

FINAL COURSE
GROUP – I

REVISION TEST PAPERS

NOVEMBER, 2026



BOARD OF STUDIES (ACADEMIC)
THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
(Set up by an Act of Parliament)
New Delhi

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Edition	:	August, 2026
Website	:	www.icaai.org
Department/Committee	:	Board of Studies (Academic)
E-mail	:	bosnoida@icaai.in
Price	:	
ISBN No.	:	
Published by	:	The Publication Directorate on behalf of The Institute of Chartered Accountants of India, ICAI Bhawan, Post Box No. 7100, Indraprastha Marg, New Delhi- 110 002, India
		Typeset and designed at Board of Studies(A)
Printed by	:	

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REVISION TEST PAPER, NOVEMBER, 2026 – OBJECTIVE & APPROACH

(Students are advised to go through the following paragraphs carefully to derive maximum benefit out of this RTP)

I. Objective of Revision Test Paper

Revision Test Papers are one among the many educational inputs provided by the Board of Studies (Academic) to its students. Popularly referred to as RTP by the students, it is one of the very old publications of the BOS(A) whose significance and relevance from the examination perspective has stood the test of time.

The primary objectives of the RTP are:

- To help students get an insight of their preparedness for the forthcoming examination;
- To update them on the latest developments relevant for the forthcoming examination in select subjects;
- To enhance the confidence level of the students adequately.

Students must bear in mind that the RTP contains a variety of questions based on different topics of the syllabi and thus a comprehensive study of the entire syllabus is a pre-requisite before answering the questions of the RTP. In other words, in order to derive maximum benefit out of the RTPs, it is advised that before proceeding to solve the questions given in the RTP, students ought to have thoroughly read the Study Materials and Statutory Update/Judicial Update, wherever applicable.

The topics on which the questions are set herein have been carefully selected and meticulous attention has been paid in framing different types of questions. Detailed answers are provided to enable the students to do a self-assessment and have a focused approach for effective preparation.

Live Virtual Classes by renowned subject experts conducted in virtual mode for the students of Foundation, Intermediate and Final levels provide the students much required support in preparing for their exams conveniently at home as these classes can be accessed live or viewed later as recorded lectures through hand-held devices such as

smart phones, laptops, I-pads, tablets, etc. anytime anywhere. Further, students are advised to attempt the Multiple-Choice Questions (MCQs) at MCQ Paper Practice Portal which is a holistic platform for self-assessment within the stipulated timeframe.

Students are welcome to send their suggestions for fine tuning the RTP to the Joint Director, Board of Studies (Academic), The Institute of Chartered Accountants of India, A-29, Sector-62, Noida 201309 (Uttar Pradesh). RTP is also available on BOS Knowledge Portal at <https://boslive.icai.org> for downloading.

II. Planning and preparing for examination

Ideally, when the RTP reaches your hand, you must have finished reading the relevant Study Materials of all the subjects. Get a good grasp of the concepts/ provisions/ amendments/ cases discussed therein.

After reading the Study Materials and Update thoroughly, then, proceed to solve the questions given in the RTP on your own. RTP is an effective tool to revise and refresh the concepts and provisions discussed in the Study Material. RTPs are provided to you to help you assess your level of preparation. Hence, you must solve the questions given therein on your own and thereafter compare your answers with the answers given therein.

Examination tips

How well a student fares in the examination depends upon the level and depth of his preparation. However, there are certain important points which can help a student better his performance in the examination. These useful tips are given below:

- Reach the examination hall well in time.
- As soon as you get the question paper, read it carefully and thoroughly. You are given separate 15 minutes for reading the question paper.
- Plan your time so that appropriate time is awarded for each question.

- First impression is the last impression. The question which you can answer in the best manner should be attempted first.
- Always attempt to do all questions. Therefore, it is important that you must finish each question within allocated time. Keep sometime for checking the answers as well.
- Read the question carefully more than once before starting the answer to understand very clearly as to what is required.
- Answer all parts of a question one after the other; do not answer different parts of the same question at different places.
- Write in neat and legible hand-writing.
- Always be concise and write to the point and do not try to fill pages unnecessarily.
- There must be logical expression of the answer.
- In case a question is not clear, you may state your assumptions and then answer the question.
- Check your answers carefully and underline important points before leaving the examination hall.
- In case of case scenario based MCQs, read the facts given in the case attentively. Also, read each MCQ based thereon and all the options carefully, before choosing the correct answer.

III. Subject-wise Applicability

PAPER 1: FINANCIAL REPORTING

For Paper 1: Financial Reporting November, 2024 edition (Reprint August 2025 and onwards) of the study material is applicable. The syllabus of Financial Reporting focuses on Ind AS integrated with Ethics and Technology. The Study Material has been divided into five modules for ease of handling by students.

For understanding the coverage of syllabus, it is important to read the Study Material along with the reference to Study Guidelines. It contains the detailed topic-wise exclusions from the syllabus. The Study Guidelines is given as part of "Applicability of Standards / Guidance

Notes/Legislative Amendments etc. for November, 2026 – Final Examination” appended at the end of this Revision Test Paper.

You have to read the Study Material thoroughly to attain conceptual clarity. Tables, diagrams and flow charts have been extensively used to facilitate easy understanding of concepts. Examples and Illustrations given in the Study Material would help you understand the application of concepts. Thereafter, work out the questions at the end of each chapter to hone your problem-solving skills. Compare your answers with the answers given to test your level of understanding.

The Revision Test Paper for Final Paper 1: Financial Reporting is divided into two parts.

1. Part I contains the amendments applicable for the November 2026 Examination. These amendments were notified after the release of the November 2024 edition of the Study Material but at least six months prior to the November 2026 Examination and are, therefore, applicable for the said examination. The applicable amendments have been appropriately summarised and explained in Part I of this RTP for the benefit of students.
2. Part II contains a set of questions and answers for students’ practice and revision to facilitate effective preparation for the examination.

Solve the questions given in this RTP independently and compare the same with the answers given to assess your level of preparedness for the examination. The Revisionary Test Paper (RTP) of Financial Reporting contains twenty questions and their answers.

Answers to descriptive questions have been given in detail along with the working notes for easy understanding and comprehending the steps in solving the problems. The answers to the questions have been presented in the manner which is expected from the students in the examination. The students are expected to solve the questions under examination conditions and then compare their solutions with the solutions given in the Revisionary Test Paper and further strategize their preparation for scoring more marks in the examination.

PAPER 2: ADVANCED FINANCIAL MANAGEMENT

Basically, the subject of Advanced Financial Management is to acquire the ability to apply financial management theories and techniques in strategic decision making. The major topics from which numerical questions are normally asked are as follows:

- Financial Policy and Corporate Strategy
- Risk Management
- Advanced Capital Budgeting Decisions
- Security Analysis & Valuation
- Portfolio Management
- Mutual Fund
- Derivatives
- Foreign Exchange Exposure and Risk Management
- International Financial Management
- Interest Rate Risk Management
- Business Valuation
- Mergers and Acquisitions

Accordingly, the detail of the topics, on which questions in this Revisionary Test Paper are based, is as follows:

Question No.	Topic
1	Case Scenario (International Financial Management)
2	Case Scenario (Foreign Exchange Exposure and Risk Management)
3	Advanced Capital Budgeting Decisions
4	Security Valuation

5	Business Valuation
6	Derivatives Analysis & Valuation
7	Interest Rate Risk Management
8	Portfolio Management
9	Mergers, Acquisitions and Corporate Restructuring
10	Mutual Funds
11	Security Analysis
12	A theoretical Question
13	A theoretical Question
14	A theoretical Question

PAPER 3: ADVANCED AUDITING, ASSURANCE AND PROFESSIONAL ETHICS

The Revision Test Paper (RTP) is a valuable tool for revising and strengthening the knowledge acquired through conceptual learning of the Study Material and other learning resources such as the Students' Journal, Saransh, Bare Acts, and other relevant sources.

This RTP for Advanced Auditing, Assurance and Professional Ethics is relevant for the November 2026 Examination. It comprises two parts: Part I – Academic Update and Part II – Questions and Answers for Practice. The RTP contains a total of 20 questions, comprising case scenario-based multiple-choice questions, independent multiple-choice questions, and descriptive questions, covering the entire syllabus across nineteen chapters.

The questions included in the RTP cover a wide range of topics, including Audit Planning, Strategy and Execution; Completion and Review; Reporting; Specialised Areas; Review of Financial Information; Prospective Financial Information and Other Assurance Services; Digital Auditing and Assurance; Group Audits; Special Features of Audit of Banks and Non-Banking Financial Companies; Overview of Audit of Public Sector Undertakings; Sustainable Development Goals (SDGs) and Environment,

Social and Governance (ESG) Assurance; Professional Ethics; and Liabilities of Auditors, etc.

The questions are designed to assess different levels of learning and application. Some of the questions given in the RTP are descriptive i.e. direct theory questions (Knowledge and Comprehension) based whereas some of them are practical case studies based i.e. application-oriented theory question (Application and Analysis / Evaluation and Synthesis). The name of the chapter is clearly indicated before each question.

The Study Guidelines, forming part of the "Applicability of Standards / Guidance Notes / Legislative Amendments, etc. for November 2026 – Final Examination", are appended at the end of this Revision Test Paper. It may be noted that the legislative amendments, notifications, circulars and other relevant updates applicable up to 30 April 2026 are relevant for the November 2026 Examination.

Examples and illustrations given in the Study Material would help you understand the application of concepts. Work out the exercise questions at the end of each chapter and then, compare your answers with the answers given to test your level of understanding. Thereafter, solve the MCQs and case scenarios based MCQs uploaded in MCQ Paper Practice Dashboard to assess your level of understanding and hone your analytical and problem-solving skills.

Finally, solve the questions given in this RTP independently and compare the same with the answers given to assess your level of preparedness for the examination.



PAPER – 1: FINANCIAL REPORTING

Part I-Amendments applicable from November, 2026 examination

In the year 2025, MCA has issued amendments viz two notifications at two different dates to amend the Companies (Indian Accounting Standards) Rules, 2015. The first amendment of the year was vide notification G.S.R. 291(E) dated 7th May, 2025 and the second amendment of the year was vide notification G.S.R. 549(E) dated 13th August, 2025. These amendments are generally brought by MCA to keep uniformity between Ind AS and IFRS.

1. Amendment in Ind AS notification G.S.R. 291(E) dated 7th May, 2025

The Ministry of Corporate Affairs (MCA) issued the Companies (Indian Accounting Standards) Amendment Rules, 2025 on May 7, 2025, primarily amending Ind AS 21 regarding a "lack of exchangeability" for foreign currencies, effective for annual periods starting on or after April 1, 2025. These amendments align Ind AS 21 with IAS 21, guiding how to determine the spot rate when a currency cannot be exchanged into another currency.

Under Ind AS 21, The Effects of Changes in Foreign Exchange Rates, a company on initial recognition, uses a spot exchange rate when translating a foreign currency transaction at the date of the transaction. Additionally, Ind AS 21 requires the use of a spot exchange rate when an entity reports foreign operation's results and financial position in its financial statements. A spot exchange rate is the exchange rate for immediate delivery.

However, in rare circumstances, it is possible that one currency cannot be exchanged into another. This lack of exchangeability can have a significant accounting impact over affected companies.

In this regard, the Ministry of Corporate Affairs (MCA) notified the Companies (Indian Accounting Standards) Amendment Rules, 2025, on May 7, 2025, amending Ind AS 21, The Effects of Changes in Foreign Exchange Rates. Effective for annual periods beginning on or after April 1, 2025, the amendments address the lack of exchangeability between two currencies by explaining -

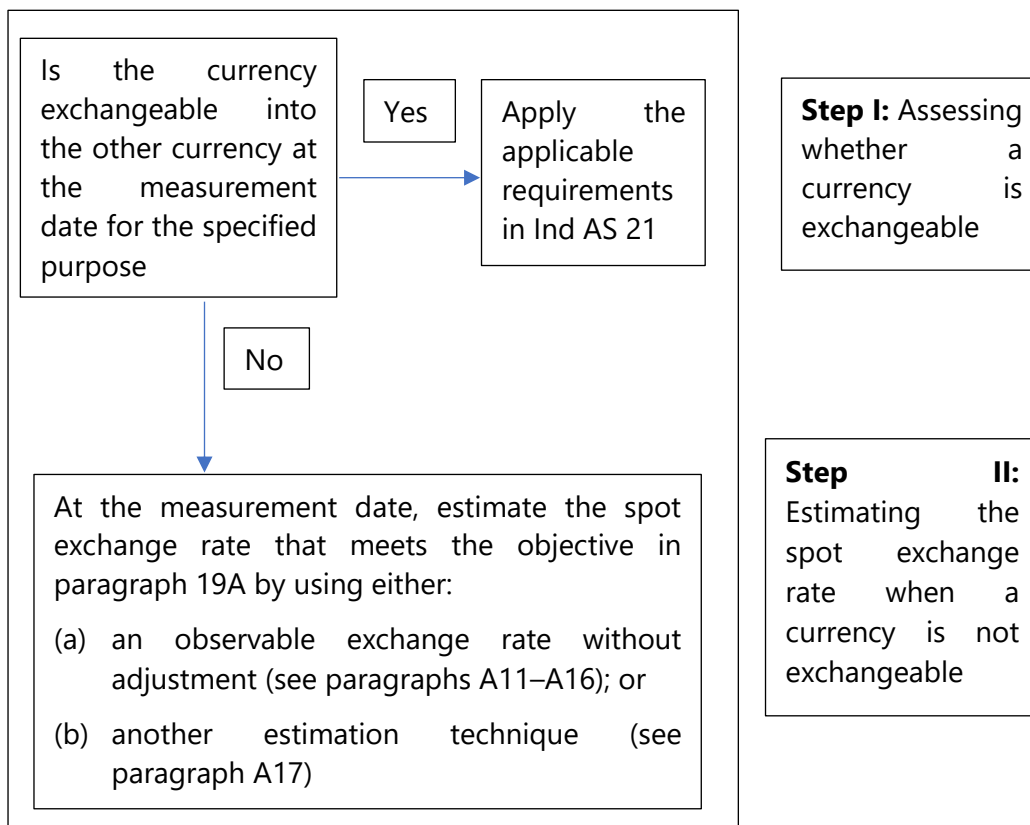
- when a currency is exchangeable,
- providing guidance on estimating spot rates, and
- enhancing disclosure requirements.

