

**PAPER – 3 : ADVANCED AUDITING AND PROFESSIONAL ETHICS**

**PART – I ACADEMIC UPDATE**

**RELEVANT AMENDMENTS FOR NOVEMBER 2022 EXAMINATION**

**(Legislative Amendments / Notifications / Circulars / Rules / Guidelines issued by  
Regulating Authority)**

**Chapter 7 Audit Committee and Corporate Governance (SEBI (LODR) Regulations, 2015)**

1. Insertion of word At least before two-thirds in point no. 1. The Audit Committee shall have minimum three directors as members. **At least** two-thirds of the members of audit committee shall be independent directors, however, in case of a listed entity having outstanding SR (Superior Rights) equity shares, the audit committee shall only comprise of independent directors. **(Refer para 4.1 Qualified and Independent Audit Committee [Regulation 18(1)]– Page no.7.4).**
2. Deletion of information on **Statement of significant related party transactions (as defined by the Audit Committee), submitted by management under** mandatorily review by Audit Committee as per Part C(B) OF Schedule II. **(Refer para 7 Review of Information by Audit Committee on Page no.7.13)**
3. Deletion of point no. (iv) The auditor shall ensure that the Chairperson of the board of the top 500 listed entities is - (a) a non-executive director; (b) not related to the Managing Director or the Chief Executive Officer as per the definition of the term “relative” defined under the Companies Act, 2013. It may be noted that this provision shall not be applicable to the listed entities which do not have any identifiable promoters as per the shareholding pattern filed with stock exchanges. It may also be noted that the top 500 entities shall be determined on the basis of market capitalisation, as at the end of the immediate previous financial year. **(Refer Para 8.5 Verification regarding Composition of Board [Regulation 17 & 17A on Page no. 7.16])**
- 3.1. Insertion in Para 8.5 Verification regarding Composition of Board i.e., Regulations 17:
  - The listed entity shall ensure that approval of shareholders for appointment of a person on the Board of Directors [or as a manager] is taken at the next general meeting or within a time period of three months from the date of appointment, whichever is earlier.
  - Provided that the appointment or a re-appointment of a person, including as a managing director or a whole-time director or a manager, who was earlier rejected by the shareholders at a general meeting, shall be done only with the prior approval of the shareholders:
  - Provided further that the statement referred to under sub-section (1) of section 102 of the Companies Act, 2013, annexed to the notice to the shareholders, for considering the appointment or re-appointment of such a person earlier rejected by the shareholders shall contain a detailed explanation and justification by the Nomination and Remuneration

Committee and the Board of directors for recommending such a person for appointment or re-appointment. (Refer Para 8.5 Verification regarding Composition of Board [Regulation 17 & 17A on Page no. 7.17])

4. Meaning of Independent Director given on Page no. 7.18 to be read as: Independent director" means a non-executive director, other than a nominee director of the listed entity:
- (i) who, in the opinion of the board of directors, is a person of integrity and possesses relevant expertise and experience;
  - (ii) who is or was not a promoter of the listed entity or its holding, subsidiary or associate company [or member of the promoter group of the listed entity];
  - (iii) who is not related to promoters or directors in the listed entity, its holding, subsidiary or associate company;
  - (iv) who, apart from receiving director's remuneration, has or had no material pecuniary relationship with the listed entity, its holding, subsidiary or associate company, or their promoters, or directors, during the **three** immediately preceding financial years or during the current financial year;
  - (v) none of whose relatives— (A) is holding securities of or interest in the listed entity, its holding, subsidiary or associate company during the three immediately preceding financial years or during the current financial year of face value in excess of fifty lakh rupees or two percent of the paid-up capital of the listed entity, its holding, subsidiary or associate company, respectively, or such higher sum as may be specified; (B) is indebted to the listed entity, its holding, subsidiary or associate company or their promoters or directors, in excess of such amount as may be specified during the three immediately preceding financial years or during the current financial year; (C) has given a guarantee or provided any security in connection with the indebtedness of any third person to the listed entity, its holding, subsidiary or associate company or their promoters or directors, for such amount as may be specified during the three immediately preceding financial years or during the current financial year; or (D) has any other pecuniary transaction or relationship with the listed entity, its holding, subsidiary or associate company amounting to two percent or more of its gross turnover or total income: Provided that the pecuniary relationship or transaction with the listed entity, its holding, subsidiary or associate company or their promoters, or directors in relation to points (A) to (D) above shall not exceed two percent of its gross turnover or total income or fifty lakh rupees or such higher amount as may be specified from time to time, whichever is lower.]
  - (vi) who, neither himself /herself, nor whose relative(s) — (A) holds or has held the position of a key managerial personnel or is or has been an employee of the listed entity or its holding, subsidiary or associate company or any company belonging to the promoter group of the listed entity, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed: Provided that

in case of a relative, who is an employee other than key managerial personnel, the restriction under this clause shall not apply for his / her employment. (B) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of — (1) a firm of auditors or company secretaries in practice or cost auditors of the listed entity or its holding, subsidiary or associate company; or (2) any legal or a consulting firm that has or had any transaction with the listed entity, its holding, subsidiary or associate company amounting to ten per cent or more of the gross turnover of such firm; (C) holds together with his relatives two per cent or more of the total voting power of the listed entity; or (D) is a chief executive or director, by whatever name called, of any nonprofit organisation that receives twenty-five per cent or more of its receipts or corpus from the listed entity, any of its promoters, directors or its holding, subsidiary or associate company or that holds two per cent or more of the total voting power of the listed entity; (E) is a material supplier, service provider or customer or a lessor or lessee of the listed entity;

(vii) who is not less than 21 years of age.

(viii) who is not a non-independent director of another company on the board of which any non-independent director of the listed entity is an independent director.

**(Refer Page no.7.18 )**

5. Deletion of word “the immediate next Board meeting or” and “whichever is later” in Regulation 25(6) i.e., sub-point no (ix) An independent director who resigns or is removed from the Board of Directors of the listed entity shall be replaced by a new independent director at the earliest but not later than three months from the date of such vacancy. **(Refer para 10 Obligations With respect to employees including Senior management, key managerial persons, directors and promoters on Page no. 7.22)**
6. The Board of Directors of every listed public company shall constitute the Nomination and Remuneration Committee which shall comprise of at least three directors, all of whom shall be non-executive directors and at least **two-thirds** shall be independent directors. Deletion of condition i.e., in case of a listed entity having outstanding SR equity shares, two thirds of the committee shall comprise of independent directors. Chairperson of the committee shall be an independent director. **(Refer Para 14 Nomination and Remuneration Committee- Regulation 19 and Part D of Schedule II, on Page No. 7.26)**
- 6.1 Insertion in the role of the Nomination and Remuneration Committee :(1A). For every appointment of an independent director, the Nomination and Remuneration Committee shall evaluate the balance of skills, knowledge and experience on the Board and on the basis of such evaluation, prepare a description of the role and capabilities required of an independent director. The person recommended to the Board for appointment as an independent director shall have the capabilities identified in such description. For the purpose of identifying suitable candidates, the Committee may: a. use the services of an external agencies, if required; b. consider candidates from a wide range of backgrounds,

having due regard to diversity; and c. consider the time commitments of the candidates.  
**(Refer Para 14 Nomination and Remuneration Committee- Regulation 19 and Part D of Schedule II, on Page No. 7.27)**

7. The provisions of regulation 21 shall be applicable to:(i). the top 1000 listed entities, determined on the basis of market capitalization as at the end of the immediate preceding financial year; and, (ii). a 'high value debt listed entity'.
- 7.1 The role of the Risk Management Committee committee shall, inter alia, include the following:
  - (1) To formulate a detailed risk management policy which shall include: (a) A framework for identification of internal and external risks specifically faced by the listed entity, in particular including financial, operational, sectoral, sustainability (particularly, ESG related risks), information, cyber security risks or any other risk as may be determined by the Committee. (b) Measures for risk mitigation including systems and processes for internal control of identified risks. (c) Business continuity plan.
  - (2) To ensure that appropriate methodology, processes and systems are in place to monitor and evaluate risks associated with the business of the Company;
  - (3) To monitor and oversee implementation of the risk management policy, including evaluating the adequacy of risk management systems;
  - (4) To periodically review the risk management policy, at least once in two years, including by considering the changing industry dynamics and evolving complexity;
  - (5) To keep the board of directors informed about the nature and content of its discussions, recommendations and actions to be taken;
  - (6) The appointment, removal and terms of remuneration of the Chief Risk Officer (if any) shall be subject to review by the Risk Management Committee. The Risk Management Committee shall coordinate its activities with other committees, in instances where there is any overlap with activities of such committees, as per the framework laid down by the board of directors.]

