1. (a) Considerations for Planning and Performing Audit in case of Special Purpose Framework:
As per SA 800 “Special Considerations-Audits of Financial Statements Prepared in accordance with Special Purpose Frameworks”, financial statements prepared in accordance with a special purpose framework may be the only financial statements an entity prepares. In such circumstances, those financial statements may be used by users other than those for whom the financial reporting framework is designed.

While planning and performing audit of such special purpose framework based company, the auditor should consider below mentioned factors:

(i) To obtain an understanding of the entity’s selection and application of accounting policies. In the case of financial statements prepared in accordance with the provisions of a contract, the auditor shall obtain an understanding of any significant interpretations of the contract that management made in the preparation of those financial statements.

(ii) Compliance of all SAs relevant to audit, the auditor may judge it necessary to depart from a relevant requirement in an SA by performing alternative audit procedures to achieve the aim of that requirement.

(iii) Application of some of the requirements of the SAs in an audit of special purpose financial statements may require special consideration by the auditor. For example, in SA 320, judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. In the case of an audit of special purpose financial statements, however, those judgments are based on a consideration of the financial information needs of the intended users.

(iv) In the case of special purpose financial statements, such as those prepared in accordance with the requirements of a contract, management may agree with the intended users on a threshold below which misstatements identified during the audit will not be corrected or otherwise adjusted. The existence of such a threshold does not relieve the auditor from the requirement to determine materiality in accordance with SA 320 for purposes of planning and performing the audit of the special purpose financial statements.

(v) Communication with those charged with governance in accordance with SAs is based on the relationship between those charged with governance and the financial statements subject to audit, in particular, whether those charged with governance are responsible for overseeing the preparation of those financial statements. In the case of special purpose financial statements, those charged with governance may not have such a responsibility.

(b) Verification of Accounts Receivable: As per SA 510 “Initial Audit Engagements – Opening Balances”, while conducting an initial audit engagement, the objective of the auditor with respect to opening balances is to obtain sufficient appropriate audit evidence about whether-

(i) Opening balances contain misstatements that materially affect the current period’s financial statements; and

(ii) Appropriate accounting policies reflected in the opening balances have been consistently applied in the current period’s financial statements, or changes thereto are properly accounted for and adequately presented and disclosed in accordance with the applicable financial
reporting framework.

When the financial statements for the preceding period were audited by another auditor, the current auditor may be able to obtain sufficient appropriate audit evidence regarding opening balances by perusing the copies of the audited financial statements.

Ordinarily, the current auditor can place reliance on the closing balances contained in the financial statements for the preceding period, except when during the performance of audit procedures for the current period the possibility of misstatements in opening balances is indicated.

For current assets and liabilities, some audit evidence about opening balances may be obtained as part of the current period’s audit procedures, say, the collection of opening accounts receivable during the current period will provide some audit evidence of their existence, rights and obligations, completeness and valuation at the beginning of the period.

In addition, according to SA 580 “Written Representations”, the auditor may consider it necessary to request management to provide written representations about specific assertions in the financial statements; in particular, to support an understanding that the auditor has obtained from other audit evidence of management’s judgment or intent in relation to, or the completeness of, a specific assertion. Although such written representations provide necessary audit evidence, they do not provide sufficient appropriate audit evidence on their own for that assertion.

In the given case, the management of Futura (P) Ltd. has restrained CA. Jack, its auditor, from obtaining appropriate audit evidence for balances of Accounts Receivable outstanding as it is from the preceding year. CA. Jack, on believing that the preceding year balances have already been audited and on the statement of the management that there are no receipts and credits during the current year, therefore excluded the verification of Accounts Receivable from his audit programme.

Thus, CA. Jack should have requested the management to provide written representation for their views and expressions; and he should also not exclude the audit procedure of closing balances of Accounts Receivable from his audit programme. Consequently, CA. Jack shall also be held guilty for professional misconduct for not exercising due diligence, or grossly negligence in the conduct of his professional duties as per the Code of Ethics.

(c) (1) Difference of Opinion Among Joint Auditors: SA 299 on, “Responsibility of Joint Auditors” deals with the professional responsibilities, which the auditors undertake in accepting such appointments as joint auditors. In respect of the work divided amongst the joint auditors, each joint auditor is responsible only for the work allocated to him, whether or not he has made a separate report on the work performed by him. On the other hand the joint auditors are jointly and severally responsible in respect of the audit conducted by them as under:

(i) in respect of the audit work which is not divided among the joint auditors and is carried out by all of them;
(ii) in respect of decisions taken by all the joint auditors concerning the nature, timing or extent of the audit procedures to be performed by any of the joint auditors;
(iii) in respect of matters which are brought to the notice of the joint auditors by any one of them and on which there is an agreement among the joint auditors;
(iv) for examining that the financial statements of the entity comply with the disclosure requirements of the relevant statute;
(v) for ensuring that the audit report complies with the requirements of the relevant statute;
(vi) it is the separate and specific responsibility of each joint auditor to study and evaluate the prevailing system of internal control relating to the work allocated to him, the extent of enquiries to be made in the course of his audit;
(vii) the responsibility of obtaining and evaluating information and explanation from the
management is generally a joint responsibility of all the auditors;

(viii) each joint auditor is entitled to assure that the other joint auditors have carried out their part of work in accordance with the generally accepted audit procedures and therefore it would not be necessary for joint auditor to review the work performed by other joint auditors.