Key highlights of the Amendment in Ind AS 21

- ❖ **Definition of Exchangeability:** A currency is exchangeable into another when an entity can **obtain the other currency within a time frame allowing for normal administrative delay**, through a mechanism that **creates enforceable rights**.
- ❖ **Estimate Spot Rate:** If exchangeability is lacking, the entity must estimate the spot rate to translate transactions, ensuring it reflects an orderly transaction.
- ❖ **Two-Step Approach**

TWO-STEP APPROACH:

The following diagram is to help entities assess whether a currency is exchangeable and estimate the spot exchange rate when a currency is not exchangeable.



STEP I: ASSESSING WHETHER A CURRENCY IS EXCHANGEABLE

An entity might determine that currency PC is not exchangeable into currency LC, even though currency LC is exchangeable into currency PC.

Following key factors are required to be considered when determining that a currency is exchangeable:

1. **Time frame:** An exchange transaction might not always complete instantaneously because of legal or regulatory requirements, or for practical reasons such as public holidays. A normal administrative delay in obtaining the other currency does not preclude a currency from being exchangeable into that other currency. What constitutes a normal administrative delay depends on facts and circumstances.
2. **Ability to obtain the other currency:** In assessing whether a currency is exchangeable into another currency, an entity shall consider its

ability to obtain the other currency, rather than its intention or decision to do so. A currency is exchangeable into another currency if an entity is able to obtain the other currency either directly or indirectly, even if it intends or decides not to do so. For example, regardless of whether the entity intends or decides to obtain PC, currency LC is exchangeable into currency PC if an entity is able to either exchange LC for PC, or exchange LC for another currency (FC) and then exchange FC for PC.

3. **Markets or exchange mechanisms:** In assessing whether a currency is exchangeable into another currency, an entity shall consider only markets or exchange mechanisms in which a transaction to exchange the currency for the other currency would create enforceable rights and obligations. It depends on facts and circumstances.
4. **Purpose of obtaining the other currency:** Different exchange rates might be available for different uses of a currency. This could affect an entity's ability to obtain those currencies and thus, lead to lack of exchangeability. Hence, it would be important for an entity to consider the purpose for which it obtains the other currency.
5. **Ability to obtain only limited amounts of the other currency:** A currency is not exchangeable into another currency if an entity is able to obtain no more than an insignificant amount of the other currency. An entity shall assess the significance of the amount of the other currency it is able to obtain for a specified purpose by comparing that amount with the total amount of the other currency required for that purpose.

For example, an entity with a functional currency of LC has liabilities denominated in currency FC. The entity assesses whether the total amount of FC it can obtain for the purpose of settling those liabilities is no more than an insignificant amount compared with the aggregated amount (the sum) of its liability balances denominated in FC.

Where a currency is exchangeable into another currency, then the existing principles of Ind AS 21 would be applied for translation of the foreign currency transaction. But, where a currency is not exchangeable, an entity has to apply Step II.

STEP II: ESTIMATING THE SPOT EXCHANGE RATE WHEN A CURRENCY IS NOT EXCHANGEABLE

When a currency is not exchangeable, a company needs to estimate a spot rate. A company's objective when estimating a spot rate is only that it reflects the rate at which an orderly exchange transaction would take place at the measurement date between market participants under prevailing economic conditions.

To estimate a spot rate, a company should consider using:

1. An observable exchange rate without adjustment

A company can use an observable rate if that rate satisfies the estimation objective – i.e. the rate reflects the price at which an orderly exchange transaction would take place at the measurement date between market participants under prevailing economic conditions.

To assess whether the exchange rates reflect the prevailing economic conditions, following needs to be considered:

- ❖ Whether several observable exchange rates exist
- ❖ The purpose for which the currency is exchangeable
- ❖ The nature of the exchange rate; and
- ❖ The frequency with which exchange rates are updated

Examples of an observable exchange rate include:

- ❖ A spot exchange rate for a purpose other than that for which the company is assessing exchangeability.
- ❖ The first exchange rate at which a company is able to obtain the other currency for its specified purpose after exchangeability is restored. If a company opts to use this rate as an observable rate, then it would also need to consider
 - the time between the measurement date and the date at which exchangeability is restored,
 - inflation rates.

2. Using another estimation technique

When estimating a spot rate, the other alternative is that a company may use any observable exchange rate and adjust it as necessary. This includes using rates from exchange transactions in markets or exchange mechanisms that do not create enforceable rights and obligations- and adjust that rate, as necessary, to meet the estimation objective.

DISCLOSURE WHEN A CURRENCY IS NOT EXCHANGEABLE

An entity shall disclose:

- (a) the currency and a description of the restrictions that result in that currency not being exchangeable into the other currency;
- (b) a description of affected transactions;
- (c) the carrying amount of affected assets and liabilities;
- (d) the spot exchange rates used and whether those rates are:
 - i. observable exchange rates without adjustment (see paragraphs A12–A16); or
 - ii. spot exchange rates estimated using another estimation technique (see paragraph A17);
- (e) a description of any estimation technique the entity has used, and qualitative and quantitative information about the inputs and assumptions used in that estimation technique; and
- (f) qualitative information about each type of risk to which the entity is exposed because the currency is not exchangeable into the other currency, and the nature and carrying amount of assets and liabilities exposed to each type of risk.

When a foreign operation's functional currency is not exchangeable into the presentation currency or, if applicable, the presentation currency is not exchangeable into a foreign operation's functional currency, an entity shall also disclose:

- (a) the name of the foreign operation; whether the foreign operation is a subsidiary, joint operation, joint venture, associate or branch; and its principal place of business;

- (b) summarised financial information about the foreign operation; and
- (c) the nature and terms of any contractual arrangements that could require the entity to provide financial support to the foreign operation, including events or circumstances that could expose the entity to a loss.

TRANSITION

In applying *Lack of Exchangeability*, the companies are not required to restate comparative information; instead, they adjust opening balance of retained earnings or cumulative amount of translation differences-accumulated in a separate component of equity.

2. Amendment in Ind AS notification G.S.R. 549(E) dated 13th August, 2025

The amendments notified in the Companies (Indian Accounting Standards) Second Amendment Rules, 2025 relate to:

- A. Classification of liabilities as current or non-current and non-current liabilities with covenants (Ind AS 1, *Presentation of Financial Statements*)
- B. Disclosure of supplier finance arrangements (Ind AS 7, *Statement of Cash Flows* and Ind AS 107 *Financial Instruments: Disclosures*)
- C. Pillar Two Model Rules (Ind AS 12, *Income Taxes*).

A. AMENDMENT IN IND AS 1 'PRESENTATION OF FINANCIAL STATEMENTS'

Current – non-current classification of liabilities: In Ind AS 1, certain paragraphs have been inserted for the classification of certain liabilities as current or non-current. Further, companies may require making new disclosures for liabilities subject to covenants.

Right to defer settlement must exist at reporting date and have substance: Prior to the notification in Ind AS 1, companies classify a liability as current when they do not have an unconditional right to defer settlement for at least 12 months after the reporting date. The amendment has removed the requirement for a right to be **unconditional** and instead now requires that a right to defer settlement must exist at the reporting date and have substance.

Liabilities with covenants – clarification on classification criteria and introduction of new disclosures: A company will classify a liability as non-current if it has a right to defer settlement for at least 12 months after the reporting date. This right may be subject to a company complying with covenants specified in a loan arrangement.

Only covenants with which a company must comply **on or before** the reporting date affect the classification of a liability as current or non-current.

Covenants with which the company must comply after the reporting date (i.e. future covenants) do not affect a liability's classification at that date. However, when non-current liabilities are subject to future covenants, **companies will now need to disclose information** to help users understand the risk that those liabilities could become repayable within 12 months after the reporting date.

Breach of covenant (effective for accounting periods beginning on or after 1 April 2025)

Ind AS 1 continues to carry the existing carve-outs from IAS 1 regarding the classification of liabilities when there is a breach of a material covenant that transforms the liability from non-current to current.

Where there is a breach of a material covenant of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand on the reporting date, the entity would not classify the liability as current, if the lender, after the reporting period and before the approval of the financial statements for issue, agreed not to demand payment as a consequence of the breach. However, in such circumstances, **the entity shall disclose information as per Ind AS 107 for each breach.**

Breach of covenant (effective for accounting periods beginning on or after 1 April 2026)

For accounting periods beginning on or after 1 April 2026, the carve-out has been removed and hence when an entity breaches any covenant of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand, it

classifies the liability as current, even if the lender agreed, after the reporting period and before the approval of the financial statements for issue, not to demand payment as a consequence of the breach. An entity classifies the liability as current because, at the end of the reporting period, it does not have the right to defer its settlement for at least 12 months after that date.

However, an entity classifies the liability as non-current if the lender agreed by the end of the reporting period to provide a period of grace ending at least 12 months after the reporting period, within which the entity can rectify the breach and during which the lender cannot demand immediate repayment.

If the following events occur between the end of the reporting period and the date the financial statements are approved for issue, those events are disclosed as non-adjusting events in accordance with Ind AS 10, *Events after the Reporting Period*:

- (a) refinancing on a long-term basis of a liability classified as current;
- (b) rectification of a breach of a long-term loan arrangement classified as current;
- (c) the granting by the lender of a period of grace to rectify a breach of a long-term loan arrangement classified as current; and
- (d) settlement of a liability classified as non-current.

Convertible debt may become current: Clarification on how a company classifies a liability that can be settled in its own shares – e.g. convertible debt.

When a liability includes a counterparty conversion option that involves a transfer of the company's own equity instruments, the conversion option is recognised as either equity or a liability separately from the host liability under Ind AS 32 Financial Instruments: Presentation. *The amendments states that when a company classifies the host liability as current or non-current, it can ignore only those conversion options that are recognised as equity.*

New disclosure requirements: As per the amendment in Ind AS 1, companies are now required to disclose information related to non-

current liabilities from loan arrangements that are subject to future covenants in the notes to the financial statements. This disclosure aims to inform users about the potential risk that such liabilities may become repayable within 12 months following the reporting date.

The following new disclosures about covenants are required:

- Information about the covenants – e.g. nature of the covenants and when the company is required to comply with them and the carrying amount of related liabilities.
- Facts and circumstances, if any, that indicate the company may have difficulty complying with the covenants within the next 12 months of the reporting date – e.g. actions taken by the company during or after the reporting period to avoid or mitigate a potential breach, or the fact that the covenants would have been breached if assessed for compliance based on the company's circumstances at the reporting date (i.e. based on a hypothetical test at the reporting date).

Effective date –retrospectively application: Amendments in Ind AS 1 apply retrospectively for annual reporting periods beginning on or after 1 April 2025.

The amendment relating to breach of covenants on or before the reporting period that are aligned to IAS 1 are applicable for annual reporting periods beginning on or after 1 April 2026, retrospectively in accordance with Ind AS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*.

B. AMENDMENT IN IND AS 7 'STATEMENT OF CASH FLOWS'

Supplier Finance Arrangements: Supplier finance arrangements are characterised by one or more finance providers offering to pay amounts an entity owes its suppliers and the entity agreeing to pay according to the terms and conditions of the arrangements at the same date as, or a date later than, suppliers are paid. These arrangements provide the entity with extended payment terms, or the entity's suppliers with early payment terms, compared to the related invoice payment due date. Supplier finance arrangements are often

referred to as supply chain finance, payables finance or reverse factoring arrangements.

Arrangements that are solely credit enhancements for the entity (for example, financial guarantees including letters of credit used as guarantees) or instruments used by the entity to settle directly with a supplier the amounts owed (for example, credit cards) are not supplier finance arrangements.

