

PAPER – 3 : ADVANCED AUDITING AND PROFESSIONAL ETHICS

PART – I ACADEMIC UPDATE

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

Chapter 5: Company Audit

1. **Definition of "Government company" [Section 2(45)]:** In this section, the following explanation has been inserted in the definition. Explanation.- For the purposes of this clause, the "paid up share capital" shall be construed as "total voting power", where shares with differential voting rights have been issued.] [insertion on page no. 5.4 of Study Material as per notification dated 2-3-2020 by way of Exemptions to Government Companies under section 462 with effect from 3-3-2020]

2. "The auditor of the company shall, in his report under section 143, make a statement as to whether the remuneration paid by the company to its directors is in accordance with the provisions of this section, whether remuneration paid to any director is in excess of the limit laid down under this section and give such other details as may be prescribed" (as per section 197(16) of the Companies Act, 2013)

As per Advisory issued by ICAI, the aforesaid reporting requirement for auditors of public companies needs to be covered in auditor's report under the Section "Report on Other Legal and Regulatory Requirements". Accordingly, auditors of public companies are advised to comply with the aforesaid reporting requirements in their auditor's reports. (in) (insertion in point no 4 on page no 5.32 of Study Material.)

3. In **section 132**—

- (i) after sub-section (1), the following sub-section shall be inserted, namely:—
“(1A) The National Financial Reporting Authority shall perform its functions through such divisions as may be prescribed.”;
[Amendment to be incorporated on Pg 5.47 of SM]
- (ii) Every auditor referred to in Rule 3 shall file a return with the NFRA on or before 30th November every year in Form NFRA-2”. (Insertion on Page no 5.48 of SM)
- (iii) The Central Government has amended the National Financial Reporting Authority Rules, 2018, by the National Financial Reporting Authority (Amendment) Rules, 2019. In the National Financial Reporting Authority Rules, 2018, after clause (c) of sub-rule (1) of **rule 3**, the following explanation shall be inserted, namely:-

“Explanation.- For the purpose of this clause, “banking company” includes ‘corresponding new bank’ as defined in clause (d) of section 2 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 (5 of 1970) and clause (b) of section 2 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 (40 of 1980) and ‘subsidiary bank’ as defined in clause (k) of section 2 of the State Bank of India (Subsidiary Bank) Act, 1959 (38 of 1959).”.
(insertion on page no 5.48 of SM.)

- (iv) Punishment in case of Non-Compliance : (Insertion on Page no 5.50 of SM)** If a company or any officer of a company or an auditor or any other person contravenes any of the provisions of NFRA Rules, the company and every officer of the company who is in default or the auditor or such other person shall be punishable as per the provisions of section 450 of the Act.

Further, as per Section 132(4) of the Companies Act, 2013 as amended by the Companies Amendment Act, 2019, National Financial Reporting Authority, where professional or other misconduct is proved, have the power to make order for:

- (A) imposing penalty of—
- I. not less than one lakh rupees, but which may extend to five times of the fees received, in case of individuals; and
 - II. not less than five lakh rupees, but which may extend to ten times of the fees received, in case of firms;
- (B) debarring the member or the firm from:
- I. being appointed as an auditor or internal auditor or undertaking any audit in respect of financial statements or internal audit of the functions and activities of any company or body corporate; or
 - II. performing any valuation as provided under section 247, for a minimum period of six months or such higher period not exceeding ten years as may be determined by the National Financial Reporting Authority.

Chapter 7: Audit Committee and Corporate Governance

As per Stock and Exchange Board of India circular no. CIR/CFD/CMD1/114/2019 dated 18th October, 2019 on resignation of statutory auditors from listed entities and their material subsidiaries:

1. Listed companies are required to make timely disclosures to investors in the securities market for enabling them to take informed investment decisions.
2. Under Sub-clause (2) of Clause A in Part C of Schedule II under Regulation 18(3) of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("SEBI LODR Regulations"), the Audit Committee of a listed entity, inter alia, has to make

recommendations for the appointment, remuneration and terms of appointment of auditors of a listed entity. Under Sub-clause (7), the Audit Committee is also responsible for reviewing and monitoring the independence and performance of auditors and the effectiveness of the audit process.

3. Further, Sub-clause (7A) inserted under Clause A in Part A of Schedule III under Regulation 30(2) of SEBI LODR Regulations requires detailed reasons to be disclosed by the listed entities to the stock exchanges in case of resignation of the auditor of a listed entity as soon as possible but not later than twenty-four hours of receipt of such reasons from the auditor.
4. Regulation 36(5) of the SEBI LODR Regulations lays down certain disclosures to be made part of the notice to the shareholders for an AGM, where the statutory auditors are proposed to be appointed/re-appointed, including their terms of appointment.
5. Resignation of an auditor of a listed entity / its material subsidiary before completion of the audit of the financial results for the year due to reasons such as pre-occupation may seriously hamper investor confidence and deny them access to reliable information for taking timely investment decisions.
6. In light of the above, the conditions to be complied with upon resignation of the statutory auditor of a listed entity/material subsidiary w.r.t. limited review / audit report as per SEBI LODR Regulations, are as under:

A. All listed entities/material subsidiaries shall ensure compliance with the following conditions while appointing/re-appointing an auditor:

- (i) If the auditor resigns within 45 days from the end of a quarter of a financial year, then the auditor shall, before such resignation, issue the limited review/ audit report for such quarter.
- (ii) If the auditor resigns after 45 days from the end of a quarter of a financial year, then the auditor shall, before such resignation, issue the limited review/ audit report for such quarter as well as the next quarter.
- (iii) Notwithstanding the above, if the auditor has signed the limited review/ audit report for the first three quarters of a financial year, then the auditor shall, before such resignation, issue the limited review/ audit report for the last quarter of such financial year as well as the audit report for such financial year.

B. Other conditions relating to resignation shall include:

- (i) Reporting of concerns with respect to the listed entity/its material subsidiary to the Audit Committee:
 - a. In case of any concern with the management of the listed entity/material subsidiary such as non-availability of information / non-cooperation by the management which may hamper the audit process, the auditor shall approach the Chairman of the Audit Committee of the listed entity and the

Audit Committee shall receive such concern directly and immediately without specifically waiting for the quarterly Audit Committee meetings.

- b. In case the auditor proposes to resign, all concerns with respect to the proposed resignation, along with relevant documents shall be brought to the notice of the Audit Committee. In cases where the proposed resignation is due to non-receipt of information I explanation from the company, the auditor shall inform the Audit Committee of the details of information I explanation sought and not provided by the management, as applicable.
 - c. On receipt of such information from the auditor relating to the proposal to resign as mentioned above, the Audit Committee I board of directors, as the case may be, shall deliberate on the matter and communicate its views to the management and the auditor.
- (ii) Disclaimer in case of non-receipt of information: In case the listed entity/ its material subsidiary does not provide information required by the auditor, to that extent, the auditor shall provide an appropriate disclaimer in the audit report, which may be in accordance with the Standards of Auditing as specified by ICAI/ NFRA.

The listed entity/ material subsidiary shall ensure that the conditions as mentioned in 6(A) and 6(B) above are included in the terms of appointment of the statutory auditor at the time of appointing/re-appointing the auditor. In case the auditor has already been appointed, the terms of appointment shall be suitably modified to give effect to 6(A) and 6(B) above.

The practicing company secretary shall certify compliance by a listed entity with 6(A) and 6(B) above in the annual secretarial compliance report issued in terms of SEBI Circular no. CIR/CFD/CMD1/27/2019 dated February 08, 2019.

