## WT 5 (Ch. 7 – Completion and Review and Ch. 8 – Audit Reports)

**Instructions:** **Part A comprises of MCQ.**

**Part B Comprises of descriptive questions.**

---

## Part – A (Multiple Choice Questions)

Q.1 (c) (2 Marks)

Q.2 (c) (2 Marks)

Q.3 (c) (2 Marks)

## Part B (Descriptive Questions)

**Q.1 (a) Financial events or conditions that may cast significant doubt on the entity's ability to continue as going concern:**

(1) Net liability or net current liability position.

(2) Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment; or excessive reliance on short-term borrowings to finance long-term assets.

(3) Indications of withdrawal of financial support by creditors.

(4) Negative operating cash flows indicated by historical or prospective financial statements.

(5) Adverse key financial ratios.

(6) Substantial operating losses or significant deterioration in the value of assets used to generate cash flows.

(7) Arrears or discontinuance of dividends.

(8) Inability to pay creditors on due dates.

(9) Inability to comply with the terms of loan agreements.

(10) Change from credit to cash-on-delivery transactions with suppliers.

(11) Inability to obtain financing for essential new product development or other essential investments.

**1 Mark for each Correct Point (Any Three)**

**(b)** DOX Limited is in business of providing courier services.

As name of the company and given facts suggest: -

- It is not a small company under section 2(85) of Companies Act, 2013.
- It is not a private company.

- It is not a one person company.
- It is not a banking or insurance company.
- It is not a Section 8 company as it does not have charitable objects etc.

Therefore, it does not qualify for any exemption from applicability of CARO, 2020. Hence, reporting requirements under CARO, 2020 are applicable. **(1 Mark)**

While reporting under CARO, 2020, statutory auditor is required to report under clause (xiv) of paragraph 3 as under:

(a) whether the company has an internal audit system commensurate with the size and nature of its business; **(1 Mark)**

(b) whether the reports of the internal auditors for the period under audit were considered by the statutory auditor. **(1 Mark)**

**Q.2 Audit procedures w.r.t. Subsequent Events:**

In the given situation, a huge fire had broken out in one of plants of company on 25th June, 2023 destroying substantial part of machinery and work-in-process resulting in loss of ₹ 5 crores. The auditor has yet to sign audit report.

Before signing audit report, he should perform following audit procedures to obtain sufficient appropriate audit evidence that all such events have been identified and are appropriately reflected in financial statements: -

- Inquiry of management whether any subsequent events have occurred
- Reading minutes of the meetings of owners, management that have been held after date of financial statements and inquiring about matters discussed at such meetings for which minutes are not available
- Reading entity's latest subsequent interim financial statements
- Obtaining Written representations from management in accordance with SA 580

**1 Mark for each Correct Point (Any Three)**

The situation is an example of subsequent event occurring between date of financial statements and date of audit report requiring disclosure in financial statements. The auditor has a responsibility to obtain sufficient appropriate audit evidence whether such an event requiring disclosure in financial statements is appropriately reflected in financial statements. **(1 Mark)**

**Q.3 Responsibilities of Auditor to communicate with Management:**

The above situation is an example of misstatement relating to noncompliance with requirements of AS 9 identified during audit.

In accordance with requirements of SA 450, the auditor shall communicate on a timely basis all misstatements accumulated during the audit with the appropriate level of management, unless prohibited by law or regulation. The auditor shall request management to correct those misstatements.

Timely communication of misstatements to the appropriate level of management is important as it enables management to evaluate whether the items are misstatements, inform the auditor if it disagrees and take action as necessary. The correction by management of all misstatements, including those communicated by the auditor, enables management to maintain accurate accounting books and records and reduces the risks of material misstatement of future financial statements because of the cumulative effect of immaterial uncorrected misstatements related to prior periods. **(2 Marks)**

If management refuses to correct some or all of the misstatements communicated by the auditor, the auditor shall obtain an understanding of management's reasons for not making the corrections and shall take that understanding into account when evaluating whether the financial statements as a whole are free from material misstatement. **(2 Marks)**

**Q.4 Limitation after Auditor has accepted the Engagement:**

In the given case, auditor has not been able to obtain sufficient appropriate audit evidence relating to inventories, debtors, creditors, revenues and expenses. The matter was brought to the knowledge of management but no result has been achieved. In such circumstances, auditor should proceed as given here under:

If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall:

(i) Withdraw from the audit, where practicable and possible under applicable law or regulation; or

(ii) If withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements. **(3 Marks)**

If auditor withdraws from such an engagement, before withdrawing, auditor shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion. **(1 Mark)**