An entity shall disclose in aggregate following information about its supplier finance arrangements that enables users of financial statements to assess the effects of those arrangements on the entity's liabilities and cash flows and on the entity's exposure to liquidity risk.

- (a) the terms and conditions of the arrangements (for example, extended payment terms and security or guarantees provided). However, an entity shall disclose separately the terms and conditions of arrangements that have dissimilar terms and conditions.
- (b) as at the beginning and end of the reporting period:
 - (i) the carrying amounts, and associated line items presented in the entity's balance sheet, of the financial liabilities that are part of a supplier finance arrangement.
 - (ii) the carrying amounts, and associated line items, of the financial liabilities disclosed under (i) for which suppliers have already received payment from the finance providers.
 - (iii) the range of payment due dates for both the financial liabilities disclosed under (i) and comparable trade payables that are not part of a supplier finance arrangement. Comparable trade payables are, for example, trade payables of the entity within the same line of business or jurisdiction as the financial liabilities disclosed under (i). If ranges of payment due dates are wide, an entity shall disclose explanatory information about those ranges or disclose additional ranges (for example, stratified ranges).

- (c) the type and effect of non-cash changes in the carrying amounts of the financial liabilities disclosed under (b)(i). Examples of non-cash changes include the effect of business combinations, exchange differences or other transactions that do not require the use of cash or cash equivalents.

Transition-Effective date: An entity shall apply the supplier finance arrangements for the annual reporting periods beginning on or after 1 April 2025.

In applying supplier finance arrangements, an entity is **not** required to disclose:

- (a) Comparative information for any reporting periods presented before the beginning of the annual reporting period in which the entity first applies these amendments;
- (b) The following information as at the beginning of the annual reporting period in which the entity first applies those amendments
- ❖ the carrying amounts and associated line items presented in the balance sheet at the beginning and end of the reporting period for both the financial liabilities that are part of supplier finance arrangements in total and those for which the supplier has already been paid.
 - ❖ the range of payment due dates for the financial liabilities that are part of supplier finance arrangements and comparable trade payables (e.g. trade payables within the same jurisdiction or business) that are not part of such arrangements as at the beginning of the annual reporting period in which the entity first applies these amendments.
- (c) The information regarding supplier finance arrangements for any interim period presented within the annual reporting period in which the entity first applies these amendments.

C. AMENDMENT IN IND AS 12 'INCOME TAXES'

Pillar Two Legislation and Pillar Two Income Taxes: Pillar Two legislation includes Pillar Two Model Rules as per Organisation for Economic Co-operation and Development (OECD) including tax law that implements qualified domestic minimum top-up taxes described in those rules.

As an exception to the requirements in this Standard, an entity shall neither recognise nor disclose information about deferred tax assets and liabilities related to Pillar Two income taxes.

The amendments to Ind AS 12 states that

- ❖ An entity shall disclose that it has applied the exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes.
- ❖ An entity shall disclose separately its current tax expense (income) related to Pillar Two income taxes.
- ❖ In periods in which Pillar Two legislation is enacted or substantively enacted but not yet in effect, an entity shall disclose known or reasonably estimable information that helps users of financial statements understand the entity's exposure to Pillar Two income taxes arising from that legislation.
- ❖ To meet the above disclosure, an entity shall disclose qualitative and quantitative information about its exposure to Pillar Two income taxes at the end of the reporting period.

This information does not have to reflect all the specific requirements of the Pillar Two legislation and can be provided in the form of an indicative range. To the extent information is not known or reasonably estimable, an entity shall instead disclose a statement to that effect and disclose information about the entity's progress in assessing its exposure.

Part II-Questions and Answers



QUESTIONS

Case Scenario 1

KK Ltd. prepares its financial statements annually with 31 March as the reporting date. The financial statements of KK Ltd. are approved for issue on 25 May 20X2.

As at 31 March 20X2, KK Ltd. had a trade receivable of ₹ 10 million from Z Ltd., which was due for payment on 30 April 20X2. Z Ltd. had been a customer of KK Ltd. for several years and had an excellent payment history. At 31 March 20X2, there was no indication that Z Ltd. would be unable to settle the amount due. However, on 20 April 20X2, significant doubt arose regarding Z Ltd.'s ability to continue as a going concern because of the failure of certain major business projects.

On 1 August 20X1, KK Ltd. supplied products manufactured by it to C Ltd. The products were subsequently found to be faulty. On 1 October 20X1, C Ltd. commenced legal proceedings against KK Ltd. claiming damages for losses arising from the faulty products.

KK Ltd. determined that the products were faulty because of defective raw materials supplied by Y Ltd. Accordingly, on 1 December 20X1, KK Ltd. commenced legal proceedings against Y Ltd. to recover damages.

KK Ltd. consistently assessed that it was probable that both legal actions would succeed.

The estimates of damages were as follows:

Date	Damages payable by KK Ltd. to C Ltd.	Damages receivable from Y Ltd.
1 October 20X1	₹ 5.00 million	-
1 December 20X1	-	₹ 3.50 million
31 March 20X2	₹ 5.20 million	₹ 3.60 million
15 May 20X2	₹ 5.25 million	₹ 3.70 million
1 June 20X2 – settlement	₹ 5.30 million	₹ 3.75 million

The case against C Ltd. was settled on 1 June 20X2, when KK Ltd. paid ₹ 5.30 million. The case against Y Ltd. was also settled on that date, when Y Ltd. paid ₹ 3.75 million to KK Ltd.

Other information

During the year, KK Ltd. purchased a machine for ₹ 2,50,000. Depreciation of ₹ 50,000 was charged in arriving at accounting profit. The tax authorities allowed a deduction of ₹ 1,00,000 against taxable profits in the current period. The remaining cost will be deductible in future periods, either through depreciation or on disposal.

KK Ltd. also had interest receivable of ₹ 60,000 on 31 March 20X2. The related interest income is taxable on a cash basis, i.e., when the interest is actually received.

Based on the facts given above, choose the most appropriate answer to Questions 1 to 5 below as per the relevant Ind AS.

1. With respect to the ₹ 10 million trade receivable from Z Ltd., which of the following is the most appropriate treatment in KK Ltd.'s financial statements for the year ended 31 March 20X2?
 - (A) No impairment allowance is required based on the information given; however, the material non-adjusting event should be disclosed if necessary to enable users to understand its financial effect.
 - (B) Recognise an impairment allowance based on the information available on 20 April 20X2 because all events occurring before approval of financial statements are adjusting events.
 - (C) Recognise a full impairment allowance because Z Ltd.'s going concern status became doubtful before approval of the financial statements.
 - (D) Derecognise the trade receivable because Z Ltd. may not be able to settle the amount.
2. What is the tax base of the machine at 31 March 20X2?
 - (A) ₹ 2,50,000
 - (B) ₹ 2,00,000

- (C) ₹ 1,50,000
 - (D) ₹ 1,00,000
3. What is the tax base of the ₹ 60,000 interest receivable?
- (A) ₹ 60,000
 - (B) Nil
 - (C) ₹ 30,000
 - (D) ₹ 60,000 less the applicable tax rate
4. What amount should KK Ltd. recognise as a provision in respect of the legal action brought by C Ltd. in its financial statements for the year ended 31 March 20X2?
- (A) ₹ 5.00 million
 - (B) ₹ 5.20 million
 - (C) ₹ 5.25 million
 - (D) ₹ 5.30 million
5. What is the appropriate accounting treatment for the amount recoverable from Y Ltd. in respect of the defective raw materials?
- (A) Recognise an asset of ₹ 3.60 million because recovery is probable.
 - (B) Recognise an asset of ₹ 3.70 million because this is the estimate closest to the date of approval of financial statements.
 - (C) Recognise an asset of ₹ 3.75 million because this is the amount ultimately received.
 - (D) Do not recognise an asset; disclose the contingent asset and its estimated financial effect because the inflow is probable.

Case Scenario 2

Alpha Ltd. prepares its financial statements annually with 31 March as its reporting date.

At 31 March 20X2, the following liabilities were included in its financial statements:

- Trade payables of ₹ 1,20,000, relating to purchases for which the entire amount had already been allowed as a tax deduction when the purchases were made.
- Accrued liabilities of ₹ 40,000, relating to an expense for which a tax deduction will be available only when the liability is actually settled.

Alpha Ltd. also supplied components to a customer on 31 December 20X1 for an invoiced amount of ₹ 5,00,000. Payment was originally expected on 28 February 20X2. However, no payment was received.

On 30 April 20X2, Alpha Ltd. obtained information that the customer had developed significant cash-flow difficulties because one of its major projects had failed in February 20X2. Alpha Ltd. remained confident that the customer would ultimately settle the amount and therefore agreed to allow the customer to pay on 31 March 20X3.

Alpha Ltd. normally charges 6% annual interest on amounts it lends to customers. The customer was, however, allowed this extended interest-free payment period.

Based on the facts given above, choose the most appropriate answer to Questions 6 to 10 below as per the relevant Ind AS.

6. What is the tax base of the ₹ 1,20,000 trade payable?
- (A) Nil
 - (B) ₹ 1,20,000
 - (C) ₹ 60,000
 - (D) ₹ 1,20,000 less applicable tax rate
7. What is the tax base of the ₹ 40,000 accrued liability?
- (A) Nil
 - (B) ₹ 40,000
 - (C) ₹ 20,000
 - (D) ₹ 40,000 less applicable tax rate

8. How should Alpha Ltd. treat the information obtained on 30 April 20X2 regarding the customer's financial difficulties in preparing its financial statements for the year ended 31 March 20X2?
 - (A) It should be ignored because the information was received after the reporting date.
 - (B) It is a non-adjusting event because the customer's financial difficulties became known only after year-end.
 - (C) It is an adjusting event because the information provides additional evidence of conditions that existed at the reporting date.
 - (D) It should be recognised only in the financial statements for the year ending 31 March 20X3.
9. Based on the information available before the financial statements are approved for issue, what amount should be recognised for the trade receivable in the financial statements for the year ended 31 March 20X2, assuming the applicable discount rate is 6%?
 - (A) ₹ 5,00,000
 - (B) ₹ 4,71,698
 - (C) ₹ 4,70,000
 - (D) ₹ 5,30,000
10. What amount of interest income should Alpha Ltd. recognise for the year ended 31 March 20X3, assuming the customer pays ₹ 5,00,000 on that date?
 - (A) Nil
 - (B) ₹ 28,302
 - (C) ₹ 30,000
 - (D) ₹ 5,00,000

Professional and Ethical Duty of a Chartered Accountant

11. AlphaTech Ltd., a listed company, manufactures specialised industrial equipment and prepares its financial statements under Ind AS. For the

year ended 31 March 20X5, its reported revenue before the following transaction was ₹ 492 crore, against management's guidance of ₹ 500 crore.

On 25 March 20X5, AlphaTech received an order of ₹ 30 crore from Beta Industries Ltd. The equipment was delivered on 28 March 20X5 and management recognised the entire ₹ 30 crore as revenue immediately.

CA Rohan Mehta, responsible for financial reporting, noted the following:

- Beta Industries had a 90-day contractual right to return the equipment if it did not meet its production requirements.
- The equipment was highly customised and could not readily be sold to another customer without substantial modification.
- Installation and acceptance testing were not completed as at 31 March 20X5.
- The sales team had separately assured Beta Industries that AlphaTech would take back the equipment and provide a full refund if it did not perform as expected although this assurance was not expressly included in the main contract.
- The consideration of ₹ 30 crore was not received; payment was due 120 days after final acceptance by the customer.
- The CFO stated that AlphaTech had historically recognised revenue on dispatch and asked Rohan to approve the ₹ 30 crore revenue to meet the company's revenue target.

On 15 April 20X5, Beta Industries informed AlphaTech that the equipment had failed acceptance testing and exercised its right to return it. The equipment was returned on 25 April 20X5.

The CFO instructed Rohan not to reconsider the financial year 20X4-20X5 revenue, stating that the return occurred in the next financial year.

Required:

- (a) Whether the ₹ 30 crore revenue should be recognised in financial year 20X4-20X5?;

- (b) How the subsequent failure of acceptance testing and return of the equipment should be considered? and
- (c) What should CA Rohan do in the given circumstances?
- (d) What would be the consequences of failure by CA. Rohan to discharge his professional responsibility?

Ind AS 1: Presentation of Financial Statements

12. ABC Ltd. has a loan of ₹ 20 crore that is contractually repayable on 31 March 20X6. The loan agreement contains the following covenants relating to the company's working capital ratio:

Covenant	Testing date	Requirement
Working Capital ratio	31 March 20X1	At least 1.20
Working Capital ratio	30 September 20X1	At least 1.50

Under the terms of the loan agreement, if ABC Ltd. fails to comply with the working capital ratio requirement on any of the specified testing dates, the lender has the right to demand immediate repayment of the entire outstanding loan.

ABC Ltd. is preparing its financial statements for the year ended 31 March 20X1.