C. Obligations of the listed entity and its material subsidiary:

- (i) Format of information to be obtained from the statutory auditor upon resignation: Upon resignation, the listed entity/ its material subsidiary shall obtain information from the Auditor in the format as specified in Annexure A to this Circular. The listed entity shall ensure disclosure of the same under Sub-clause (7A) of Clause A in Part A of Schedule III under Regulation 30(2) of SEBI LODR Regulations.
- (ii) Co-operation by listed entity and its material subsidiary: During the period from when the auditor proposes to resign till the auditor submits the report for such quarter I financial year as specified above, the listed entity and its material subsidiaries shall continue to provide all such documents/information as may be necessary for the audit I limited review.
- (iii) Disclosure of Audit Committee's views to the Stock Exchanges: Upon resignation of the auditor, the Audit Committee shall deliberate upon all the concerns raised by the auditor with respect to its resignation as soon as

possible, but not later than the date of the next Audit Committee meeting and communicate its views to the management. The listed entity shall ensure the disclosure of the Audit Committee's views to the stock exchanges as soon as possible but not later than twenty-four hours after the date of such Audit Committee meeting.

7. In case an entity is not mandated to have an Audit Committee, then the board of directors of the entity shall ensure compliance of this circular.
8. The Stock Exchanges are advised to bring the provisions of this circular to the notice of all listed entities and their material subsidiaries and also disseminate it on their websites.
9. In case the auditor is rendered disqualified due to operation of any condition mentioned in Section 141 of the Companies Act, 2013, then the provisions of this Circular shall not apply.
10. The Circular is issued in exercise of the powers conferred under Section 11 (1) of the Securities and Exchange Board of India Act, 1992 read with regulations 18(3), 30(2) and 36(5) of the SEBI LODR Regulations and shall be in addition to the provisions of Companies Act, 2013. For more details visit: https://www.sebi.gov.in/legal/circulars/oct-2019/resignation-of-statutory-auditors-from-listed-entities-and-their-material-subsidaries_44703.html

Chapter 18: Professional Ethics

Joining/Association with “Networks” by Members in Practice

It is hereby clarified that associations with “Network” as a medium of referral of professional work is permissible only if the Network is registered with the Institute, comprising only of Chartered Accountants/ Chartered Accountant Firms, and governed by the Institute’s Network Guidelines, which may be accessed at <https://resource.cdn.icai.org/24427announ14280.pdf>

Members’ attention is also drawn towards following provisions of Chartered Accountants Act, 1949 (hereinafter referred to as the “Act”) :

Clause (2) of Part I of First Schedule to the Act

A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he pays or allows or agrees to pay or allow, directly or indirectly, any share, commission or brokerage in the Fees or profits of his professional business, to any person other than a member of the Institute or a partner or a retired partner or the legal representative of a deceased partner, or a member of any other professional body or with such other persons having such qualifications as may be prescribed, for the purpose of rendering such professional services from time to time in or outside India.

Explanation — In this item, “partner” includes a person residing outside India with whom a chartered accountant in practice has entered into partnership which is not in contravention of item (4) of this Part;

Clause (3) of Part I of First Schedule to the Act

A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he accepts or agrees to accept any part of the profits of the professional work of a person who is not a member of the Institute:

Provided that nothing herein contained shall be construed as prohibiting a member from entering into profit sharing or other similar arrangements, including receiving any share commission or brokerage in the fees, with a member of such professional body or other person having qualifications, as is referred to in item (2) of this Part;

Clause (5) of Part I of First Schedule to the Act

A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he secures, either through the services of a person who is not an employee of such Chartered Accountant or who is not his partner or by means which are not open to a chartered accountant, any professional business.

Provided that nothing herein contained shall be construed as prohibiting any arrangement permitted in terms of items (2), (3) and (4) of this Part;

Clause (6) of Part I of First Schedule to the Act

A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he solicits clients or professional work either directly or indirectly by circular, advertisement, personal communication or interview or by any other means:

Provided that nothing herein contained shall be construed as preventing or prohibiting —

- (i) any chartered accountant from applying or requesting for or inviting or securing professional work from another chartered accountant in practice; or
- (ii) a member from responding to tenders or enquiries issued by various users of professional services or organisations from time to time and securing professional work as a consequence;

In view of the above provisions, it is not permissible for members in practice to join Networks (by whatever name called) other than the Networks registered with the Institute.

Members may note that joining such Networks as mentioned above may result in noncompliance of the above stated provisions of the Act resulting in disciplinary proceedings in accordance with the provisions of the Act.

A - Meaning of Network & Network Firm –

Network - A larger structure (a) That is aimed at co-operation; and (b) That is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.

Network Firm – “Network Firm” means a firm or Entity that belongs to a Network.

B - Concept of Network

1. To enhance their ability to provide professional services, firms frequently form larger structures with other firms and entities. Whether these larger structures create a network depends on the particular facts and circumstances and does not depend on whether the firms and entities are legally separate and distinct. For example, a larger structure may be aimed only at facilitating the referral of work, which in itself does not meet the criteria necessary to constitute a network. Alternatively, a larger structure might be such that it is aimed at co-operation and the firms share a common brand name, a common system of quality control, or significant professional resources and consequently is deemed to be a network.
2. The judgment as to whether the larger structure is a network shall be made in light of whether a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that the entities are associated in such a way that a network exists. This judgment shall be applied consistently throughout the network.
3. Where the larger structure is aimed at co-operation and it is clearly aimed at profit or cost sharing among the entities within the structure, it is deemed to be a network. However, the sharing of immaterial costs does not in itself create a network. In addition, if the sharing of costs is limited only to those costs related to the development of audit methodologies, manuals, or training courses, this would not in itself create a network.

Further, an association between a firm and an otherwise unrelated entity to jointly provide a service or develop a product does not in itself create a network.
4. Where the larger structure is aimed at cooperation and the entities within the structure share common ownership, control or management, it is deemed to be a network. This could be achieved by contract or other means.
5. Where the larger structure is aimed at co-operation and the entities within the structure share common quality control policies and procedures, it is deemed to be a network. For this purpose, common quality control policies and procedures are those designed, implemented and monitored across the larger structure.
6. Where the larger structure is aimed at co-operation and the entities within the structure share a common business strategy, it is deemed to be a network. Sharing a common business strategy involves an agreement by the entities to achieve common strategic objectives. An entity is not deemed to be a network firm merely because it co-operates with another entity solely to respond jointly to a request for a proposal for the provision.
7. Where the larger structure is aimed at co-operation and the entities within the structure share the use of a common brand name, it is deemed to be a network. A common brand name includes common initials or a common name. A firm is deemed to be using a common brand name if it includes, for example, the common brand name as part of, or along with, its firm name, when a partner of the firm signs an audit report.

8. Even though a firm does not belong to a network and does not use a common brand name as part of its firm name, it may give the appearance that it belongs to a network if it makes reference in its stationery or promotional materials to being a member of an association of firms.

Accordingly, if care is not taken in how a firm describes such memberships, a perception may be created that the firm belongs to a network.

