

CA Final Paper 5 – Auditing & Ethics

Suggested Answers: May 2025 Exams (Part II – Descriptive Questions)

Question 1

- (a) M/s YZW & Co., Chartered Accountants, have been appointed as the statutory auditors of First Health Private Limited for the financial year 2024-25. CA Y is the engagement partner for this assignment. First Health Private Limited operates in the business of hospitals and pharmaceuticals, with 60 hospitals and 200 pharmacy stores across the country. The company has a turnover of ₹ 680 crores and PAT of 32 crores in the current year.
- While verifying the assertions about book debts, CA Y was informed about the availability of the client's ledger invoices, debit notes, and credit notes as audit evidence. CA Y accepts these documents as audit evidence, considering them to be "available."
- (i) Is this decision correct, based on the meaning of the term "available"? (3 Marks)
- (ii) Also, explain how an auditor should select the most appropriate evidence when testing the accuracy of any assertion to form an opinion. (2 Marks)

Ans.: Audit Evidence:

- (i) The term "available" in the context of audit evidence simply means that the evidence exists and can be accessed by the auditor. However, availability alone does not determine whether the evidence is sufficient or appropriate. As per SA 500 "Audit Evidence", audit evidence must be both relevant and reliable to support the auditor's conclusions.

Appropriateness of audit evidence depends on its relevance to the financial statement assertions (e.g., completeness, accuracy, occurrence, valuation, and presentation of book debts) and its reliability, which is influenced by factors such as the source, nature, and circumstances under which the evidence is obtained. Ledger invoices, debit notes, and credit notes are internally generated documents; while these documents are useful for verifying book debts, they are considered less reliable than external evidence (e.g., customer confirmations, bank statements, or third-party payment records) because they are subject to management bias or potential manipulation.

Conclusion: CA Y's decision to accept ledger invoices, debit notes, and credit notes as audit evidence solely because they are "available" is not entirely correct. While these documents are a starting point and can be considered "available" evidence, their acceptance as sufficient and appropriate audit evidence requires further evaluation of their reliability and relevance to the assertions about book debts.

- (ii) **Selection of Most Appropriate Evidence:**

An auditor should select the most appropriate evidence when testing the accuracy of any assertion by considering the sufficiency and appropriateness of the audit evidence.

- (a) Sufficiency refers to the quantity of audit evidence required, which is influenced by:

- Materiality: More evidence is needed for material assertions.
- Risk of Material Misstatement (RoMM): Higher RoMM necessitates more evidence.

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	<ul style="list-style-type: none"> Size of Population: Smaller, homogeneous populations require less evidence compared to larger, heterogeneous ones. <p>(b) Appropriateness measures quality of audit evidence, focusing on its relevance and reliability. The reliability of evidence is affected by:</p> <ul style="list-style-type: none"> Source of the evidence (direct evidence is more reliable than indirect). Nature of the evidence (documentary evidence is more reliable than oral). Original documents are more reliable than photocopies. 																				
(b)	<p>Mention the types of control in an automated environment. (1 Mark)</p> <p>Identify the type of control in the following table in Column B against Column A which contains areas where controls are to be implemented in an automated environment.</p> <table> <tr> <th>Column A</th><th>Column B</th></tr> <tr> <td>Access security</td><td>?</td></tr> <tr> <td>Sequence number checks</td><td>?</td></tr> <tr> <td>Data centre and network operations</td><td>?</td></tr> <tr> <td>Mandatory data fields</td><td>?</td></tr> </table> <p style="text-align: right;">(4 Marks)</p> <p>Ans.: Types of Controls in an automated environment:</p> <p>Controls in an automated environment can be categorized as under:</p> <p>(A) General IT controls</p> <p>(B) Application controls</p> <p>(C) IT-dependent controls</p> <table> <tr> <th>Column A</th><th>Column B</th></tr> <tr> <td>Access security</td><td>General IT controls</td></tr> <tr> <td>Sequence number checks</td><td>Application controls</td></tr> <tr> <td>Data centre and network operations</td><td>General IT controls</td></tr> <tr> <td>Mandatory data fields</td><td>Application controls</td></tr> </table>	Column A	Column B	Access security	?	Sequence number checks	?	Data centre and network operations	?	Mandatory data fields	?	Column A	Column B	Access security	General IT controls	Sequence number checks	Application controls	Data centre and network operations	General IT controls	Mandatory data fields	Application controls
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(c)	<p>M/s BPA & Associates, Chartered Accountants, was appointed as the auditors of Nissan Ltd., a company with PAN-India presence, for the financial year 2023-24. The audit report was issued on August 20, 2024. Following the issuance of audit report, CA P instructed junior team member Mr. Y to assemble the final audit file and prepare the Completion Memorandum.</p> <p>(i) Explain the meaning and significance of a Completion Memorandum. (2 Marks)</p> <p>(ii) Team Member Y completed the assembly of the final audit file in March 2025 and handed it over to CA P. Was team member Y correct in his approach? (2 Marks)</p> <p>Ans.: (i) Meaning and Significance of Completion Memorandum:</p> <p>SA 230 "Audit Documentation" defines the term as "Record of audit procedures performed, relevant audit evidence obtained and the conclusions the auditor reached". Accordingly, auditor may consider it helpful to prepare and retain as part of the audit documentation a summary (known as a completion memorandum) that describes:</p>																				

