

INTER COURSE: GROUP II
PAPER-5: AUDITING AND ETHICS

(MTP 2: Ch. 11 – Ethics and Terms of Audit Engagement)

Time Allowed- 20 Minutes

Maximum Marks-100

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. During the statutory audit of Alpha Green Infrastructure Ltd., the engagement partner, CA Meera, discovered that her firm had recently undertaken a large non-audit assignment for the same client — implementation of a new ERP costing ₹80 lakh — approved by the audit committee six months before her appointment. The ERP project was being supervised by the company's CFO, who was a close professional acquaintance of Meera, with whom she had earlier worked in another company.

While finalizing the audit plan, Meera realized that the ERP output data would form the base for valuation of closing inventories and cost allocation. The client assured her that “since your firm designed the system, accuracy can be taken for granted.” Meera sensed the ethical dilemma but believed that her professional judgment would remain unbiased because she had no financial interest in the client.

Which of the following statements MOST ACCURATELY reflects the ethical and independence issue in this case, as per the Code of Ethics and ICAI guidance?

- (a) Meera's independence remains intact because she has no financial interest; therefore, the only requirement is to maintain professional competence and due care while auditing the ERP outputs.
- (b) Meera faces a familiarity threat, as she knows the CFO personally; however, since the ERP work was completed before her appointment, no further safeguard is required.
- (c) Meera faces both a self-review and familiarity threat, since her firm's prior involvement in designing the ERP system means she would be evaluating her own firm's work, possibly impairing objectivity; safeguards such as assigning an independent partner or declining the engagement may be necessary.
- (d) Meera only faces a self-interest threat, because her firm earned substantial fees from the ERP work; independence in appearance is unaffected if the engagement partner believes her judgment is not influenced.

Case Scenario [MCQ 2-5]

Orion Pharmaceuticals Ltd. (OPL), a listed company engaged in the manufacture of life-saving drugs, appointed M/s AKV & Associates, Chartered Accountants, as its statutory auditors for FY 2024–25. The firm was selected through a competitive bidding process. During pre-engagement discussions, the CFO informed the audit partner, CA Ananya, that the company had been facing increasing regulatory scrutiny and needed “audit cooperation” to ensure timely filing of financials.

Ananya conducted a due diligence of the client and found that the previous auditors had resigned mid-term citing “management pressure regarding certain disclosures.” She sent a professional communication to the outgoing auditors but received no response despite reminders. After discussing the matter internally, AKV & Associates decided to proceed, noting that no disqualification existed under the Companies Act.

At the first meeting, the Managing Director requested Ananya to provide an “assurance letter” to banks before completion of the statutory audit, certifying that “no significant misstatements were expected.” Ananya declined, clarifying that such assurance before completing audit procedures would violate professional requirements. Later, the MD hinted that early certification could help the firm secure a large consultancy assignment for implementation of a new costing system.

Meanwhile, Ananya noticed that her cousin’s spouse was employed in the internal audit department of OPL. Though she had no personal relationship or financial connection, she disclosed this fact to her partners and evaluated whether any threat to independence existed. The firm documented the matter and decided that the engagement could continue with adequate safeguards, including rotating audit team members.

During the audit planning, OPL management refused to provide written acknowledgment of their responsibility for the preparation of financial statements and internal control design, claiming such matters were “understood.” Ananya explained that such written confirmation was a precondition under SA 210 and declined to proceed until acknowledgment was received.

While the audit progressed, the finance head informally offered AKV & Associates an opportunity to design OPL’s internal control framework for inventory costing next year, stating that the “same team could do both audit and advisory more efficiently.” The offer was tempting due to high professional fees, but Ananya was aware of self-review and advocacy threats arising from such dual roles.

At year-end, Ananya performed a final engagement quality control review. She ensured compliance with the firm’s internal policies under SQC 1 and SA 220, reviewed documentation for independence evaluation, and finalized the audit report. A few weeks later, the ICAI’s Quality Review Board sought clarification regarding her firm’s independence declaration and engagement acceptance process, which AKV & Associates could fully substantiate through proper documentation and communication trail.

Based on these facts, answer the following MCQs [Q.2-Q.5]

2. When the Managing Director requested an “assurance letter” before audit completion and hinted at consultancy work in return, which course of action BEST upholds professional ethics?
 - (a) Accepting the request after mentioning that the report is preliminary and subject to final audit, since it helps retain the client’s confidence.