9. Where the larger structure is aimed at co-operation and the entities within the structure share a significant part of professional resources, it is deemed to be a network. Professional resources include:
- Common systems that enable firms to exchange information such as client data, billing and time records;
 - Partners and staff;
 - Technical departments that consult on technical or industry specific issues, transactions or events for assurance engagements;
 - Audit methodology or audit manuals; and
 - Training courses and facilities.
10. The determination of whether the professional resources shared are significant, and therefore the firms are network firms, shall be made based on the relevant facts and circumstances. Where the shared resources are limited to common audit methodology or audit manuals, with no exchange of personnel or client or market information, it is unlikely that the shared resources would be significant. The same applies to a common training endeavor. Where, however, the shared resources involve the exchange of people or information, such as where staff are drawn from a shared pool, or a common technical department is created within the larger structure to provide participating firms with technical advice that the firms are required to follow, a reasonable and informed third party is more likely to conclude that the shared resources are significant.

C- Forms of the Network: The different forms of Network can be as under:-

1. A network can be constituted as a mutual entity which will act as a facilitator for the constituents of the Network. In such a case the Network itself will not carry out any professional practice.
2. A network can be constituted as a partnership firm subject to the condition that the total number of partners does not exceed twenty.
3. A network can be constituted as a Limited Liability Partnership subject to the provision of the Chartered Accountant Act and Rules and such other laws as may be applicable.
4. A network can be constituted as company subject to the guidelines prescribed by Institute for corporate form of practice and formation of management consultancy services company.

5. Network Firms shall consist of sole Practitioner/proprietor, partnership or any such entity of professional accountants as may be permitted by the Act
6. A firm is allowed to join only one network.
7. Firms having common partners shall join only one Network.

D - Approval of Name of Network amongst firms registered with Institute:

1. The Network may have distinct name which should be approved by the Institute. To distinguish a "Network" from a "firm" of Chartered Accountants, the words "& Affiliates" shall be used after the name of the network and the words "& Co." / "& Associates" shall not be used. The prescribed format of application for approval of Name for Network is at Form 'A' (enclosed). Illustrative examples of names of Network: -
 - (a) If the Network is a Mutual Entity or Partnership Firm: AB & Affiliates
 - (b) If the Network is a LLP: AB Affiliates LLP
 - (c) If the Network is a Limited Company: AB Affiliates P. Ltd/Limited
2. Provisions of Regulation 190 of the Chartered Accountants Regulations, 1988 shall be applicable to the name of Network. However, even if a name is approved and subsequently it is found that the same is undesirable then, the said name may be withdrawn at any time by the Institute. The Institute shall reject any undesirable name and the provisions in respect of names of companies as prescribed in the Companies Act, 1956 shall be applicable in spirit.
3. The Institute shall approve or reject the name of the Network and intimate the same to the Network at its address mentioned in Form 'A' within a period which shall not be later than 30 days from the date of receipt of the said Form.
4. Mere approval of the name of the Network shall not entitle the Network to carry on practice in its own name.

E - Registration of Network with entities in India

1. After the name of a Network is approved as per provision under Guideline 5, the Institute same shall reserve such name for a period of three (3) months from the date of approval.
2. The Network shall get itself registered with the Institute by applying in Form B within the period of 3 months, failing which the name assigned shall stand cancelled on the expiry of the said period.
3. Registration of Network with Institute is mandatory.
4. If different Indian firms are networked with a common Multinational Accounting Firm, they shall be considered as a part of network.

F - Listing of Network with entities outside India

1. The duly authorized representative(s) of the Indian Member firm (s)/Member constituting the Network with entities outside India shall file a declaration with the Institute in Form 'D'

for Listing of such Network within 30 days from the date of entering into the Network arrangement.

2. Proprietary/individual members, partnership firms as well as members in LLP or any such other entity of members as may be permitted by the Act, shall be permitted to join such network with entities outside India provided that the proprietary/individual members, partnership firms as well as members in LLP or any such other entity of members are allowed to join only one network and firms having common partners shall join only one such network.

G - Change in constitution of registered Network: In case of change in the constitution of registered Network on account of any entry into or exit from the Network, the network shall communicate the same to the Institute by filing Form 'C' within a period of thirty (30) days from the date of change in the constitution.

H - Ethical Compliance: Once the relationship of network arises, it will be necessary for such a network to comply with all applicable ethical requirements prescribed by the Institute from time to time in general and the following requirements in particular: -

1. If one firm of the network is the statutory auditor of an entity then the associate [including the networked firm(s)] or the said firm directly/indirectly shall not accept the internal audit or book-keeping or such other professional assignments which are prohibited for the statutory auditor firm.
2. The guidelines of ceiling on Non-audit fees is applicable in relation to a Network as follows: i) For a Network firm who is doing statutory audit (including its associate concern and/or firm(s) having common partnership), it shall be the same as mentioned in the said notification; and ii) For other firms of the same Network collectively, it shall be 3 times of the fee payable for carrying out the statutory audit of the same undertaking/company.
3. In those cases where rotation of firms is prescribed by any regulatory authority, no member firm of the network can accept appointment as an auditor in place of any member firm of the network which is retiring.
4. The Network may advertise the Network to the extent permitted by the Advertisement Guidelines issued by Institute. The firms constituting the network are permitted to use the words "Network Firms" on their professional stationery.
5. The constituent member firms of a Network and the Network shall comply with all the Ethical Standards prescribed by the Council from time to time.

I - Consent of Client: The effect of registration of network with Institute will be deemed to be a public notice of the network and therefore consent of client will be deemed to be obtained.

J - Framework of Internal Byelaws of Network: To streamline the networking, a network shall formulate operational bye-laws. Bye-laws may contain the following clauses on which the affiliates of the network may enter into a written agreement among themselves:

- (i) Appointment of a Managing Committee, from among the managing partners of the member firms of the network and the terms and conditions under which it should function. The minimum and maximum number of members of the Managing Committee shall also be agreed upon.
- (ii) Administration of the network
- (iii) Contribution of membership fees to meet the cost of the administration of the network.
- (iv) Identifying a partner of any of the member firms of the network to be responsible for the assignment (engagement partner)
- (v) Dispute settlement procedures through arbitration and conciliation
- (vi) Development of training materials for members of the network
- (vii) Issue of News-letters for staff and clients
- (viii) Development of softwares for different types of assignments
- (ix) Development and maintenance of data bases relevant for different types of assignments
- (x) Library
- (xi) Appointment of a technical director to whom references can be made
- (xii) Determining the methodology for drawing resources from each member firm
- (xiii) Determining compensation to member firms for resources to be drawn from them
- (xiv) Peer review of the member firms These clauses are illustrative.

K - Repeal and Saving: The erstwhile “Rules/Guidelines of Network” issued by the Institute stands repealed from the date of commencement of these Guidelines.

Provided that notwithstanding such repeal, anything done or any action taken or purported to have been done or taken in respect of the erstwhile Rules/Guidelines prior to the date of applicability of these Guidelines shall be deemed to have been done or taken under the corresponding provisions of these Guidelines.

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.**

YS & Associates, a firm of Chartered Accountants, having CA. Y and CA. S as partners, is based at Mumbai. YS & Associates get their website developed as www.ysassociates.com from KPY Ltd. The colour of their website was very bright and attractive to run on a “push” technology. Names of the partners of the firm and the major clients were also displayed on the web-site without any disclosure obligation from any regulator.

CA. Y, accepted his appointment as tax auditor of a firm under Section 44AB, of the Income-tax Act, and commenced the tax audit within two days of appointment since the client was in a hurry to file Return of Income before the due date. After commencing the audit, CA. Y realised his mistake of accepting this tax audit without sending any communication to the previous tax auditor. In order to rectify his mistake, before signing the tax audit report, he sent a registered post to the previous auditor and obtained the postal acknowledgement.

