

FINAL COURSE: GROUP I

PAPER-3: ADVANCED AUDITING, ASSURANCE AND PROFESSIONAL ETHICS

(MTP 3: Ch. 2 – General Auditing Principles and Auditor's Responsibilities)

Time Allowed- 20 Minutes

Maximum Marks-10

Write the most appropriate answer to each of the following multiple-choice questions by choosing one of the four options given. All MCQs are compulsory and carry 2 Marks each.

1. ABM & Co. and RKS & Associates were appointed as joint statutory auditors of Zenith Infrastructure Ltd., a listed construction company engaged in government EPC projects. The engagement letter states that ABM will audit northern and western divisions, while RKS will handle southern and eastern divisions. The overall financial statements will be consolidated at the head office in Delhi, where ABM will compile the draft audit report.

During the audit:

- RKS discovered possible revenue overstatement in two EPC contracts in the southern division where work completion certificates were pre-dated.
- RKS informed ABM over a phone call that they were investigating the issue and would revert once management clarifications were obtained.
- ABM finalized the consolidated draft audit report on 10 June 2025 without waiting for RKS's final observations, assuming that RKS had not raised any formal objection.
- On 14 June 2025, RKS sent an email noting potential overstatement of ₹95 crore and suggested a qualification. The audit report, however, had already been uploaded by ABM on 12 June 2025 after joint digital signatures from both firms (using tokens maintained at the client's office by the CFO's staff for convenience).
- RKS claims they had authorized only a draft and not the final upload. ABM contends that since the audit was jointly conducted, both auditors are equally responsible for the report.

Based on SA 299, which of the following interpretations most appropriately reflects the professional responsibilities and possible implications for each joint auditor?

- (a) Since the engagement letter divided the audit areas, each joint auditor is responsible only for the work performed in their respective divisions; hence, RKS cannot be held liable for misstatements in the divisions audited by ABM, irrespective of overall reporting lapses.
- (b) Joint auditors are individually responsible for the work they perform and jointly responsible for the report as a whole. However, if a material misstatement in a component audited by one auditor affects the consolidated financial statements, the other auditor's failure to perform adequate overall review or to obtain written concurrence before report issuance may constitute negligence under SA 299.

- (c) Because the final report was uploaded using both firms' digital signatures, it implies joint acceptance of the opinion; therefore, even if RKS had objected orally, both firms share equal legal and professional responsibility for the opinion, and no reliance can be placed on division of work documentation.
- (d) Under SA 299, joint auditors are not required to communicate significant findings or differences before signing; the responsibility rests solely with the engagement partner who compiles the report, provided he ensures compliance with applicable auditing standards in his areas.

Case Scenario [MCQ 2-5]

Orion Retail Limited ("Orion"), a national listed retail chain with presence in 18 states, is engaged in fast-moving consumer goods and operates through company-managed stores and franchisees. Orion reported consolidated revenue of ₹ 4,200 crore for FY 2024-25. The audit for the year ended 31 March 2025 is being conducted by a mid-sized audit firm, appointed three years ago. The engagement partner (EP) has rotated out this year; a new partner commenced oversight from 2 May 2025. The interim audit was performed in January 2025 and substantive procedures in April–May 2025.

Significant facts and developments relevant to the audit:

1. **Whistleblower Allegation:** On 10 May 2025 the firm received an anonymous e-mail alleging manipulative practices in recognition of promotional income and undisclosed related-party rebates in certain subsidiaries. The e-mail named a senior sales executive and alleged that management had directed store managers to record promotional allowances as contra-sales rather than as reductions in expenses. The e-mail also referred to communications between the sales executive and a vendor whose invoices were routed through a third-party distribution service.
2. **Regulatory Notices:** Orion received a show-cause notice dated 18 March 2025 from the Goods & Services Tax (GST) department alleging irregular input tax claims amounting to ₹ 45 crore for FY 2023-24 in respect of a group of franchisee accounts. Separately, SEBI issued a query on 5 April 2025 regarding late disclosures of related-party transactions. Orion's board discussed the GST notice on 20 March 2025 and instructed management to respond through tax counsel; the response was filed on 28 April 2025. No final adjudication has occurred as at the date of the audit report.
3. **Related Party and Unusual Transactions:** During ledger review, the audit team observed several payments to an entity named 'Helix Distribution Pvt. Ltd.' (Helix). Helix is a logistics aggregator providing services to multiple retailers. The entity appears in Orion's vendor master as a service provider, and certain transactions were designated as rebates to franchisees. Company records show that a director of Helix is a close associate of Orion's head of distribution. The contract with Helix was executed on 15 February 2025 and contains clauses for retrospective credit notes to be issued at the year-end.