**(Refer Para 16 Risk Management Committee- Regulation 21 and Part D of Schedule II, on Page No. 7.29)**

8. **Para 18 Information to Shareholders [Regulation 36] to be read as:** (1) The listed entity shall send the annual report in the following manner to the shareholders: (a) Soft copies of full annual report to all those shareholder(s) who have registered their email address(es) either with the listed entity or with any depository; (b) Hard copy of statement containing the salient features of all the documents, as prescribed in Section 136 of Companies Act, 2013 or rules made thereunder to those shareholder(s) who have not so registered; (c) Hard copies of full annual reports to those shareholders, who request for the same.

- (2) The listed entity shall send annual report referred to in sub-regulation (1), to the holders of securities, not less than twenty-one days before the annual general meeting.
- (3) In case of the appointment of a new director or re-appointment of a director the shareholders must be provided with the following information: (a) a brief resume of the director; (b) nature of expertise in specific functional areas; (c) disclosure of relationships between directors inter-se; (d) names of listed entities in which the person also holds the directorship and the membership of Committees of the board along with listed entities from which the person has resigned in the past three years; and (e) shareholding of non-executive directors in the listed entity, including shareholding as a beneficial owner; (f) In case of independent directors, the skills and capabilities required for the role and the manner in which the proposed person meets such requirements.

The auditor should ascertain from the communications sent, whether in the case of appointment of a new director or re-appointment of a director, the shareholders have been provided with the information stipulated above. **(Refer Para 18 Information to Shareholders [Regulation 36] on Page no. 7.30)**

9. The listed entity shall submit a quarterly compliance report on corporate governance in the format as specified by the Board from time to time to the recognised stock exchange(s) within twenty one (21) days from the end of each quarter.

The listed entity is also required to formulate a policy on materiality of related party transactions and on dealing with related party transactions. This policy should also include clear threshold limits duly approved by the board of directors. Further, such policy shall be reviewed by the board of directors at least once every three years and updated accordingly. A related party transaction shall be considered material, if the transaction(s) to be entered into individually or taken together with previous transactions during a financial year, exceeds rupees one thousand crore or ten per cent of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity, whichever is lower. **[Regulation 23(1)]**

All related party transactions and subsequent material modifications shall require prior approval of the independent directors in audit committee of the listed entity **[Regulation 23(2)]**

Audit committee may grant omnibus approval for related party transactions proposed to be entered into by the listed entity subject certain conditions **[Regulation 23(3)]**.

The listed entity shall submit to the stock exchanges disclosures of related party transactions in the format as specified by the Board from time to time, and publish the same on its website **[Regulation 23(8)]**.

Provided that a 'high value debt listed entity' shall submit such disclosures along with its standalone financial results for the half year.

Provided further that the listed entity shall make such disclosures every six months within fifteen days from the date of publication of its standalone and consolidated financial results .

Provided further that the listed entity shall make such disclosures every six months on the date of publication of its standalone and consolidated financial results with effect from April 1, 2023. **(Refer Para 22.3 Related Party Disclosures given on Page no. 7.35)**

9.1 As per Schedule V - Annual Report, the annual report shall contain the following additional disclosures relating to Related Party:

1. The listed entity which has listed its non-convertible securities] shall make disclosures in compliance with the Accounting Standard on “Related Party Disclosures”.
2. The disclosure requirements shall be as follows:

Sr. no.	In the accounts of	Disclosures of amounts at the year end and the maximum amount of loans/ advances/ Investments outstanding during the year.
1.	Holding Company	<ul style="list-style-type: none"> <li>• Loans and advances in the nature of loans to subsidiaries by name and amount.</li> <li>• Loans and advances in the nature of loans to associates by name and amount.</li> <li>• Loans and advances in the nature of loans to firms/companies in which directors are interested by name and amount.</li> </ul>
2.	Subsidiary	Same disclosures as applicable to the parent company in the accounts of subsidiary company.
3.	Holding Company	Investments by the loanee in the shares of parent company and subsidiary company, when the company has made a loan or advance in the nature of loan.

For the purpose of above disclosures directors' interest shall have the same meaning as given in Section 184 of Companies Act, 2013.

(2A) Disclosures of transactions of the listed entity with any person or entity belonging to the promoter/promoter group which hold(s) 10% or more shareholding in the listed entity, in the format prescribed in the relevant accounting standards for annual results.

3. The above disclosures shall not be applicable to listed banks.

**(Refer Para 22.3 Related Party Disclosures given on Page no. 7.35)**

**Note:** Students are also advised to refer RTP of Paper 1 Financial Reporting (for AS, Ind AS and other updates) and Paper 4 Part A -Corporate Laws (for academic updates relating to Company Law).

## PART – II : QUESTIONS AND ANSWERS

## QUESTIONS

## PART A: MULTIPLE CHOICE QUESTIONS

## Integrated Case Scenario 1.

Mr. K is a practicing-chartered accountant and also member of CPA Ireland. He handles only GST related work and tax audits for clients. Currently, he is having 19 companies for which he is handling the tax audit. At the beginning of the current Financial Year, he was approached by 40 new clients for tax audit assignments. He was reluctant to accept all the work as he feared breaching the permissible limit of handling clients. After consulting several friends of his, he finally decided to accept the work of just 2 big clients who approached him.

Mr. J, (K's friend) a chartered accountant in practice and a member empanelled as insolvency professional was acting as the statutory auditor for a listed entity. The audit for the current Financial Year was completed but there was some difference of opinion between auditor and the management. As a result of this, the company did not send the notice for AGM to Mr. J. When enquired, it was said that the company is not obliged to send notices to the auditor and it's the responsibility of the auditor to be aware of the AGM. Having heard this, Mr. J went to his friend to clarify the above matter. As a result of this incident, the management had not paid a part of the agreed audit fees to Mr. J. In retaliation, Mr. J took lien over few documents pertaining to the company. Having come to know about this, Mr. K immediately informed his friend that his act would lead to professional misconduct.

Mr. K & his friend Mr. J decided to start a partnership firm. They completed all formalities and went ahead and printed their visiting card as follows:

M/s KJ & Associates	M/s KJ & Associates
Mr. K, Chartered Accountant, CPA Ireland Partner	Mr. J, Chartered Accountant, Insolvency Professional Partner
No.3, MMM Street, Delhi Phone: 9xxxxxxx0	No.3, MMM Street, Delhi Phone: 9xxxxxxx0

The firm had also received the following assignments:

- (i) Concurrent audit for T Bank Ltd.
- (ii) Statutory audit for BBT Bank Ltd. (it is to be noted that the bank was not sponsored by T Bank)
- (iii) Offer to act as settlor of ZZ Charitable Trust.

- (iv) Internal audit of PF Trust of Government Company Ltd.
- (v) Statutory Auditor of Government Company Ltd.

On the basis of the abovementioned facts, you are required to choose the most appropriate answer for the following MCQs:

**QUESTIONS:**

1. In the given case scenario, has Mr. K breached the maximum limit of clients. If yes, can he be held guilty of professional misconduct?
  - (a) Yes. The ceiling on number of tax audits which can be accepted by a chartered accountant is 20. In this given case, Mr. K is already having 19 clients and has now accepted 2 more ( $19+2=21$ ). Also, he shall be held guilty of professional misconduct as per the Chartered Accountants Act, 1949.
  - (b) Yes. The ceiling on number of tax audits which can be accepted by a chartered accountant is 20. In this given case, Mr. K is already having 19 clients and has now accepted 2 more ( $19+2=21$ ). However, this shall not be considered as guilty of professional misconduct as per the Chartered Accountants Act, 1949.
  - (c) No. In the above case, the maximum ceiling is 25 in number (as per the latest decision taken by the ICAI council). The assignments (existing + new) handled by Mr. K is well below the prescribed limit and hence there is no breach.
  - (d) No. In the above case, the maximum ceiling is 60 in number. The assignments (existing + new) handled by Mr. K is well below the prescribed limit and hence there is no breach.
2. Assuming yourself to be Mr. K, what would be your advice to Mr. J on the above matter?
  - (a) The company has not followed the provisions of section 146 of Companies Act, 2013. All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company. Also, as per section 147, the company shall be punishable with fine which shall not be less than ₹ 25,000/- but which may extend to ₹ 5 lakh.
  - (b) The company has not followed the provisions of section 146 of Companies Act, 2013. All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company. Also, as per section 147, the company shall be punishable with fine which shall not be less than ₹ 10,000/- but which may extend to ₹ 1 lakh.