CA. S, provides management consultancy and other services to his clients. During 2019, looking to the growing needs of his clients to invest in the stock markets, he also advised them on Portfolio Management Services whereby he managed portfolios of some of his clients. Looking at his expertise in financial management, Mr. Tarak, a student of Chartered Accountancy course, is very much impressed with his knowledge. He approached CA. S to take guidance on some topics of financial management subject related to his course. CA. S, on request, decided to spare some time and started providing classes to Mr. Tarak along with some other aspirants for 3 days in a week and for 1 hours in a day. However, he has not taken any specific permission for such private tutorship from the Council.

YS & Associates is appointed to conduct statutory audit of XYZ Ltd. XYZ Ltd is required to appoint internal auditor as per statutory provisions given in the Companies Act, 2013 and appointed CA. IA as its internal auditor. YS & Associates asked Mr. IA to provide direct assistance to him regarding evaluating significant accounting estimates by the management and assessing the risk of material misstatements. He also seeks his direct assistance in assembling the information necessary to resolve exceptions in confirmation responses with respect to external confirmation requests and evaluation of the results of external confirmation procedures.

XYZ Ltd is seeking advice of YS & Associates to appoint CA. IA for conducting GST Audit.

Question No.: (1-5)

1. YS & Associates sought direct assistance from CA. IA, internal auditor as stated in the above scenario. Advise as to whether he is permitted to do so in accordance with relevant Standards on Auditing.
 - (a) YS & Associates cannot ask CA. IA for direct assistance regarding evaluating significant accounting estimates and assessing the risk of material misstatements. However, CA. IA may assist YS & Associates in assembling information necessary to resolve exceptions in confirmation responses as per SA 610.
 - (b) CA. IA cannot assist YS & Associates in assembling information necessary to resolve exceptions in confirmation responses. However, YS & Associates can ask Mr. IA for direct assistance regarding evaluating significant accounting estimates and assessing the risk of material misstatements as per SA 610.
 - (c) YS & Associates cannot ask CA. IA for direct assistance regarding evaluating significant accounting estimates and assessing the risk of material misstatements and in assembling the information necessary to resolve exceptions in confirmation responses as per SA 610.
 - (d) YS & Associates can ask CA. IA for direct assistance regarding evaluating significant accounting estimates and assessing the risk of material misstatements and in assembling the information necessary to resolve exceptions in confirmation responses as per SA 610.
2. Whether CA S is guilty of professional misconduct in providing private tutorship to Mr. Tarak along with some other aspirants for 3 days in a week and for 1 hours in a day in the absence of specific approval.
 - (a) CA. S is not guilty of professional misconduct as he is teaching within prescribed hours i.e. not exceeding 25 hours a month as per Regulation 192A
 - (b) CA. S is not guilty of professional misconduct as he is teaching within prescribed hours i.e. not exceeding 25 hours a month as per Regulation 190A
 - (c) CA. S is guilty of professional misconduct as he has not obtained specific permission for the same.
 - (d) CA. S is not guilty of professional misconduct as he is teaching within prescribed hours i.e. not exceeding 25 hours a week as per Regulation 190A
3. Before signing the tax audit report, CA. Y sent a registered post to the previous auditor and obtained the postal acknowledgement. Will CA. Y be held guilty of professional misconduct under the Chartered Accountants Act, 1949?
 - (a) As per Clause (8) of Part I of First Schedule to the Chartered Accountants Act, 1949 CA. Y will not be held guilty of professional misconduct as he communicated with the previous tax auditor before signing the audit report.

- (b) As per Clause (8) of Part I of First Schedule to the Chartered Accountants Act, 1949, CA. Y will not be held guilty of professional misconduct since the requirement for communicating with the previous auditor being a chartered accountant in practice would apply to statutory audit only.
 - (c) As per Clause (8) of Part I of First Schedule to the Chartered Accountants Act, 1949, CA. Y will be held guilty of professional misconduct since he has accepted the tax audit, without first communicating with the previous auditor in writing.
 - (d) As per Clause (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949, CA. Y will be held guilty of professional misconduct since he has accepted the tax audit, without first communicating with the previous auditor in writing.
4. In view of YS & Associates, whether CA. IA is eligible to undertake Goods and Service Tax (GST) Audit of XYZ Ltd simultaneously?
- (a) CA. IA is internal auditor of XYZ Ltd and therefore, is eligible to undertake Goods and Service Tax (GST) Audit of XYZ Ltd simultaneously
 - (b) CA. IA is internal auditor of XYZ Ltd and therefore, not eligible to undertake Goods and Service Tax (GST) Audit of XYZ Ltd simultaneously
 - (c) Being Internal Auditor CA. IA is appropriate person to carry out Goods and Service Tax (GST) Audit of XYZ Ltd
 - (d) None of the above
5. Whether, website designed for www.ysassociates.com is in compliance with the guidelines given in Clause (6) of Part I of First Schedule to the Chartered Accountants Act, 1949:
- (a) Yes, website can have names of partners and major clients along with its fess.
 - (b) Yes, as the websites can be designed on a “push” technology.
 - (c) Yes, as there is no restriction on the colours used in the website.
 - (d) No, as names of the partners of the firm and the major clients were displayed without any disclosure obligation from any Regulator.

Integrated Case Scenario 2.

M/s ANS & Associates have been appointed as statutory auditors of Delco Ltd., listed company (referred to as ‘Company’) for the Financial Year 2019-20. Delco Ltd. deals in the manufacture of shoes.

During the course of the audit, the auditor found that the company has acquired two subsidiaries namely Sole Ltd. dealing in the manufacture of shoe soles and Soccer Ltd. dealing in the manufacture of kid shoes. The auditors of Sole Ltd. and Soccer Ltd. are M/s XYZ & Associates.

Delco Ltd. has prepared the consolidated financial statements under Indian Accounting Standards and consolidated the financial statements of subsidiary Sole Ltd. during the current financial year. However, the company has not consolidated the financial statements of Soccer

Ltd. which was also acquired during the current financial year as the company has not yet been able to ascertain the fair values of certain material assets and liabilities of Soccer Ltd. as on the acquisition date. This acquisition is accounted for as an investment in the books of Delco Ltd. Had the company consolidated the financial statements of both the subsidiary, there would have been material impact on important elements of the financial statements.

At the time of finalization of the Audit Report of the company for the year ended March 31, 2020, the auditors are considering their reporting responsibility for non-consolidation of the financial statements of Soccer Limited.

The auditors also asked the management to disclose their reason for non-consolidation of financial of Soccer Ltd. in the notes to accounts.

Also the financial statements of Delco Ltd. of the current financial year include the corresponding figures (without consolidation) of the previous financial year i.e. FY 2018-19.

Further, the auditors are also considering the implications on their responsibilities and the management's responsibilities with respect to the financial statements and in the audit of such financial statements.

Question No.: (6-10)

6. With respect to the non-consolidation of financial statements of Soccer Ltd. with the financial statements of Delco Ltd., how should the auditor deal with the same in their audit report?
 - (a) The auditor should give a disclaimer of opinion.
 - (b) The auditor should give an adverse opinion if the impact is material and pervasive in his audit report.
 - (c) The auditor should mention this fact in the emphasis of matter paragraph pervasive in his audit report.
 - (d) The auditor should mention this fact in other matter paragraph pervasive in his audit report.
7. What are the auditors reporting responsibility with respect to the corresponding figures of the financial year 2018-19 in the current year financial statements, for the same?
 - (a) The auditor's opinion should refer to each period for which the financial statements are presented.
 - (b) The auditors need to report on the current year financials only be it comparative or corresponding figures.
 - (c) The auditor's opinion shall not refer to the corresponding figures except if the previous period audit report is other than an unqualified opinion or the auditor has sufficient evidence that a material misstatement exist in the financial statement of prior period which was not addressed earlier.