The following information is available:

- The working capital ratio of ABC Ltd. on 31 March 20X1 is 1.30.
- Based on its approved budgets and forecasts, management expects the working capital ratio to be 1.40 on 30 September 20X1.
- Accordingly, although ABC Ltd. has complied with the covenant applicable at the reporting date, management expects that it will not comply with the covenant applicable on 30 September 20X1.
- There are no other terms in the loan agreement that could result in the loan becoming repayable on demand as at 31 March 20X1.

Assume that the remaining terms of the loan are unchanged and that the lender has not waived or modified the covenant requirements.

Required:

- (a) Determine whether the loan should be classified as current or non-current in the balance sheet of ABC Ltd. as at 31 March 20X1, giving reasons.
- (b) Explain whether the expected failure to meet the working capital ratio of 1.50 on 30 September 20X1 affects the classification of the loan as at 31 March 20X1.
- (c) State the additional disclosures, if any, required in the financial statements for the year ended 31 March 20X1 in respect of the future covenant.
- (d) Assuming that the actual working capital ratio on 30 September 20X1 is 1.40, explain the consequence of such failure on the loan after the reporting date.

Ind AS 21: The Effects of Changes in Foreign Exchange Rates

13. A Ltd., whose functional currency is LC, has the following foreign currency liabilities denominated in FC as at 31 March 20X2:

Particulars	FC
Long-term foreign currency borrowing	10,00,000
Trade payables relating to import of electronic goods	10,000

During the year ended 31 March 20X2, A Ltd. imported electronic goods having a total value of FC 70,000.

The following additional information is available:

1. The relevant authority in A Ltd.'s jurisdiction permits A Ltd. to obtain FC up to 1,00,000 per year for payment for imports of electronic goods.
2. For repayment of long-term foreign currency borrowings, the relevant authority permits A Ltd. to obtain FC only up to 50,000 per year.
3. The restrictions are applicable at the level of the specified purpose for which FC is required. The authority does not permit

A Ltd. to use the FC obtained under the import quota for repayment of its long-term borrowing.

4. As at 31 March 20X2, the following exchange rates are observable:
 - LC 1.20 = FC 1. This is the rate at which A Ltd. is permitted to obtain FC for payment for imported electronic goods.
 - LC 1.32 = FC 1. This is the rate quoted in an unofficial / parallel market. However, transactions in this market do not create enforceable rights and obligations and therefore cannot be considered when assessing whether FC is exchangeable for the purpose of the borrowing.
5. The rate of LC 1.20 per FC is an observable exchange rate for a purpose other than repayment of the borrowing and, based on the facts and circumstances, A Ltd. concludes that this rate meets the objective of estimating the spot exchange rate at 31 March 20X2.
6. Assume that there are no other changes in the foreign currency liabilities during the year and ignore interest and transaction costs.

Required:

- (a) Determine whether FC is exchangeable into LC at 31 March 20X2 separately for each of the two liabilities, giving reasons.
- (b) Determine the exchange rate to be used for translating each liability into LC at 31 March 20X2 in accordance with the amended Ind AS 21.
- (c) Calculate the amount of each liability to be recognised in LC in the financial statements of A Ltd. as at 31 March 20X2.
- (d) Explain whether the LC 1.32 per FC unofficial market rate can be used in determining the exchangeability of FC and, if FC is determined to be non-exchangeable, whether such a rate can nevertheless be considered in estimating the spot exchange rate.

Ind AS 109: Financial Instruments

14. A Ltd. purchases ₹ 10 lakh, 10%, five-year government bonds on 1 April 20X5, with semi-annual interest payable on 30 September and 31 March, for ₹ 10.6 lakh (premium of ₹ 60,000). A Ltd. classifies the bonds as held to maturity (HTM) investments at amortised cost. The amortisation of the bonds to maturity, using the effective interest method is shown below:

Date	Opening balance (a)	Cash received (b)	Effective interest rate @ 4.251% (c)	Carrying amount (d)
1 April 20X5				10,60,000
1 October 20X5	10,60,000	50,000	45,061	10,55,061
1 April 20X6	10,55,061	50,000	44,851	10,49,912
1 October 20X6	10,49,912	50,000	44,632	10,44,544
1 April 20X7	10,44,544	50,000	44,404	10,38,948
1 October 20X7	10,38,948	50,000	44,166	10,33,114
1 April 20X8	10,33,114	50,000	43,918	10,27,032
1 October 20X8	10,27,032	50,000	43,659	10,20,691
1 April 20X9	10,20,691	50,000	43,390	10,14,081
1 October 20X9	10,14,081	50,000	43,109	10,07,190
31 March 2X10	10,07,190	<u>50,000</u>	<u>42,810</u>	10,00,000
Total		<u>5,00,000</u>	<u>4,40,000</u>	

On 1 October 20X6, A Ltd. sells the bond at its fair value of ₹ 10.50 lakh to a third party, with an agreement to repurchase the bond on 1 October 20X7 for ₹ 10.56 lakh. The transferee will be entitled to receive the interest due on 1 April 20X7 and 1 October 20X7 (i.e. ₹ 1 lakh), together with the difference between the repurchase price and sale price of ₹ 6,000, representing a lender's return of 10.081% per annum on the sale price.

Note: A Ltd. has decided to adopt the policy of not recording the said forward contract to repurchase the financial asset at a fixed price as an asset.

Required:

Determine profit/loss on the above transaction at the time of sale and repurchase of the transaction and also pass necessary journal entries for the same.

Ind AS 110: Consolidated Financial Statements

15. E Ltd. owns 90% of a subsidiary X Ltd., and the balance is NCI. It disposes of 60% of its interest in the subsidiary X Ltd. for ₹ 6,120 and loses control of the subsidiary X Ltd. It will de-consolidate the subsidiary X Ltd. and account for the remaining 30% interest as an associate using the equity method of accounting.

At the disposal date, the fair value of the retained investment is determined to be ₹ 4,080. The carrying value of the identifiable net assets of the subsidiary is ₹ 7,480, excluding goodwill. There is ₹ 1,020 of goodwill recorded related to the previously acquired interests in the subsidiary. The carrying value of NCI is ₹ 850. E Ltd. tested the subsidiary's goodwill and fixed assets prior to disposal and there was no impairment. There is ₹ 68 credit in the FVTOCI arising from a debt instrument and ₹ 170 credit in the revaluation reserve (revaluation of fixed assets) relating to the subsidiary. Ignore tax consequences.

Required:

- (i) Determine the gain/loss on disposal of controlling interest
- (ii) Determine the gain/loss on retained investment
- (iii) Pass the journal entry on the disposal for 60% stake in X Ltd.

Ind AS 111: Joint Arrangements

16. K Ltd. prepares its financial statements to 31st March each year. The financial statements are approved for issue on 25th May.

On 1st April 20X1, K Ltd. entered into a joint arrangement with Y Ltd. to jointly operate a delivery depot. Y Ltd. is located and has major customers in the same geographical region as K Ltd. K Ltd. and Y Ltd. each made the following payments in respect of the arrangement on 1st April 20X1:

- ₹ 25 million each to purchase a joint 25-year leasehold interest in a depot which was close to both K Ltd. and Y Ltd.'s business premises. This depot was to act as headquarters for the delivery vehicles.
- ₹ 7.5 million each to purchase a fleet of delivery vehicles. The vehicles have an expected useful life of five years, with no expected residual value.

K Ltd. and Y Ltd. agreed to jointly use the delivery vehicles to deliver products to their customers and to share the operating costs of the depot equally. Any delivery charges to customers were levied by K Ltd. and Y Ltd. directly at the discretion of the individual entities.

During the year ended 31st March 20X2, the total cash cost of operating the depot was ₹ 8 million. This was paid equally by K Ltd. and Y Ltd. In the year ended 31st March 20X2, K Ltd. charged its customers a total of ₹ 2 million in delivery charges.

Required:

Explain how the above transaction would be reported in the financial statements of K Ltd. for the year ended 31 March 20X2.

Ind AS 12: Income Taxes

17. A Ltd. prepares financial statements to 31 March each year. The rate of income tax applicable to A Ltd. is 20%. The following information relates to transactions, assets, and liabilities of A Ltd. during the year ended 31 March 20X2
- (i) A Ltd. has a 40% shareholding in L Ltd. A Ltd. purchased this shareholding for ₹ 45 million. The shareholding gives A Ltd. significant influence over L Ltd. but not control and therefore A Ltd. accounts for its interest in L Ltd. using the equity method. The equity method carrying value of A Ltd.'s investment in L Ltd. was ₹ 70 million on 31 March 20X1 and ₹ 75 million on 31 March 20X2. In the tax jurisdiction in which A Ltd. operates, profits recognised under the equity method are taxed if and when they are distributed as a dividend or the relevant investment is disposed of.

- (ii) A Ltd. measures its head office property using the revaluation model. The property is revalued every year on 31 March. On 31 March 20X1, the carrying value of the property (after revaluation) was ₹ 40 million and its tax base was ₹ 22 million. During the year ended 31 March 20X2, A Ltd. charged depreciation in its statement of profit or loss of ₹ 2 million and claimed a tax deduction for tax depreciation of ₹ 1.25 million.

On 31 March 20X2, the property was revalued to ₹ 45 million. In the tax jurisdiction in which A Ltd. operates, revaluation of property, plant and equipment does not affect taxable income at the time of revaluation.

There are no other temporary differences other than those indicated above.

Compute:

- The deferred tax liability of A Ltd. at 31 March 20X2.
- The charge or credit to both profit or loss and other comprehensive income relating to deferred tax for the year ended 31 March 20X2.

Include brief explanations to support your computations.

Ind AS 102: Share-based Payments

18. C Ltd. prepares its financial statements to 31 March each year. The financial statements are approved for issue on 20 May.

On 1 April 20X1, C Ltd. granted 2,000 employees 1,000 share options each. The options are due to vest on 31 March 20X4 provided the relevant employees remain in employment over the three-year period ending on 31 March 20X4.

On 1 April 20X1, the directors of C Ltd. estimated that 1,800 employees would qualify for the options on 31 March 20X4. This estimate was amended to 1,850 employees on 31 March 20X2, and further amended to 1,840 employees on 31 March 20X3.

On 1 April 20X1, the fair value of an option was ₹ 1.20. The fair value increased to ₹ 1.30 by 31 March 20X2 but, due to challenging trading

conditions, the fair value declined after 31 March 20X2. On 30 September 20X2, when the fair value of an option was 90 paise, the directors repriced the options and this caused the fair value to increase to ₹ 1.05. Trading conditions improved in the second half of the year and by 31 March 20X3 the fair value of an option was ₹ 1.25.

Any additional costs that have occurred because of the repricing of the options on 30 September 20X2 should be spread over the remaining vesting period from 30 September 20X2 to 31 March 20X4.

Required:

Explain how the above event would be reported in the financial statements of C Ltd. for the year ended 31 March 20X3. Also provide necessary journal entries for the year ended 31 March 20X2 and 31 March 20X3.

Ind AS 24: Related Party Disclosures

19. CC Ltd prepares its financial statements to 31 March each year. The financial statements are approved for issue on 20 May.

On 1 June 20X1, the spouse of one of the directors of CC Ltd. purchased a controlling interest in O Ltd., a long-standing customer of CC Ltd.

Sales of products from CC Ltd. to O Ltd. in the two-month period from 1 April 20X1 to 31 May 20X1 totalled ₹ 8,00,000.

Following the share purchase by the spouse of one of the directors of CC Ltd. on 1 June 20X1, CC Ltd. began to supply the products at a discount of 20% to their normal selling price and allow O Ltd. three months' credit (previously O Ltd. was only allowed one month's credit, CC Ltd.'s normal credit policy).

Sales of products from CC Ltd. to O Ltd. in the ten-month period from 1 June 20X1 to 31 March 20X2 totalled ₹ 6 million.

On 31 March 20X2, the trade receivables of CC Ltd. included ₹ 1.8 million in respect of amounts owing by O Ltd.

Required:

Explain how the above event would be reported in the financial statements of CC Ltd. for the year ended 31 March 20X2.

Ind AS 7: Statement of Cashflows

20. The following details of P Ltd. pertain to the year ended 31st March 20X2:

- Paid lease liabilities (principal portion): ₹ 3,00,000
- The information on equity share capital and securities premium account is as under:

	1/4/20X1	31/3/20X2
Equity share capital (par value ₹ 1)	2,50,000	5,00,000
Securities premium	50,000	50,000

- On 10 October 20X1, a bonus issue of 1 share for every 5 ordinary shares was made utilising the securities premium account. The remainder of the increase in equity shares was due to an issue of shares for cash on 21st November 20X1.

From the above information, show the cash flows from financing activities to be shown in the statement of Cash flows for the year ended 31st March 20X2.



