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Question Paper	
ADV. Audit & Professional Ethics	Duration: 75
Details: Test – 2	Marks: 40

Instructions:

- All the questions are compulsory
- Properly mention test number and page number on your answer sheet, Try to upload sheets in arranged manner.
- In case of multiple choice questions, mention option number only Working notes are compulsory wherever required in support of your solution
- Do not copy any solution from any material. Attempt as much as you know to fairly judge your performance.

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TEST-2 CH-1, 4, 7, 15

SA- 200, 210, 220, 230, 240, 250, 260, 265, 299

Q-1 Mr. Ibrahim was appointed as statutory auditor of New Limited and Old Limited. Both the Companies were having their base in Chennai they had recently listed their shares on the Stock Exchange. For the financial year 2020-21, Mr. Ibrahim had signed limited review reports for each quarter, till the quarter ended 31st December 2020 for both the companies. Owing to his personal commitments and increased workload, he tendered his resignation to M/s New Limited for the remaining quarter and the FY 2020 -21 as a whole. But the management of the Company did not accept the same.

Mr. Ibrahim continued to as act as auditor for M/s Old limited. During the 1st week of March 2021, Mrs. W (wife of Mr. Ibrahim) had borrowed a sum of Rs. 6lakh from the Company for her personal use. Having come to know about this, Mr. Ibrahim immediately informed the management that he had been disqualified to act as auditor and told them that he won 't issue audit report for last quarter. But management of the Company argued that it's the legal responsibility of Mr. Ibrahim to do the same.

Whether contention of management of New Limited and Old Limited is justified in asking Mr. Ibrahim to issue audit report for the last quarter and the FY 2020-21 as a whole, despite his resignation? Discuss.

(6 marks)

Q-2 Identify the controls which are automated, manual or IT dependent manual for the below mentioned cases?

(i) Price master configured in the sales master can only be edited by authorized personnel in the system.

(ii) Invoice cannot be booked in SAP in case Purchase orders are not approved

(iii) Inventory ageing report is pulled out from the system based on which provisioning is calculated after analyzing the future demand by the inventory personnel and approved by the controller.

(iv) All invoices are signed by warehouse personnel before the goods are dispatched to the customer.

(v) Credit limit is assigned to the customer and goods cannot be sold in excess of credit limit configured in the system.

(vi) All changes to the credit limit is approved manually by sales manager.

(vii) Ageing report is pulled out from SAP based on which provisioning is calculated by accounting personnel and approved by financial controller.

(viii) PO, GRN (Good received note) and invoice are matched by the system before it is posted in the financial records.

(6 Marks)

Q-3 ABC Ltd. is engaged in manufacturing of Yarns and Towels. It sells its product in both domestic as well as in International Market. It has achieved turnover of 200 crores in the F.Y. 2021 -22. Directors of the company realized that they are not managing the company professionally and thereby request your firm of Internal Auditors for appraisal of its organizational structure to ascertain whether it is in harmony with the objectives of ABC (P) Ltd.
Comment

(5 marks)

Q-4 XYZ Yarns Ltd. is a manufacturing company engaged in manufacturing of different types of yarns. Its annual turnover is Rs. 100 Crores and net profit Rs. 10 crores. It has two manufacturing units. Company is facing difficulties in maintaining adequate system of internal control. Company wants to appoint Internal Auditor who would help in the above task and also various other functions including compliance. In view of above, you are required to explain the main responsibility of Internal Auditors.

(4 marks)

Q-5 “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)

Q-6 KRP Ltd., at its annual general meeting, appointed Mr. X, Mr. Y and Mr. Z as joint auditors to conduct auditing for the financial year 2020-21. For the valuation of gratuity scheme of the company, Mr. X, Mr. Y and Mr. Z wanted to refer their own known Actuaries. Due to difference of opinion, all the joint auditors consulted their respective Actuaries. Subsequently, major difference was found in the actuary reports. However, Mr. X agreed to Mr. Y's actuary report, though, Mr. Z did not. Mr. X contends that Mr. Y's actuary report shall be considered in audit report due to majority of votes. Now, Mr. Z is in dilemma.

You are required to briefly explain the responsibilities of auditors when they are jointly and severally responsible in respect of audit conducted by them and also guide Mr. Z in such situation.

(5 marks)

Q-7 Case Study Based MCQ

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.

(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.

(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. 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.