- (d) The auditor has no reporting responsibility for the financial statements of any year other than the current financial year for which they have been appointed.
8. What is the reporting responsibility of the auditor in case, the prior period financial statements are not audited?
- (a) The auditors need to report such matter in the Key Audit Matters paragraph in his report.
- (b) The auditors need to report such matter in the other matter paragraph in his report.
- (c) The auditor will be responsible for obtaining sufficient appropriate audit evidence that opening balance so not contain any material misstatement.
- (d) Both b & c.
9. Preparation of the financial statements in accordance with the applicable financial reporting framework is the responsibility of the management of Delco Ltd. Which of the following is correct in regard to the disclosure of such management responsibility:-
- (a) This is implied responsibility of management and is presumed in an audit of financial statements and therefore need not be specifically mentioned anywhere.
- (b) The management may undertake to accept such responsibility through an engagement letter itself.
- (c) The auditor report should describe the management responsibility in a section with heading "responsibility of management for financial statements".
- (d) The auditor's report should refer to the responsibility of auditors and not that of the management as the same is obvious.
10. If the auditors of Delco Ltd. decides to give a qualified/ adverse opinion in the current financial year with respect to the non-consolidation of financials of Soccer Ltd., which of the following is true with regard to the use of EOM paragraph for some other matter:-
- (a) The auditor cannot add EOM paragraph in his report on any matter as a qualified/ adverse opinion is given by the auditor.
- (b) EOM paragraph on a matter can be added if auditors opinion is neither qualified/ nor adverse in respect to that particular matter and the matter is fundamental to the user's understanding of financial statements.
- (c) EOM paragraph on any matter can be added in the auditor's report even if the report is qualified/ adverse with respect to that particular matter.
- (d) EOM paragraph indicates that the auditor's opinion is modified in respect to the matter emphasized.

Independent MCQs

11. NIC Chartered Accountants was appointed as statutory auditors by PNG Ltd. for the audit of their financial statements. During the course of audit the auditors noticed a fraud of ₹ 101 lac committed by an officer of the Company. The officer sanctioned and made the payment to fake vendors for purchase of fixed assets, however, the assets were not entered in the Fixed Assets Register. The auditor reported the fraud in his audit report to the shareholders of the Company presented in the Annual General Meeting, but did not mention the name of the parties involved. The Board of Directors of the Company asked ICAI to take necessary action against the auditor as he did not comply with his duty to report fraud as per Section 143(12) of the Companies Act, 2013. What is the duty of the auditor as per the Companies Act, 2013 in reporting the fraud committed by officers / employees of the Company?
- (a) As per the Companies Act, 2013, since the amount of fraud is more than ₹ 100 lac; the auditor should have reported the matter within 2 days of his knowledge to the Board of Directors/ Audit committee of the Company seeking their reply or observations within 45 days. After completion of 45 days, the auditor should forward his report to the Central Government along with the reply, if any, received from Board/ Audit Committee.
 - (b) As per the Companies Act, 2013, during the course of audit if the auditor has reason to believe that a fraud has been committed by the officers or employees of the Company, the auditor shall report the matter to the Central Government immediately.
 - (c) The auditor's duty is restricted to reporting the fraud to shareholders and he is not required to report the matter to the Board of Directors/ Audit Committee/ Central Government.
 - (d) The auditor can submit his report on fraud to shareholders but is required to mention the name of the parties involved in fraud, as per Section 143(12) of the Companies Act, 2013.
12. Before concluding the audit, there was a difference of opinion between the audit committee and the auditors as to which among the following are the areas which the auditor should take into account to determine "Key Audit Matter" as per SA 701:
- (I) The effect on audit of significant transactions that took place in the FY.
 - (II) Areas of high risk as assessed and reported by management's expert.
 - (III) Significant auditor judgement relating to areas in the financials that involved significant management judgement.
- As per SA 701- Communicating Key audit matters in the Independent auditor's Report, which among the above-mentioned areas should CA & Co. take into account to determine "Key Audit Matter"?
- (a) (I) & (III)

- (b) (II) only
- (c) (I) & (II)
- (d) (I), (II) & (III)

PART B : DESCRIPTIVE QUESTIONS

Standards on Auditing, Statements and Guidance Notes

13. (a) MEA Limited is a listed company having its operation across India. MEA Limited appointed Mr. X, Mr. Y and Mr. Z, as its joint auditors for the year 2019-20. After making sure that all of them are qualified to be appointed as statutory auditor, MEA Limited issued engagement letter to all of them. But Mr. X was not clear on some points, so he requested MEA Limited to slightly change the terms of his engagement. This change will not impact the ultimate opinion on the financial statement. The engagement letter contains the details on objective and scope of audit, responsibilities of auditor and identification of framework applicable. It also contains the reference to expected form and content of report from all three joint auditors. In your opinion what was the discrepancy in the Audit engagement letter issued by MEA Limited?

- (b) ENN Limited is availing the services of APP Private Limited for its payroll operations. Payroll cost accounts for 65% of total cost for ENN Limited. APP Limited has provided the type 2 report as specified under SA 402 for its description, design and operating effectiveness of control.

APP Private Limited has also outsourced a material part of payroll operation M/s SMP & Associates in such a way that M/s SMP & Associates is sub-service organization to ENN Limited. The Type 2 report which was provided by APP Private Limited was based on carve-out method as specified under SA 402.

CA Raman while reviewing the unmodified audit report drafted by his assistant found that, a reference has been made to the work done by the service auditor. CA Raman hence asked his assistant to remove such reference and modify report accordingly.

Comment whether CA Raman is correct in removing the reference of the work done by service auditor?

The Company Audit & Audit Report

14. (a) Petro Ltd. is engaged in generation of electricity for captive consumption through Captive Generating Plant. The Company also maintains cost records in its books of account as required under Cost Records and Audit Rules. Mr. Xylo, friend of Managing Director of the Company, suggested name of his brother, who is a Cost Accountant in Practice, for the purpose of cost audit. However, the statutory auditor of the company, is of the view that the Company is not legally required to conduct cost audit. Now, the Managing Director is in dilemma about the requirement of cost audit. Being an expert in cost records and audit rules, you are required to guide in this regard.

- (b) AKB Associates, a renowned audit firm in the field of CA practice for past two decades. The firm was appointed to conduct statutory audit of Rica Ltd. an unlisted company, which is engaged in the business of paper manufacturing. It decided to commence the audit for the recently concluded financial year. Once after making significant progress in the audit, the auditors made the following observations:

Observation 1: The management had disclosed in the financials that, during the year, one of the warehouses of the Company was affected due to a major flood. As a result of the same, the Company had incurred some losses. But the management was of the view that it was not material.

Observation 2: Due to flood, few records maintained by the Company with respect to a particular transaction was completely destroyed and there was no duplicate record maintained by the Company. However, those details were not pervasive, but material.

You are required to advise, whether AKB Associates should report Observation 1 and 2 in its audit report? If so, under which heading should it be reported?