- (c) The company has not followed the provisions of section 147 of Companies Act, 2013. All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company. However, the company shall not be punishable for this act.
  - (d) The argument of the management is right. The Companies Act, 2013 does not mandate that the company shall send the notices for its general meetings to the auditor. It is the responsibility of the auditor (in this case Mr. J) to attend the AGM irrespective of getting the notice for it or not. The auditor shall be punishable under the provisions of the Act if he doesn't attend the AGM.
3. Will the retaliating act of Mr. J against the company make him guilty of professional misconduct?
- (a) No. The above act will not lead to professional misconduct. However, under section 147 of the Companies Act, 2013, Mr. J shall be punishable for exercising lien over the company's documents.
  - (b) No. The Chartered Accountants Act, 1949 is silent about the above situation and hence it will not lead to professional misconduct.
  - (c) Yes. As per the recent decision of Ethical Standards Board, a chartered accountant cannot exercise lien over client documents/ records for non-payment of his fees.
  - (d) Yes. As per Clause 7 of Part I of Second Schedule of Chartered Accountants Act, 1949, the above act of Mr. J will make him guilty of professional misconduct.
4. In the given case scenario, visiting cards printed by Mr. K & Mr. J, is there anything which may lead to professional misconduct? If so, under what provisions?
- (a) Mentioning 'CPA Ireland' & the term 'Insolvency Professional' by Mr. K & Mr. J respectively violates the provisions of clause 7 of part I of First schedule of the Chartered Accountants Act, 1949. Hence, both of them shall be held guilty of professional misconduct.
  - (b) There is no information contained in both the visiting cards, which leads to professional misconduct. All details mentioned are abiding the provisions of clause 7 of part I of First schedule of the Chartered Accountants Act, 1949.
  - (c) Mentioning 'CPA Ireland' by Mr. K violates the provisions of clause 6 & clause 7 of part I of First schedule of the Chartered Accountants Act, 1949. Hence, Mr. K shall be held guilty of professional misconduct. However, as far as Mr. J's card is concerned, nothing mentioned in it is against the provision of Chartered Accountants Act, 1949, so he shall not be held guilty of professional misconduct.

- (d) Mentioning the term 'Insolvency Professional' by Mr. J violates the provisions of clause 7 of part I of First schedule of the Chartered Accountants Act, 1949. Hence, he shall be held guilty of professional misconduct. However, as far as Mr. K's card is concerned, nothing mentioned in it is against the provision of Chartered Accountants Act, 1949, so he shall not be held guilty of professional misconduct
5. The firm had received the following assignments:
- (i) Concurrent audit for T Bank Ltd.
  - (ii) Statutory audit for BBT Bank Ltd. (it is to be noted that the bank was not sponsored by T Bank)
  - (iii) Offer to act as settlor of ZZ Charitable Trust.
  - (iv) Internal audit of PF Trust of Government Company Ltd.
  - (v) Statutory Auditor of Government Company Ltd.
- Among the above assignments, which assignments can be accepted by the firm?
- (a) Either (i) or (ii), (iii) & Either (iv) or (v)
  - (b) (i), (ii), (iii) & Either (iv) or (v)
  - (c) Either (i) or (ii) & Either (iv) or (v)
  - (d) (ii) only

**Independent MCQs**

6. Mr. B one of the partners of the firm is facing a dilemma as to whether the firm BMY LLP should accept the appointment as Statutory Auditors of M/s Foam Limited wherein Mr. B had sent a communication in writing addressed to the outgoing auditor Mr. Dalai under certificate of posting and the outgoing auditor has sent an acknowledgement vide their official email, but this email address of the outgoing auditor is not registered with the Institute of Chartered Accountants of India. Mr. B is of the opinion that this is not positive evidence of delivery and violates the provisions of Code of Ethics if the firm accepts the audit assignment.
- With respect to the dilemma being faced by Mr. B, partner of the firm regarding acknowledgment of the communication from the retiring auditor's vide their official email is not positive evidence of delivery?
- (a) The dilemma of Mr. B is correct as it is not positive evidence of delivery.
  - (b) The dilemma of Mr. B is not correct as it is positive evidence of delivery as the same is received from the official email of the outgoing auditor, as per the Code of Ethics.
  - (c) The dilemma of Mr. B is not correct as statutory auditors are not required to communicate with the retiring or outgoing auditors in this case.

- (d) The dilemma of Mr. B is correct as the email address of the outgoing auditor from which acknowledgement has come is not registered with the Institute of Chartered Accountants of India.
7. CA Z is appointed as a Statutory Auditor of JB Finance Limited (a Non-Banking Financial Company covered under Non-Banking Financial Company — Systematically important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016) for the year 2021-22. Following information is available with CA Z with respect to JB Finance Limited as at 31<sup>st</sup> March, 2022:

Particulars	₹ (in Lakh)
Standard Assets	700.00
Sub-standard Assets	200.00
Doubtful Assets (Secured and up-to one year)	10.00
Doubtful Assets (Secured and more than three years)	50.00

What will be the total provision required to be made in the books of JB Finance Limited for the year ended 31 March, 2022 for the above stated Assets?

- (a) ₹ 49.8 Lakh
- (b) ₹ 47 Lakh
- (c) ₹ 34.8 Lakh
- (d) ₹ 52.8 Lakh
8. While auditing with respect to compliance with CARO, 2020, Mr. Omprakash, for additional reporting purpose, observed the following, relevant to Para 3(vii) of CARO, 2020:

Statutory Dues	Undisputed Amount (₹ in lakh)	Date Payable	Date Paid
Provident Fund	1.5	24 <sup>th</sup> September, 2021	27 <sup>th</sup> March, 2022
GST	2.45	23 <sup>rd</sup> October, 2021	24 <sup>th</sup> April, 2022
Customs Duty	0.65	20 <sup>th</sup> September, 2021	10 <sup>th</sup> April, 2022
Income Tax Demand for A.Y. 2019-20	0.55	18 <sup>th</sup> October, 2021	Not Paid till date

Also, a representation was made to GST Department for waiving a penalty of ₹ 1 lakh for late payment of GST demand. What total amount of statutory dues need to be reported by Mr. Omprakash as per Para 3 of CARO?

- (a) ₹ 3.10 lakh.

