating to recognition of Provision under AS–29 are not satisfied. Hence no need to report the same. (See CARO Hint answer at the end) Note: CARO applicable only upto FY ending 31.03.2014. Hence, not considered relevant under Companies Act, 2013 , for May 2015 Exams.	3
	(b) The Auditor's Report of ABC Ltd for the year 2013–14 contained a qualification regarding non-provision of Doubtful Debts. As the Statutory Auditor of the Company for the year 2014–15, how would you report, if – (i) The Company does not make Provision for Doubtful Debts in 2014–15? (ii) The Company makes adequate Provision for Doubtful Debts in 2014–15?	Refer: Q. No. 5, Page 94 of SA Book. Hint: As per SA–510, Qualified or Adverse Opinion is required in Situation (i), and not in Situation (ii), in the above case.	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?	Refer: Q. No.54, Page 20.34 of This Book. Hint: Auditor to send a written communication to the BOD, giving reasons. A copy of such communication shall be sent to ICAI . Incoming Auditor, before accepting appointment, should obtain a copy of such communication, and consider the same before accepting the appointment.	5

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	(d) Discuss the Auditor's responsibility to provide access to his audit working papers to Regulators and Third Parties.	Refer: Point 3, Pg 26 SA–230 SA Book & Q. No. 67, Pg 20.43 of This Book. Hint: Permissible in case of Regulators, where there is a legal or professional duty to disclose. For Third Parties, Client's consent is specifically required.	3										
4	(a) A Private Limited Company reports the following position as on 31 st March, 2014: <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th></th> <th>₹</th> </tr> </thead> <tbody> <tr> <td>Paid up Capital</td> <td>35,00,000</td> </tr> <tr> <td>Revaluation Reserve</td> <td>12,00,000</td> </tr> <tr> <td>Capital Reserve</td> <td>10,00,000</td> </tr> <tr> <td>Profit & Loss (Dr.) Balance</td> <td>12,00,000</td> </tr> </tbody> </table> <p>The Management of the Company contends that CARO, 2003 is not applicable to it. Comment.</p>		₹	Paid up Capital	35,00,000	Revaluation Reserve	12,00,000	Capital Reserve	10,00,000	Profit & Loss (Dr.) Balance	12,00,000	Refer: Q. No. 29, Page 5.13 of This Book Same as M 10 (See CARO Hint answer at the end) Note: CARO applicable only upto FY ending 31.03.2014. Hence, not considered relevant under Companies Act, 2013 , for May 2015 Exams.	4
		₹											
Paid up Capital	35,00,000												
Revaluation Reserve	12,00,000												
Capital Reserve	10,00,000												
Profit & Loss (Dr.) Balance	12,00,000												
(b) You are appointed to compile Financial Statement of Z & Company (a Partnership Firm) for tax purposes. During the course of work, you learn that the Inventory is grossly understated. On pointing out the same, the Partners of Z & Co., tell you that it is outside your scope since you are not conducting an audit and the said figures duly certified by the Firm should be accepted. Comment.	Refer: Q. No. 70, Page 20.44 of This Book & Para 16,17,23 Page 255 of SA Book Same as M 97, M 99, N 00, M 13 Hint: As per SRS–4410 The Accountant should withdraw from the engagement in this case.	4											
	(c) C Ltd has defaulted in repayments of dues to a Financial Institution during the financial year 2013–14 and the same remained outstanding as at March 31, 2014. However, the Company settled the total outstanding dues including interest in April 2014 subsequent to the year end and before completing of the audit. Discuss how you would deal with this matter and draft a suitable Auditor's Report.	Refer: Q. No. 85, Page 5.33 of This Book Same as M 13 (See CARO Hint answer at the end) Note: CARO applicable only upto FY ending 31.03.2014. Hence, not considered relevant under Companies Act, 2013 , for May 2015 Exams.	4										
	(d) In the course of your audit you have come across a Related Party Transaction which prima facie appears to be biased. How would you deal with this?	Refer: Q. No. 49 & 58, Page 5.20 & 5.24 of This Book. (See CARO Hint answer at the end) Hint: Auditor to consider SA–550, AS–18, 143(1)(b) and Register u/s 189.	4										
5	(a) XYZ Ltd pays ₹ 90,000 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 ₹ 15,000. 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?	Refer: Q. No.14, Page 9.7 of This Book. Hint: Inadmissible Expenses u/s 40A(3). Auditor to report under Clause 21(d) of Form 3CD.	4										
	(b) ABC & Co., Chartered Accountants are the Auditors of Just Care General Insurance Company Limited. As on March 31 st 2014 the Management made a provision for Claims Outstanding. Enumerate the steps to be taken by the Auditor while verifying the "Claims Provision".	Refer: Q. No. 14, Page 9.7 of This Book. Same as N 09	6										
	(c) Compare and Explain the following: (i) Reporting to Shareholders vs Reporting to Those Charged with Governance (ii) Audit Qualification vs Emphasis of Matter	(i) Refer Principles of SA 700 and SA 260 (ii) Refer Principles of SA 705 and SA 706 of SA Book and This Book.	3 + 3										