Normally, the joint auditors are able to arrive at an agreed report. However where the joint auditors are in disagreement with regard to any matters to be covered by the report, each one of them should express their own opinion through a separate report. A joint auditor is not bound by the views of majority of joint auditors regarding matters to be covered in the report and should express his opinion in a separate report in case of a disagreement.

In the instant case, there are three auditors, namely, Mr. X, Mr. Y and Mr. Z, jointly appointed as an auditor of KRP Ltd. For the valuation of gratuity scheme of the Company they referred their own known Actuaries. Mr. Z (one of the joint auditor) is not satisfied with the report submitted by Mr. Y’s referred actuary. He is not agreed with the matters to be covered by the report whereas Mr. X agreed with the same.

Hence, as per SA 299, Mr. Z is suggested to express his own opinion through a separate report whereas Mr. X and Mr. Y may provide their joint report for the same.

(2) Using the work of an Auditor’s Expert: As per SA 620 “Using the Work of an Auditor’s Expert”, the expertise of an expert may be required in the actuarial calculation of liabilities associated with insurance contracts or employee benefit plans etc., however, the auditor has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the auditor’s use of the work of an auditor’s expert.

The auditor shall evaluate the adequacy of the auditor’s expert’s work for the auditor’s purposes, including the relevance and reasonableness of that expert’s findings or conclusions, and their consistency with other audit evidence as per SA 500.

Further, in view of SA 620, if the expert’s work involves use of significant assumptions and methods, then the relevance and reasonableness of those assumptions and methods must be ensured by the auditor and if the expert’s work involves the use of source data that is significant to that expert’s work, the relevance, completeness, and accuracy of that source data in the circumstances must be verified by the auditor.

In the instant case, Mr. X, Mr. Y and Mr. Z, jointly appointed as an auditor of KRP Ltd., referred their own known Actuaries for valuation of gratuity scheme. Actuaries are an auditor’s expert as per SA 620. Mr. Y’s referred actuary has provided the gratuity valuation report, which later on found faulty. Further, Mr. Z is not agreed with this report therefore he submitted a separate audit report specifically for such gratuity valuation.

In such situation, it was duty of Mr. X, Mr. Y and Mr. Z, before using the gratuity valuation report of Actuary, to ensure the relevance and reasonableness of assumptions and methods used. They were also required to examine the relevance, completeness and accuracy of source data used for such report before expressing their opinion.

Mr. X and Mr. Y will be held responsible for grossly negligence and using such faulty report without examining the adequacy of expert actuary’s work whereas Mr. Z will not be held liable for the same due to separate opinion expressed by him.

2. **(a) Internal Control System:** In order to achieve proper internal control over the sale of tickets and its collection by Funtooosh Ltd., following system should be adopted-

(i) **Printing of tickets:** Serially numbered pre-printed tickets should be used and designed in such a way that any type of ticket used cannot be duplicated by others in order to avoid
forgery. Serial numbers should not be repeated during a reasonable period, say a month or year depending on the turnover. The separate series of the serial should be used for such denomination.

(ii) **Ticket sales:** The sale of tickets should take place from the Central ticket office at each of the 5 centres, preferably through machines. There should be proper control over the keys of the machines.

(iii) **Daily cash reconciliation:** Cash collection at each office and machine should be reconciled with the number of tickets sold. Serial number of tickets for each entertainment activity/denomination will facilitate the reconciliation.

(iv) **Daily banking:** Each day’s collection should be deposited in the bank on next working day of the bank. Till that time, the cash should be in the custody of properly authorized person preferably in joint custody for which the daily cash in hand report should be signed by the authorized persons.

(v) **Entrance ticket:** Entrance tickets should be cancelled at the entrance gate when public enters the centre.

(vi) **Advance booking:** If advance booking of facility is made available, the system should ensure that all advance booked tickets are paid for.

(vii) **Discounts and free pass:** The discount policy of the Y Co. Ltd. should be such that the concessional rates, say, for group booking should be properly authorized and signed forms for such authorization should be preserved.

(viii) **Surprise checks:** Internal audit system should carry out periodic surprise checks for cash counts, daily banking, reconciliation and stock of unsold tickets etc.