- (b) ₹ 0.65 lakh.
  - (c) ₹ 3.65 lakh.
  - (d) ₹ 2.70 lakh.
9. With respect to audit of public sector undertaking, which among the below is related to propriety audit?
- (a) This audit is carried out by assessing whether activities, financial transactions and information comply in all material aspects, with the regulatory and other authorities which govern the audited entity.
  - (b) This auditing focuses on the areas in which it can add value which have the greatest potential for development. It provides constructive incentives for the responsible parties to take appropriate action.
  - (c) It is an audit under which the C&AG does not really cover again the field which has already been covered. He conducts an appraisal or an efficiency cum performance audit.
  - (d) It stands for verification of transactions on the tests of public interest, commonly accepted customs and standards of conduct. This audit is directed towards an examination of managements decisions in sales, purchases, contracts, etc.
10. In case of peer review, which among the following the review shall covered?
- (a) Compliance with legal regulations governing the firm
  - (b) Check whether the qualification of the articled assistants and other staffs are sufficient to be employed
  - (c) Compliance with tax regulations of the firm, which includes filing IT return of the firm, payment of tax, etc.
  - (d) Training program for staff concerned with assurance function, including availability of infrastructure

## PART B : DESCRIPTIVE QUESTIONS

### Standards on Auditing, Statements and Guidance Notes

11. Abhinandan Limited a chemical manufacturing company, having its factory located at Nanded Village, for the year 2021-22 appointed Subahu & Co. as their statutory auditors. During the course of the audit, Subahu & Co. identified that Abhinandan Limited received a show cause notice from National Green Tribunal based on the investigation performed by the regional forest department for violating environmental laws. Upon gathering a further understanding of the said matter, it was identified that Abhinandan Limited was dumping toxic solid waste, without treating it, on the nearby grounds, and because of this, the nearby water bodies were getting polluted. Based on the preliminary investigation performed by

the regional forest department under the directions of the National Green Tribunal, it was identified that these practices were carried out since 2009 and a lot of damage has been done to the environment by Abhinandan Limited. A show cause notice was already issued to Abhinandan Limited by the National Green Tribunal for levying the penalty of an amount of ₹ 500 crore. The unaudited profit for the financial year 2021-22 of Abhinandan Limited was ₹ 35 crore and the unaudited turnover was ₹ 100 crore. Upon inquiry it was identified that Abhinandan Limited has disclosed this matter in the financial statements by way of footnote, the extract of which is provided below:

*“The company has received a show cause notice from the National Green Tribunal for some potential violation of environmental laws and the company's legal department has assessed and found that the judgment would be in favour of the company. Accordingly, no provision has been created for such notices.”*

In the light of the above scenario kindly provide what should be the appropriate option for the statutory auditor of the company to report this matter.

12. Chintamani Ltd appoints Chintan & Mani as statutory auditors for the financial year 2021-2022. Chintan & Mani seem to have different opinions on Audit approach to be adopted for audit of Chintamani Ltd. Mani is of the opinion that 100% checking is not required and they can rely on Audit Sampling techniques in order to provide them a reasonable basis on which they can draw conclusions about the entire population.

Chintan is concerned that whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

You are required to guide Chintan about his role if audit sampling has not provided a reasonable basis for conclusions about the population that has been tested in accordance with SA 530,

### **Risk Assessment and Internal Control**

13. Arihant Limited was engaged in the business of owning and managing hotels and resorts, selling tourism packages and performing airline bookings for corporate and individuals. It appointed Upadhyay & Co. as its statutory auditor for the financial year 2021-22. While planning the audit, the audit team decided that the risk of improper revenue recognition from hotel business should not be treated as a fraud risk. This conclusion was based on the assessment of earlier years, wherein no fraud was identified in revenue recorded from such business. While testing the internal financial controls over the process of revenue recognition, it was identified that the controls are not properly designed to mitigate the risk of fraud and risk of improper revenue recognition. As a result, the audit team decided to perform additional substantive testing. However, the audit team still were to the conclusion that there is no risk of fraud in revenue recognition. During the course of substantive testing, it was identified that the management did not account for revenue received from corporate hotel bookings amounting to ₹ 35 crore. These amounts were partially received in the company's bank accounts and partially received in the CFO's personal account. The

amounts received in the bank account of the company were disclosed as advances received against the future bookings.

In the light of above scenario, kindly guide the statutory auditors with respect to their responsibility relating to fraud in an audit of a financial statement.

### Special Aspects of Auditing in an Automated Environment

14. M/s RST & Associates have been appointed as auditors of ADI Ltd. for the financial year 2021-22. The processes, operations, accounting and decisions are carried out by using computers in ADI Ltd. M/s RST & Associates understand that there are several aspects that they should consider to determine the level of automation and complexity in the business environment of ADI Ltd. While planning the audit work, the engagement partners discussed with the audit staff about the various types of controls in the automated environment that are put in place to mitigate the IT risks and to maintain the confidentiality, integrity, availability and security of data such as General IT Controls; Application Controls; and IT-Dependent Controls.

You are required to briefly explain:

- (i) General IT Controls.
- (ii) Application Controls.
- (iii) IT-Dependent Controls.

### The Company Audit

15. The Balance Sheet Extract of Siddha Limited, required to prepare financial statement under Ind-AS, as at 31<sup>st</sup> March, 2022 is as under. Comment on the presentation in terms of Division II of Schedule III to the Companies Act, 2013.

Particulars	As at 31 <sup>st</sup> March, 2022	As at 31 <sup>st</sup> March, 2021
<u>Property Plant and Equipment</u>		
Trademark	xxxx	xxxx
<u>Other Non-current Assets</u>		
Bank deposit with more than 12 months maturity	xxxx	xxxx
<u>Equity</u>		
Share Options Outstanding Account	xxxx	xxxx
<u>Other Current Liabilities</u>		
Application money received for allotment of securities to the extent refundable and interest accrued thereon.	xxxx	xxxx

16. Gautam Limited had borrowed ₹ 1000 crore from XYZ Bank, the principal of which was repayable after 5 years and interest was payable at the end of each year. For 4 years, Gautam Limited paid the interest amount on time. Gautam Limited defaulted the 5<sup>th</sup> instalment of interest payment and principal which was due on June 30, 2021. On March 31, 2021, Gautam Limited approached XYZ bank and MNO bank to restructure the existing liability. As a result, the existing principal and outstanding and overdue interest was restructured into a new loan amounting to ₹ 1,100 crore. The management did not provide any disclosure for the default on the loan on the belief that the old loan ceased to exist and the new loan has maturity after 5 years.

During the statutory audit for the financial year 2021-22, KP & Co. identified this transaction and obtained the relevant documents and understanding. Based on the underlying documents, it was identified that the said restructuring agreement was approved and signed on April 8, 2022, by both of the banks. As a result, on March 31, 2022, the restructuring was still not approved.

In the light of the above scenario, kindly guide the statutory auditors in the reporting of this transaction.

#### **Audit Report**

17. (a) CA Bahubali is the statutory auditor of Bharat Ltd. for the FY 2021-22. During the course of audit CA Bahubali noticed the following:
- (i) With respect to the debtors amounting to ₹ 240 crore, no balance confirmation was received by the audit team. Further, there have been defaults on the payment obligations by debtors on the due dates during the year under audit. The Company has created a provision for doubtful debts to the tune of ₹40 crore during the year under audit. The Company has stated that the provision is based on receivables which are older than 39 months, which according to the audit team is inadequate and as such the audit team is unable to ascertain the carrying value of trade receivables.
  - (ii) In respect of Inventories (which constitutes 38% of the total assets of the company), during the reporting period, the management has not undertaken physical verification of inventories at periodic intervals. Also, the Company has not maintained adequate inventory records at the factory. The audit team was unable to undertake the physical inventory count as such the value of inventory could not be verified.
- Under the above circumstances what kind of opinion should CA Bahubali give? Write the opinion paragraph and basis of opinion paragraph to be included in the Independent Auditor's Report.
- (b) How should auditor give description of auditor's responsibilities for the audit of the financial statements when the auditor disclaims an opinion on the financial statements?

**Audit of Consolidated Financial Statements**

18. Jambu & Sudharma Investments Ltd. is a company having paid up share capital of ₹ 1 crore, it has a subsidiary, Investors Fund Management Ltd. Major business of Jambu & Sudharma Investments Ltd. is to pool money from investors on a collective basis and invest this money in various funds. This company pooled ₹ 12 crore from a number of clients, which represent the Company's shareholders.

While auditing books of accounts of Jambu & Sudharma Investments Ltd. CA Vardhman observed that whole amount of ₹ 12 crore pooled has been invested in shares and debentures of various companies and profit earned due to appreciation of the prices of these shares has been distributed to various shareholders of the company. Performance of all of its investments is measured on fair value basis.

Now, CA Vardhman raised an issue while auditing financial statements of Jambu & Sudharma Investments Ltd. whether the consolidated financial statements are required as per Section 129(3) of the Companies Act, 2013? Analyse the above issue and give your opinion.