Audit Committee and Corporate Governance

15. M/s FCA & Associates, Chartered Accountants is one of the leading auditing firms in Guwahati. The firm received an assignment to examine the compliance conditions [as stated in SEBI (LODR) Regulations] of corporate governance by ABC Ltd., a listed entity with no outstanding SR equity shares. The firm had made the following observations:

Observation No. 1: Mr. Fine, one of the Director of the Company, also the Chairman of the Stakeholder Relationship Committee, was acting as the audit committee Chairman in 4 other listed companies as well & 1 private company, simultaneously.

Observation No. 2: The Nomination & Remuneration Committee consisted of 6 members, which regularly met biannually.

Observation No. 3: The Risk Management Committee consisted of 9 directors, out of which, the number of independent directors is the majority, but it was less than two thirds of the total strength.

Which among the above three observations made by the auditor of ABC Ltd. should be reported by M/s. FCA & Associates?

Audit of Banks & Insurance Company

16. (a) ABN Bank was engaged in the business of providing Portfolio Management Services to its customers, for which it took prior approval from RBI. Your firm has been appointed as the statutory auditors of the Bank's financial statements for the year 2019-20. Your senior has instructed you to verify the transactions of Portfolio Management Services (PMS). While verifying the transactions you noticed that the bank has not maintained separate record for PMS transactions from the Bank's own investments. As a statutory auditor what methodology will be adopted by you for

verification of PMS transactions?

- (b) M/s MPS & Associates, Chartered Accountants started the statutory audit of their client Contingencies Ltd., a General Insurance company, which has a paid-up capital of ₹ 16,800/- lac. During the course of the audit, it was found that the Company was not maintaining the required solvency margin as per the provisions of Insurance Act, 1938. When the issue was escalated to the management, they replied that solvency margin needs to be maintained as per limits prescribed only on last day of the financial year. Comment whether reply of management is tenable or not.

Audit under Fiscal Laws

17. (a) M/s PQRS & Associates is appointed for conducting tax audit as per Income Tax Act, 1961 of QW Ltd., a cotton textile company. The Company had incurred ₹ 6 lac towards advertisement expenditure on a brochure/ pamphlet published by a political party in Pune. Advise the auditor whether such expenditure should be included in the tax audit report or not.
- (b) Mr. Ramanuj, a Chartered Accountant by profession, has been appointed as GST auditor for ABC Ltd. The management has asked Mr. Ramanuj for GST audit and to file GSTR-3B for the months of July and August 2019 and filing of annual return in FORM GSTR-9. Mr. Ramanuj contended that he has been appointed only for GST audit and the above are his scope limitations and cannot be conducted as the compliances and returns are to be filed by the management. In context of above dispute, you have to suggest whether the contention of Mr. Ramanuj is correct or not. Justify.

Due Diligence, Investigation and Forensic Audit

18. APK Bank Ltd., received an application from a Pharmaceutical Company for takeover of their outstanding term loans secured on its assets, availed from and outstanding with a nationalised bank. APK Bank Ltd., requires you to conduct a due diligence audit in the areas of assets of Pharmaceutical Company especially with reference to valuation aspect of assets. State what may be your areas of analysis in order to ensure that the assets are not stated at overvalued amounts.

Professional Ethics

19. Comment on the following with reference to the Chartered Accountants Act, 1949 and schedules thereto:
- (a) CA. Srishti and CA. Mishti are two partners of the CA firm 'Srishti Mishti & Associates'. Being very pious, CA. Srishti organised a religious ceremony at her home for which she instructed her printing agent to add her designation "Chartered Accountant" with her name in the invitation cards. Later on, the invitations were distributed to all the relatives, close friends and clients of both the partners.

- (b) Ms. Preeto, a CA, had an account with a bank. The normal balance in this account remained at a level below ₹ 5,000. The bank inadvertently credited this account with a cheque of ₹ 2,70,000 belonging to another account holder. When CA. Preeto came to know about this she withdrew the amount of ₹ 2,75,000 and closed the bank account. After 1 year the bank noticed the mistake and claimed ₹ 2,75,000 with interest. CA. Preeto contested this claim. Can the bank approach the Institute of Chartered Accountants of India for disciplinary action against CA. Preeto?
- (c) CA. Moni is practicing since 2009 in the field of company audit. Due to her good practical knowledge, she was offered editorship of a 'Company Audit' Journal which she accepted. However, she did not take any permission from the Council regarding such editorship.
20. Write a short note on the following:
- (a) Selection of sample by the reviewer in case of peer review.
 - (b) Classification of frauds by NBFC.
 - (c) General steps in the conduct of risk based audit.
 - (d) Contents of an audit plan.

SUGGESTED ANSWERS/HINTS

PART A : ANSWERS TO MULTIPLE QUESTIONS

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

PART B

13. (a) **Agreement on Audit Engagement Terms** : As per SA 210, "Agreeing the Terms of Audit Engagements", the auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate.

Subject to prescribed details under Law or Regulations, the agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include:

- (i) The objective and scope of the audit of the financial statements;
- (ii) The responsibilities of the auditor;
- (iii) The responsibilities of management;
- (iv) Identification of the applicable financial reporting framework for the preparation of the financial statements; and
- (v) Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

In the given scenario, MEA Limited appointed Mr. X, Mr. Y and Mr. Z, as its joint auditors for the year 2019-20 and issued engagement letter to all of them. The engagement letter contains the details on objective and scope of audit, responsibilities of auditor, identification of framework applicable and reference to expected form and content of report from all three joint auditors. However, engagement letter issued by MEA Ltd. doesnot specify the responsibilities of management, whereas as per SA 210, it should also specify responsibilities of management.

- (b) **Reporting by the User Auditor**: As per SA 402, "Audit Considerations Relating to an Entity Using a Service Organisation", the user auditor shall modify the opinion in the user auditor's report in accordance with SA 705, "Modifications to the Opinion in the Independent Auditor's Report", if the user auditor is unable to obtain sufficient appropriate audit evidence regarding the services provided by the service organisation relevant to the audit of the user entity's financial statements.

The user auditor shall not refer to the work of a service auditor in the user auditor's report containing an unmodified opinion unless required by law or regulation to do so. If such reference is required by law or regulation, the user auditor's report shall indicate that the reference does not diminish the user auditor's responsibility for the audit opinion.

Thus, in view of above, contention of CA. Raman in removing reference of the work done by service auditor is in order as in case of unmodified audit report, user auditor cannot refer to the work done by service auditor.

14. (a) **Applicability of Provisions related to Cost Records and Audit:** The provisions relating to cost records and audit are governed by section 148 of the Companies Act, 2013 read with the Companies (Cost Records and Audit) Rules, 2014. The audit conducted under this section shall be in addition to the audit conducted under section 143.

Rule 3 of the Companies (Cost Records and Audit) Rules, 2014 provides the classes of companies, engaged in the production of goods or providing services, required to include cost records in their books of account.

However, the requirement for cost audit under these rules shall not be applicable to a company which is covered under Rule 3, and,

- (i) whose revenue from exports, in foreign exchange, exceeds 75 per cent of its total revenue; or
- (ii) which is operating from a special economic zone.
- (iii) which is engaged in generation of electricity for captive consumption through Captive Generating Plant.

In the given case, Petro Ltd. is engaged in generation of electricity for captive consumption through Captive Generating Plant. Therefore, Petro Ltd. is not required to conduct cost audit as it is falling under the exemption criteria. Hence, the opinion of statutory auditor of the Company regarding non-applicability of cost audit is correct.