**Services not to be rendered by Auditor:** Section 144 of the Companies Act, 2013 prescribes certain services not to be rendered by the auditor. An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case may be, but which shall not include any of the services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company), as prescribed.

Further section 141(3)(i) of the Companies Act, 2013 disqualifies a person for appointment as an auditor of a company who, directly or indirectly, renders any service referred to in section 144 to the company or its holding company or its subsidiary company. Section 144 of the Companies Act, 2013 prescribes certain services not to be rendered by the auditor which includes investment advisory services.

Additionally, in accordance with section 141(4) of the Act, where a person appointed as an auditor of a company incurs any of the disqualifications mentioned in sub-section (3) after his appointment, he shall vacate his office as such auditor and such vacation shall be deemed to be a casual vacancy in the office of the auditor.

In the given case, M/s Raga & Co., Chartered Accountants, was appointed as an auditor of R Ltd. Further, the company offered investment advisory services to M/s Swara & Co., an associate of M/s Raga & Co., which has also been duly accepted by the firm. Therefore, M/s Raga & Co. is disqualified to hold office as an auditor of R Ltd. as per the provisions explained above.

Subsequently, M/s Raga & Co. shall have to vacate the office of auditor of R Ltd. accordingly.

**Special Features of Co-operative Society Audit:** The special features of co-operative society audit, to be borne in mind in general while conducting the audit are examination of overdue debts, overdue Interest, certification of bad debts, valuation of assets and liabilities, adherence to co-operative principles, reporting infringement of act and rules, verification of members’ register and
examination of their pass books, special report to the registrar, audit classification of co-operative society, discussion of draft audit report with managing committee etc.

Besides the other special features mentioned above the Examination of overdue debts, audit classification of society and reporting the infringement of provisions of the Act, are some of special features of audit of a co-operative society which are explained as follows:

(i) **Examination of overdue debts**: Auditor of a co-operative society has to classify the overdue debts for a period from 6 months to five years and more than 5 years. Further these debts are to be analyzed in 'good' or 'bad' depending on the recoverability of the debts. The bad and doubtful debts require some provision and the auditor has to ascertain whether proper provision for bad & doubtful debts has been made. The current year's amount of overdue debts and its ratio to the working capital and loans outstanding is to be compared with last year to know whether the trend is increasing or decreasing. The status of the court cases for recovery of the overdue debts is also to be mentioned in the audit report. While calculating the profit the interest on the overdue debts is not to be taken into account. The Bad debts portion of the overdue debts is to be certified by the auditor for the purpose of writing off.

(ii) **Audit Classification of Co-operative Society**: It is a unique feature of the Co-operative audit. After completion of the audit the auditor has to evaluate the working of the society on the basis of various parameters and criteria which are specified by the Registrar. It may be noted here that if the management of the society is not satisfied about the award of audit class, it can make an appeal to the Registrar, and the Registrar may direct to review the audit classification. The auditor should be very careful, while making a decision about the class of society. For good performance having certain marks “A class is given. The D class is given to the society which shows very poor performance. In the same way B or C class is awarded on the basis of the marks obtained by the society.

(iii) **Reporting infringement of Act and Rules**: The auditor of the co-operative Society is required to report the non compliance of the various provisions of the Co-operative Societies Act, Rules framed under that Act and the by laws of the society. He has to assess the financial implications of such infringements and disclose the same in his report. The infringements of serious nature are to be reported separately and infringements which do not have financial implications and which have no serious effect on the working of the society or rights of the members may be reported separately.

Thus, we can say that Examination of overdue debts, audit classification of society and reporting the infringement of provisions of the Act, are only some of special features of audit of a co-operative society.

(d) **Control Procedure While Applying Computer Assisted Auditing Techniques (CAATs)**: Computer Assisted Auditing Techniques (CAATs) involve performing audit procedures while conducting audit through the computer. Audit software and Test Data are two common types of CAATs. Using CAATs involves taking various measures including monitoring so that the use of CAATs by the auditor provides reasonable assurance that the audit objectives and detailed specifications of CAATs have been met. It is to be seen that CAATs are not manipulated by staff of the entity. The specific procedures necessary to control the use of CAATs will depend on the particular application.

Procedures carried out by the auditor to control CAATs applications may include:

(i) participating in the design and testing of CAAT;

(ii) checking, if applicable, the coding of the program to ensure that it conforms with the detailed program specifications;

(iii) asking the entity’s staff to review the operating system instructions to ensure that the software will run in the entity’s computer installation;
running the audit software on small test files before running it on the main data files;
checking whether the correct files were used, for example, by checking external evidence, such as control totals maintained by the user, and that those files were complete;
obtaining evidence that the audit software functioned as planned, for example, by reviewing output and control information; and
establishing appropriate security measures to safeguard the integrity and confidentiality of the data.