SUGGESTED ANSWERS

Answer to Multiple Choice Questions

1.	(A)
2.	(C)
3.	(B)
4.	(C)
5.	(D)

6.	(B)
7.	(A)
8.	(C)
9.	(B)
10.	(B)

11. (a) Correct Accounting treatment under Ind AS 115 'Revenue from Contracts with Customers'

Under Ind AS 115, revenue is recognised when, or as, a performance obligation is satisfied by transferring control of the promised goods or service to the customer. Accordingly, physical delivery or dispatch alone does not necessarily establish that revenue should be recognised.

In the present case, the following factors are relevant:

1. **Acceptance testing:** Testing had not been completed by 31 March 20X5. If the acceptance condition is substantive and control cannot be considered to have transferred before successful acceptance, revenue should be deferred.
2. **Right of return:** Beta Industries had a contractual right to return the equipment. Accordingly, if control had otherwise transferred, AlphaTech would recognise revenue only to the extent to which it expects to be entitled, together with a refund liability and an asset for its right to recover the product, as applicable.
3. **Other terms:** The equipment was highly customised, payment was conditional upon final acceptance, and the sales team had assured the customer of a full refund. These facts are relevant in determining the substance of the arrangement and whether control had transferred.

Therefore, AlphaTech cannot recognise the entire ₹ 30 crore merely because the equipment was dispatched on 28 March 20X5. It must first establish whether control had transferred by 31 March 20X5 and apply the right-of-return requirements, as applicable.

(b) Subsequent failure of acceptance testing and return

The fact that Beta Industries failed the acceptance test shortly after year-end and returned the equipment is significant.

At 31 March 20X5:

1. acceptance testing was pending;

2. the customer already had a contractual right of return;
3. payment was conditional upon final acceptance; and
4. the equipment had not successfully passed acceptance testing.

Accordingly, the subsequent failure may provide additional evidence about conditions existing at the reporting date, rather than representing an entirely new condition arising in Financial Year 20X5-20X6.

Therefore, the return cannot simply be ignored on the ground that it physically occurred after year-end. It should be considered in determining whether the original revenue recognition in Financial Year 20X4-20X5 was appropriate.

(c) Responsibility of CA Rohan

Rohan should not approve the ₹30 crore revenue merely to enable AlphaTech to achieve its revenue target. Management's revenue target is not a criterion for revenue recognition.

He should:

1. apply Ind AS 115 based on the facts and substance of the transaction;
2. exercise professional integrity, objectivity and professional judgement;
3. explain to management why the proposed accounting treatment may not comply with Ind AS;
4. document his assessment and the relevant evidence; and
5. if management refuses to make an appropriate adjustment, escalate the matter to the Audit Committee or those charged with governance, as appropriate.

Rohan should not allow management pressure or revenue targets to override the requirements of Ind AS 115 and his professional responsibilities.

(d) Consequences of failure to discharge professional responsibility:

In case CA Rohan succumbs to the undue influence of the CFO and knowingly approves an accounting treatment that is not in accordance with Ind AS, he may be liable for professional misconduct under Clause 1 of Part II of the Second Schedule to the Chartered Accountants Act, 1949. The Clause 1 states that a member of the Institute, whether in practice or not, shall be deemed to be guilty of professional misconduct, for contravening the provisions of this Act or the regulations made thereunder or any guidelines issued by the Council. As per the Guidelines issued by the Council, a member of the Institute who is an employee shall exercise due diligence and shall not be grossly negligent in the conduct of his duties.

Accordingly, Rohan must exercise due care and professional judgment and should not allow management pressure or undue influence to override his professional responsibilities.

12. (a) Classification of the loan as at 31 March 20X1: The loan should be classified as a non-current liability as at 31 March 20X1.

The reason is that the covenant requiring a working capital ratio of at least 1.20 is tested on 31 March 20X1, i.e., on the reporting date. ABC Ltd. has a working capital ratio of 1.30 on that date and therefore complies with the covenant.

Accordingly, ABC Ltd. has the right to defer settlement of the loan for at least 12 months after the reporting date, subject to the requirements of Ind AS 1.

(b) Effect of the covenant to be tested on 30 September 20X1: The covenant requiring a working capital ratio of at least 1.50 is tested on 30 September 20X1, which is after the reporting date.

Under the amendment in Ind AS 1, covenants that an entity is required to comply with after the reporting date do not affect the classification of the liability as current or non-current at the reporting date.

Therefore, even though management expects the working capital ratio to be only 1.40 on 30 September 20X1 and consequently expects to fail the covenant, the loan will continue to be classified as non-current as at 31 March 20X1.

- (c) **Disclosure relating to the future covenant:** Although the future covenant does not affect classification, ABC Ltd. is required to provide disclosures that enable users of the financial statements to understand the risk that the liability could become repayable within 12 months after the reporting date.

The disclosure should include information about:

- the covenant requiring a working capital ratio of at least 1.50 on 30 September 20X1;
- the fact that the company expects to fail this covenant; and
- the fact that failure would result in the loan becoming repayable on demand.

A suitable disclosure could be:

"The loan of ₹ 20 crore, classified as a non-current liability, is subject to a covenant requiring the Company to maintain a working capital ratio of at least 1.50 as at 30 September 20X1. Based on the Company's current forecasts, the working capital ratio is expected to be 1.40 on that date. Consequently, the Company expects not to comply with the covenant, which could result in the loan becoming repayable on demand within 12 months after the reporting date."

- (d) **Consequence if the actual working capital ratio is 1.40 on 30 September 20X1:** If the actual working capital ratio on 30 September 20X1 is 1.40, ABC Ltd. will fail to meet the required ratio of 1.50.

Consequently, under the terms of the loan agreement, the lender will have the right to demand immediate repayment of the loan.

However, this does not retrospectively change the classification made at 31 March 20X1. The loan was appropriately classified as

non-current at that reporting date because ABC Ltd. had complied with the covenant applicable on 31 March 20X1.

The failure on 30 September 20X1 would be relevant to the financial statements for the subsequent reporting period, subject to the applicable requirements of Ind AS 1.

13. (a) **Assessment of exchangeability:** The amendment in Ind AS 21 requires exchangeability to be assessed at the measurement date and for a specified purpose. Therefore, the fact that A Ltd. can obtain FC for one purpose does not automatically establish that it can obtain FC for another purpose. Consequently, the same currency may be exchangeable for settling trade payables but not exchangeable for repayment of a long-term borrowing.

Trade payables: A Ltd. is required to assess exchangeability for the specified purpose of settling trade payables arising from imports. The total imports during 20X1-20X2 are FC 70,000, which are within the annual permitted limit of FC 1,00,000. Accordingly, A Ltd. is able to obtain sufficient FC to settle the trade payables. Therefore, FC is exchangeable into LC for the purpose of settling the trade payables.

Long-term borrowing: For repayment of the long-term borrowing, A Ltd. can obtain only FC 50,000 in a year against the outstanding borrowing of FC 10,00,000. FC 50,000 is only 5% of the outstanding liability and is considered no more than an insignificant amount in relation to the amount required to settle the borrowing. Accordingly, FC is not exchangeable into LC for the purpose of settling the long-term borrowing.

Thus, the exchangeability assessment is made separately for the specified purposes rather than for FC as a currency generally.

- (b) **Exchange rates to be applied:** For the trade payables, since FC is exchangeable for the specified purpose, A Ltd. applies the applicable requirements of Ind AS 21. Accordingly, the exchange rate is LC1.20 per FC.

For the long-term borrowing, FC is not exchangeable for the specified purpose. Therefore, A Ltd. is required to estimate the

spot exchange rate at 31 March 20X2. Since the observable rate of LC 1.20 per FC for another purpose meets the objective of the amended Ind AS 21, A Ltd. may use that observable exchange rate without adjustment.

Therefore:

- Trade payables: LC 1.20 per FC
- Long-term borrowing: LC 1.20 per FC (estimated spot rate)

(c) Translation into LC

Liability	FC	Rate (LC/FC)	LC amount
Long-term borrowing	10,00,000	1.20	LC 12,00,000
Trade payables	<u>10,000</u>	1.20	<u>LC 12,000</u>
	<u>10,10,000</u>		<u>LC 12,12,000</u>

- (d) Treatment of the unofficial market rate:** The LC 1.32 per FC rate cannot be considered when determining whether FC is exchangeable because the unofficial/parallel market does not result in enforceable rights and obligations. However, once A Ltd. has determined that FC is not exchangeable for the purpose of the borrowing, observable exchange rates from unofficial or parallel markets may be considered as an input in estimating the spot exchange rate, subject to appropriate adjustments where necessary to meet the objective of paragraph 19A. The amendment in Ind AS 21 does not prescribe a hierarchy of observable exchange rates for this purpose.

- 14.** Since the repurchase price is fixed at the outset, A Ltd. is precluded from de-recognising the bond. The transferee will be entitled to receive the interest due on 1 April 20X7 and 1 October 20X7 (i.e., ₹ 1 lakh), together with the difference between the repurchase price and sale price of ₹ 6,000. This represents a lender's return of 10.081% per annum on the sale price. Therefore, A Ltd. will continue to recognise the bond and the interest on it, as if it still holds the bonds.

A Ltd. will also record a liability of ₹ 10.50 lakh for the proceeds received. This liability accretes to the amount payable on repurchase

of ₹ 10.56 lakh at 1 October 20X7, using the effective interest rate method. A Ltd. will continue to recognise a notional interest income in the periods to 1 April 20X7 and 1 October 20X7, and it will also account for an equal amount of notional interest paid to the third party. On 1 October 20X7 following repurchase of the bond by A Ltd., the liability of ₹ 10.56 lakh will be eliminated, as shown below:

Liability carrying value

Particulars	₹
Liability at 1 October 20X6	10,50,000
Interest payable for the half year to 31 March 20X7 @ 10.081%	52,926
Notional cash paid to third party on 31 March 20X7*	<u>(50,000)</u>
Balance at 31 March 20X7	10,52,926
Interest payable for the half year to 30 September 20X7 @ 10.081%	53,074
Notional cash paid to third party on 30 September 20X7*	<u>(50,000)</u>
Balance at 30 September 20X7	10,56,000
Liability repaid on 1 October 20X7 at repurchase price	<u>(10,56,000)</u>
	<u>Nil</u>

* Third party will receive interest directly from the bond as legal owner.

The transferee might be able to pledge or sell the bond during its period of ownership. In that situation, the transferor should reclassify the bond on its balance sheet as a loaned asset or repurchase receivable.

Sale and repurchase transaction (net settled in cash)

On 1 October 20X6, A Ltd. sells a bond at its fair value of ₹ 10.50 lakh to a third party, with an agreement to repurchase the bond on 1 October 20X7 for ₹ 10.56 lakh. The amortised cost of the bond at the sale date is ₹ 10,44,544.

The repurchase contract is to be settled net in cash (i.e. A Ltd. will not physically receive the bond back at the settlement date). The fair value of the asset at the settlement date amounts to ₹ 10.60 lakh. This means that A Ltd. will receive an additional ₹ 4,000 from the third party.

The fact that the forward repurchase agreement requires net settlement does not automatically lead to de-recognition. A Ltd. continues to recognise the asset. Since, A Ltd. will not physically receive the bond back, the bond will be de-recognised following receipt of the additional consideration of ₹ 4,000 at the settlement date. It would not be appropriate to continue to classify the bond as HTM at amortised cost. Instead, A Ltd. would need to reclassify the bond at FVTPL at the sale date of 1 October 20X6.

The entries are shown below:

Particulars	₹
Fair value of bond at 1 October 20X6	10,50,000
Amortised cost of bond at 1 October 20X6	(10,44,544)
Gain	5,456

Therefore, A Ltd. will record the bond at its fair value of ₹ 10.50 lakh and a corresponding liability of ₹ 10.50 lakh. The liability accretes to the repurchase price of ₹ 10.56 lakh, using the effective interest rate method.

At the settlement date of 1 October 20X7, immediately before de-recognition the bond will be fair valued to ₹ 10.60 lakh and a further gain of ₹ 10,000 will be recorded in P&L. Since the contract will be net settled in cash, the bond is then de-recognised. A Ltd. will record the following entries, from inception to settlement:

Particulars	Dr. ₹	Cr. ₹
Bank Dr.	10,50,000	
To Liability		10,50,000
Bond at fair value Dr.	10,50,000	
To Bond at HTM		10,44,544
To Gain on disposal (P&L)		5,456
Interest expense Dr.	6,000	
To Liability		6,000

Bond at fair value (increase)	Dr.	10,000	
To P&L gain			10,000
Liability	Dr.	10,56,000	
Bank	Dr.	4,000	
To Bond at fair value			10,60,000

Although a forward repurchase agreement that requires net settlement in cash is economically equivalent to a deferred sale, A Ltd. cannot de-recognise the asset, because the risks and rewards of ownership have been retained until settlement.

- 15. (i)** If a parent loses control of a subsidiary, the parent shall account for all amounts previously recognised in other comprehensive income (OCI) in relation to that subsidiary on the same basis as would be required if the parent had directly disposed of the related assets or liabilities. Therefore, if a gain or loss previously recognised in OCI would be reclassified to profit or loss on the disposal of the related assets or liabilities, the parent shall reclassify the gain or loss from equity to profit or loss (as a reclassification adjustment) when it loses control of the subsidiary.

