

CA INTERMEDIATE

3rd Edition

**AUDITING
AND
ETHICS**



Q & A - SCANNER



QUESTION & ANSWER SCANNER

By India's Most Dynamic Faculty For Audit

CA AARTI LAHOTI

 www.aartilahoti.com

MODES OF LEARNING : Pendrive / Google Drive / Face to Face / Livestream

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NEW SCHEME - GROUP - II

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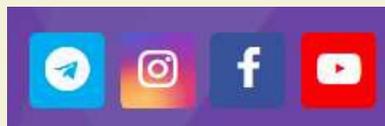
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CA Aarti N. Lahoti

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“Right Concept. Right Practice. Right Result.”

Dear Students,

IT'S ALL ABOUT PRACTICE — THE KEY TO PERFORMANCE!

*It gives me immense pleasure to present before you **Module II – Q & A Scanner** of Auditing & Ethics for CA Intermediate, the second part of a carefully designed three-module learning system comprising:*

Module I – Theory Notes

Module II – Q & A Scanner and

Module III – MCQ Compiler

Auditing is a subject where success is achieved not only by understanding concepts, but by presenting them correctly, systematically and within the framework expected by ICAI. This module has been specially prepared to help you develop the art and discipline of writing high-scoring audit answers.

The questions included in this book cover a wide range of important, frequently tested and concept-oriented areas of the syllabus. Each answer has been framed in a precise, logical and exam-oriented manner, with emphasis on proper structure, relevant content and professional language.

*For complete and effective preparation, this module should be used in close coordination with — **Module I – Theory Notes** for strengthening conceptual clarity, and — **Module III – MCQ Compiler** for improving accuracy and objective-type problem solving.*

Always remember — understanding builds confidence, but correct presentation earns marks. Regular writing practice from this module will significantly enhance your speed, structure and examination readiness.

Any constructive suggestions for further improvement are always welcome.

Wishing you disciplined preparation and excellent success in the forthcoming examinations.

Happy Auditing!

Regards,

CA Aarti Lahoti

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CA Aarti Lahoti Classes



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LIST OF ABBREVIATIONS

AFRF (SA 200)	APPLICABLE FINANCIAL REPORTING FRAMEWORK
FRF	FINANCIAL REPORTING FRAMEWORK
GPF	GENERAL PURPOSE FRAMEWORK
SPF (SA 800)	SPECIAL PURPOSE FRAMEWORK
RMM (SA 200)	RISKS OF MATERIAL MISSTATEMENT
SAAE (SA 200)	SUFFICIENT APPROPRIATE AUDIT EVIDENCE
TCWG (SA 260)	THOSE CHARGED WITH GOVERNANCE
MGMT	MANAGEMENT
WR (SA 580)	WRITTEN REPRESENTATIONS
FS	FINANCIAL STATEMENTS
AFS	AUDITED FINANCIAL STATEMENTS
CG	CENTRAL GOVERNMENT
NTE	NATURE, TIMING & EXTENT
EP (SQC 1 & SA 220)	ENGAGEMENT PARTNER
EQCR (SQC 1 & SA 220)	ENGAGEMENT QUALITY CONTROL REVIEW
KAM (SA 701)	KEY AUDIT MATTERS
EOM (SA 706)	EMPHASIS OF MATTER
OM (SA 706)	OTHER MATTER