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- (a) the significant matters identified during the audit and
- (b) how they were addressed.

Such a summary may facilitate effective and efficient reviews and inspections of the audit documentation, particularly for large and complex audits.

Preparation of such a summary may assist the auditor's consideration of the significant matters. Further, the preparation of such a summary may assist the auditor's consideration of the significant matters.

It may also help the auditor to consider whether, in light of the audit procedures performed and conclusions reached, there is any individual relevant SA objective that the auditor has not met or is unable to meet that would prevent the auditor from achieving the auditor's overall objective.

(ii) Assembly of Final Audit File:

- SA 230 requires that the auditor shall prepare audit documentation on a timely basis. Preparing sufficient and appropriate audit documentation on a timely basis helps to enhance the quality of the audit and facilitates the effective review and evaluation of the audit evidence obtained and conclusions reached before the auditor's report is finalized.
- SQC 1, however, requires auditor to complete assembly of final audit file in ordinarily not more than 60 days after the date of the auditor's report.
- In the given case, audit report for financial year 2023-24 was issued on August 20, 2024 and assembly of the final audit file was completed in March 2025.

Conclusion: Approach of team member Y is not correct as final audit file need to be assembled within 60 days from the date of the auditor's report.



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Question 2	
(a)	<p>Mention any three standards issued under authority of ICAI Council which are collectively known as 'Engagement Standards'. (3 Marks)</p> <p>Also mention the purpose of issue of these standards. (2 Marks)</p> <p>Ans.: Engagement Standards:</p> <p>The following Standards issued under authority of ICAI Council are collectively known as Engagement Standards:</p> <ol style="list-style-type: none"> (1) Standards on auditing (SAs) which apply in audit of historical financial information. (2) Standards on review engagements (SREs) which apply in review of historical financial information. (3) Standards on Assurance engagements (SAEs) which apply in assurance engagements other than audits and review of historical financial information. (4) Standards on Related Services (SRSs) which apply in agreed upon procedures to information, compilation engagements and other related service engagements. <p>Purpose of issue of these standards:</p> <p>The purpose of issue of these standards is to establish high quality standards and guidance in the areas of financial statement audits and in other types of assurance services.</p>
(b)	<p>Give five examples of operating events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern. (5 Marks)</p> <p>Ans.: Operating events or conditions:</p> <ol style="list-style-type: none"> (1) Management intentions to liquidate the entity or to cease operations (2) Loss of key management without replacement (3) Loss of a major market, key customer(s), franchise, license, or principal supplier(s) (4) Labour difficulties (5) Shortages of important supplies (6) Emergence of a highly successful competitor
(c)	<p>TS Ltd. has raised funds by issuing fully convertible debentures. These funds were raised for the expansion and diversification of the business. The company had clearly outlined in its board resolution that these funds will be used for business expansion and diversification purposes only. However, the company utilised these funds for repayment of long-term loans and advances rather than for the intended purpose of business growth and expansion.</p> <p>State the reporting responsibility of the auditor under paragraph 3, clause (x) of the Companies Auditor's Report Order, 2020 (CARO 2020). (4 Marks)</p> <p>Ans.: Reporting responsibility of the auditor under Para 3 (x) of CARO, 2020:</p> <ol style="list-style-type: none"> (i) Whether moneys raised by way of IPO or FPO (including debt instruments) during the year were applied for the purposes for which those are raised, if not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported; (ii) Whether the company has made any preferential allotment or private placement of shares or convertible debentures (fully, partially or optionally convertible) during the year and if so, whether the requirements of Sec. 42 and Sec. 62 of the Companies Act, 2013 have been complied with and the funds raised have been used for the purposes for which the funds were raised, if not, provide details in respect of amount involved and nature of noncompliance.