**Audit of Banks**

19. CA Prachi was conducting statutory audit of branch of a nationalized bank for the year 2021-22. While reviewing operations and documents/papers of a borrower enjoying overdraft credit facilities of ₹ 50 crore (availed against security of stocks and book debts), following observations were jotted down by her: -
- (i) The balance in overdraft credit facility as on 31st March, 2022 was ₹ 55.65 crore. The balance in account exceeded sanctioned limit during the whole month of March 2022.
  - (ii) As per terms of sanction letter, stock/book debt statements were required to be submitted monthly. Latest available stock/book debt statement for the month of February, 2022 showed drawing power of ₹ 48.50 crore only. However, stock/book debt statements of previous months showed adequate drawing power.
  - (iii) Stock audit of borrower was also conducted during the year by one of empanelled stock auditors of the bank. Stock audit report dated 31<sup>st</sup> December, 2021 placed on the record showed adequate drawing power in the account. However, it has commented adversely on the declining turnover of borrower in year 2021-22 (till the date of stock audit report) as compared to proportionate turnover in preceding year.
  - (iv) The renewal of overdraft facilities was due on 20<sup>th</sup> October, 2021. The account was short renewed by competent authority for a period of 3 months pending submission of complete papers.

However, borrower has not submitted complete renewal papers till 31<sup>st</sup> March, 2022. There is a request letter from borrower on record stating that valuation report of a property located at a faraway location was taking time.



The branch has classified the account as 'Standard Asset'. Considering above, CA Prachi is in dilemma relating to proper classification of above advance. Guide her.

### Audit of Non-Banking Financial Company

20. Sudarshan Ltd. is a company registered under the Companies Act, 2013. The company is engaged in the business of loans and advances, acquisition of shares / stocks / bonds / debentures/securities issued by Government or local authorities. For the year ended 31<sup>st</sup> March, 2022 following are some extracts from the financial statements:

(i)	Paid-up share capital	₹ 40.53 Cr.
(ii)	Non-Current Assets - Loans & Advances	₹ 75.50 Cr.
(iii)	Current Assets - Loans and advances	₹ 294.33 Cr.
(iv)	Total assets of the company	₹ 618.55 Cr.
(v)	Intangible assets	₹ 6.35 Cr.
(vi)	Profit for the Year	₹ 8.15 Cr.
(vii)	Income from interest and dividends	₹ 62.31 Cr.
(viii)	Gross income	₹ 111.23 Cr.

Directors intend to apply for registration as Non-Banking Financial Company (NBFC) under Section 45-IA of the Reserve Bank of India (Amendment) Act, 1997. Advise.

### Audit under Fiscal Laws

21. Billimoria & Billimoria, a partnership firm, is engaged in providing engineering consultancy services to insurance corporates in automobile sector. The firm conducts risk inspection of vehicles and submit their reports to insurance companies. Both the partners are Chartered Engineers. The Firm is one of your regular tax audit clients. The following information is culled out from the account books of the company for financial year 2021-22 by the firm:

Particulars	Rupees in Crore
Turnover	8.50
Receipt on account of sales/debtors	6.00
Cash receipt from debtors	0.10
Expenditure during year	7.00
Cash expenditure	0.21
Cash loan repayment	0.05

The partner of said firm informs you that due to changes in income-tax laws, their firm is not liable for audit under section 44 AB of Income tax Act (commonly called as tax audit). How would you deal with the matter? Is contention of partner in accordance with law?

**Audit of Public Sector Undertakings**

22. Comptroller & Auditor General appointed Sambhav & Associates, a chartered accountant firm, to conduct Performance audit of MAP Ltd., a public sector undertaking of Government of India. The firm conducted the audit with a view to check all the expenses of the unit are in conformity with the public interest and publicly accepted customs. The audit report submitted by audit firm was rejected by C&AG. Give your opinion on the action of C&AG.

**Peer Review and Quality Review**

23. (a) Evaluating the professional judgment exercised by the auditor is one of the important aspect under Quality Review, please explain the situation with reference to applicable Standard on Auditing.
- (b) Prabhu & Co LLP is a large firm of Chartered Accountants based out of Mumbai. Prabhu & Co. LLP is subject to peer review which was last conducted 3 years back. For the peer review of the financial year ended 31<sup>st</sup> March 2021, the firm got an intimation on 29<sup>th</sup> May 2021. The process of peer review got started and was completed on 27<sup>th</sup> September 2021. In view of peer reviewer, the systems and procedures of Prabhu & Co. LLP are deficient / non-compliant. The peer reviewer did not share any of his observations with Prabhu & Co LLP as draft and final report was submitted to the Board. Comment.

**Professional Ethics**

24. Comment on the following with reference to the with reference to the Chartered Accountants Act, 1949 and Schedules thereto:
- (a) CA Dev started practice in Punjab in the year 2019. CA Dev issued 'Turnover Certificate' for M/s. ASAUS Traders to be forwarded to the Bank for the purpose of availing cash credit facility and machinery term loan. Brother of CA Dev was proprietor of M/s. ASAUS Traders.
- (b) Aagam Private Limited requested CA Sheetal, a practicing Chartered Accountant, to digitally sign the form related to resignation of Mr. Rohit, one of the Director of Aagam Private Limited, along with the copy of Resignation Letter to be uploaded on the website of Registrar of Companies. The signature of Mr. Rohit was simply copied and pasted by another Director of Aagam Private Limited. CA Sheetal, without verifying the genuineness of the resignation letter, digitally signed the form and the said form was uploaded on the website of Registrar of Companies.
25. Write a short note on the following:
- (a) Management audit questionnaire.
- (b) Free look Cancellation (FRC)
- (c) Services rendered by Forensic Auditors

**SUGGESTED ANSWERS****PART A : ANSWERS TO MULTIPLE QUESTIONS**

1. (d)
2. (a)
3. (c)
4. (b)
5. (b)
6. (b)
7. (a)
8. (b)
9. (d)
10. (d)

**PART B****PART B : DESCRIPTIVE QUESTIONS**

11. As per SA 250, "Consideration of Laws and Regulations in an Audit of Financial Statements", the auditor is required to obtain an understanding and need to evaluate the impact of other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties (for example, compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations); non-compliance with such laws and regulations may therefore have a material effect on the financial statements.

The auditor shall perform the following audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements:

- (a) Inquiring of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations; and
- (b) Inspecting correspondence, if any, with the relevant licensing or regulatory authorities

As per Section 143(3)(j) read with Rule 11(a), the auditor is required to report whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement.

As per SA 570, “Going Concern”, if the auditor concludes that management’s use of the going concern basis of accounting is appropriate in the circumstances but a material uncertainty exists, the auditor shall determine whether the financial statements:

- (i) Adequately disclose the principal events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern and management’s plans to deal with these events or conditions; and
- (ii) Disclose clearly that there is material uncertainty related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern and, therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business.

If adequate disclosure about the material uncertainty is not made in the financial statements, the auditor shall (a) Express a qualified opinion or adverse opinion, as appropriate, in accordance with SA 705; and (b) In the Basis for Qualified (Adverse) Opinion section of the auditor’s report, state that a material uncertainty exists that may cast significant doubt on the entity’s ability to continue as a going concern and that the financial statements do not adequately disclose this matter.

In the current scenario, Abhinandan Limited has received a show cause notice from the National Green Tribunal of an amount which is more than the net profit and the turnover of the company for the year. In the event of an unfavourable order for Abhinandan Limited, there will be an impact on Abhinandan Limited’s ability to continue as a going concern.

As a result, appropriate disclosure should be provided by management for such events which cast significant doubt on the entity’s ability to continue as a going concern. As no appropriate disclosure has been provided by Abhinandan Limited for such show cause notice, Subahu & Co. should report this matter in their audit report under “Going Concern Para” as per SA 570 and under clause (j) of Section 143(3) of the Companies Act, 2013. Also, the auditor is required to issue an adverse opinion as per SA 705, **“Modifications to the Opinion in the Independent Auditor’s Report”**.

12. As per SA 530, “Audit Sampling”, the auditor shall evaluate:

- (a) The results of the sample; and
- (b) Whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

If the auditor concludes that audit sampling has not provided a reasonable basis for conclusions about the population that has been tested, the auditor may:

- (I) Request management to investigate misstatements that have been identified and the potential for further misstatements and to make any necessary adjustments; or
- (II) Tailor the nature, timing and extent of those further audit procedures to best achieve the required assurance. For example, in the case of tests of controls, the auditor might

extend the sample size, test an alternative control or modify related substantive procedures.

