

Roll No.

FINAL

Total No. of Questions – 7

GROUP-I PAPER-3

Total No. of Printed Pages – 8

Time Allowed – 3 Hours

**ADVANCED AUDITING AND
PROFESSIONAL ETHICS**

Maximum Marks – 100

GCE

Answers to questions are to be given only in English except in the case of candidates who have opted for Hindi Medium. If a candidate has not opted for Hindi medium, his/her answers in Hindi will not be valued.

Question No. 1 is compulsory.

Candidates are also required to answer any five from the remaining six questions.

Marks

1. (a) X Limited, a newly incorporated company in India commenced its business from April 1, 2012. The Company purchased fixed assets costing ₹ 4,000 lakhs on 01-04-2012 and the same was fully financed by foreign currency loan (U.S. Dollars) payable in three annual equal installments. Exchange rates were 1 Dollar = ₹ 40.00 and ₹ 42.50 as on 01-04-2012 and 31-03-2013 respectively. The company worked out foreign exchange loss as per AS 11 at ₹ 250 Lakhs and expensed the entire amount in the profit and loss account. The Managing Director of the company was worried about this heavy revenue loss and asked the accountant not to follow AS 11 issued by the ICAI for this particular transaction. The Accountant of the company, followed the instruction of the Managing Director and removed exchange loss from the profit and loss account but then he added the entire exchange loss to the value of fixed asset and computed the depreciation thereon. As an Auditor of X Limited how you would deal with this particular transaction ?

GCE**P.T.O.**

- (b) 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.
- (c) Beta Limited, is a company registered with SEBI, having five subsidiaries. M/s XYZ, Chartered Accountants, have been appointed as Statutory Auditors for the audit of the Consolidated Financial Statements for the year ending March 31, 2013. Out of five subsidiaries, the audit of one subsidiary was conducted by another auditor, M/s Badnam and Company, Chartered Accountants. The "Opinion" para of audit report furnished by M/s XYZ Chartered Accountants is given below :

Opinion

In our opinion and to the best of our information and according to the explanations given to us the consolidated financial statements give a true and fair view, except the financial statement of one subsidiary whose accounts were audited by M/s Badnam and Company, Chartered Accountants and about the same we are not in a position to express our opinion as the audit has not been performed by us :

- (i) in the case of the consolidated Balance Sheet, of the state of affairs of the Company as at March 31, 2013.
- (ii) in the case of the consolidated Profit and Loss Account, of the profit/loss for the year ended on that date.

Do you find any deficiencies in the opinion para ? If yes, you are required to give your suggestions and redraft the opinion para.

- (d) M/s Honest Limited has entered into a transaction on 5th March, 2013, near year-end, whereby it has agreed to pay ₹ 5 lakhs per month to Mr. Y as annual retainer-ship fee for "engineering consultation". No amount was actually paid, but ₹ 60 lakhs is provided in books of account as on March 31, 2013. 5
- Your inquiry elicits a response that need-based consultation was obtained round the year, but there is no documentary or other evidence of receipt of the service. As the auditor of M/s Honest Limited, what would be your approach ?
2. (a) Mr. X who passed his CA examination of ICAI on 18th July, 2013 and started his practice from August 15, 2013. On 16th August 2013, one female candidate approached him for articleship. In addition to monthly stipend, Mr. X also offered her 1% profits of his CA firm. She agreed to take both 1% profits of the CA firm and stipend as per the rate prescribed by the ICAI. The Institute of Chartered Accountants of India sent a letter to Mr. X objecting the payment of 1% profits. Mr. X replies to the ICAI stating that he is paying 1% profits of his firm over and above the stipend to help the articled clerk as the financial position of the articled clerk is very weak. Is Mr. X Liable to professional misconduct ? 4
- (b) Mr. Honest, a Chartered Accountant in practice, wrote two letters to M/s XY Chartered Accountants a firm of CAs; requesting them to allot him some professional work. As he did not have a significant practice or clients he also wrote a letter to M/s ABC, a firm of Chartered Accountants for securing professional work. Mr. Clever, an another CA, informed ICAI regarding Mr. Honest's approach to secure the professional work. Is Mr. Honest wrong in soliciting professional work ? 4

(4)

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Marks

- (c) C & Co., hired Mr. A, Chartered Accountant, to compile its financial statements for the interim period ending on 31st December 2012. Kindly assist Mr. A in drafting scope of engagement letter with specific focus on C & Co's responsibility.
- (d) 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.
3. (a) Excellent Limited, a Company incorporated in India and listed with SEBI, has a scheme for payment of settlement allowance to retiring employees. Under the scheme, retiring employees are entitled to reimbursement of certain travel expenses for class they are entitled to as per company rules and regulations. Employees are also entitled to claim a lump-sum payment to cover expenses on food and stay during the travel. The Company also gives option to employees that they can claim a lump-sum amount equal to three months pay last drawn.
- Excellent Limited have following accounting policies to record these travel expenses :
- (i) Settlement allowance does not depend upon the length of service of employee. It is restricted to employee's eligibility under the travel rule of the company therefore all travel expenses fall under the category of defined contribution plans.

