

WT 1 (Ch. 1 – Quality Control & Ch. 2 – General Auditing Principles)

Instructions: Part A comprises of MCQ.

Part B comprises of descriptive questions.

Part – A (Multiple Choice Questions)

- Q.1** (b) (2 Marks)
Q.2 (d) (2 Mark)
Q.3 (c) (1 Mark)
Q.4 (d) (1 Mark)
Q.5 (b) (1 Mark)

Part B (Descriptive Questions)

Q. No. 1 is Compulsory. Attempt Any two from the rest.

Q.1(a): Issues to be addressed before withdrawing from audit engagement:

As per SQC 1, “Quality Control for Firms that Perform Audit and Reviews of Historical Financial Information, and other Assurance and Related Services Engagements”, firm should establish the policies w.r.t. withdrawal from engagement and communication requirements, if circumstances warrant. Policies and procedures on withdrawal from an engagement or from both the engagement and the client relationship address issues that include the following:

- (i) Discussing with the appropriate level of mngt. & TCWG regarding the appropriate action that the firm might take based on the relevant facts and circumstances. (1 Mark)
- (ii) If the firm determines that it is appropriate to withdraw, discussing with the appropriate level of the client’s management and TCWG withdrawal from the engagement or from both the engagement and the client relationship, and the reasons for the withdrawal. (1 Mark)
- (iii) Considering whether there is a professional, regulatory or legal requirement for the firm to remain in place, or for the firm to report the withdrawal from the engagement, or from both the engagement and the client relationship, together with the reasons for the withdrawal, to regulatory authorities. (1 Mark)
- (iv) Documenting significant issues, consultations, conclusions and the basis for the conclusions. (1 Mark)

Q.1(b): Responsibilities of Joint Auditors w.r.t. Common Areas of working:

- As per SA 299 "Joint Audit of Financial Statements", in respect of common areas, joint auditors are only responsible for appropriateness of NTE of planned audit procedures agreed among them. **(1 Mark)**
- The responsibility of individual execution lies with concerned joint auditor. **(1 Mark)**
- In the instant case, audit procedures relating to testing design and operating effectiveness of controls over computer operations including back-up, batch-processing and data center security have been planned jointly as it is a common area. However, audit procedures relating to testing controls over batch processing were actually performed by team of DES & Associates although these were planned jointly. **(1 Mark)**

Conclusion: In case of any lapses in performing such procedures, DES & Associates would be responsible.

(1 Mark)

Q.2: Auditor's responsibilities relating to Fraud in an audit of F.S.:

- SA 240, "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements," emphasize that fraud can be perpetrated by management override of controls, such as the creation of fictitious journal entries, particularly towards the end of an accounting period, to manipulate operating results or achieve specific objectives. **(1 Mark)**
- In the case of Supreme Ltd., where purchases of ₹ 1.50 crore were recorded at year-end without supporting evidence, it became apparent during the investigation that the company had entered fictitious journal entries to manipulate the operating results. **(1 Mark)**
- Given this situation, the auditor would align their approach based on the impact of the misstatement resulting from such fictitious journal entries. If, due to fraud or suspected fraud, the auditor encounters exceptional circumstances that cast doubt on their ability to continue the audit, they must assess the professional and legal responsibilities applicable. This includes considering reporting obligations to those who appointed the auditor or, in some cases, to regulatory authorities. The appropriateness of withdrawal from the engagement is also a consideration, where legally permitted. **(1 Mark)**
- Furthermore, the auditor is mandated to report in accordance with Section 143(12) of the Companies Act, 2013. According to Section 143(12) read with Rule 13 of Companies (Audit & Auditor's) Rules, 2014, if the auditor, during the performance of their duties, has reason to believe that an offence of fraud involving an amount of ₹ 1 crore or more has been committed by the company's officers or employees, reporting to the Central Government is required in the prescribed manner. **(1 Mark)**
- Additionally, reporting obligations extend to Clause (xi) of Paragraph 3 of Companies (Auditor's Report) Order, 2020. The auditor is obligated to disclose whether any fraud by the company or against the company by its officers or employees has been observed or reported during the year. If affirmative, the nature and amount involved are to be indicated. This comprehensive reporting framework ensures transparency, adherence to legal requirements, and protection of stakeholders' interests in the face of potential fraudulent activities. **(1 Mark)**

Q.3(a): Potential effects of inherent limitations on the auditor's ability to detect material misstatements in respect of non-compliance with laws and regulations:

Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements in the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the SAs.

In the context of laws and regulations, the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for such reasons as the following:

- There are many laws and regulations, relating principally to the operating aspects of an entity that typically do not affect the financial statements and are not captured by the entity's information systems relevant to financial reporting. **(1 Mark)**
- Non-compliance may involve conduct designed to conceal it, such as collusion, forgery, deliberate failure to record transactions, management override of controls or intentional misrepresentations being made to the auditor. **(1 Mark)**
- Whether an act constitutes non-compliance is ultimately a matter for legal determination by a court of law. **(1 Mark)**

Q.3(b): Functions of QRB:

- (a) To make recommendations to the Council regarding the quality of services provided by the members of the Institute;
- (b) To review the quality of services provided by the members of the Institute including audit services and
- (c) To guide the members of the Institute to improve the quality of services and adherence to the various statutory and other regulatory requirements.

(1 Mark for each correct Point – Any Two)

Q.4(a): Matters to be taken care of while determining sufficiency and appropriateness of the audit evidence provided by a Type 1 or Type 2 report:

In determining the sufficiency and appropriateness of the audit evidence provided by a Type 1 or Type 2 report, the user auditor shall be satisfied as to:

- (a) The service auditor's professional competence (except where the service auditor is a member of the ICAI) and independence from the service organisation; and **(1 Mark)**
- (b) The adequacy of the standards under which the Type 1 or Type 2 report was issued. **(1 Mark)**

Q.4(b): Audit procedures, if auditor plans to use a Type 1 or Type 2 report as audit evidence to support his understanding about the design and implementation of controls at the service organisation:

- (a) Evaluate whether the description and design of controls at the service organisation is at a date or for a period that is appropriate for the user auditor's purposes; **(1 Mark)**
- (b) Evaluate the sufficiency and appropriateness of the evidence provided by the report for the understanding of the user entity's internal control relevant to the audit; and **(1 Mark)**
- (c) Determine whether complementary user entity controls identified by service organisation are relevant to the user entity and, if so, obtain an understanding of whether the user entity has designed and implemented such controls. **(1 Mark)**



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