13. As per SA 240, "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements" and SA 315, "Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment", the auditor shall identify and assess the risks of material misstatement due to fraud at the financial statement level, and at the assertion level for classes of transactions, account balances and disclosures. When identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions or assertions give rise to such risks.

In accordance with SA 240, "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements" and 330, "The Auditor's Responses to Assessed Risks" the auditor shall determine overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level and assertion level.

The presumption that there are risks of fraud in revenue recognition may be rebutted. For example, the auditor may conclude that there is no risk of material misstatement due to fraud relating to revenue recognition in the case where there is a single type of simple revenue transaction, for example, leasehold revenue from a single unit rental property. However, when there is a complex revenue structure or when there is lack of controls on revenue recognition, then there is a high probability of fraud risk in revenue recognition.

Obtaining an understanding of the entity and its environment, including the entity's internal control (referred to hereafter as an "understanding of the entity"), is a continuous, dynamic process of gathering, updating and analysing information throughout the audit.

In the current scenario, the company was earning revenue from multiple streams. Also, it was identified that the controls are not properly designed to mitigate the risk of fraud and risk of improper revenue recognition. During the year it was identified that the management did not account for revenue from corporate hotel bookings amounting to ₹ 35 crore. These amounts were partially received in the company's bank accounts and partially received in the CFO's personal account. The amounts received in the bank account of the company were disclosed as advances received against future bookings.

Therefore, the auditor while performing the risk assessment procedures should consider the complexity and nature of the revenue for determining the fraud risks in revenue recognition. Also, there were no adequate controls addressing the risk of improper revenue recognition or fraud risk, the audit team rebutted the fraud risk. Moreover, the audit team should have recognised fraud risk by identifying the deficiencies of internal control over the revenue recognition process and should have treated the risk of improper revenue recognition as a significant risk. Also, as per Section 143(12), the auditor is required to report all the frauds identified during the course of the audit involving amounts above ₹ 1 crore within the prescribed time frame to the Central Government

14. The controls that are put in place to mitigate the IT risks and to maintain the confidentiality, integrity, availability and security of data are General IT Controls, Application Controls and IT-Dependent Controls.

**General IT Controls:** “General IT controls are policies and procedures that relate to many applications and support the effective functioning of application controls. They apply to mainframe, miniframe, and end-user environment. General IT controls that maintain the integrity of information and security of data commonly include controls over the following:” (SA 315)

- Data center and network operations;
- System software acquisition, change and maintenance
- Program change;
- Access security;
- Application system acquisition, development, and maintenance (Business Applications).

These are IT controls generally implemented to mitigate the IT specific risks and applied commonly across multiple IT systems, applications and business processes. Hence, General IT controls are known as “pervasive” controls or “indirect” controls.

**Application Controls:** Application controls include both automated or manual controls that operate at a business process level. Application controls can be preventive as well as detective in nature and are designed to ensure the integrity of the accounting records. application controls relate to procedures used to initiate, record, process and report transactions or other financial data. These controls help ensure that transactions occurred, are authorised, and are completely and accurately recorded and processed. Automated Application controls are embedded into IT applications viz., ERPs and help in ensuring the completeness, accuracy and integrity of data in those systems. Examples of automated applications include edit checks and validation of input data, sequence number check, limit check, format check, range check, reasonableness check, mandatory data fields, existence check etc.

**IT dependent controls:** IT dependent controls are basically manual controls that make use of some form of data or information or report produced from IT systems and applications. In this case, even though the control is performed manually, the design and effectiveness of such controls depend on the reliability of source data.

Due to the inherent dependency on Information Technology, the effectiveness and reliability of Automated application controls and IT dependent controls require the General IT Controls to be effective.

**15. Following Errors have been noticed in presentation, as per Division II of Schedule III:**

- (i) "Trademark" is not to be classified under "Property Plant and Equipment" since they are specifically to be disclosed under 'Other Intangible Assets" as per Division II of Schedule III.
- (ii) "Bank deposit with more than 12 months maturity" is not to be classified under "Other Non-current Assets" since they are specifically to be disclosed under "Other Financial Assets" as per Division II of Schedule III.
- (iii) "Share Option Outstanding Accounts" is not to be classified under "Equity", since it has to be disclosed under "Other Equity" as per Division II of Schedule III.
- (iv) Interest accrued thereon" is not to be classified under "Other non-current assets", since they are specifically to be disclosed under the head "Other Financial Liabilities" as per Division II of Schedule III.

**16. As per Clause 3(ix) of CARO 2020, the auditor is required to report whether the company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, the period and the amount of default to be reported as per the format below.**

Nature of borrowing, including debt securities	Name of lender	Amount not paid on due date	Whether principal or interest	No. of days delay or unpaid	Remarks, if any
	lender wise details to be provided in case of defaults to banks, financial institutions and Government.				

In the given case, the company Gautam Limited defaulted in payment of the principal amount of the loan due of ₹ 1000 crore on 30 June 2021 and the interest instalment of ₹ 100 crore. The said default continued till the end of the year and on 8 April 2022, a restructuring agreement was signed by the banks and company for re-structuring the outstanding loan. Moreover, no disclosure was provided by the company with respect to the said matter.

Hence the auditor is required to report the same matter under Clause (ix) of Para 3 of CARO 2020, i.e., whether the company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, then provide the details of the period and the amount of default. Also, the auditor needs to consider the impact of such non-disclosure and the non-compliance with the financial reporting framework and accordingly the auditor needs to either issue a qualified opinion or an adverse opinion as per SA 705, **“Modifications to the Opinion in the Independent Auditor’s Report”**.

17. (a) In the present case, CA Bahubali is unable to obtain sufficient and appropriate audit evidence with respect to the following:
- (i) The balance confirmation with respect to debtors amounting to ₹ 240 crore is not available. Further there has been default in payment by the debtors and the provision so made is not adequate. The audit team is also unable ascertain the carrying value of trade receivables.
  - (ii) With respect to 38% of the company’s inventory, neither the physical verification has been done by the management nor are adequate inventory records maintained. The audit team is also unable to undertake the physical inventory count as such the value of inventory could not be verified.

In the above two circumstances the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

Thus, CA Bahubali should give a Disclaimer of Opinion.

**The relevant extract of the Disclaimer of Opinion Paragraph and Basis for Disclaimer of Opinion paragraph is as under:**

**Disclaimer of Opinion**

We do not express an opinion on the accompanying financial statements of Bharat Ltd. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

**Basis for Disclaimer of Opinion**

We are unable to obtain balance confirmation with respect to the debtors amounting to ₹ 240 crore. Further, there have been defaults on the payment obligations by debtors on the due dates during the year under audit. The Company has created a provision for doubtful debts to the tune of ₹ 40 crore during the year under audit which is inadequate in the circumstances of the company. The carrying value of trade receivables could not be ascertained.



Further, in respect of Inventories (which constitutes 38% of the total assets of the company), during the reporting period, the management has not undertaken physical verification of inventories at periodic intervals. Also, the Company has not maintained adequate inventory records at the factory. We were unable to undertake the physical inventory count and as such the value of inventory could not be verified.

- (b) When the auditor disclaims an opinion on the financial statements due to an inability to obtain sufficient appropriate audit evidence, the auditor shall amend the description of the auditor's responsibilities required by SA 700, **"Forming an Opinion and Reporting on Financial Statements"**, to include only the following:
- (i) A statement that the auditor's responsibility is to conduct an audit of the entity's financial statements in accordance with Standards on Auditing and to issue an auditor's report;
  - (ii) A statement that, however, because of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and
  - (iii) The statement about auditor independence and other ethical responsibilities required in SA 700.
18. According to Section 129(3) of the Companies Act, 2013, where a company has one or more subsidiaries, including associate company and joint venture, it shall, in addition to its own financial statements prepare a consolidated financial statement of the company and of all the subsidiaries in the same form and manner as that of its own.

As per sub-section 6 of the section 129 of the Companies Act, 2013, the Central Government may, on its own or on an application by a class or classes of companies, by notification, exempt any class or classes of companies from complying with any of the requirements of section 129 or the Rules made thereunder.