Accordingly, a revaluation surplus previously recognised in other comprehensive income would be transferred directly to retained earnings on the disposal of the asset. Hence, the parent shall transfer the revaluation surplus directly to retained earnings when it loses control of the subsidiary. The revaluation reserve relating to the fixed assets, ₹ 170 is transferred to retained earnings in accordance with Ind AS 16 'Property, Plant and Equipment'.

The FVTOCI reserve arising from debt instrument under Ind AS 109 is recycled to P&L on disposal and is therefore included in the gain on disposal of controlling interest and on retained investment.

The gain or loss on the interest sold, and on the retained investment recognised in the income statement, is calculated as follows:

Particulars	₹
Fair value of the consideration (60%)	6,120
Fair value of retained investment (30%)	4,080
Carrying value of the NCI (10%)	<u>850</u>
Total	11,050
Less: Carrying value of former subsidiary's net assets	<u>(8,500)*</u>
	2,550
Add: FVTOCI reserve transferred to P/L as income	<u>68</u>
Gain on interest sold and on retained investment	<u>2,618</u>

$$* 7,480 + 1,020 = 8,500$$

- (ii) Ind AS 112 requires a parent entity to separately disclose both the total gain or loss on the subsidiary's loss of control and the portion of the gain or loss related to the retained non-controlling investment. To obtain the information necessary for disclosure, a calculation of the portion related to the gain or loss on the retained non-controlling investment is, therefore, necessary. The ₹ 2,618 gain on the interest sold and the retained investment is recognised in the P&L and is disclosed in the consolidated financial statements. Additionally, Ind AS 112 requires the disclosure of the portion of the gain or loss related to the remeasurement of the retained non-controlling investment to fair value. This is calculated as follows:

Particulars	₹
Fair value of retained investment	4,080
Less: Percentage retained of carrying value of subsidiary $[(7,480 + 1,020) \times 30\%]$	<u>(2,550)</u>
Gain on retained investment	<u>1,530</u>

(iii) **Journal entry on the disposal date**

Particulars		₹	₹
Cash	Dr.	6,120	
Investment in associate	Dr.	4,080	
FVTOCI reserve	Dr.	68	
Revaluation reserve	Dr.	170	
NCI	Dr.	850	
	To Net assets (including goodwill)		8,500
	To Retained earnings		170
	To Gain on disposal of controlling interest		2,618
(The accounting entry on the disposal date for the 60% interest sold, the gain recognised on the 30% retained investment and the de-recognition of the subsidiary)			

16. The joint arrangement with Y Ltd. is a joint operation because K Ltd. and Y Ltd. have equal rights to the assets and joint obligations for the liabilities relating to the arrangement. In a joint operation, the operators include their share of any jointly held assets. Therefore, the property, plant and equipment of K Ltd. at 31st March 20X2 will include:

- Leasehold property of ₹ 25 million x 24 years / 25 years
= ₹ 24 million
- Plant and equipment of ₹ 7.5 million x 4 years / 5 years
= ₹ 6 million

In a joint operation, the operators include their share of jointly incurred costs. Therefore, the statement of profit or loss of K Ltd. for the year ended 31st March 20X2 will include the following costs:

- Amortisation of lease premium ₹ 1 million.
- Depreciation of plant and equipment ₹ 1.5 million.

- Cash cost of operating the depot ₹ 4 million.

K Ltd. will also include its own discretionary delivery charges of ₹ 2 million as a reduction in its operating costs.

17. Deferred tax liability @ 20% as at 31 March, 20X2

Component	Explanation/working	₹ in million
Investment in L Ltd.	Carrying value is ₹ 75 million. Tax base is ₹ 45 million. Taxable temporary difference is ₹ 30 million. (20% × {₹ 75 million – ₹ 45 million})	6.00
Head office property	Carrying value is ₹ 45 million. Tax base is ₹ 20.75 million	4.85
	Total	10.85

* ₹ 22 million – ₹ 1.25 million = ₹ 20.75 million.

Deferred tax charge/(credit) to profit or loss for the year ended 31 March, 20X2

Component	Explanation/working	₹ in million
Investment in L Ltd.	Opening deferred tax liability is ₹ 5 million (20% × {₹ 70 million – ₹ 45 million}). Share of profits under the equity method is recognised in profit or loss. Tax charge is the difference between the closing and opening liability.	1.00
Head office property	Refer Working Note	(0.15)
	Total	0.85

Deferred tax charge/(credit) to other comprehensive income for the year ended 31 March 20X2

Component	Explanation/working	₹ in million
Head office property	Refer Working Note	1.40

Working Note:

Computation of deferred tax on property revaluation: The deferred tax liability at 31 March 20X1 is ₹ 3.6 million (20% of {₹ 40 million - ₹ 22 million}).

At 31 March 20X2, prior to revaluation, the carrying amount of the property is ₹ 38 million and its tax base is ₹ 20.75 million (₹ 22 million - ₹ 1.25 million). The deferred tax liability at this point is ₹ 3.45 million (20% x {₹ 38 million - ₹ 20.75 million}).

The reduction in this liability is ₹ 0.15 million (₹ 3.6 million - ₹ 3.45 million). This would be credited to income tax expense in arriving at profit or loss.

Following revaluation, the carrying value becomes ₹ 45 million and the tax base stays the same. So, the new deferred tax liability is ₹ 4.85 million [20% x (₹ 45 million - ₹ 20.75 million)].

The increase in the deferred tax liability of ₹ 1.4 million (₹ 4.85 million - ₹ 3.45 million) is debited to other comprehensive income.

18. Ind AS 102 'Share-based Payments', requires that equity settled share-based payments should be measured based on their fair value at the grant date, based on the number of options expected to vest based on estimates at the reporting date.

The cost should be spread over the vesting period - three years in this case.

This means that the charge to profit or loss in the year ended 31 March 20X2 = $1,850 \times 1,000 \times ₹ 1.20 \times 1/3 = ₹ 7,40,000$

Journal Entry as on 31 March 20X2

Employee benefits expenses (transferred to P/L)	Dr.	7,40,000	
To Share-based payment reserve (equity) (1/3 of expected vested equity instruments value)			7,40,000

Based on the original arrangements, the cumulative balance in equity on 31 March 20X3 = ₹ 14,72,000 ($1,840 \times 1,000 \times ₹ 1.20 \times 2/3$).

The impact of the repricing on 30 September 20X2 is to charge the incremental increase in fair value over the remaining vesting period on the same basis as the original charge.

Therefore, the additional credit to equity in respect of the repricing

$$= 1,840 \times 1,000 \times \{\text{₹ } 1.05 - \text{₹ } 0.90\} \times 6/18 = \text{₹ } 92,000$$

The closing balance in equity

$$= \text{₹ } 14,72,000 + \text{₹ } 92,000 = \text{₹ } 15,64,000.$$

The charge to profit or loss in the year ended 31 March 20X3

$$= \text{₹ } 15,64,000 - \text{₹ } 7,40,000 = \text{₹ } 8,24,000.$$

Journal Entry as on 31 March 20X2

Employee benefits expenses (transferred to P/L)	Dr.	8,24,000	
To Share-based payment reserve (equity) (2/3 of expected vested equity instruments value)			8,24,000

19. CC Ltd. would include the total revenue of ₹ 6.8 million (₹ 6 million + ₹ 0.8 million) from O Ltd. receivable in the year ended 31 March 20X2 within its revenue and show ₹ 1.8 million within trade receivables at 31 March 20X2.

The spouse of a director of CC Ltd. would be regarded as a related party of CC Ltd. because he/she is a close family member of one of the key management personnel of CC Ltd.

From 1 June 20X1, O Ltd. would also be regarded as a related party of CC Ltd. because from that date O Ltd. is an entity controlled by another related party.

Because O Ltd. is a related party with whom CC Ltd. has transactions, then CC Ltd. should disclose:

- The nature of the related party relationship.
- The revenue of ₹ 6 million from O Ltd. since 1 June 20X1.
- The outstanding balance of ₹ 1.8 million at 31 March 20X2.

In the current circumstances it may well be necessary for CC Ltd. to also disclose the favourable terms under which the transactions are carried out.

20. Extract of Statement of cashflows - showing cash flow from financing activities

	₹
Proceeds from issue of equity share capital (2,00,000 + 50,000) (W.N.1 and W.N.2)	2,50,000
Payment to lease liabilities	<u>(3,00,000)</u>
Net cash outflow from financing activities	<u>(50,000)</u>

Working Notes:

1. Equity Share Capital Account

	₹		₹
To Balance c/d	5,00,000	By Balance b/d	2,50,000
		By Bonus issue (1/5 × 2,50,000)	50,000
		By Bank (Issue of shares on 21 st November (bal. fig.))	2,00,000
Total	<u>5,00,000</u>	Total	<u>5,00,000</u>

2. Securities Premium Account

	₹		₹
To Bonus issue (1/5 × 2,50,000)	50,000	By Balance b/d	50,000
To Balance c/d	50,000	By Bank (Premium received on issue of shares for cash on 21 st November (bal. fig.))	50,000
Total	<u>1,00,000</u>	Total	<u>1,00,000</u>



PAPER – 2

ADVANCED FINANCIAL MANAGEMENT



QUESTIONS

International Financial Management

1. A US parent company has subsidiaries in France, Germany, UK and Italy. The amounts due to and from the affiliates is converted into a common currency viz. US dollar and entered in the following matrix.

Inter Subsidiary Payments Matrix (US \$ Thousands)

Paying affiliate						
		France	Germany	UK	Italy	Total
Receiving affiliate	France	---	80	120	200	400
	Germany	120	---	80	160	360
	UK	160	120	---	140	420
	Italy	200	60	120	---	380
	Total	480	260	320	500	1560

The treasurer of US Parent company is suggesting that by applying Multilateral Netting system the company can save a lot of transfer/exchange costs. The company's Board agreed with Treasurer's proposal.

From the information given above, choose the correct answer to the following questions:

- I. Before applying Multilateral Netting it is necessary to apply.....
 - (a) Unilateral Netting
 - (b) Bilateral Netting

- (c) Multilateral Netting
- (d) Interest Rate Swapping
- II. Through Multinational Netting these transfers will be reduced to
.....
 - (a) \$ 50,000
 - (b) \$ 100,000
 - (c) \$ 150,000
 - (d) \$ 200,000
- III. The Net Payment/ Net Receipts for France after netting off shall
be.....
 - (a) Net Receipt \$ 40,000
 - (b) Net Payment \$ 80,000
 - (c) Net Payment \$ 40,000
 - (d) Net Receipt \$ 80,000

Foreign Exchange Exposure and Risk Management

2. On 20.10.2024, the credit balance of an Indian bank in NOSTRO account with LMN Bank in London was £ 1,60,000 and the overbought position was £ 1,00,000. During the day, the following transactions have taken place.

Events	Time	Amount (£)
DD Purchased	11:08	50,000
Purchased a bill on London	11:50	150,000
Sold forward TT	13:15	100,000
Forward purchase contract cancelled	13:55	50,000
Remitted by TT	14:45	85,000
Draft in London cancelled	15:00	40,000

Based on the above scenario, choose the most appropriate answer for the following multiple-choice questions:

- I. How much was the total amount of purchase commitments made during the day by the Indian Bank?
 - (a) £ 2,00,000
 - (b) £ 1,50,000
 - (c) £ 3,40,000
 - (d) £ 50,000

- II. The final cash balance in the NOSTRO account at the end of 20.10.24 stands at
 - (a) £ 85,000
 - (b) £ 75,000
 - (c) £ 20,000
 - (d) £ 160,000

- III. The transaction took place atshall affect both exchange & cash position of the bank with LMN Bank.
 - (a) 11:08
 - (b) 11:50
 - (c) 14:45
 - (d) 15:00

- IV. If at the end of day bank is required to maintain a credit balance of £ 20,000 in the NOSTRO account, then it.....
 - (a) shall buy forward £ 15,000
 - (b) shall sell spot TT £ 55,000
 - (c) shall buy spot TT £ 55,000
 - (d) shall sell forward £ 55,000

- V. If bank takes required steps to maintain a credit balance of £ 20,000 in the Nostro account, then what additional step was required to achieve the overbought position of £ 65,000?
- Buying forward £ 15,000
 - Selling forward £ 65,000
 - Buying forward £ 60,000
 - Selling forward £ 15,000

Advanced Capital Budgeting Decisions

3. KLM Ltd., is considering taking up one of the two projects-Project-A and Project-B. Both the projects having same life require equal investment of ₹ 8.00 crore each. Both are estimated to have almost the same yield. As the company is new to this type of business, the cash flow arising from the projects cannot be estimated with certainty. An attempt was therefore, made to use probability to analyse the pattern of cash flow from other projects during the first year of operations. This pattern is likely to continue during the life of these projects. The results of the analysis are as follows:

Project A		Project B	
Cash Flow (in ₹ Crore)	Probability	Cash Flow (in ₹ Crore)	Probability
1.10	0.10	0.90	0.10
1.30	0.20	1.30	0.25
1.50	0.40	1.70	0.30
1.70	0.20	2.10	0.25
1.90	0.10	2.50	0.10

Advise which of the two projects should be accepted, keeping in view the risk assumed in relation to the expected return on the investment.