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Question 3

- (a) **LMN Ltd., a mid-sized manufacturing company, generates revenue primarily through the sale of consumer electronics in domestic and international market. The company reported sales of ₹ 2 crores in the Financial Year 2024-25. The company generates revenue through sale of standard electronics devices, customized product orders with specific delivery terms and extended warranties and after-sales services.**
- The auditor has to verify that all sales are accurately measured as per applicable accounting standards and correctly journalized, summarized and posted in the financial statements.**
- Explain the audit procedures to ensure the same. (5 Marks)**

Ans.: Audit Procedure to check that sales are accurately measured:

While checking sales of the client, the auditor has to ensure that all sales are accurately measured as per applicable accounting standards and correctly journalized, summarized, and posted. The auditor can perform the following procedures to ensure the same.

- (1) Trace a few transactions from inception to completion. (Examination in depth)
E.g.: Take few sales transaction, and check from the receipt of sales order to the payment of receivable balance, every underlying document to ensure if it is properly recorded at every stage and measured accurately taking into consideration all the incentives, discounts, if any. The recognition shall be according to the revenue recognition policy of the entity.
- (2) If the client is engaged in export sales, then compliance with AS 11 shall be ensured.
- (3) Auditor must understand client's operations and related GAAP issues *e.g.* point of sale revenue recognition vs. percentage of completion, wherever applicable.
- (4) Compare the rate of sales affected with related parties and review them for collectability, as well as whether they were properly authorized and the value of such transactions were reasonable and at arm's length.

- (b) **SA 701 "Communicating Key Audit Matters in the Auditor's Report" deals with the auditor's responsibility to communicate key audit matters in the auditor's report.**
- Explain the definition of Key Audit Matter and how an auditor will determine the Key Audit Matters? (5 Marks)**

Ans.: Key Audit Matters:

Definition: As per SA 701 "Communicating Key Audit matters in the Independent Auditor's Report" Key Audit Matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the F.S. of the current period. Key audit matters are selected from matters communicated with TCWG.

Determination of Key Audit Matters:

The auditor shall determine, from the matters communicated with TCWG, those matters that required significant auditor attention in performing the audit.

In making this determination, the auditor shall consider the following:

- (a) Areas of higher assessed RoMM, or significant risks identified in accordance with SA 315;
- (b) Significant auditor judgments relating to areas in the F.S. that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty;
- (c) The effect on the audit of significant events or transactions that occurred during the period.