1 NATURE, OBJECTIVE & SCOPE OF AUDIT

1.	<p>An audit is independent examination of financial information of any entity, whether profit oriented or not, & irrespective of its size or legal form when such an examination is conducted with a view to expressing an opinion thereon. What the auditor is supposed to do to satisfy himself that nothing contained in the statements will mislead anybody? (RTP May 2020/Nov 2015)</p>
	<ul style="list-style-type: none"> ➤ “An audit is an independent examination of financial information of any entity, whether profit oriented or not, & irrespective of its size or legal form, when such an examination is conducted with a view to expressing an opinion thereon”. ➤ An incisive analysis of above meaning of auditing brings out following points clearly: - <ol style="list-style-type: none"> 1. Audit is an independent examination of financial information. <ul style="list-style-type: none"> ➤ Independence, here, implies that the judgement of a person is not subordinate to the wishes or direction of another person who might have engaged him. ➤ The auditor should be independent of entity whose FS are subject to audit so that he can form an opinion without being affected by any influence. ➤ Independence increases auditor’s ability to act objectively without creeping in of any biases. 2. Of any entity, whether profit oriented or not, & irrespective of its size or legal form, <ul style="list-style-type: none"> ➤ The entity whose financial information is examined need not necessarily be profit oriented like in case of a business. It can be a non-profit organization like an NGO or a charitable trust. Audit can be undertaken in respect of any organization be it a small, medium or large. ➤ Further, it can be conducted for any entity irrespective of its legal structure i.e. such an entity may be a proprietary concern, a partnership firm, a LLP, a private company, a public company, a society or a trust. 3. The purpose of audit is to express an opinion on the financial statements <ul style="list-style-type: none"> ➤ Understand that preparation & presentation of FS of an entity is responsibility of management of entity. The auditor expresses an opinion on FS by means of written audit report. 4. In doing so, he has to see that financial statements would not mislead anybody by ensuring that: - <ul style="list-style-type: none"> ➤ The accounts have been drawn up with reference to entries in the books of account; ➤ The entries in the books of account are adequately supported by sufficient & appropriate evidence; ➤ None of the entries in the books of account has been omitted in the process of compilation; ➤ The information conveyed by the statements is clear & unambiguous; ➤ Financial statement amounts are properly classified, described & disclosed in conformity with AS; & ➤ Statement of accounts presents a true & fair picture of operational results & of the assets & liabilities.
2.	<p>CA students Sriranga & Manga were discussing on the assurance, which the auditing services provide to the users, in the form of opinion on FS, by means of a written report. Such an assurance lends credibility to FS. You are required to state some of the aspects examined by the auditor, to ensure that the FS which are audited are not misleading. (4 Marks Sep 2025)</p>
	<ul style="list-style-type: none"> ➤ Aspects to be examined by the auditor to ensure that the FS which are audited are not misleading are as under: ➤ Refer Point 4 in answer above
3.	<p>“The purpose of an audit is to enhance the degree of confidence of intended users in the FS. This is achieved by the expression of an opinion by the auditor on whether the FS are prepared, in all material respects, in accordance with an applicable financial reporting framework.” Explain stating the objectives of audit as per SA 200. (RTP May 2021/2020/2019/Nov 2023/19)</p>
	<p>In conducting audit of FS, objectives of auditor in accordance with SA-200 “Overall Objectives of the Independent auditor & the conduct of an audit in accordance with Standards on Auditing” are: -</p> <ul style="list-style-type: none"> ➤ To obtain reasonable assurance about whether the FS as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the FS are prepared, in all material respects, in accordance with an AFRF; & ➤ To report on the FS, & communicate as required by the SAs, in accordance with the auditor’s findings.