- (b) **Observation 1 - The management had disclosed in the financials that, during the year, one of the warehouses of the Company was affected due to a major flood. As a result of the same, the Company had incurred some losses. But the management was of the view that it was not material:** As per SA 706, "Emphasis of Matter Paragraph & Other Matter Paragraph in the Independent Auditor's Report", an Emphasis of Matter Paragraph refers to matter appropriately disclosed in the financials, that in the auditor's judgement is of such importance that it is fundamental to users' understanding of the financials. Hence, in this case, the auditor shall report about the consequences of the flood which affected the Company's warehouse under Emphasis of Matter Paragraph.

Observation 2 - Due to flood, few records maintained by the Company with respect to a particular transaction was completely destroyed and there was no duplicate record maintained by the Company. However, those details were not pervasive, but material: As per SA 705, "Modification to Opinion in the Independent Auditor's Report", where the auditor is unable to obtain sufficient and appropriate audit evidence and where such matter is material but not pervasive, the auditor shall issue a qualified opinion.

Thus, in the given situation, on account of flood few records pertaining to particular transactions was completely destroyed and in the absence of duplicate records, the auditor was unable to obtain sufficient and appropriate audit evidence and those

details were material but not pervasive. Therefore, in accordance with SA 705, the auditor is required to issue qualified opinion.

15. **Observation No. 1 - Mr. Fine, one of the Director of the Company, also the Chairman of the Stakeholder Relationship Committee, was acting as the Audit committee Chairman as well in 4 other listed companies & 1 private Company, simultaneously:** As per Regulation 26 of SEBI (LODR) Regulations, a Director cannot be a Chairman in more than 5 committees across all listed entities. However, for the purpose of reckoning the limit under this Regulation, chairmanship of committees in a private company shall be excluded. In this case, since Mr. Fine is the Chairman of audit committee in ABC Ltd. and Chairman in 4 other listed companies, there is no violation of the limit specified under the Regulation 26. Accordingly, **this observation need not be reported by the auditor.**

Observation No. 2: The Nomination & Remuneration Committee consisted of 6 members, who regularly met biannually: As per Regulation 19, Part D of Schedule II of SEBI (LODR) Regulations, every listed company should have a Nomination & Remuneration Committee, which shall meet at least once in a year. **Since, in the given case the committee met biannually (i.e. once in 2 years), the said observation needs to be reported by the auditor.**

Observation No. 3: The Risk Management committee consisted of 9 directors, out of which the number of independent directors is the majority, but it was less than two thirds of the total strength: As per Regulation 21 of SEBI (LODR) Regulations, only in case of a listed entity having outstanding SR equity shares, at least two thirds of Risk Management Committee shall comprise of independent directors. In the given case, ABC Ltd. does not have outstanding SR equity shares. **Accordingly, this observation need not be reported by the auditor.**

Thus, in the given scenario, only observation 2 will be reported.

16. (a) **Separation of Investment Functions:** The auditor needs to examine whether the bank, as required by the RBI, is maintaining separate accounts for the investments made by it on their own Investment Account, PMS clients' account, and on behalf of other Constituents (including brokers). As per the RBI guidelines, banks are required to get their investments under PMS separately audited by external auditors.

Thus, in the instant case, ABN Bank is required to prepare separate records for PMS and as per RBI guidelines PMS investments need to be audited separately by the external auditors and the auditors are required to give a certificate separately for the same. So, in the above case the auditor should not verify the PMS transactions and advise the bank to segregate the PMS transactions from its own investments and provide the certificate of external auditor as described above. In case ABN Bank does not provide the same the auditor may report accordingly.

- (b) **Maintenance of Solvency Margin:** Section 64VA of the Insurance Act, 1938 as amended by Insurance Laws (Amendment) Act, 2015 requires every insurer and re-insurer to maintain an excess of the value of assets over the amount of liabilities at all times which shall not be less than 50% of the amount of minimum capital as stated under section 6 (requirement as to capital) of the Act and arrived at in the manner specified by the regulations.

If, at any time, an insurer or re-insurer does not maintain the required control level of solvency margin, he is required to submit a financial plan to the Authority indicating the plan of action to correct the deficiency. If, on consideration of the plan, the Authority finds it inadequate, the insurer has to modify the financial plan.

Sub-section (2) of section 64VA states that if an insurer or re-insurer fails to comply with the prescribed requirement of maintaining excess of value of assets over amount of liabilities, it shall be deemed to be insolvent and may be wound up by the Court on an application made by the authority.

Therefore, in the said case Contingencies Ltd has not maintained the Solvency Margin throughout the year. Accordingly, contention of Contingencies Ltd. that solvency margin is required to be maintained as per limits prescribed only on last day of the financial year is not tenable.

17. (a) **Expenses on Advertisement in the Media of a Political Party:** In the given situation, M/s PQRS & Associates is appointed for conducting tax audit as per Income Tax Act, 1961 of QW Ltd., a cotton textile company. The Company had incurred ₹ 6 lac towards advertisement expenditure on a brochure/ pamphlet published by a political party.

As per Clause 21(a) of Form 3CD, the auditor is required to furnish the details of amounts debited to the Profit and Loss Account, being in the nature of advertisement expenditure in any souvenir, brochure, tract, pamphlet or the like published by a political party in his tax audit report.

Therefore, advertisement expenditure of ₹ 6 lac on brochure/pamphlet published by a political party shall be reported in the tax audit report as per Clause 21 (a) of Form 3CD.

- (b) **Responsibility of Compliances and filing of Returns:** GST auditor's prime responsibility on this engagement is limited to GST audit, audit of reconciliation statement between books of accounts *vis-a-vis* GST returns prepared by the Company. The GST auditor is, however, not responsible for any compliances like uploading GST periodic returns for the relevant audit period.

Since, in the given situation, Management has asked the auditor Mr. Ramanuj to conduct besides GST Audit filing of GSTR-3B for the months of July and August 2019 and filing of annual return in FORM GSTR-9.

Accordingly, Mr. Ramanuj has rightly refused that his scope is limited to GST Audit and the scope does not cover any of the management functions.

In view of above, **Contention of Management to Ramanuj is not tenable** as preparation of annual returns and its filing was the responsibility of management.

18. **Over-Valued Assets** : The areas of analysis in order to ensure that the assets are not stated at overvalued amounts during conduct of Due Diligence are:

- ✍ Uncollected/uncollectable receivables.
- ✍ Obsolete, slow non-moving inventories or inventories valued above NRV; huge inventories of packing materials etc. with name of company.
- ✍ Underused or obsolete Plant and Machinery and their spares; asset values which have been impaired due to sudden fall in market value etc.
- ✍ Assets carried at much more than current market value due to capitalization of expenditure/foreign exchange fluctuation, or capitalization of expenditure mainly in the nature of revenue.
- ✍ Litigated assets and property.
- ✍ Investments carried at cost though realizable value is much lower.
- ✍ Investments carrying a very low rate of income / return.
- ✍ Infertuous project expenditure/deferred revenue expenditure etc.
- ✍ Group Company balances under reconciliation etc.
- ✍ Intangibles of no value.

19. (a) **Printing of Designation “Chartered Accountant” on Invitations for Religious Ceremony**: As per Clause (6) of Part I of the First Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice shall be deemed to be guilty of professional misconduct if he solicits clients or professional work either directly or indirectly by circular, advertisement, personal communication or interview or by any other means.

However, the Council of the ICAI is of the view that the designation “Chartered Accountant” as well as the name of the firm may be used in greeting cards, invitations for marriages, religious ceremonies and any other specified matters, provided that such greeting cards or invitations etc. are sent only to clients, relatives and close friends of the members concerned.