Note: Round off calculations upto three decimal points.

Security Valuation

4. Shares of V Ltd. are currently quoted at a trailing Price-to-Earnings (P/E) ratio of 8 times. As per the existing policy, the company recently retained ₹ 5 per share, representing 45% of its Earnings per Share (EPS), for ploughing back into the business.

You are required to compute:

- (i) The cost of equity to the company if the market expects a growth rate of 15% p.a.
- (ii) If the anticipated growth rate is 16% per annum, calculate the indicative market price with the same cost of capital.
- (iii) If the company's cost of capital is 20% p.a. & the anticipated growth rate is 19% p.a., calculate the market price per share.

Note: Round off calculations upto 2 decimals.

Business Valuation

5. Following information is given in respect of Alpha Ltd., which is expected to grow at a rate of 20% p.a. for the next three years, after which the growth rate will stabilize at 8% p.a. normal level, in perpetuity.

	For the year ended March 31, 2023
Revenues	₹ 15,000 Crores
Cost of Goods Sold (COGS)	₹ 6,000 Crores
Operating Expenses	₹ 4,500 Crores
Capital Expenditure	₹ 1,500 Crores
Depreciation (included in Operating Expenses)	₹ 1,200 Crores

During high growth period, Revenues & Earnings before Interest & Tax (EBIT) will grow at 20% p.a. and capital expenditure net of depreciation will grow at 15% p.a.

From year 4 onwards, i.e. normal growth period revenues and EBIT will grow at 8% p.a. and incremental capital expenditure will be offset by the depreciation. During both high growth & normal growth period, net working capital requirement will be 25% of revenues.

Out of total capital, 60% constitute Equity and rest is Debt. The cost of equity is 17.53% and pre-tax cost of debt is 16%.

Corporate Income Tax rate is 30%.

Required:

Estimate the value of Alpha Ltd. using Free Cash Flows to the Firm (FCFF).

The PVIF @ 15 % for the three years are as below:

Year	t ₁	t ₂	t ₃
PVIF	0.8696	0.7561	0.6575

Note: Carry out calculation in ₹ Crore and round off figures upto two decimal points.

Derivatives Analysis & Valuation

6. Following is the information available pertaining to shares of O Ltd.:

Current Market Price (₹)	₹ 840.00
Maximum Expected Price (₹) in 6 Months, with a 45% Probability	₹ 1050.00
Minimum Expected Price (₹) in 6 Months	₹ 756.00
Continuously Compounded Rate of Interest (p.a.) (%)	7.00%

Required:

- Assuming that a 6-month European call option on the shares of O Ltd. is available with a strike price of ₹ 900.00, calculate the value of the call option using the Replicating Portfolio Approach and the Risk-Neutral Valuation Method.
- Examine whether the given probability can be applied to determine the value of the option using the Risk-Neutral Valuation Method.

Note: (1) $e^{0.035} = 1.0356$

(2) Round off all calculations upto 2 decimal points.

Interest Rate Risk Management

7. Two companies ABC Ltd. and XYZ Ltd. approach the DEF Bank for FRA (Forward Rate Agreement). Both companies want to borrow a sum of ₹ 100 crores after 2 years for a period of 1 year. Bank has calculated Yield Curve of both companies as follows:

Year	XYZ Ltd.	ABC Ltd.
1	3.86%	4.12%
2	4.20%	5.48%
3	4.48%	5.78%

Required:

- Identify at least one reason for difference in the Yield Curve for the companies.
- Calculate the rate of interest DEF Bank would quote to both companies for 2V3 FRA, using the company's yield information as quoted above.
- Suppose DEF Bank offers Interest Rate Guarantee at 5% for a premium of 0.10% of the amount of loan, calculate the cost of interest for XYZ Ltd. if interest rate for one year in 2 years turns out to be
 - 4.50%
 - 5.50%

Portfolio Management

8. You are given the following information related to the return from various securities:

	Effective Annual Return			
	Probability	LMN Ltd.	XYZ Ltd.	Risk free Bond
Economic Situation I	0.40	5%	15%	4%
Economic Situation II	0.60	25%	5%	4%

Portfolio Mix Matrix

	Shares of LMN Ltd.	Shares of XYZ Ltd.	Risk Free Bond
Portfolio A	75%	25%	0%
Portfolio B	75%	0%	25%
Portfolio C	100%	0%	0%

Required:

- (i) Calculate the expected return and risk of each Portfolio.
- (ii) Assess these Portfolios from the perspective of:
 - (I) a Risk Averse investor and,
 - (II) a Risk Seeker investor.

Mergers, Acquisitions and Corporate Restructuring

9. The directors of E. Ltd. are considering the acquisition of the entire capital of a private limited company, A (P) Ltd. Both companies being financed by equity.

The acquisition would take place on 1st April 2027. E Ltd. has deputed a person to collect sufficient relevant information. This person has discovered that a public limited company, named T Ltd. most closely resembling A(P) Ltd. It has equity cost of capital of 19.30% and has a PE Ratio of 7.9. T Ltd. is engaged in the same line of business as A (P) Ltd. and possess similar business and financial risk.

The following details relating to E Ltd. and A (P) Ltd. have been compiled by the same person:

- (i) The cost of capital of E Ltd. is 15.85%. As per his estimates, if A (P) Ltd. is acquired, the cash flow of E Ltd. for the year 2027-28 will be increased by an amount equal to 105% of the net profit of the year 2026-27 of A(P) Ltd. before deducting director's emoluments.
- (ii) In addition to that post acquisition cash flow generated by A (P) Ltd. shall constitute 30% of total cash generated of the combined firm. Further it is predicted that the cash flows of E Ltd. will increase

by 5% per annum in 2028-29 and subsequent years whether A(P) Ltd. is acquired or not.

- (iii) Following is the net profit figures of A(P) Ltd. (after deduction of director's emoluments).

Year	Net Profit
2021-22	₹ 6.19 Crore
2022-23	₹ 6.00 Crore
2023-24	₹ 5.24 Crore
2024-25	₹ 6.04 Crore
2025-26	₹ 6.28 Crore
2026-27 (Estimated)	₹ 7.90 Crore

The draft annual statements of the year 2026-27 also show that the net assets of A (P) Ltd. are ₹ 36.18 crore on historic cost basis and ₹ 63.75 crore on replacement cost basis. He also estimated that the net assets of A (P) Ltd. would realise ₹ 40 Crore on liquidation.

- (iv) The two directors and only shareholders are Mr. and Mrs. A, whose emoluments appear to average 10% of the net profits figures, after deducting those emoluments.

Required:

You as CFO of E Ltd. has been asked to suggest the maximum amount the directors of E Ltd. would be willing to pay for the acquisition of A (P) Ltd.

Note: Carry out calculation in ₹ Crore and round off figures upto four decimal points.

Mutual Funds

10. The Investment portfolio of a Fund is as follows:

Government Bond	Coupon Rate (%)	Purchase Rate (FV ₹ 100 per Bond)	Duration (Years)
GOI 2026	11.68	106.50	3.50
GOI 2030	7.55	105.00	6.50

GOI 2035	7.38	105.00	7.50
GOI 2042	8.35	110.00	8.75
GOI 2052	7.95	101.00	13.00

Face value of total Investment is ₹ 5 crores in each Government Bond.

Required:

- (i) Identify the type of the Fund.
- (ii) Calculate NAV per unit of the Fund if number of units is 2.50 crore.
- (iii) Suggest a suitable action to reduce risk by churning out investment portfolio in the following scenario:
 - A. Interest rates are expected to lower by 25 basis points.
 - B. Interest rates are expected to raise by 75 basis points.

Also calculate the revised duration of investment portfolio in each scenario.

Note: Use simple average to make calculations.

Security Analysis

11. The data pertains to the share prices of A Ltd. is as follows:

Days	Date	Open Price (₹)	High Price (₹)	Low Price (₹)	Close Price (₹)
1	14-12-20xx	334.71	335.14	334.38	334.54
2	15-12-20xx	334.54	334.78	334.28	334.35
3	16-12-20xx	334.14	334.40	333.98	334.32
4	17-12-20xx	334.35	334.46	333.78	333.83
5	18-12-20xx	333.73	333.80	333.52	333.71
6	21-12-20xx	333.76	333.89	333.31	333.41
7	22-12-20xx	333.41	333.41	333.11	333.31
8	23-12-20xx	333.27	333.41	333.06	333.35
9	24-12-20xx	333.07	333.28	332.96	333.02

10	28-12-20xx	332.99	333.19	332.54	332.59
11	29-12-20xx	332.60	332.29	332.42	332.52
12	30-12-20xx	332.56	332.89	332.49	332.86
13	31-12-20xx	332.89	335.36	332.56	333.29
14	04-01-20x1	333.35	333.46	332.77	332.84
15	05-01-20x1	332.94	333.11	332.79	332.99
16	06-01-20x1	333.00	333.38	333.00	333.25
17	07-01-20x1	333.23	333.56	333.22	333.30
18	08-01-20x1	333.23	333.46	333.17	333.20
19	11-01-20x1	333.18	333.21	332.94	333.02
20	14-12-20x1	332.91	333.25	332.80	333.20

Evaluate whether the Relative Strength Index (RSI) of A Ltd.'s stock indicates a bullish or bearish trend using the 14-day RSI.

Note: Round off calculations upto 2 decimal points.

Theoretical Questions

12. Explain the areas in which the role of the CFO has expanded beyond the traditional role in the post-pandemic era.
13. Explain the term "Political Risk" and its various forms. Is Political Risk covered under Financial Risk? If so, explain the reasons for the same.
14. Explain how the performance Securitization performance is impacted by market risk.

OR

Explain the term Angel Investor and its role in context of Startup Finance.



SUGGESTED ANSWERS/HINTS

Question No.	Answer
1. I	(b)
II	(d)
III	(b)
2. I	(c)
II	(b)
III	(c)
IV	(b)
V	(a)

3. Calculation of Variance and Standard Deviation

Project A

Expected Net Cash Flow

$$= (0.10 \times 1.10) + (0.20 \times 1.30) + (0.40 \times 1.50) + (0.20 \times 1.70) + (0.10 \times 1.90)$$

$$= 0.11 + 0.26 + 0.60 + 0.34 + 0.19 = 1.50$$

$$\sigma^2 = 0.10(1.10 - 1.50)^2 + 0.20(1.30 - 1.50)^2 + 0.40(1.50 - 1.50)^2 + 0.20(1.70 - 1.50)^2 + 0.10(1.90 - 1.50)^2$$

$$= 0.016 + 0.008 + 0 + 0.008 + 0.016 = 0.048$$

$$\sigma = \sqrt{0.048} = 0.219$$

Project B

Expected Net Cash Flow

$$= (0.10 \times 0.90) + (0.25 \times 1.30) + (0.30 \times 1.70) + (0.25 \times 2.10) + (0.10 \times 2.50)$$

$$= 0.09 + 0.325 + 0.51 + 0.525 + 0.25 = 1.70$$

$$\sigma^2 = 0.1(0.90 - 1.70)^2 + 0.25(1.30 - 1.70)^2 + 0.30(1.70 - 1.70)^2 + 0.25(2.10 - 1.70)^2 + 0.10(2.50 - 1.70)^2$$

$$= 0.064 + 0.04 + 0 + 0.04 + 0.064 = 0.208$$

$$\sigma = \sqrt{0.208} = 0.456$$

To advise which of the two projects should be accepted, keeping in view the risk assumed in relation to the expected return on the investment we shall calculate the Coefficient of Variation as follows:

$$\text{Coefficient of Variation} = \frac{\text{Standard Deviation}}{\text{Mean}}$$

$$\text{Project A} = \frac{0.219}{1.50} = 0.146$$

$$\text{Project B} = \frac{0.456}{1.70} = 0.268$$

Advice: Since Project A has lower Coefficient of Variation it has a better the risk-return tradeoff.