When using a CAAT, the auditor may require the cooperation of the entity’s staff who have extensive knowledge of the computer installation. In such circumstances, the auditor should have reasonable assurance that the entity’s staff did not improperly influence the results of the CAATs.

3. (a) Reporting under CARO, 2016

(i) Utilisation of Term Loans: According to clause (ix) of Para 3 of CARO, 2016, the auditor is required to report “whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans were applied for the purposes for which they are raised. If not, the details together with delays or default and subsequent rectification, if any, as may be applicable”.

The auditor should examine the terms and conditions of the term loan with the actual utilisation of the loans. If the auditor finds that the fund has not been utilized for the purpose for which they were obtained, the report should state the fact.

In the instant case, term loan taken for the purpose of R&D equipment has been utilized for the purchase of car which has no relation with R&D equipment.

Therefore, car though used for R&D Director cannot be considered as R&D equipment. The auditor should state the fact in his report as per Paragraph 3 clause ix of the CARO 2016, that out of the term loan taken for R&D equipment, Rs. 15 lakh was not utilised for the purpose of acquiring R&D equipment.

(ii) Non-Compliance of Laws and Regulations & Reporting Requirements: As per SA 250 “Consideration of Laws and Regulations in an Audit of Financial Statement”, it is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity’s operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity’s financial statements. The auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether caused by fraud or error. In conducting an audit of financial statements, the auditor takes into account the applicable legal and regulatory framework. If the auditor concludes that the non-compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements, the auditor shall express a qualified or adverse opinion on the financial statements.

Further, the auditor is required to report under clause (vii)(a) of Para 3 of CARO, 2016 whether the company is regular in depositing undisputed statutory dues including employees’ state insurance with the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as at the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated by the auditor.

In the instant case, even though accrual principles have been followed, disclosure of non-payment is necessary. The auditor should disclose the fact of non-payment of rupees 7.50 lakhs in his report.

(b) Bringing Disrepute to the Profession: A member is liable to disciplinary action under section 21 of the Chartered Accountants Act, 1949, if he is found guilty of any professional or “Other
“Misconduct”. As per Clause (2) of Part IV of the First Schedule to the said Act, a member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he, in the opinion of the Council, brings disrepute to the profession or the Institute as a result of his action whether or not related to his professional work.

A member may be found guilty of “Other Misconduct” as per Clause (2) under the aforesaid provisions rendering himself unfit to be member if he retains the books of account and documents of the client and fails to return these to the client on request without a reasonable cause.

In the given case, CA. X failed to return the books of accounts and other documents of his client without any reasonable cause, therefore, he would be guilty of other misconduct under the aforesaid provisions.

(c) Responsibility of Holding Company for Preparation of Consolidated Financial Statements:

As per section 129(3) of the Companies Act, 2013, where a company has one or more subsidiaries, it shall, in addition to its own financial statements prepare a consolidated financial statement of the company and of all the subsidiaries in the same form and manner as that of its own. The responsibility for the preparation and presentation of consolidated financial statements, among other things, is that of the management of the parent/holding company. This includes:

(i) identifying components, and including the financial information of the components to be included in the consolidated financial statements;
(ii) where appropriate, identifying reportable segments for segmental reporting;
(iii) identifying related parties and related party transactions for reporting;
(iv) obtaining accurate and complete financial information from components; and
(v) making appropriate consolidation adjustments.

Apart from the above, the parent ordinarily issues instructions to the management of the component specifying the parent’s requirements relating to financial information of the components to be included in the consolidated financial statements. The instructions ordinarily cover the accounting policies to be applied, statutory and other disclosure requirements applicable to the parent, including the identification of and reporting on reportable segments, and related parties and related party transactions, and a reporting timetable.

4. (a) (1) Advances to DOT COM Companies:

(i) Evaluate the efficacy of internal control system in general to ascertain whether an advance is made only after satisfying itself as to the credit worthiness of the borrower and after obtaining sanction from the appropriate authorities of the bank. The sanction for an advance must specify, among other things, the limit of borrowing, nature of security, margin to be kept, interest, terms of repayment, etc. Also see that all the necessary documents, e.g., agreements, demand promissory notes, letters of hypothecation, etc. have been executed by the parties before advances are made.

(ii) Examine loan documents such as certificate of commencement of business, resolution of board of directors, and resolution of shareholders.

(iii) Verify the business plan of the company especially where the revenue model is in place. Verify whether the company depends only on outside funding or can self generate funds.

(iv) Examine in case the security is in the form of mortgage, apart from mortgage deed (in the case of English Mortgage) or letter of intent to create mortgage (in the case of Equitable Mortgage), the evidence of registration of the charge with the Registrar of Companies.