In the given case, CA. Srishti has instructed to write designation “Chartered Accountant” on invitation cards for a religious ceremony and distributed the same to all the relatives, close friends and clients of both the partners.

In this context, it may be noted that the Council has allowed using designation “Chartered Accountant” in invitations for religious ceremony, provided these are sent to clients, relatives and close friends of the members concerned only.

Therefore, CA. Srishti would be held guilty of professional misconduct under the said clause for sending such invitations to the relatives, close friends and clients of CA. Mishti as well.

- (b) **Disrepute to the Profession:** As per Clause 2 of Part IV of First Schedule of the Chartered Accountant Act, 1949, a Chartered Accountant will be deemed to be guilty of other misconduct if he in the opinion of the Council brings disrepute to the profession or the Institute as a result of his action whether or not related to his professional work.

In the instant case, CA. Preeto, a CA, had an account with a bank from which she withdrew the amount of ₹ 2,75,000 and closed the account. This amount of ₹ 2,75,000 was pertaining to ₹ 5,000 minimum balance and ₹ 2,70,000 belonging to other account holder and inadvertently credited to his account by the bank. The said act of CA. Preeto to withdraw the money which does not belongs to her will bring disrepute to the profession. Hence under this clause the bank can file a suitable complaint under Clause 2 of Part IV of First Schedule of the Chartered Accountant Act, 1949 with the Institute of Chartered Accountants of India.

- (c) **Permission from the Council:** As per Clause (11) of Part I of First Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice will be deemed to be guilty of professional misconduct if he engages in any business or occupation other than the profession of Chartered Accountant unless permitted by the Council so to engage.

However, the Council has granted general permission to the members to engage in certain specific occupation. In respect of all other occupations specific permission of the Institute is necessary.

In the instant case, CA. Moni accepted editorship of a journal for which she did not take any permission from the Council. In this context, it may be noted that the editorship of professional journals is covered under the general permission and specific permission is not required.

Therefore, CA. Moni shall not be held guilty of professional misconduct in terms of Clause (11) of Part I of First Schedule to the Chartered Accountants Act, 1949.

20. (a) Selection of Sample by the Reviewer in case of Peer Review:

- (i) The Reviewer shall within 15 days of receiving the information from the Practice Unit select a sample of the assurance services that he would like to Review and intimate the same to the Practice Unit.

- (ii) The Reviewer may also seek further / additional clarification from the Practice Unit on the information furnished / not furnished.
 - (iii) The Reviewer shall plan for an on-site Review visit or initial meeting in consultation with the Practice Unit. The Reviewer shall give the Practice Unit at least fifteen days' time to keep ready the necessary records of the selected assurance services.
 - (iv) The Reviewer and Practice Unit shall mutually cooperate and ensure that the entire Review process is completed within 90 days from the date of notifying the Practice Unit about its selection for Review.
- (b) **Classification of Frauds by NBFC:** In order to have uniformity in reporting, frauds have been classified as under based mainly on the provisions of the Indian Penal Code:
- (i) Misappropriation and criminal breach of trust.
 - (ii) Fraudulent encashment through forged instruments, manipulation of books of account or through fictitious accounts and conversion of property.
 - (iii) Unauthorised credit facilities extended for reward or for illegal gratification.
 - (iv) Negligence and cash shortages.
 - (v) Cheating and forgery.
 - (vi) Irregularities in foreign exchange transactions.
 - (vii) Any other type of fraud not coming under the specific heads as above.
- Cases of 'negligence and cash shortages' and 'irregularities in foreign exchange transactions'** referred to in items (d) and (f) above are to be reported as fraud if the intention to cheat/ defraud is suspected/ proved. However, the following cases where fraudulent intention is not suspected/ proved, at the time of detection, will be treated as fraud and reported accordingly:
- (I) cases of cash shortages more than ₹ 10,000/- and
 - (II) cases of cash shortages more than ₹ 5000/- if detected by management/ auditor/ inspecting officer and not reported on the occurrence by the persons handling cash.

- (c) **General Steps in the Conduct of Risk Base Audit:** RBA consists of four main phases starting with the identification and prioritization of risks, to the determination of residual risk, reduction of residual risk to acceptable level and the reporting to auditee of audit results. These are achieved through the following:

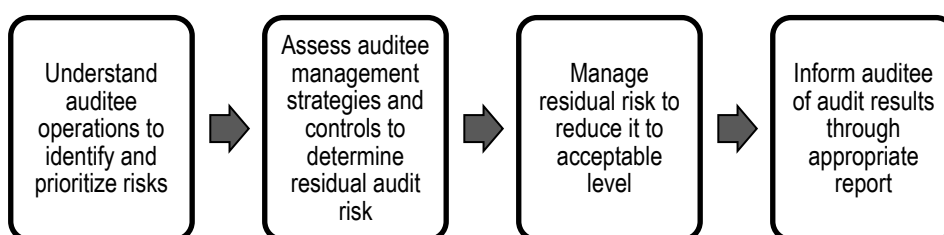
Step 1 Understand auditee operations to identify and prioritize risks: Understanding auditee operations involves processes for reviewing and understanding the audited organization's risk management processes for its

strategies, framework of operations, operational performance and information process framework, in order to identify and prioritize the error and fraud risks that impact the audit of financial statements. The environment in which the auditee operates, the information required to monitor changes in the environment, and the process or activities integral to the audited entity's success in meeting its objectives are the key factors to an understanding of agency risks. Likewise, a performance review of the audited entity's delivery of service by comparing expectations against actual results may also aid in understanding agency operations.

Step 2 Assess auditee management strategies and controls to determine residual audit risk: Assessment of management risk strategies and controls is the determination as to how controls within the auditee are designed. The role of internal audit in promoting a sound accounting system and internal control is recognized, thus the SAI should evaluate the effectiveness of internal audit to determine the extent to which reliance can be placed upon it in the conduct of substantive tests.

Step 3 Manage residual risk to reduce it to acceptable level: Management of residual risk requires the design and execution of a risk reduction approach that is efficient and effective to bring down residual audit risk to an acceptable level. This includes the design and execution of necessary audit procedures and substantive testing to obtain evidence in support of transactions and balances. More resources should be allocated to areas of high audit risks, which were earlier known through the analytical procedures undertaken.

Step 4 Inform auditee of audit results through appropriate report: The results of audit shall be communicated by the auditor to the audited entity. The auditor must immediately communicate to the auditee reportable conditions that have been observed even before completion of the audit, such as weaknesses in the internal control system, deficiencies in the design and operation of internal controls that affect the organization's ability to record, process, summarize and report financial data.



(d) **Contents of an Audit Plan:** The auditor shall develop an audit plan that shall include a description of-

- (i) The nature, timing and extent of planned risk assessment procedures, as determined under SA 315 "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment".

- (ii) The nature, timing and extent of planned further audit procedures at the assertion level, as determined under SA 330 "The Auditor's Responses to Assessed Risks".
- (iii) Other planned audit procedures that are required to be carried out so that the engagement complies with SAs.

The audit plan is more detailed than the overall audit strategy that includes the nature, timing and extent of audit procedures to be performed by engagement team members. Planning for these audit procedures takes place over the course of the audit as the audit plan for the engagement develops. For example, planning of the auditor's risk assessment procedures occurs early in the audit process. However, planning the nature, timing and extent of specific further audit procedures depends on the outcome of those risk assessment procedures. In addition, the auditor may begin the execution of further audit procedures for some classes of transactions, account balances and disclosures before planning all remaining further audit procedures.