4. **Service Organisation Usage:** Orion outsources its centralised billing and invoice processing for franchisee settlements to 'BlueLex Services Pvt. Ltd.' (BlueLex), a cloud-based service organisation. BlueLex performs invoice generation, automated matching of store receipts, and remittance instructions to franchisees. Orion receives daily exception reports but does not perform independent reconciliations for a monthly sample beyond cursory checks. BlueLex maintains a standard SOC 2 type report for the period October 2024-March 2025 but it is an internal control report prepared by an external consultant engaged by BlueLex and is labelled 'Management Assertion with Controls Description'. Orion did not obtain a formal independent assurance report that meets SA 402 expectations.
5. **Internal Control and IT Environment:** Orion implemented a new ERP module for franchisee settlements in December 2024. The module interfaces with BlueLex via APIs. Change management logs show several emergency patches applied in March 2025; however, the ERP change log lacks signatures of the authoriser for two critical patches deployed on 22 March 2025. IT logs indicate that a privileged user account was used to post manual adjustments to franchisee balances on 31 March 2025. The IT head resigned on 4 April 2025 and cited 'operational stresses' in an exit note.
6. **Audit Committee and Governance:** Orion's audit committee (AC) comprises three non-executive directors; two are independent. Minutes of the AC meeting held on 25 April 2025 indicate that management represented there were no material frauds and that all regulatory communications were being addressed. The AC minutes show limited discussion on the whistleblower e-mail, and no decision regarding escalation to regulators. The AC requested the internal audit (IA) to perform follow-up; IA provided a high-level note on 5 May 2025 that noted 'process lapses' but no specifics.
7. **Prior Year Findings:** The prior year audit disclosed weaknesses in controls over vendor master maintenance and a recommendation for surprise verification of franchisee receivables. Management response indicated remedial measures; however, evidence of the implementation of these measures is limited.
8. **Management Representations:** On 7 May 2025 management provided a written representation asserting there were no unidentified related-party relationships beyond those disclosed and that BlueLex's services were governed by a master services agreement that ensured segregation of duties. CEO's representation included that Orion had no knowledge of fraudulent activity by staff. The CFO, who was directly involved in vendor negotiations, was promoted in February 2025 and attended audit meetings until 10 May 2025 when he took medical leave; his laptop was reported unavailable for the audit team's forensic review.
9. **Substantive Audit Findings:** During confirmation of vendor balances, the audit team noted discrepancies in remittance advices, duplicate invoice numbers for Helix, and adjusted franchisee settlement amounts subsequently reversed by entries dated 31 March 2025. External confirmations from a sample of franchisees returned different settlement terms than those recorded in Orion's ledgers. Testing of journal entries identified several year-end manual journals authored by the privileged IT account and posted with narratives labelled 'franchisee adjustment' between 29–31 March 2025. The audit team could not reconcile certain automated remittance instructions generated by BlueLex with bank payment files maintained by Orion.

10. **Engagement Constraints:** The engagement partner requested more time on 12 May 2025 to perform further procedures but was instructed by the audit committee chair to complete the audit report to meet statutory filing timelines. The firm is under pressure from Orion's management, a significant fee-paying client, to issue the report without delay. The EP is aware of these pressures.

Based on the above facts, answer the following:

2. Considering the facts and SA 240, which of the following actions by the auditor most appropriately reflects an adequate professional response to the assessed fraud risks?
- (a) Expand substantive analytical procedures around promotional income and perform additional confirmation with franchisees, but accept management representations and proceed to conclude if no further contradictory evidence is found.
 - (b) Design and perform targeted procedures to test for management override (including forensic examination of privileged IT account activity and testing of year-end journal entries), obtain corroborative external evidence for Helix transactions, and communicate suspicions to those charged with governance promptly.
 - (c) Rely on BlueLex's daily exception reports and the SOC-type documents provided by BlueLex to limit additional procedures, since the service organisation performs controls of invoice processing.
 - (d) Withdraw from the engagement immediately upon receipt of the whistleblower email and report the matter to regulatory authorities without attempting further evidence gathering.
3. In relation to the GST show-cause notice and SEBI query, which of the following best describes the auditor's responsibilities under SA 250 and appropriate actions to be taken? _____
- (a) Since management has engaged tax counsel and filed a response, the auditor's responsibility is limited to obtaining a copy of the response and relying on management's conclusions unless evidence suggests otherwise.
 - (b) The auditor should evaluate whether the GST matter and SEBI query could have a material effect on the financial statements, obtain legal advice where necessary, inspect correspondence with regulators, expand audit procedures on affected balances, and consider the need for modification of the audit opinion if non-compliance is material and not adequately disclosed.
 - (c) The auditor should treat regulatory communications as matters outside the scope of financial statement audit and only disclose them in the audit committee communication without further audit action.
 - (d) Where the auditor suspects that management or governance is involved in non-compliance, the auditor must immediately report the matter to enforcement authorities even if the legal process is ongoing.