(v) Review the operation of advance account to see that limit is not generally exceeded; that the account is not becoming stagnant; that the customer is not drawing against deposits
which are not free from lien; that the account is not window-dressed by running down
overdrafts at the year end and again drawing further advances in the new year, etc.

(vi) Examine whether there is a healthy turnover in the account. It should be seen that the
frequency and the amounts of credits in the account are commensurate with the
sanctioned limit and the nature and volume of business of the borrower. Any unusual
items in the account should be carefully examined by the auditor. If the auditor's review
indicates any unhealthy trends, the account should be further examined. The auditor's
examination should also cover transactions in the post-balance sheet date period. Large
transactions in major accounts particularly as at the year-end may be looked into to
identify any irregularities in these accounts.

(vii) Review periodic statements, cash flow statements, latest financial statements, etc. to
assess the recoverability of advances.

(viii) Verify whether the advance is secured and determine whether the security is legally
enforceable, i.e., whether the necessary legal formalities regarding documentation,
registration, etc., have been complied with; whether the security is in the effective control
of the bank; and to what extent the value of the security, assessed realistically, covers
the amount outstanding in the advance.

(ix) Ensure that proper provisioning norms have been applied in view of non-observance of
terms, coupled with irregular payment of interest and default in repayment of instalments,
if any.

(2) Balances in Account of a Bank situated in a Foreign Country:

(i) Verify the ledger balances in each account with reference to the bank confirmation
certificates and reconciliation statements as at the year-end.

(ii) Review the reconciliation statements and pay particular attention to the following.

(1) Examine that no debit for charges or credit for interest is outstanding and all the
items which ought to have been taken to revenue for the year have been so taken.
This should be particularly observed when the bills collected, etc., are credited with
net amount and entries for commission, etc. are not made separately in the
statement of account.

(2) Examine that no cheque sent or received in clearing is outstanding. As per the
practice prevalent among banks, any cheques returned unpaid are accounted for
on the same day on which they were sent in clearing or on the following day.

(3) Examine that all bills or outstanding cheques sent for collection and outstanding as
on the closing date have been credited subsequently.

(iii) Examine the large transactions in inter-bank accounts, particularly towards the year-end,
to ensure that no transactions have been put through for window-dressing.

(iv) Check original deposit receipts in respect of balances in deposit accounts in addition to
confirmation certificates obtained from banks in respect of outstanding deposits.

(v) Check whether these balances are converted into the Indian currency at the exchange
rates prevailing on the balance sheet date and ensure compliance with AS 11 on
"Accounting for the Effects of Changes in Foreign Exchange Rates".

(b) Specific Permission for Holding Office of Managing Director: As per Clause (11) of Part I of
the First Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice
shall be deemed to be guilty of professional misconduct if he engages in any business or
occupation other than the profession of chartered accountant unless permitted by the Council so
to engage.
Further, regulation 190A of the Chartered Accountants Regulation, 1988 provides that a Chartered Accountant in practice shall not engage in any other business or occupation other than the profession of accountancy except with the permission granted in accordance with a resolution of the Council. According to the same, specific permission from the council would be necessary for holding office of managing director or a whole-time director of a body corporate.

In the given case, CA. Laxya has immediately joined the office of managing director of Rahi Pvt. Ltd. without obtaining specific or prior approval of the Council. Therefore, CA. Laxya will be held guilty of professional misconduct under Clause (11) of Part I of the First Schedule to the Chartered Accountants Act, 1949.

(c) **Main Areas to be covered in the Case of Environment Audit of an Industrial Unit:**

(i) **Layout and Design** – The layout to be sketched in the style which will allow adequate provisions for installing pollution control devices, as well as provision for upgradation of pollution control measures and the meeting of the requirements of the regulations framed by the Government. In the course of the audit, the area which requires attention but not attended to by the industry to be pinpointed as well as the future requirements of the environmental measures required in commensuration with the proposed future course of working plan are to be identified.

(ii) **Management of Resources** – Management resources includes air, water, land, energy, raw materials and human resources besides others. The use of all resources is interlinked and the best uses in a synchronised manner results the best output and minimum waste. The waste of resources to the minimum possible extent is good for the health of the industry as well as the environment.

(iii) **Pollution Control System** – An effective system of pollution control should be in existence. One aspect should be whether all required pollution control measures are in vogue or not. Next aspect should be whether the same is effective or not. Further, it is to investigate, whether more measures are required, keeping in view the type of industry and its nature of working with respect to its grade of polluting the environment.

(iv) **Emergent Safety Arrangement** – The chemical, gas, etc., industries which are prone to sudden requirement of safety arrangements, must remain alert all the while. The emergency plans are to be reviewed periodically; sufficient staff along with other required safety amenities should be kept ready. The staff, remained so engaged, must possess the required awareness and alertness to meet the contingency. The degree of awareness, however, can be upgraded with proper training provisions.