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	The auditor shall determine which of the matters so determined above were of most significance in the audit of the F.S. of the current period and therefore are the key audit matters.
(c)	<p>Luck Ltd., a mid-sized manufacturing company, has approached CA S, a qualified Chartered Accountant, to conduct the audit for the financial year ended March 31, 2025. The company requests CA S to give acceptance for the audit so that audit can be commenced within time. With reference to SA 210, how the auditor will establish that whether the preconditions for an audit are present?</p> <p style="text-align: right;">(4 Marks)</p> <p>Ans.: Preconditions for an Audit:</p> <p>As per SA 210 “Agreeing the terms of Audit Engagement” before accepting audit engagement, auditor is required to ensure existence of preconditions. Accordingly, preconditions to be examined are:</p> <ul style="list-style-type: none">(a) Determine whether FRF to be applied in preparation of financial statements is acceptable; and(b) Obtain the agreement of management that it acknowledges and understands its responsibilities for followings:<ul style="list-style-type: none">(i) the preparation of the F.S. in accordance with the applicable FRF.(ii) exercising necessary internal control to enable the preparation of F.S. that are free from material misstatement, whether due to fraud or error.(iii) to provide the auditor with:<ul style="list-style-type: none">(a) access to all relevant information such as records, documentation and other matters;(b) additional information that the auditor may request from management for the purpose of the audit; and(c) unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.



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Question 4

- (a) CA Pari is conducting the audit of Heavy Ltd., a company with large number of customers which are generally small retail shop owners. While verifying sundry debtors, CA Pari assesses the risk of material misstatement (ROMM) as low and internal control is operating effectively.
- With reference to SA 505 (External Confirmations):**
- (i) Which type of confirmation request is most likely to be used by CA Pari in this scenario?
(1 Mark)
- (ii) What are the conditions necessary for using such a confirmation request effectively?
(4 Marks)

Ans.: External Confirmations:

- (i) In the given situation, Negative confirmation request is most likely to be used by CA Pari.
- Negative confirmation request:** A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.
- (ii) **Conditions that should be present to use Negative Confirmation requests:**
- Negative confirmations provide less persuasive audit evidence than positive confirmations. Accordingly, the auditor shall not use negative confirmation requests as the sole substantive audit procedure to address an assessed risk of material misstatement at the assertion level unless all of the following are present:
- (a) Auditor has assessed risk of material misstatement as low & has obtained sufficient appropriate audit evidence regarding the operating effectiveness of controls relevant to the assertion;
 - (b) The population of items subject to negative confirmation procedures comprises a large number of small, homogeneous, account balances, transactions or conditions;
 - (c) A very low exception rate is expected; and
 - (d) The auditor is not aware of circumstances or conditions that would cause recipients of negative confirmation requests to disregard such requests.

- (b) M/s ABC & Co., Chartered Accountants, have been appointed as the statutory auditors of DEF Ltd., which is a listed company, for the Financial Year 2024-25. CA X, a seasoned Chartered Accountant with over 15 years of experience has been assigned as the engagement partner for this audit. CA X takes responsibility for maintaining overall quality on this audit engagement in accordance with SA 220.
- What do the actions of engagement partner and appropriate messages to the other members of the engagement team, in taking responsibility for the overall quality on audit engagement emphasize?**
(5 Marks)

Ans.: Leadership responsibilities for quality on audits:

As per SA 220 "Quality Control for an Audit of Financial Statements" the engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned.

Actions of engagement partner and appropriate messages to the other members of the engagement team, in taking responsibility for the overall quality on each audit engagement, emphasize:

- (1) The importance to audit quality of:
- (i) Performing work that complies with professional standards and regulatory and legal requirements;