4. With reference to the whistleblower allegation, limited audit committee discussion and management representations, which course of action best fulfils SA 260 requirements?
- (a) Communicate orally to the audit committee chair that the matter is being investigated and keep records in the audit file; escalate to regulators only if formal evidence of fraud emerges.
 - (b) Provide a draft of the auditor's report to the audit committee and request their written acceptance of management representations; no further communication is required unless adjustments are proposed.
 - (c) Communicate in writing to those charged with governance (entire audit committee) the whistleblower allegation, the nature and timing of planned audit procedures to address it, significant difficulties encountered, and any limitations imposed by management; document the communications and follow up until matters are resolved.
 - (d) Limit communication to internal firm channels and discuss the matter only with the engagement partner and senior audit staff to preserve client confidentiality and avoid premature escalation.
5. Regarding Orion's use of BlueLex (a service organisation) and the SOC-type report provided, which of the following best describes the auditor's responsibilities and appropriate next steps under SA 402?
- (a) Accept the SOC-type management assertion prepared by BlueLex's consultant as sufficient evidence of control effectiveness and limit testing to user entity procedures over exception reconciliation.
 - (b) Obtain an understanding of the services provided by BlueLex, evaluate the design and implementation of controls relevant to the audit, request an appropriate independent assurance report (e.g., SOC 1 or equivalent) or perform additional procedures at BlueLex (or through the service auditor), and perform substantive procedures to reconcile BlueLex outputs with Orion's bank and ERP files.
 - (c) Require Orion to bring the outsourced function in-house before concluding the audit since reliance on a third-party invalidates auditor's ability to obtain sufficient appropriate evidence.
 - (d) Rely solely on management representations that BlueLex is reputable and that no irregularities have occurred, documenting this reliance in the audit file.

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MCQ – Mock Test Series 1: Nov. 2025

Detailed Schedule of MCQ Test Series – Nov. 2025

Date	Day	Topic	MCQ Style	Marks
6 Nov.	Wed.	Ch. 19 - Professional Ethics	1 Case Study with 4 MCQ + 1 General MCQ	10
7 Nov.	Thu.	Ch. 1 - Quality Control		10
8 Nov.	Fri.	Ch. 2 - General Auditing Principles & A.R.		10
9 Nov.	Sat.	Module Test - Ch. 19, 1 and 2	3 Case Studies comprising 12 MCQs + 3 MCQs	30
10 Nov.	Mon.	Ch. 3 - Audit Planning	1 Case Study with 4 MCQ + 1 General MCQ	10
11 Nov.	Tue.	Ch. 4 - Materiality, Risk Assessment and I.C.		10
12 Nov.	Wed	Ch. 5 - Audit Evidence		10
13 Nov.	Thu.	Ch. 6 - Completion and Review		10
14 Nov.	Fri.	Ch. 7 - Reporting		10
15 Nov.	Sat.	Module Test - Ch. 3 to Ch. 7	3 Case Studies comprising 12 MCQs + 3 MCQs	30
17 Nov.	Mon.	Ch. 8 - Specialised Areas	1 Case Study with 4 MCQ + 1 General MCQ	
18 Nov.	Tue.	Ch. 9 – Related Services & Ch. 10 – Review of F.I.		10
19 Nov.	Wed	Ch. 11 - Financial info. & Other Assurance		10
20 Nov.	Thu.	Ch. 12 - Digital Auditing and Assurance		10
21 Nov.	Fri.	Ch. 13 - Group Audits		10
22 Nov.	Sat.	Module Test - Ch. 8 to Ch. 13	3 Case Studies comprising 12 MCQs + 3 MCQs	30
24 Nov.	Mon.	Ch. 14 - Audit of Banks and NBFC	1 Case Study with 4 MCQ + 1 General MCQ	10
25 Nov.	Tue.	Ch. 15 - Audit of PSU		10
26 Nov.	Wed	Ch. 16 - Internal Audit		10
27 Nov.	Thu.	Ch. 17 - Investigation, Diligence & Forensic		10
28 Nov.	Fri.	Ch. 18 - SDG and ESG Assurance		10
29 Nov.	Sat.	Module Test - Ch. 14 to Ch. 18	3 Case Studies comprising 12 MCQs + 3 MCQs	30

Note: Test Papers and Answer Key will be uploaded on Knowledge Portal of www.altclasses.in

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WT - 2	Ch. 2 - General Auditing Principles	29 Nov. 2025
	Ch. 3 - Audit Planning, Strategy & Execution	
	Ch. 4 - Materiality, Risk Assessment & IC	
WT - 3	Ch. 5 - Audit evidence	03 Dec. 2025
	Ch. 6 - Completion and Review	
	Ch. 7 - Reporting	
WT - 4	Ch. 8 - Specialised Areas	06 Dec. 2025
	Ch. 9 - Audit Related Services	
	Ch. 10 - Review of Financial Information	
	Ch. 11 - PFI & Other Assurance Services	
WT - 5	Ch. 12 - Digital Auditing and Assurance	10 Dec. 2025
	Ch. 16 - Internal audit	
	Ch. 17 - DD, Investigation & Forensic Accounting	
	Ch. 18 - SDG & ESG Assurance	
WT - 6	Ch. 13 - Group Audits	13 Dec. 2025
	Ch. 14 - Special Features of Audit of Banks and NBFC	
	Ch. 15 - Overview of Audit of PSU	
WT - 7	Full Syllabus Test 1	17 Dec. 2025
WT - 8	Full Syllabus Test 1	24 Dec. 2025

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