(v) **Medical & Healthcare Facilities** – The medical services should be maintained. The health of the workers should be a big consideration for the management.

(vi) **Industrial Hygiene** – Proper system should be in vogue to eliminate industrial unhygienic state.

(vii) **Occupational Health** – The requirement for safeguarding against occupational health hazards should be available for all the workers. As the occupational health hazards varies from industry to industry due to the difference in the nature of working atmosphere and the pollutants present in it, the concerned industry must pay proper weightage to those diseases which are prone to that particular type of industry.

(viii) **Information Assimilation and Reporting System** – The information system should be strengthened to generate and its reporting system should be proper, keeping in view, the authorities, responsibilities and subsequent delegations. A report of compliance of all statutory environmental laws along with other preventive and precautionary measures should be put to Board at regular intervals.
(ix) **EIA Methodology** – The Environmental Impact Assessment (EIA) is usually a pre-requisite to start an industry. This is done considering the known spheres of activities on the existing environmental conditions. But the predictions necessarily deviate from the actual happenings when the industry starts working. To accommodate the deviation in the system is also to be incorporated in the EIA report, if it is noticed that the degradation to the environment caused on the establishment and running of the industry is much higher than what was predicted, the mitigatory measures suggested must also be furthered.

(x) **Compliance to the Regulatory Mechanism** – As the persons who are directly working with the system, may be unaware of the latest developments and requirements for the compliance of stipulations and standards prescribed by the various regulatory authorities, they should be trained and instructed on regular basis, to avoid making the Board/owner vulnerable to prosecution and penalty.

(xi) **Concern for the Society** – The industry very often transforms the agrarian environment into an industrial environment. The people so displaced by industrialisation feel alienated and develop a feeling of facing the gaseous, dustful, clumsy state of surroundings. The audit should look into this aspect how the industry is making a balance between its own development and the society’s concern.

5. **(a) The following areas need to be verified in case of embezzlement in cash receipts:**

   (i) Issuing a receipt to the payee for the full amount collected and entering only a part of the amount on the counterfoil.

   (ii) Showing a larger cash discount than actually allowed.

   (iii) Adjusting a fictitious credit in the account of a customer for the value of goods returned by him.

   (iv) Adjusting a cash sale as a credit sale, and raising a debit in the account of the customer.

   (v) Writing off a good debt as bad and irrecoverable to cover up the amount collected which has been misappropriated.

   (vi) Short-debiting the customer’s account in the ledger with an intention to withdraw the difference when the full amount payable by him is collected.

   (vii) Under-casting the receipts side of the Cash Book or over-casting the payment side; carrying over a shorter total of the receipts from one page of the Cash Book to the next or over-carrying the total of the payment from one page of the Cash Book to the next with a view to covering up misappropriation; either short banking of cash collection or apart of the amount withdrawal from the bank.

   **(b) Examination of Claims Paid in respect of a General Insurance Company:** The auditor may determine the extent of checking of claims paid on the same line as suggested for outstanding claims. Other aspects in respect of claims paid to be examined by the auditors are as follows -

   (i) that in case of co-insurance arrangements, claims paid have been booked only in respect of company’s share and the balance has been debited to other insurance companies;

   (ii) that in case of claims paid on the basis of advices from other insurance companies (where the company is not the leader in co-insurance arrangements), whether share of premium was also received by the company. Such claims which have been communicated after the year-end for losses which occurred prior to the year end must be accounted for in the year of audit;

   (iii) that the claims payments have been duly sanctioned by the authority concerned and the payments of the amounts are duly acknowledged by the claimants;

   (iv) that the salvage recovered has been duly accounted for in accordance with the procedure applicable to the company and a letter of subrogation has been obtained in accordance with the laid down procedure;
(v) that the amounts of the nature of pure advances/deposits with Courts, etc., in matters under litigation/arbitration have not been treated as claims paid but are held as assets till final disposal of such claims. In such cases, full provision should be made for outstanding claims;

(vi) that payment made against claims partially settled have been duly vouched. In such cases, the sanctioning authority should be the same as the one which has powers in respect of the total claimed amount;

(vii) that in case of final settlement of claims, the claimant has given an unqualified discharge note, not involving the company in any further liability in respect of the claim; and

(viii) that the figures of claims, wherever communicated for the year by the Division to the Head Office for purposes of reinsurance claims, have been reconciled with the trial balance-figure.

(c) Failure to Observe Regulations: As per Clause (1) of Part II of Second Schedule to the Chartered Accountants Act, 1949, a member shall be held guilty of professional misconduct if he contravenes any of the provisions of the Act or the regulations made thereunder or any guidelines issued by the Council. The chartered accountant, as per Regulations also, is expected to impart proper practical training.