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	<p>(ii) Complying with the firm's quality control policies and procedures as applicable;</p> <p>(iii) Issuing auditor's reports that are appropriate in the circumstances; and</p> <p>(iv) The engagement team's ability to raise concerns without fear of reprisals; and</p> <p>(2) The fact that quality is essential in performing audit engagements.</p>
(c)	<p>While auditing the accounts of PQR Ltd., a member of the audit team wants to carry out test of controls for checking the effectiveness of internal control over sales as a part of debtor's audit procedure. State any four points that need to be considered in respect of trade receivables. (4 Marks)</p> <p>Ans.: Verification of Systems for receivables:</p> <p>In relation to credit sales, it becomes imperative to carry out compliance procedures so as to ensure that the system for receivables has the following features:</p> <ol style="list-style-type: none">(1) Only <i>bona fide</i> sales lead to trade receivables.(2) All such sales are made to approved customers.(3) All such sales are properly recorded in the books of account.(4) Once recorded, the debtors can be settled only by receipt of cash or on the authority of a responsible official.(5) Segregation of duties at every point in sales transaction.(6) Debtors are collected on time.(7) In case debtors are not collected in time, sending reminders and taking legal actions if required.(8) Balances are regularly reviewed.(9) A proper system of follow up exists and if necessary, adequate provision for bad debt should be made by preparing adequate ageing schedule of the debtors. <p>(Note: Any four points may be stated)</p>



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Question 5

- (a) **As per SA 299 "Joint Audit of Financial Statements", Joint audit basically implies pooling together the resources and expertise of more than one firm of auditors to render an expert job in a given time period which may be difficult to accomplish acting individually. Explain by stating any five advantages of joint audit. (5 Marks)**

Ans.: Advantages of Joint Audit:

The practice of appointing Chartered Accountants as joint auditors is quite widespread in big companies and corporations. Joint audit basically implies pooling together the resources and expertise of more than one firm of auditors to render an expert job in a given time period which may be difficult to accomplish acting individually. It essentially involves sharing of the total work. This is by itself a great advantage. Other advantages of joint audit are:

- (a) Sharing of expertise.
- (b) Advantage of mutual consultation.
- (c) Lower workload.
- (d) Better quality of performance.
- (e) Improved service to the client.
- (f) In respect of MNCs, work can be spread using the expertise of the local firms which are in a better position to deal with detailed work and the local laws and regulations.
- (g) Lower staff development costs.
- (h) Lower costs to carry out the work.
- (i) A sense of healthy competition towards a better performance.

(Note: Any five points may be stated)

- (b) **The Management of Sun Shine Ltd. has provided the auditor with a written representation regarding its responsibilities for the preparation of the financial statements. In addition to this, the auditor may request other written representations about the financial statements.**

Mention such other representations which may supplement but do not form part of the written representation relating to management's responsibilities regarding preparation of financial statements. (5 Marks)

Ans.: Supplementary Representations:

In addition to the written representation about management's responsibilities regarding preparation of financial statements, the auditor may consider it necessary to request other written representations about the financial statements. Such written representations may supplement, but do not form part of, the written representation relating to management's responsibilities regarding preparation of financial statements.

They may include representations about the following:

- (i) Whether the selection and application of accounting policies are appropriate; and
- (ii) Whether matters such as the following, where relevant under the applicable financial reporting framework, have been recognized, measured, presented or disclosed in accordance with that framework:
 - Plans or intentions that may affect the carrying value or classification of assets and liabilities;
 - Liabilities, both actual and contingent;
 - Title to, or control over, assets, the liens or encumbrances on assets, and assets pledged as collateral; and

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- Aspects of laws, regulations and contractual agreements that may affect the financial statements, including non-compliance.

(c) Compute the Drawing power for Cash Credit limit granted to S Ltd. by Trust Bank for the month of March 2025 from the following information:

Particulars	Amount in (₹)
Value of stocks	50,000
Value of debtors (including debtors of ₹ 5,000 for an invoice dated 17.11.2024)	45,000
Value of creditors for goods	15,000
Sanctioned limit	45,000

Margin on stock is 20% and on debtors is 50%.

Note: Debtors older than 3 months are ineligible for calculation of D.P.