- (b) Declining the request, as issuing such a letter before audit completion compromises integrity and objectivity, creating a self-interest threat.
 - (c) Accepting the request with management's written confirmation, since professional judgment can justify early communication of results.
 - (d) Declining the request only if fees for consultancy are contingent upon audit completion, otherwise it does not impair independence.
3. Ananya's cousin's spouse worked in the client's internal audit team. Which of the following responses MOST APPROPRIATELY reflects correct application of independence principles?
- (a) The relationship automatically breaches independence, and the firm must withdraw from the engagement immediately.
 - (b) The firm may continue with engagement, but should apply safeguards such as rotation of audit staff and documentation of evaluation of threat.
 - (c) Such relationship is irrelevant as there is no direct financial link, hence no need to record it or apply any safeguard.
 - (d) The firm should accept the engagement but disclose the relationship to management only after audit completion to avoid unnecessary issues.
4. OPL's management initially refused to provide written acknowledgment of responsibility for preparing financial statements and internal controls. As per SA 210, what should the auditor do in this case?
- (a) Proceed with audit, since acknowledgment can be implied from management's conduct and oral assurance.
 - (b) Proceed only if the client agrees to disclose this refusal in notes to accounts.
 - (c) Decline the engagement until such acknowledgment is obtained, as it is a necessary precondition for accepting an audit.
 - (d) Accept engagement after including a disclaimer in the audit report that management did not provide such acknowledgment.
5. Ananya ensured documentation of independence evaluation, supervision, and engagement quality control review. Which statement MOST CORRECTLY distinguishes SQC 1 and SA 220 in this context?
- (a) Both SQC 1 and SA 220 apply at the engagement level and govern performance of individual audit teams.
 - (b) SQC 1 applies at firm level establishing overall quality control policies, whereas SA 220 applies to specific audit engagements.
 - (c) SQC 1 applies only to audits of listed entities, while SA 220 applies to all assurance engagements including reviews.
 - (d) Both SQC 1 and SA 220 apply only to partner-level decisions and exclude documentation or supervision responsibilities of assistants.

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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. 1 - Nature, Objective and Scope of Audit	1 Case Study with 4 MCQ + 1 General MCQ	10
7 Nov.	Thu.	Ch. 11 - Ethics and Terms of Audit Engagements		10
8 Nov.	Fri.	Ch. 2 - Audit Strategy, Planning & Programme		10
9 Nov.	Sat.	Module Test - Ch. 1, 2 and 11	3 Case Studies comprising 12 MCQs + 3 MCQs	30
10 Nov.	Mon.	Ch. 3 - Risk Assessment and Internal Control	1 Case Study with 4 MCQ + 1 General MCQ	10
12 Nov.	Wed	Ch. 4 - Audit Evidence		10
14 Nov.	Fri.	Ch. 6 - Audit Documentation		10
15 Nov.	Sat.	Module Test - Ch. 3, 4 and 6	3 Case Studies comprising 12 MCQs + 3 MCQs	30
17 Nov.	Mon.	Ch. 5 - Audit of Items of Financial Statements	1 Case Study with 4 MCQ + 1 General MCQ	10
19 Nov.	Wed	Ch. 7 - Completion and Review		10
22 Nov.	Sat.	Module Test - Ch. 5 and 7	3 Case Studies comprising 12 MCQs + 3 MCQs	30
24 Nov.	Mon.	Ch. 8 - Reporting	1 Case Study with 4 MCQ + 1 General MCQ	10
26 Nov.	Wed	Ch. 9 - Audit of Different Types of Entities		10
28 Nov.	Fri.	Ch. 10 - Audit of Banks		10
29 Nov.	Sat.	Module Test - Ch. 8, 9 and 10	3 Case Studies comprising 12 MCQs + 3 MCQs	30

**Note: Test Papers and Answer Key will be uploaded
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MTP No.	Chapter No. and Name	Date of Test
1	Ch. 1 - Nature, Objective and Scope of Audit	26 Nov. 2025
	Ch. 11 - Ethics and Terms of Audit Engagements	
2	Ch. 2 - Audit strategy, Planning and Programme	29 Nov. 2025
	Ch. 3 - Risk Assessment and Internal Control	
3	Ch. 4 - Audit evidence	03 Dec. 2025
	Ch. 6 - Audit Documentation	
4	Ch. 5 - Audit of Items of Financial Statements	06 Dec. 2025
5	Ch. 7 - Completion and Review	10 Dec. 2025
	Ch. 8 - Audit Report	
6	Ch. 9 - Sp. features of Audit of Different Entities	13 Dec. 2025
	Ch. 10 - Audit of Banks	
7	Full Syllabus Test	17 Dec. 2025
8	Full Syllabus Test	24 Dec. 2025

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		Cracker – (Vol 1 & Vol 2)	17th Edition (Oct. 2025)	1195	855	
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