In the instant case, the articled assistant is not attending office on timely basis and the explanation of the Chartered Accountant that the articled assistant was on audit of the company cannot be accepted particularly in view of the fact that articled assistant is getting monthly salary from that company. Under the circumstances, the Chartered Accountant would be held guilty of professional misconduct in regard to the discharge of his professional duties.

6. (a) Classification of Frauds by NBFC and its Reporting: In order to have uniformity in reporting, frauds have been classified as under based mainly on the provisions of the Indian Penal Code-

(i) Misappropriation and criminal breach of trust.
(ii) Fraudulent encashment through forged instruments, manipulation of books of account or through fictitious accounts and conversion of property.
(iii) Unauthorised credit facilities extended for reward or for illegal gratification.
(iv) Negligence and cash shortages.
(v) Cheating and forgery.
(vi) Irregularities in foreign exchange transactions.
(vii) Any other type of fraud not coming under the specific heads as above.

Cases of ‘negligence and cash shortages’ and ‘irregularities in foreign exchange transactions’ referred to in items (iv) and (vi) above are to be reported as fraud if the intention to cheat/defraud is suspected/ proved. However, the following cases where fraudulent intention is not suspected/ proved, at the time of detection, will be treated as fraud and reported accordingly:

(i) cases of cash shortages more than Rs. 10,000/- and
(ii) cases of cash shortages more than Rs. 5000/- if detected by management/ auditor/ inspecting officer and not reported on the occurrence by the persons handling cash.

NBFCs having overseas branches/offices should report all frauds perpetrated at such branches/offices also to the Reserve Bank as per the prescribed format and procedures.

(b) Form 3CD: The audit under section 44AB of the Income Tax Act 1961 requires that the tax auditor should report whether in his opinion the particulars in respect of Form 3CD are true and correct. It is the primary responsibility of the assessee to prepare the information in form 3CD. The auditor has to examine whether the information given is true and correct. The form 3CD is not a report of Tax Auditor. The report is in the form of 3CA or 3CB depending on the nature of the organization of the entity. If the tax auditor is satisfied that the information contained in form 3CD is true and correct then he can give unqualified report in form 3CA or 3CB saying “in my opinion and to the
best of my information and according to the explanations given to me and considering the materiality the particulars given in form 3CD are true and correct." But in the given case the tax auditor has found that the form 3CD contains the incomplete, misleading and false information.

Disallowance under section 40A(3) is attracted if the assessee incurs any expenses in respect of which payment of aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on bank or account payee draft exceeds Rs. 10,000. However, exemption is provided in respect of certain expenditure in Rule 6DD. In such cases, disallowance under section 40A(3) would not be attracted.

Under clause 21(d)(A) of Form 3CD, the tax auditor has to scrutinize on the basis of the examination of books of account and other relevant documents/evidence, whether the expenditure covered under section 40A(3) read with rule 6DD were made by account payee cheque drawn on a bank or account payee bank draft. If not, the same has to be reported under abovementioned clause.

Cash payment made on insistence of other parties on the contention that they do not have bank accounts is not covered under the list of exceptions provided under Rule 6DD. Therefore, Mr. R has to report the payments inadmissible under section 40A(3) under clause 21(d)(A) of Form 3CD.

(c) **The factors to be considered to analyse causes for high employee attrition rate are as under:**

2. Wrong policies of the Management.
3. Unbearable behaviour of Senior Staff.
5. Limited opportunities for promotion.
7. Lack of labour welfare schemes.
8. Whether the organization has properly qualified and experienced personnel for the various levels of works?
9. Is the number of people employed at various work centres excessive or inadequate?
10. Does the organization provide facilities for staff training so that employees and workers keep themselves abreast of current techniques and practices?

(d) **Charging of Fees Based on Percentage of Profits:** According to Clause (10) of Part I of First Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice shall be deemed to be guilty of professional misconduct if he charges or offers to charge, accepts or offers to accept in respect of any professional employment fees which are based on a percentage of profits or which are contingent upon the findings, or results of such employment, except as permitted under any regulations made under this Act.

However, CA Regulation allow the Chartered Accountant in practice to charge the fees in respect of any professional work which are based on a percentage of profits, or which are contingent upon the findings or results of such work, in the case of a receiver or a liquidator, and the fees may be based on a percentage of the realization or disbursement of the assets.

In the given case, CA. M, a practicing Chartered Accountant, has acted as liquidator of XYZ & Co. and charged his professional fees on percentage of the realisation of assets.

Therefore, CA. M shall not be held guilty of professional misconduct as he is allowed to charge fees on percentage of the realisation of assets being a liquidator.

7. **Focus of a Peer Review:** As per the Statement of Peer Review issued by the Institute of Chartered Accountants of India, Peer Review - means an examination and Review of the systems and
procedures to determine whether the same have been put in place by the Practice Unit for ensuring the quality of assurance services as envisaged by the Technical, Professional and Ethical Standards and whether the same were consistently applied in the period under review.