4.	CA N is the auditor of SR Ltd. The auditor expressed his opinion on the FS without ascertaining as to whether the FS as a whole were free from material misstatements or not. In your opinion, whether CA N has complied with objectives of audit considering the applicability of relevant SA? (3 Marks May 2022)
	<ul style="list-style-type: none"> ➤ Refer – Objectives of Audit – in answer above ➤ In the given case of SR Ltd, CA N expressed his opinion on the FS of SR Ltd without obtaining reasonable assurance about whether the FS as a whole are free from material misstatement or not. Therefore, it can be concluded that CA N did not comply with the objective of audit as stated in SA 200.
5.	M Motors Ltd is a leading Indian automobile manufacturer with many offerings across commercial, passenger & electric vehicles. The Company is pioneering India's electric vehicle transition & enjoys considerable advantage in one of the fastest growing automotive markets. GR & Associates have been appointed as its statutory auditors for financial year 2022-23. J & K are newly appointed audit assistants in the firm & are part of engagement team constituted for purpose of audit of M Motors Ltd. However, they are confused about what such an audit tends to achieve. They perceive audit as a guarantee against possible errors or frauds in FS. Do you agree with perception of both the assistants? In this context, outline objectives of an independent audit conducted in accordance with Standards on Auditing. (RTP May 2024)
	<ul style="list-style-type: none"> ➤ Refer – Objectives of Audit – in answer above ➤ Therefore, perception of both assistants is not proper. Auditor of FS does not seek to provide guarantee that FS are free from material misstatements caused by frauds or errors. He obtains reasonable assurance.
6.	You are auditing the FS of JEN Ltd., a manufacturing company. During a meeting, Mr. Jai CEO questions the auditor's ability to detect all material misstatements, including those caused by fraud. He insists that since the auditor is a professional, the audit should provide absolute assurance on the accuracy of the FS. Is the contention of Mr. Jai correct. Discuss the objectives of auditor in accordance with relevant SA.
	<ul style="list-style-type: none"> ➤ Refer – Objectives of Audit – in answer above ➤ Audit of FS is carried out by the auditor with professional competence & skills in accordance with Standards on Auditing. Audit procedures are applied in accordance with SAs, audit evidence is obtained & evaluated. On basis of that, conclusions are drawn, & opinion is formed. It leads to high level of assurance which is called as reasonable assurance, but it is not absolute assurance. ➤ It may be noted that absolute assurance is a complete assurance or a guarantee that FS are free from material misstatements. However, reasonable assurance is not a complete guarantee. Although it is a high-level of assurance, but it is not complete assurance. ➤ Misstatements in FS can occur due to fraud or error or both. The auditor seeks to obtain reasonable assurance whether FS as a whole are free from material misstatements caused by fraud or error. ➤ In the given case, Mr. Jai, CEO of JEN Ltd., questions the auditor's ability to detect all material misstatements & insists that auditor should provide absolute assurance. As per SA 200, the auditor's objective is to obtain reasonable assurance. Therefore, contention of the CEO Mr. Jai is not correct.
7.	Distinguish between absolute & reasonable assurance. Identify the type of assurance that is expected in an audit of the FS, clearly outlining the reasons to justify your point of view. (6 Marks May 2017) (RTP May 2019)
	<ul style="list-style-type: none"> ➤ Absolute assurance is the highest level of assurance an auditor can give, if he checks each & every transaction. Therefore, absolute assurance is the level of assurance that can only be given if the auditor does not perform sampling testing. However, it is not possible to give absolute assurance because of time & cost involved. Therefore, auditors give reasonable assurance. Reasonable assurance is less than absolute assurance. ➤ Refer – Objectives of Audit – in answer above ➤ Reasonable assurance is a high level of assurance. It is obtained when the auditor has obtained SAAE to reduce audit risk to an acceptably low level. However, reasonable assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions & bases the auditor's opinion being persuasive rather than conclusive.
8.	Micky & Associates, Chartered Accountants, were appointed as the auditors of STI Ltd., a Textile manufacturing company, for the financial year 2024-25. Management of the company discussed with the newly appointed auditors that the company has been suffering losses for the last few years & also the Directors are suspecting that accounts are not properly maintained & might contain errors & frauds. So, in the given situation, management of the company requested the auditors to give complete assurance/guarantee about the FS of the company.