Qn	Questions	Reference/Hint Answer	Marks
6	(a) A Firm of Chartered Accountants was appointed by a Company to evaluate the costs of the various products manufactured by it for their information system. One of the Partners of the Firm of Chartered Accountants was a Non-Executive Director of the Company. Comment.	Refer: Illustration in Page 20.48 of This Book. Same as N 01 N 04 N 10 Hint: No Expression of Opinion. Not guilty of Professional Misconduct – Clause (4) of Part I of Second Schedule.	3
	(b) Mr. Z, a CA, was invited by the Chamber of Commerce to present a paper in a symposium on the issues facing Indian Textile Industry. During the course of his presentation he shared some vital information of his client's business under the impression that it will help the Nation to compete with other countries at the international level. Comment.	Refer: Q. No. 68, Page 20.48 of This Book. Same as M 04 Hint: Guilty of Professional Misconduct – Clause (1) of Part I of Second Schedule	4
	(c) M/s ABC, a Firm of CAs, received ₹ 2 Lakhs in March, 2014 from a Client to pay the Advance Tax. However, the Firm has used that money for its own purpose and later on adjusted the same with the O/s Fee Payable. Comment.	Refer: Illustration in Page 20.59 of This Book. Same as M 10 Hint: Guilty of Professional Misconduct – Clause (10) of Part I of Second Schedule	4
	(d) M/s. XYZ, a Firm of Chartered Accountants has taken a Loan for acquiring a home from a Company whose Managing Director's son is an Articled Assistant with A, a Partner of M/s. XYZ the Articled Assistant had no direct interest in the Company and the Loan was not related to his engagement. Comment.	Refer: Q. No. 90, Page 20.61 of This Book. Similar to N 97 Hint: If the Articled Clerk has already been engaged and his engagement is not related to the loan transaction, Regulation 47 will not be attracted. Otherwise, guilty of Professional Misconduct – Clause (1) of Part II of Second Schedule.	4
7	Write short notes on the following – (a) Market Wide Circuit Breaker (MWCB)	Refer: Q. No. 16, Page 11.7 of This Book. Same as N 07 N 10 N 12	4
	(b) Restriction on Shareholding in a Co-Operative Society	Q. No. 8, Page 12.6 of This Book. Same as M 04 M 09	4
	(c) Importance of KYC requirements for a Chartered Accountant's practice	Refer SA Book Hint: Refer Provisions of SA 250, SA 300, SA 315, relating to the Importance of Knowledge about Clients' Business in Understanding the Entity and its Environment including its Internal Control	4
	(d) Intangible Asset vs. Intangible Item.	Refer: Q. No. 25, Pg. 10.7 of AS Book	4
	(e) Cost Audit.	Refer: Q. No. 1, Page 7.1 of This Book	4

Hint Answers for CARO related Questions

Q.No.3(a): Hint: There is a mere Show Cause Notice and reply for the Same. No Demand made by the Department. Auditor need not report the same under CARO Clause (ix).

Q.No.4(a): Hint: P&L (Dr) can be deducted only from Revenue Reserves. Total of Paid Up Capital and Reserves = 30 + 10 + 11 = ₹ 57 Lakhs. CARO is applicable.

Q.No.4(c): Hint: Reporting under CARO Clause (xi) required.

Q.No.4(d): Hint: Duties under CARO Clause (iii)(a) and (v)(b) are applicable in this case.