The Review shall cover:

(i) Compliance with Technical, Professional and Ethical Standards.
(ii) Quality of reporting.
(iii) Systems and procedures for carrying out assurance services.
(iv) Training programmes for staff (including articled and audit assistants) concerned with assurance functions, including availability of appropriate infrastructure.
(v) Compliance with directions and / or guidelines issued by the Council to the Members, including Fees to be charged, Number of audits undertaken, register for Assurance Engagements conducted during the year and such other related records.
(vi) Compliance with directions and / or guidelines issued by the Council in relating to article assistants and / or audit assistants, including attendance register, work diaries, stipend payments, and such other related records.

(b) Principle Methods of Selection of Samples: According to SA 530 “Audit Sampling”, the principal methods of selecting samples are the use of random selection, systematic selection, monetary unit sampling selection, haphazard selection and block selection. Each of these methods is discussed below-

(i) Random selection: This method is applied through random number generators, for example, random number tables.
(ii) Systematic selection: In this method the number of sampling units in the population is divided by the sample size to give a sampling interval, for example 50, and having determined a starting point within the first 50, each 50th sampling unit thereafter is selected. Although the starting point may be determined haphazardly, the sample is more likely to be truly random if it is determined by use of a computerised random number generator or random number tables.
(iii) Monetary Unit sampling: This method is a type of value-weighted selection in which sample size, selection and evaluation results in a conclusion in monetary amounts.
(iv) Haphazard selection: In this method the auditor selects the sample without following a structured technique. Although no structured technique is used, the auditor would nonetheless avoid any conscious bias or predictability and thus attempt to ensure that all items in the population have a chance of selection. Haphazard selection is not appropriate when using statistical sampling.
(v) Block selection: This method involves selection of a block(s) of contiguous items from within the population. Block selection cannot ordinarily be used in audit sampling because most populations are structured such that items in a sequence can be expected to have similar characteristics to each other, but different characteristics from items elsewhere in the population. Although in some circumstances it may be an appropriate audit procedure to examine a block of items, it would rarely be an appropriate sample selection technique when the auditor intends to draw valid inferences about the entire population based on the sample.

(c) Advantages of Cost Audit to Management: Cost Audit will be advantageous to the management in the following manner-

(i) Management will get reliable data for its day-to-day operations like price fixing, control, decision-making, etc.
(ii) A close and continuous check on all wastages will be kept through a proper system of reporting to management.
(iii) Inefficiencies in the working of the company will be brought to light to facilitate corrective action.

(iv) Management by exception becomes possible through allocation of responsibilities to individual managers.

(v) The system of budgetary control and standard costing will be greatly facilitated.

(vi) A reliable check on the valuation of closing inventory and work-in-progress can be established.

(vii) It helps in the detection of errors and fraud.

(d) **Propriety Audit**: Propriety Audit stands for verification of transactions on the tests of public interest commonly accepted customs and standards of conduct. E.L. Kohler has defined the term propriety as “that which meets the tests of public interest, commonly accepted customs and standards of conduct, and particularly as applied to professional performance, requirements of law, government regulations and professional codes”. Instead of too much dependence on documents, vouchers and evidence, it shifts the emphasis to the substance of the transactions and looks into the appropriateness thereof on a consideration of financial prudence, public interest and prevention of wasteful expenditure. Thus propriety audit is concerned with scrutiny of executive actions and decisions bearing on financial and profit and loss situation of the company with special regard to public interest and commonly accepted customs, and standards of conduct. It is also seen whether every offer has exercised the same vigilance in respect of expenditure incurred from public money, as a person of ordinary prudence would exercise in respect of expenditure of his own money under similar circumstances. Propriety requires the transactions, and more particularly expenditure, to conform to certain general principles. These principles are:

(i) that the expenditure is not prima facie more than the occasion demands and that every official exercises the same degree of vigilance in respect of expenditure as a person of ordinary prudence would exercise in respect of his own money;

(ii) that the authority exercises its power of sanctioning expenditure to pass an order which will not directly or indirectly accrue to its own advantage;

(iii) that funds are not utilised for the benefit of a particular person or group of persons and

(iv) that, apart from the agreed remuneration or reward, no other avenue is kept open to indirectly benefit the management personnel, employees and others.

(e) **Key Audit Matters— As per SA 701, “Communicating Key Audit Matters in the Independent Auditor’s Report (New)”**, those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance.

**Circumstances in Which a Matter Determined to Be a Key Audit Matter Is Not Communicated in the Auditor’s Report**: The auditor shall describe each key audit matter in the auditor’s report unless:

(i) Law or regulation precludes public disclosure about the matter; or

(ii) In extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor’s report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication. This shall not apply if the entity has publicly disclosed information about the matter.