(2*3= 6 Marks)

4. GENERAL MCQs:-

i. You have only eight working hours for raw material inventory verification. Based on your observation during these eight hours, you have to form an opinion with respect to the correctness of inventory value calculated by the management. The company uses ERP system for updating and recording raw material inventory. The ERP system of the company has passed all the ITGC checks and inventory rates are calculated by ERP on moving average price (MAP) basis. The company has done ABC analysis of all raw material inventory items and has vast number of items in each category. You will form your opinion based on.

(a.) Based on ABC analysis, check physical inventory of all “A” class items during allotted time and matching it with ERP stock.

(b.) Understand the process of recording of inventory in ERP to ascertain potential weaknesses and checking physical inventory of mostly “A” class items, some “B” class items and some “C” class items.

(c.) Check physical inventory of “A” class items as much as possible along with certain “B” class items and certain “C” class items on sample basis in value wise descending order, compare the physical stock with ERP system, and tabulate the result. The exercise should be continued till the end of allotted eight hours.

(d.) Check physical stock of only those items, which have standard packaging so that verification is faster considering the eight hour time limit.

ii. AJ Private Ltd is in the business of construction and infrastructure having an annual turnover of INR 1,100 crore. The operations of the company are run efficiently driven by the well laid out policies and procedures. The processes of the company are very strong and are well documented and properly communicated to its employees, as required. The management had also done a detailed risk assessment in the earlier years and currently the risk management

system of the company is considered to be very effective. The internal controls include both automated and manual.

During the course of the audit of the financial statements of the company for the financial year ended 31 March 2020, the statutory auditors did their risk assessment and also reviewed the general IT controls which were found to be effective.

Considering the same, one of the senior audit team members asked the team to start performing the substantive audit procedures taking the approach that controls are effective. However, the audit team did not find this approach correct and discussed that they should also check the effectiveness of other manual and automated controls by testing them and then move on to substantive testing.

The audit team recently had a training on the internal controls and hence their understanding was different from the audit senior. This led to a conflicting situation between the audit senior and remaining audit team. In the given situation, please advise which of the following would be correct.

- (a) The audit senior is correct because general IT controls were found to be effective and hence no further work may be required on controls.
- (b) The view of the audit team looks fine because without testing of internal controls covering all types of controls (manual and automated), those controls cannot be said to be operating effectively.
- (c) The audit senior seems reasonable in his approach because general IT controls were found to be effective. However, it would be more appropriate to also test application controls before concluding on the effectiveness of the controls.
- (d) The argument of the audit team looks better because every audit requires significant time to be spent on testing of internal controls and by only covering general IT controls; it would be difficult to justify this requirement later on in the audit file.

iii. XYZ Ltd. is a Public Limited Company engaged in the manufacturing of TMT Bars. M/s. UV & Associates are the statutory auditors of XYZ Ltd. for the Financial Year 2019-20. The company is listed on National Stock Exchange. CA Udhav, the engagement partner is considering the requirements with respect to Regulation 27 and Schedule II (LODR) for corporate governance compliance of XYZ Ltd. Which of the following is correct in this regard?

(a) XYZ Ltd. shall submit a quarterly compliance report on corporate governance in the format as specified by its Board from time to time to NSE within 21 days from the end of each quarter. The report shall be signed either by the Compliance Officer or the Chief Executive Officer of XYZ Ltd.

(b) XYZ Ltd. shall submit a monthly compliance report on corporate governance in the format as specified by its Board from time to time to NSE within 15 days from the end of the month. The report shall be signed either by the General Manager of the accounts department of XYZ Ltd.

(c) XYZ Ltd. shall submit a quarterly compliance report on corporate governance in the format as specified by its Board from time to time to NSE within 30 days from the close of quarter. The report shall be signed either by the Compliance Officer or the Chief Executive Officer of XYZ Ltd.

(d) XYZ Ltd. shall submit the annual compliance report on corporate governance in the format as specified by its Board from time to time to NSE within 30 days from the year end. The report shall be signed either by the General Manager of the Accounts Department of the Company.

iv. As per Regulation 20 and Part D of Schedule II of SEBI (LODR) Regulations, 2015, who among the following shall be appointed as Chairman of Stakeholder Relationship Committee?

(a) Small Shareholder Director

(b) Whole time director

(c) Any of the Executive Director

(d) Any of the Non-Executive Director

(1×4 = 4 Marks)