	<p>Can the auditors give complete assurance/guarantee in the above situation? Discuss with reference to objectives of Audit. (RTP Jan 2026)</p>
	<ul style="list-style-type: none"> ▶ As per SA 200 “Overall Objectives of the Independent Auditor & the Conduct of an Audit in Accordance with Standards on Auditing”, auditor’s objective is to obtain a reasonable assurance whether FS as a whole are free from material misstatement whether due to fraud or error. <ul style="list-style-type: none"> (i) Reasonable assurance is to be distinguished from absolute assurance. Absolute assurance is a complete assurance or a guarantee that FS are free from material misstatements. However, reasonable assurance is not a complete guarantee. Although it is a high-level of assurance, but it is not complete assurance. Audit of FS is carried out by the auditor with professional competence & skills in accordance with Standards on Auditing. Audit procedures are applied in accordance with SAs, audit evidence is obtained & evaluated. On basis of that, conclusions are drawn, & opinion is formed. It leads to high level of assurance which is called reasonable assurance but it is not absolute assurance. (ii) Misstatements in FS can occur due to fraud or error or both. The auditor seeks to obtain reasonable assurance whether FS as a whole are free from material misstatements caused by fraud or error. He has to see effect of misstatements on FS as a whole, in totality. (iii) Obtaining reasonable assurance that FS as a whole are free from material misstatements enables the auditor to express an opinion on whether the FS are prepared, in all material respects, in accordance with an AFRF. (iv) The opinion is reported & communicated in accordance with audit findings through a written report as required by Standards on Auditing. ▶ Thus, it can be concluded that auditors can provide reasonable assurance instead of absolute assurance.
9.	<p>Explain the term “Applicable Financial Reporting framework” in context of the relevant Standard on Auditing. (4 Marks Nov 2019/2017) (RTP Nov 2011)</p> <ul style="list-style-type: none"> ▶ Applicable financial reporting framework means a framework adopted in the preparation and presentation of the FS that is acceptable in view of the nature of the entity and the objective of the FS, or that is required by law or regulation. ▶ For eg., in case of companies in India, financial reporting framework is provided under Schedule III of Companies Act, 2013.
10.	<p>Mini & Associates, Chartered Accountants, were appointed as the auditor of CIN Ltd., a construction company. During the audit, CA Mini, a Partner of the firm noticed the following:</p> <ul style="list-style-type: none"> ▶ The company has several ongoing projects, but only selected project revenues have been reported. ▶ Several expense vouchers are either missing or are handwritten & lack proper authorisation. ▶ The company has changed its depreciation method from the straight-line method to the written-down value method without adequate disclosure in the FS. <p>These matters were brought to the attention of management. However, management argued that these issues fall outside the auditor’s scope of responsibility. Whether contention of the management is correct? (RTP Sep 2025)</p>
	<p>THE FOLLOWING POINTS ARE INCLUDED IN SCOPE OF AUDIT OF FS:</p> <ol style="list-style-type: none"> 1. Coverage of all aspects of entity <ul style="list-style-type: none"> ▶ Audit of FS should be organised adequately to cover all aspects of the entity relevant to the FS being audited. 2. Reliability & sufficiency of financial information <ul style="list-style-type: none"> ▶ The auditor should be reasonably satisfied that information contained in underlying accounting records & other source data (like bills, vouchers, documents etc.) is reliable & sufficient basis for preparation of FS. ▶ The auditor makes a judgment of reliability & sufficiency of financial information by making a study & assessment of accounting systems & internal controls & by carrying out appropriate tests, enquiries & procedures. 3. Proper disclosure of financial information <ul style="list-style-type: none"> ▶ The auditor should decide whether relevant information is properly disclosed in the FS. He should also keep in mind applicable statutory requirements in this regard. ▶ It is done by ensuring that FS properly summarize transactions & events recorded therein & by considering the judgments made by management in preparation of FS. <p>In view of above, the management’s contention is not correct. The matters identified by CA Mini such as incomplete revenue recognition, missing or unauthorised expense vouchers, & inadequate disclosure of changes in accounting</p>