**An investment entity is an entity that:**

- (a) obtains funds from one or more investors for the purpose of providing those investor(s) with investment management services;
- (b) commits to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and
- (c) measures and evaluates the performance of substantially all of its investments on a fair value basis.

An investment entity need not present consolidated financial statements if it is required, in accordance with paragraph 31 of Ind AS 110, to measure all of its subsidiaries at fair value through profit or loss. A parent shall determine whether it is an investment entity.

However, as per paragraph 33 of Ind AS 110, parent of an investment entity shall consolidate all entities that it controls, including those controlled through an investment entity subsidiary, unless the parent itself is an investment entity.

Applying the above to the given case of Jambu & Sudharma Investments Ltd., which fulfils all the conditions stated above, it is an investment entity. By applying Para 31 and 33 of Ind AS 110, it can be concluded that Jambu & Sudharma Investments Ltd. is not required to consolidate as per Section 129 (3) of the Companies Act, 2013.

19. The borrower was enjoying overdraft credit facilities of ₹ 50 crore against security of stocks and debts. Further, though latest available stock statement for the month of February, 2022 showed inadequate drawing power, there was adequate drawing power available throughout the year. Stock audit report dated 31.12.2021 also reflected adequate drawing power. Hence, it shows that borrower had adequate drawing power during the year. Further, comment on declining sales is of general informative value to management for making credit decisions.

The fact of over drawings in account during the month of March, 2022 and inadequate drawing power in a month are in nature of temporary deficiencies and do not require account to be classified as NPA in accordance with asset classification and provisioning norms of RBI.

RBI instructions lay down that ordinarily credit limits need to be reviewed not later than three months from the due date. As per Guidance note on Audit of Banks, in case of constraints such as non-availability of financial statements and other data from the borrowers, the branch should furnish evidence to show that renewal/ review of credit limits is underway and would be completed soon. In any case, delay beyond six months is not considered desirable as a general discipline. Hence, an account where the credit limits have not been reviewed/ renewed within 180 days from the due date will be treated as NPA.

It would be pertinent to note that the counting of 180 days would be required to be done from the date of original due date for renewal and not from the date of expiry of short reviews / technical reviews. In the instant case, the original date of renewal was 20<sup>th</sup> October, 2021 and period of 180 days has still not expired as on balance sheet date.

Keeping in view all above factors, CA Prachi should accept classification of account as 'Standard Asset' made by branch.

20. In order to identify a particular company as Non-Banking Financial Company (NBFC), it will consider both assets and income pattern as evidenced from the last audited balance sheet of the company to decide its principal business. The company will be treated as NBFC when a company's
- (i) Financial assets constitute more than 50 per cent of the total assets (netted off by intangible assets) and
  - (ii) Income from financial assets constitute more than 50 per cent of the gross income.

A company which fulfils both these criteria shall qualify as an NBFC and would require to be registered as NBFC by RBI.

In the given case, applying the Criteria (i) Financial assets constitute more than 50 per cent of the total assets (netted off by intangible assets),

A. Financial Assets of Sudarshan Ltd. are =

Non-Current Assets - Loans & Advances	₹ 75.50 Cr.
Add: Current Assets - Loans and advances	₹ 294.33 Cr.
Total Financial Assets	₹ 369.83 Cr.

B. Total Assets (netted off by intangible assets) of Sudarshan Ltd. are=

Total assets of the company	₹ 618.55 Cr.
Less: Intangible assets	₹ 6.35 Cr.
Total Assets (netted off by intangible assets)	₹ 612.20 Cr.

In view of above, Financial assets of Sudarshan Ltd. constitute more than 50 per cent of the total assets (netted off by intangible assets).

**Applying the Criteria (ii) Income from financial assets constitute more than 50 per cent of the gross income.**

Income from financial assets = ₹ 62.31 Cr

Gross Income = ₹ 111.23 Cr

From the above, it is clear that Sudarshan Ltd.'s financial assets constitute more than 50 per cent of the total assets (netted off by intangible assets) and income from financial assets constitutes more than 50 per cent of the gross income. Hence, Sudarshan Ltd. fulfils both these criteria to qualify as an NBFC.

Thus Sudarshan Ltd. can apply for registration under Section 45-IA of Reserve Bank of India (Amendment) Act, 1997 in prescribed form along with the necessary documents.

21. Section 44 AB(a) of the Income Tax Act, 1961 prescribes that a person carrying on business shall get his accounts audited if his total sales, turnover or gross receipts exceed ₹ 1 crore in any previous year. However, this limit was enhanced to ₹ 10 crore in the following case where: -

- aggregate of all amounts received including amount received for sales, turnover or gross receipts during the previous year, in cash, does not exceed five per cent of the said amount; and
- aggregate of all payments made including amount incurred for expenditure, in cash, during the previous year does not exceed five per cent of the said payment.

However, section 44 AB(b) of the Income Tax Act, 1961 states that in case of profession, every person shall get his accounts audited, if his gross receipts in profession exceed ₹ 50 lakh. The above said firm is engaged in providing engineering consultancy services to insurance corporates. Hence, the benefit of enhanced threshold limit is not available to persons engaged in professional activities.

The information regarding cash receipt and payment although falling within 5% of total receipts/payments is not relevant in the instant case.

Hence, contention of partner is not correct, and firm is required to get its accounts audited under income tax law.

22. In the given scenario, C&AG appointed Sambhav & Associates, a chartered accountant firm, to conduct Performance Audit of MAP Ltd., a PSU of Government of India. The firm conducted audit with a view to check all the expenses of the unit are in conformity to the public interest and publicly accepted customs which is not Performance Audit.

A performance audit is an objective and systematic examination of evidence for the purpose of providing an independent assessment of the performance of a government organization, program, activity, or function in order to provide information to improve public accountability and facilitate decision-making by parties with responsibility to oversee or initiate corrective action.

Performance audit in PSUs is conducted by the C&AG (Supreme Audit Institutions) through various subordinate offices of Indian Audit and Accounts Department (IAAD). In conducting performance audit, the subordinate offices are guided by manual and auditing standards prescribed by C&AG.

Therefore, the objectives of performance auditing are evaluation of economy, efficiency, and effectiveness of policy, programmes, organization and management. It also promotes accountability by assisting those charged with governance and oversight responsibilities to improve performance; and transparency by affording taxpayers, those targeted by government policies and other stakeholders an insight into the management and outcomes of different government activities.

Performance auditing focuses on areas in which it can add value which have the greatest potential for development. It provides constructive incentives for the responsible parties to take appropriate action.

Regulations on Audit and Accounts issued by C&AG lay down that the responsibility for the development of measurable objectives and performance indicators as also the systems of measurement rests with the Government departments or Heads of entities. They are also required to define intermediate and final outputs and outcomes in measurable and monitorable terms, standardise the unit cost of delivery and benchmark quality of outputs and outcomes.

Thus, rejection of audit report (submitted by audit firm) by C&AG is in order as audit with a view to mere check all the expenses of the unit are in conformity to the public interest and publicly accepted customs done by audit firm is not performance audit in all aspects.

23. (a) **Evaluating the professional judgment exercised by the auditor:** It is also important for the Technical Reviewer (hereinafter referred as TR) to understand that “professional judgment”, as defined in SA 200, “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing” is an integral concept in the context of an audit and application of SAs in real life audit scenarios. SA 200 defines professional judgment as “the application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the course of action that is appropriate in the circumstances of the audit engagement.”

The concept of “professional judgment” underscores the fact that Standards, particularly, Standards on Auditing are written to lay down the fundamental principles that would apply to an audit situation. Hence, no Standard can have straight jacketed application/solutions for all audit scenarios. Above all, the Standards on Auditing issued by the Institute of Chartered Accountants of India are principle based rather than rule based. Hence, almost all the SAs envisage exercise of professional judgment by the auditor in their application in real life audit scenarios.

The TR would need to appreciate that the exercise of professional judgment in any particular case is based on the facts and circumstances that are known to the auditor as at the time of exercising that professional judgment. Normally, exercise of professional judgement by an auditor is preceded by consultation on the relevant matters both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm.