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- (ii) Since it is not related to the length of service of the employees, it is difficult to estimate reliably and there is no present obligation to pay employees as per AS 29 "Provisions, Contingent Liabilities and Contingent Assets", hence it is accounted for on claim basis.

You are statutory auditor of Excellent Limited. What would be your guidance to audit team ?

- (b) Q Ltd. operates in an ERP environment. Its auditor requires your assistance on the aspects that are needed to be looked into in respect of control over input and output of transactions. Kindly help him. 4
- (c) In the audit of Hotel Great Stay Ltd. its auditor wants to use the analytical procedure as substantive procedure in respect of room rental income as well as payroll costs. Guide him as to how it can be done. 4
- (d) C.A. Prabhu, is a leading income tax practitioner and consultant for derivative products. He resides in Mumbai near to the ABC commodity stock exchange and does trading in commodity derivatives. Every day, he invests nearly 50% of his time to settle the commodity transactions. Is C.A. Prabhu liable for professional misconduct ? 4
4. (a) H Limited, a company registered with SEBI, has three subsidiaries and one associate. While doing the audit of Consolidated Financial Statements (CFS) of H Limited you have come to know that the associate entity had made a provision for proposed dividend in its financial statements. H Limited computed its share of the results of operations of the associate after taking into account the proposed dividend. Comment. 4

(6)

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Marks

- (b) While doing the audit of a nationalized bank, your Audit Assistant informed you that there are a lot of irregularities in Telegraphic Transfers and Demand Drafts. What guidance would be give to the Audit Assistant ? 4
- (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
- (d) The Auditor of S Limited has just commenced the statutory audit. What should be considerations for the effectiveness of a system of internal check ? 4
5. (a) X Ltd is engaged in the business of newspaper and radio broadcasting. It operates through different brand names. During FY 12-13 it incurred substantial amounts on external trade, business communication and branding expenses by participation in various corporate social responsibility initiatives. The company expects to benefits by this expenditure by attracting new customers over a period of time and accordingly it has capitalized the same under brand development expenses and intends to amortize the same over the period in which it expects the benefits to flow. As the statutory auditor of the company do you concur ? Give reasons. 4

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- (b) M Limited is going to acquire S Limited. The purchase consideration has been decided at ₹ 4000 Crores. M Limited is worried about hidden liabilities or overvalued assets of S Limited and approached you to examine the same. List out eight important transactions/items which you would like to investigate in the Due Diligence exercise. 4
- (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, 1956. Kindly guide him. 4
- (d) X Ltd closed its manufacturing operations and sold all its manufacturing fixed assets during the financial year ended 31st March, 2013. However it intends continue its operations as a trading company. In respect of other fixed assets, the company carried out a physical verification as at the end of 31st March, 2013 and found a material discrepancy to the tune of ₹ 1 lac, which was written off and is disclosed separately in the profit and loss account. Kindly incorporate the above in your audit report. 4
6. (a) M Ltd. intends to intensify its advertisement strategy of hoarding advertisements to increase its sale during the impending festival season. You have been appointed as the special auditor to examine the expenditure under this head. What will be usual evidence you will look for in this case to justify the expenditure ? 4
- (b) Mr. Nigal, a Chartered Accountant in practice, delivered a speech in the national conference organized by the Ministry of Textiles. While delivering the speech, he told to the audience that he is a management expert and his firm provides services of taxation and audit at reasonable rates. He also requested the audience to approach his firm of chartered accountants for these services and at the request of audience he also distributed his business cards and telephone number of his firm to those in the audience. Comment. 4

- (c) Mr. A engaged in business as a sole proprietor presented the following information to you for the FY 12-13. Turnover made during the year ₹ 124 lacs. Goods returned in respect of sales made during FY 10-11 is ₹ 20 lacs not included in the above. Cash discount allowed to his customers ₹ 1 lac for prompt payment. Special rebate allowed to customer in the nature of trade discount ₹ 5 lacs. Kindly advise him whether he has to get his accounts audited u/s 44AB of the Income Tax Act, 1961. 4
- (d) Dishonest Limited, a company incorporated in India has six members in its Audit Committee. Due to recessionary conditions in India the revenue of the company is going down and there is slow down in other activities of the company. Therefore, it was expected that there would not be significant work for members of the Audit Committee. Considering the overall recession in the company and the economy, the members of the Committee decided unanimously to meet once in a year only on March 31, 2013. They reviewed monthly information system of the Company and found no errors. As an auditor of Dishonest Limited would you consider the decision taken by the Audit Committee is in line with the Clause 49 of the (SEBI) Listing Agreement ? 4

7. Write short notes on any four of the following :

- (a) Scope of peer review 4
- (b) Cost records in respect of by products 4
- (c) Content of Management Discussion and Analysis 4
- (d) Aspects to be covered in the books of accounts to be maintained by a multi-state co-operative society. 4
- (e) Environment Impact Assessment 4