	policy are well within the scope of the audit of FS, as they impact the reliability, completeness, & proper presentation of financial information.
11.	<p>“Choosing of appropriate accounting policies in relation to accounting issues is responsibility of management”. Do you agree? Discuss duty of auditor, if any, in relation to accounting policies.</p> <ul style="list-style-type: none"> ➤ Choosing of appropriate accounting policies is responsibility of management. The role of auditor lies in evaluating selection & consistent application of accounting policies by management. ➤ Refer - Scope of audit- what it includes – in answer above
12.	<p>The auditor should decide whether relevant information is properly disclosed in the FS. Explain with reference to scope of audit.</p> <ul style="list-style-type: none"> ➤ Refer – Proper Disclosure of Financial Information - Scope of audit- what it includes – in answer above
13.	<p>The auditor should decide whether relevant information is properly disclosed in the FS. Explain with reference to scope of audit.</p> <ul style="list-style-type: none"> ➤ Refer – Proper Disclosure of Financial Information - Scope of audit- what it includes – in answer above ➤ The management responsible for preparation & presentation of FS makes many judgments in this process of preparing & presenting FS. For example, choosing of appropriate accounting policies in relation to various accounting issues like choosing method of charging depreciation on fixed assets or choosing appropriate method for valuation of inventories. ➤ The auditor evaluates selection & consistent application of accounting policies by management; whether such a selection is proper & whether chosen policy has been applied consistently on a period-to-period basis.
14.	<p>XYZ Ltd., a manufacturing company based in India, operates multiple plants across the country & deals in complex machinery, which requires specialized maintenance & valuation expertise. XYZ Ltd. appointed CA Dhruv as Statutory auditor. During the audit, he observed that the management consistently applied the same method for valuation of inventory over the past few years, but this year, without proper disclosure, they switched to a different valuation method, which resulted in higher reported profits. Does such a matter fall within scope of audit? (RTP May 2025)</p> <ul style="list-style-type: none"> ➤ The purpose of an audit is to enhance the degree of confidence of intended users in the FS. The scope of audit of FS includes coverage of all aspects of entity, reliability & sufficiency of financial information & proper disclosure of financial information. ➤ In the given situation, CA. Dhruv observed that the management consistently applied the same method for valuation of inventory over the past few years, but this year, without proper disclosure, they switched to a different valuation method, which resulted in higher profits. Since proper disclosure of financial information is covered under the scope of audit, thus, the auditor should decide whether relevant information is properly disclosed in the FS. He should also keep in mind applicable statutory requirements in this regard. ➤ Refer answer above ➤ Thus, it can be concluded that proper disclosure of financial information is well within scope of audit.
15.	<p>RST Ltd., a mid-sized trading company, recently faced challenges in securing a bank loan due to doubts about the reliability of its FS. The management realised the importance of having audited accounts to build confidence among lenders & other stakeholders. Elucidate the benefits & need of an audit. OR</p> <p>The chief utility of audit lies in reliable FS on the basis of which the state of affairs may be easy to understand. Apart from this obvious utility, there are other advantages of audit. Some or all of these are of considerable value even to those enterprises & organisations where audit is not compulsory. Explain. OR</p> <p>“Having accounts audited by independent auditor, among other advantages, acts as a moral check on the employees from committing fraud.” Explain stating the advantages of independent audit.</p> <p style="text-align: right;">(5/8 Marks May 2015/2012/2008) (RTP May 2019/2015/2011/Nov 2018/2016/2013)</p>
	<p>Benefits & need of Audit:</p> <ul style="list-style-type: none"> ➤ Audited accounts provide high quality information. It gives confidence to users that information on which they are relying is qualitative & it is the outcome of an exercise carried out by following Auditing Standards recognized globally. ➤ In case of companies, shareholders may or may not be involved in daily affairs of the company. The FS are prepared by management consisting of directors. As shareholders are owners of the company, they need an independent mechanism so that financial information is qualitative & reliable. Hence, their interest is safeguarded by an audit.