**In evaluating the professional judgment exercised by the auditor, the TR should consider the following factors:**

- whether the judgment reached reflects a due consideration and application of the relevant auditing and accounting principles; and
- whether the judgment is appropriate in the light of, and consistent with, the facts and circumstances that were known to the auditor up to the date of the auditor's report. Hence, the TR and the QR Team should not, under any circumstance, use “hindsight” (i.e. perception or retrospection) in their evaluation of exercise of professional judgment by the auditor.

Since the auditor needs to exercise professional judgment throughout the audit, the latter also needs to be appropriately documented. Hence, the TR can expect to find such audit documentation as a part of the audit engagement file. It is important to note that professional judgment cannot be used by an auditor as a justification for decisions that are not otherwise supported by the facts and circumstances of the engagement or sufficient appropriate audit evidence.

- (b) **Peer Review Report of Reviewer:** After completing the on-site Review, the Peer Reviewer, before making his Report to the Board, **shall communicate his findings in the Preliminary Report to the Practice Unit** if in his opinion, the systems and procedures are deficient or non-compliant with reference to any matter that has been noticed by him or if there are other matters where he wants to seek clarification.

The Practice Unit shall within 5 days after the date of receipt of the findings, make any submissions or representations, in writing to the Reviewer. (i.e. Response to the Preliminary Report).

At the end of an on-site Review if the Reviewer is satisfied with the reply received from the Practice Unit, he shall submit a Peer Review Report to the Board along with his initial findings, response by the Practice Unit and the manner in which the responses have been dealt with. A copy of the report shall also be forwarded to the Practice Unit.

In case the Reviewer is of the opinion that the response by the Practice Unit is not satisfactory, the Reviewer shall accordingly submit a modified Report to the Board incorporating his reasons for the same. The Reviewer shall also submit initial findings **(i.e. Preliminary Report)**, response by the Practice Unit **(Response to Preliminary Report)** and the manner in which the responses have been dealt with. A copy of the report shall also be forwarded to the Practice Unit.

In case of a modified report, The Board shall order for a **“Follow On”** Review after a period of one year from the date of issue of report as mentioned above. If the Board so decides, the period of one year may be reduced but shall not be less than six months from the date of issue of the report.

In the instant case, in view of Peer Reviewer systems and procedures in Prabhu & Co. LLP are deficient, therefore, Peer Reviewer should not submit the report directly to the Board. Thus, contention of Prabhu & Co. LLP is correct.

24. (a) As per Clause (4) of Part I of Second Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice is deemed to be guilty if he expresses his opinion on financial statements of any business or enterprise in which he, his firm, or a partner in his firm has a substantial interest.

Further, it is not permissible for a member to undertake the assignment of certification, wherein the client is relative of the member. The "relative" for this purpose would refer to the definition mentioned in Accounting Standard (AS) - 18.

In the given situation, CA Dev started practice in Punjab in the year 2019. CA Dev issued Turnover certificate for M/s. ASAUS Traders to be forwarded to the Bank for the purpose of obtaining Loan. Brother of CA Dev is proprietor of M/s. ASAUS Traders. Brother is very well covered in the definition of relative mentioned in Accounting Standard (AS)-18.

Hence, CA Dev is guilty of professional misconduct.

- (b) As per Clause (7) of Part I of Second Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice is deemed to be guilty if he does not exercise due diligence or is grossly negligent in the conduct of this professional duties.

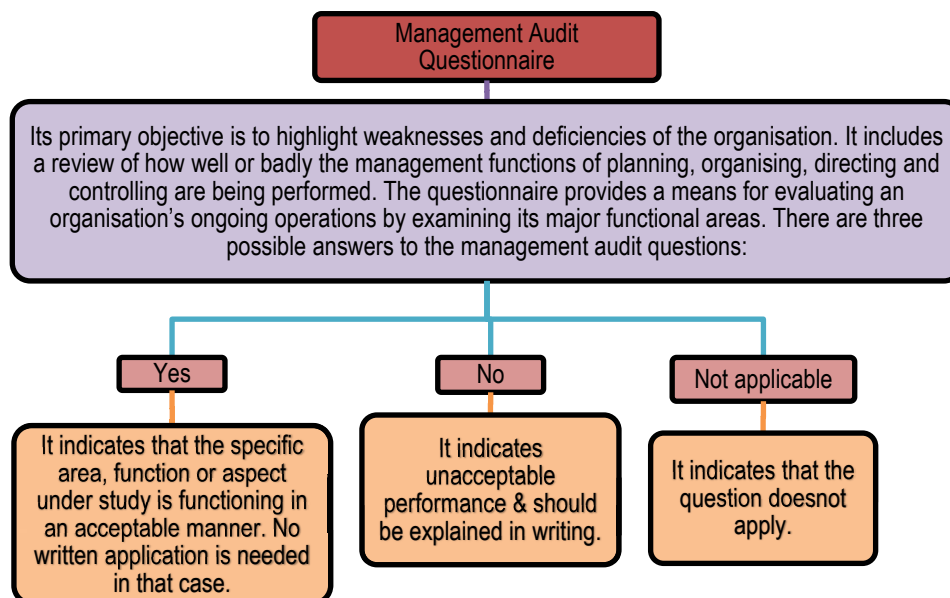
In the given case, Aagam Private Limited requested CA Sheetal, a practicing chartered accountant, to digitally sign the form related to resignation of Mr. Rohit, one of the Director of Aagam Private Limited, along with the copy of Resignation Letter to be uploaded on the website of Registrar of Companies. The signature of Mr. Rohit was simply copied and pasted by another Director of Aagam Private Limited.

CA Sheetal, without verifying the genuineness of the Resignation Letter, digitally signed the Form and the said form was uploaded on the website of Registrar of Companies.

Due to forged resignation letter, the resignation of Mr. Rohit from directorship of the Aagam Private Limited had been occurred. It was noted that CA Sheetal had not taken any step to verify forged signature on resignation letter which anyone would have taken in normal circumstances.

Consequently, CA. Sheetal would be held liable for professional misconduct as per Clause (7) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

25. (a) A management audit questionnaire is an important tool for conducting a management audit. It is through these questionnaires that the auditors make an inquiry into important facts by measuring current performance. Such questionnaires aim at a comprehensive and constructive examination of an organisation's management and its assigned tasks. Overall it is concerned with the appraisal of management actions in accomplishing the organisation's objectives.



Thus, management audit questionnaire for this part of the audit not only serves as a management tool to analyse the current situation; more importantly, it enables the management auditors to synthesis those elements that are causing organisational difficulties and deficiencies.

- (b) **Free Look Cancellation (FLC)** : As per clause 6(2) of IRDA (Protection of Policyholders Interest) Regulations, 2002, “the insurer shall inform by the letter forwarding the policy that he has a period of 15 days from the date of receipt of the policy document to review the terms and conditions of the policy and where the insured disagrees to any of those terms or conditions, he has the option to return the policy stating the reasons for his objection, when he shall be entitled to a refund of the premium paid, subject only to a deduction of a proportionate risk premium for the period on cover and the expenses incurred by the insurer on medical examination of the proposer and stamp duty charges”.

Accordingly, FLC is an option provided to the policyholder wherein he has a period of 15 days from the date of receipt of the policy document to review the Terms & Conditions of the policy and in case of disagreement to any of the terms & conditions, he/ she has the option to return the policy stating the reason for policy's cancellation. FLC requests can be received through any mode –e-mail, fax and letters depending on insurer's policy. In case of written letters, the signature of the policy holder should be matched with the original proposal form. FLC request is processed only when the



policy holder is not satisfied with the terms and conditions of the policy document and not for any other reasons. FLC refund is paid either by cheque or in case the policy holder wants direct credit, then consent for direct credit along with cancelled cheque for bank account details is submitted.

**(c) Services rendered by Forensic Auditors are:**

- Crafting questions to be posed
- Responding to questions posed
- Identifying documents to be requested and/or subpoenaed
- Identifying individuals to be most knowledgeable of facts
- Conducting research relevant to facts of the case
- Identifying and preserving key evidence
- Evaluating produced documentation and information for completeness
- Analysing produced records and other information for facts
- Identifying alternative means to obtain key facts and information
- Providing questions for deposition and cross examination of fact and expert witnesses