(4 Marks)

Ans.: Computation of Drawing Power:

Particulars of Current Assets		Drawing power (₹)
(A) Stock		
Stock at realisable value	50,000	
Less: Unpaid Stocks		
Creditors	15,000	
Paid for Stocks	35,000	
Less: Margin @ 20%	7,000	28,000
(B) Debtors		
Total debtors	45,000	
Less: Ineligible debtors	5,000	
	40,000	
Less: Margin @ 50%	20,000	20,000
Total eligible amount		48,000
Drawing Power (Cannot exceed sanctioned limit)		45,000



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Question 6	
(a)	<p>T Ltd. has appointed NFO & Co., Chartered Accountants, as statutory auditors. Since inventory is a material component of the financial statements, CA F plans to attend the physical inventory counting. Provide any five matters that CA F should consider when planning their attendance at the physical inventory counting. (5 Marks)</p> <p>Ans.: Matters relevant in planning attendance at physical inventory counting:</p> <ol style="list-style-type: none"> (1) Nature of inventory. (2) Stages of completion of work-in-progress. (3) The risks of material misstatement related to inventory. (4) The nature of the internal control related to inventory. (5) Whether adequate procedures are expected to be established and proper instructions issued for physical inventory counting. (6) The timing of physical inventory counting. (7) Whether the entity maintains a perpetual inventory system. (8) The locations at which inventory is held, including the materiality of the inventory and the risks of material misstatement at different locations, in deciding at which locations attendance is appropriate. (9) Whether the assistance of an auditor's expert is needed. <p><i>(Note: Any five points may be stated)</i></p>
(b)	<p>M/s PQ & Co., Chartered Accountants have been appointed as statutory auditors of CBD Multiplex Cinema Ltd. The audit team started the audit and verified the ledger and other books of accounts for the F.Y. 2024-2025. However, one of the team members is of the view that the internal control mechanism of the company should also be verified. Can you guide the audit team about the areas that will be covered in verifying the internal control mechanism? (5 Marks)</p> <p>Ans.: Verification of Internal Control Mechanism in audit of Multiplex:</p> <ol style="list-style-type: none"> (a) Verify that entrance to the cinema-hall during show is only through printed tickets; (b) Verify that they are serially numbered and bound into books; (c) Verify that the number of tickets issued for each show and class, are different though the numbers of the same class for the show on the same day, each week, run serially; (d) Verify that for advance booking a separate series of tickets is issued; (e) Verify that the inventory of tickets is kept in the custody of a responsible official.
(c)	<p>The auditor shall take into consideration the reporting objectives of the engagement so as to plan timing of different audit procedures and also nature of communications while establishing audit strategy. Give any four instances of reporting objectives.</p> <p align="center">OR</p> <p>As an auditor of Star Ltd., a company covered under Section 135 of the Companies Act, 2013, what matters should auditor verify to ensure that proper disclosures regarding Corporate Social Responsibility (CSR) activities is made in Additional Information to notes to account. Mention any four such matters. (4 Marks)</p>

Ans.: Instances of Reporting Objectives:

As per SA 300 "Planning an Audit of Financial Statements" the auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. In establishing the overall audit strategy, the auditor shall, among other ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of communication required.

Some of the instances are given under:

- (1) Entity's timetable for reporting, such as at interim and final stages.
- (2) Organization of meetings with management and TCWG to discuss the NTE of the audit work.
- (3) Discussion with management regarding expected type and timing of reports to be issued.
- (4) Discussion with management regarding the expected communications on the status of audit work throughout the engagement.
- (5) Expected nature and timing of communications among ET members, including the nature and timing of team meetings and timing of the review of work performed.

(Note: Any four points may be stated)

OR

Disclosures regarding CSR Activities:

Where the company covered u/s 135 of the Companies Act, 2013, the following shall be disclosed with regard to CSR activities:

- (a) amount required to be spent by the company during the year,
- (b) amount of expenditure incurred,
- (c) shortfall at the end of the year,
- (d) total of previous years shortfall,
- (e) reason for shortfall,
- (f) nature of CSR activities,
- (g) details of related party transactions, e.g., contribution to a trust controlled by the company in relation to CSR expenditure as per relevant Accounting Standard,
- (h) where a provision is made with respect to a liability incurred by entering into a contractual obligation, the movements in the provision during the year should be shown separately.

(Note: Any four points may be stated)



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