4. (i) Cost of Capital

Retained earnings (45%) ₹ 5 per share

Dividend (D_0) (55%) ₹ 6.11 per share

EPS (E_0) (100%) ₹ 11.11 per share

P/E Ratio 8 times

Market price ₹ 11.11 × 8 = ₹ 88.88

Cost of equity capital

$$= \left(\frac{\text{Div}}{\text{Price}} \times 100 \right) + \text{Growth \%} = \frac{6.11(1+0.15)}{88.88} \times 100 + 15\% = 22.91\%$$

$$\begin{aligned} \text{(ii) Market Price} &= \left(\frac{\text{Dividend}}{\text{Cost of Capital(\%)} - \text{Growth Rate(\%)}} \right) \\ &= \frac{₹ 6.11(1+0.16)}{(22.91 - 16)\%} = ₹ 102.57 \text{ per share} \end{aligned}$$

$$\text{(iii) Market Price} = \frac{₹ 6.11(1+0.19)}{(20 - 19)\%} = ₹ 727.09 \text{ per share}$$

5. Determination of forecasted Free Cash Flow to the Firm (FCFF)

(₹ in crores)

	Yr. 1	Yr. 2	Yr. 3	Terminal Year
Revenue	18000.00	21600.00	25920.00	27993.60
COGS	7200.00	8640.00	10368.00	11197.44
Operating Expenses	3960.00*	4752.00	5702.40	6158.59
Depreciation	1440.00	1728.00	2073.60	2239.49
EBIT	5400.00	6480.00	7776.00	8398.08
Tax @30%	1620.00	1944.00	2332.80	2519.42
EAT	3780.00	4536.00	5443.20	5878.66
Capital Exp. – Dep.	345.00	396.75	456.26	-
Δ Working Capital	750.00	900.00	1080.00	518.40
Free Cash Flow (FCF)	2685.00	3239.25	3906.94	5360.26

* Excluding Depreciation.

Calculation of WACC

$$= 60\% \times 17.53\% + 40\% \times 16\% (1-0.30)$$

$$= 15\%$$

Present Value (PV) of FCFF during the explicit forecast period is:

FCFF (₹ in crores)	PVF @ 15%	PV (₹ in crores)
2685.00	0.8696	2334.88
3239.25	0.7561	2449.20
3906.94	0.6575	2568.81
		7352.89

PV of the terminal, value is:

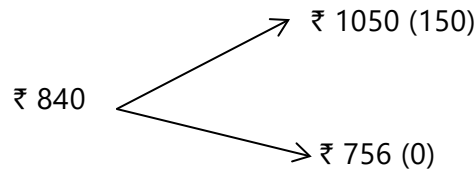
$$\frac{5360.26}{0.15 - 0.08} \times (\text{PVIF } 15\%, 3) = ₹ 76575.14 \text{ Crore} \times 0.6575$$

$$= ₹ 50348.15 \text{ Crore}$$

The value of the firm is:

$$₹ 7352.89 \text{ Crores} + ₹ 50348.15 \text{ Crores} = ₹ 57701.04 \text{ Crores}$$

6. (i) (A) Call Option value using Replicating Portfolio Approach



$$\Delta = \frac{₹ 150 - ₹ 0}{₹ 1050 - ₹ 756} = 0.51$$

$$\text{Initial Investment} = 0.51 \times ₹ 840 = ₹ 428.40$$

Value of Portfolio if Price goes down to ₹ 756.

$$\text{Value of holding } 0.51 \times ₹ 756 = ₹ 385.56$$

Accordingly Let 'P' be the option price, then

$$₹ 428.40 - P = ₹ 385.56 / 1.0356 = ₹ 372.31$$

$$P = ₹ 56.09$$

(B) Value of Call Option using Risk Neutral Method

Let 'P' be the probability of Price increase, then

$$p \times 1050 + (1 - p) \times 756 = 840(1.0356)$$

$$147p = 50.48$$

$$p = 0.39$$

Probability of Price increase = 0.39

Probability of Price decrease = 0.61

Accordingly, the price of the options shall be:

$$\frac{0.39 \times 150 + 0.61 \times 0}{1.0356} = ₹ 56.49$$

- (ii) In Risk Neutral Model, valuation of options is based on arbitrage and is therefore independent of risk preferences; one should be able to value options assuming any set of risk preferences and get the same answer. Hence, the given probability cannot be used to

value the option. Instead, the risk-neutral probability should be computed and used for valuing the option.

7. (i) The difference in yield curve may due to the lower credit rating of ABC Ltd. compared to XYZ Ltd.

- (ii) DEF Bank will fix interest rate for 2V3 FRA after 2 years as follows:

XYZ Ltd.

$$(1+r) (1+0.0420)^2 = (1+0.0448)^3$$

$$(1+r) (1.0420)^2 = (1.0448)^3$$

$$r = 5.04\%$$

Bank will quote 5.04% for a 2V3 FRA.

ABC Ltd.

$$(1+r) (1+0.0548)^2 = (1+0.0578)^3$$

$$(1+r) (1.0548)^2 = (1.0578)^3$$

$$r = 6.38\%$$

Bank will quote 6.38% for a 2V3 FRA.

- (iii) Interest payable by XYZ Ltd. under two scenarios will be computed as follows:

		4.50% Option is allowed to be lapsed	5.50% Option is Exercised
Interest	₹ 100 crores X 4.50%	₹ 4.50 crores	-
	₹ 100 crores X 5.04%*	-	₹ 5.04 crores
Premium (Cost of Option)	₹ 100 crores X 0.10%	₹ 0.10 crores	₹ 0.10 crores
		₹ 4.60 crores	₹ 5.14 crores

* Since after 2 years 1 year interest rate turned out to be 5.50%, it will be beneficial for XYZ Ltd. to exercise its option.

8. (i) Expected Return of different Portfolios

To calculate expected return of different Portfolios first we shall calculate the expected return each security as follows:

$$\text{Share of LMN } E(R_L) = 5\% \times 0.40 + 25\% \times 0.60 = 17\%$$

$$\text{Share of XYZ } E(R_X) = 15\% \times 0.40 + 5\% \times 0.60 = 9\%$$

$$\text{Risk Free Bond} = 4\%$$

Expected Returns from Portfolios

$$\text{Portfolio A} = 0.75 \times 17\% + 0.25 \times 9\% = 15\%$$

$$\text{Portfolio B} = 0.75 \times 17\% + 0.25 \times 4\% = 13.75\%$$

$$\text{Portfolio C} = 17\%$$

To calculate risk of each Portfolio, first we shall calculate risk i.e. Variance and Standard Deviations of each security and covariance between LMN & XYZ and LMN & Risk Free Bonds as follows:

Variance of LMN Ltd.

$$= 0.40 \times (5 - 17)^2 + 0.60 \times (25 - 17)^2$$

$$= 0.40 \times 144 + 0.60 \times 64 = 96$$

Variance of XYZ Ltd.

$$= 0.40 \times (15 - 9)^2 + 0.60 \times (5 - 9)^2$$

$$= 0.40 \times 36 + 0.60 \times 16 = 24$$

Variance of Risk free Bond – 0

Covariance between LMN and XYZ

Scenario	Prob. (P)	$(R_L - \bar{R}_L)$	$(R_X - \bar{R}_X)$	$(R_L - \bar{R}_L) (R_X - \bar{R}_X) P$
Situation I	0.40	(5% - 17%)	(15% - 9%)	28.80%
Situation II	0.60	(25% - 17%)	(5% - 9%)	- 19.20%
				- 48.00%

Covariance between share of LMN and Risk Free Bond shall be Zero.

$$\text{Variance of Portfolio} = (w_1)^2 (\sigma_1)^2 + (w_2)^2 (\sigma_2)^2 + 2 w_1 w_2 \text{Cov}_{12}$$

Variance of Portfolio A

$$= (0.75)^2 (96) + (0.25)^2 (24) + 2 (0.75) (0.25) (-48) = 54 + 1.50 - 18 = 37.50$$

$$\text{Risk of Portfolio A } (\sigma_A) = \sqrt{37.50} = 6.12$$

Variance of Portfolio B

$$= (0.75)^2 (96) + (0.25)^2 (0) = 54$$

$$\text{Risk of Portfolio B } (\sigma_B) = \sqrt{54} = 7.35$$

$$\text{Risk of Portfolio C } (\sigma_C) = \sqrt{96} = 9.80$$

- (ii) (I) Since a Risk neutral investor judges the portfolio only by expected return and ignore the risk factor and hence will choose Portfolio C having maximum return and that too without any risk.
- (II) Risk Seeker investor chooses the portfolio taking into account both risk and return. Though greater return is penalized depending on how much extra risk is taken considering return achieved. There can be two ways to select the Portfolio one on the basis of covariance as due to negative covariance he may opt for Portfolio A as return is bit higher than Portfolio B.

Alternatively, Portfolio can also be chosen based on Coefficient of Variation as follows:

$$\text{Portfolio A} = 6.12/15 = 0.408$$

$$\text{Portfolio B} = 7.35/13.75 = 0.535$$

$$\text{Portfolio C} = 9.80/17 = 0.576.$$

Since CV is best in case of Portfolio A it should be opted for as it results better risk- return trade off.

9. The maximum amount which the directors of E Ltd. should pay for the acquisition of A (P) Ltd. is equal to the increase in wealth of E Ltd.'s shareholders as a result of the acquisition. This increase will come from extra cash flows generated for the shareholders of E Ltd. either as an

income-producing going concern or by sale of its assets, on by combination of the two.

Since from the fact given there is no hint that the directors of E Ltd. have any intention to liquidate the A (P) Ltd. the present value of additional cash generated will be used to calculate the addition in the wealth (equivalent to the value of A (P) Ltd.) of shareholders of E Ltd. consequent upon acquisition. Using analyst's estimate first we shall Calculate additional cash flow to be generated due to acquisition is as follows.

	₹ Crore
Profit of A (P) Ltd. for the year 2026-27	7.90
Add: Director's Remuneration	0.79
	8.69
Addition of Cash in the year 2027-28 @105%.	9.1245

Now the addition to the shareholder's wealth can be calculated using following two approaches:

Approach I

Assuming 5%. (as used above) growth rate be continued the PV of additional Cash generated Shall be:

$$₹ 9.1245 \text{ crore} / (0.193 - 0.05) = ₹ 63.8077 \text{ crores}$$

Approach II

Alternatively, 30%. of additional cash flow generated for combined can also be used to compute the same value as follows: -

However, in such situation the discount rate to be used shall be weighted average cost of capital i.e.

$$0.70 \times 15.85\% + 0.30 \times 19.30\% = 16.89\%$$

	₹ Crore
Cash Flow of A(P) Ltd. for the year 2027-28	9.1245
Thus, combined cash flow of E Ltd. $(100/30) \times 9.1245$	30.4150
The Combined Value of Firm = $30.4150 / (0.1689 - 0.05)$ (A)	255.8032

Portion of Cash flow pertain to E Ltd. 0.70×30.4150	21.2905
Value of E Ltd. alone = $21.2905 / (0.1585 - 0.05)$ (B)	196.2258
Increase in Value & Firm due to acquisition (A) – (B)	59.5774

Decision: - Though any of Value ₹ 63.8077 crore or ₹ 59.5774 crore can be offered to acquire A (P) Ltd. but the amount of ₹ 59.5774 is more appropriate to offer as it accounts for direct impact on cash flow of E Ltd. due to acquisition of A (P) Ltd.

10. (i) This type of Fund is a Gilt Fund as the amount of fund is invested in dated Government Securities.
- (ii) To calculate NAV per unit first we shall calculate of actual investment of Funds as follows:

Security	Purchase price	Investment (₹ in lakhs)
GOI 2026	106.50	532.50*
GOI 2030	105.00	525.00
GOI 2035	105.00	525.00
GOI 2042	110.00	550.00
GOI 2052	101.00	505.00
	Total	<u>2,637.50</u>

$$* \frac{\text{₹ 5 crores}}{\text{₹ } 100 \times 1,00,000} \times \text{₹ } 106.50$$

Accordingly, the NAV per units shall be:

$$\frac{\text{₹ } 2637.50 \text{ Lakhs}}{250 \text{ Lakhs}} = \text{₹ } 10.55$$

- (iii) Suitable action to churn out investment portfolio in following scenario is to reduce risk and to maximize profit or minimize losses.

$$\text{Average Duration} = \frac{3.5 + 6.5 + 7.5 + 8.75 + 13.00}{5} = \frac{39.25}{5} = 7.85 \text{ years}$$

- (A) Interest rates are expected to be lower by 25 basis points in such case increase the average duration by purchasing GOI

2052 and disposing of GOI 2026.

$$\begin{aligned}\text{Revised average duration shall be} &= \frac{39.25 - 3.5 + 13}{5} \\ &= \frac{48.75}{5} = 9.75 \text{ years}\end{aligned}$$

- (B) Interest rates are expected to rise by 75 basis points in such case reduce the average duration by (*) Purchasing GOI 2030 and disposing of GOI 2052.

$$\begin{aligned}\text{Revised average duration shall be} &= \frac{39.25 - 13 + 6.5}{5} \\ &= \frac{32.75}{5} = 6.55 \text{ years}\end{aligned}$$

(*) Purchasing of GOI 2026 is not beneficial as maturity period is very short and 75 basis points is comparatively higher change.

Thus, it can be said that the in first case the duration of portfolio is revised from 7.85 years to 9.75 years. In second case it stands revised from 7.85 years to 6.55 years.

11. To calculate the RSI, we shall use the **closing prices** of A Ltd.'s stock. For the 14-day RSI, we shall first calculate the moving averages of gains and losses for the initial 14-day period and subsequently update these moving averages for each succeeding day, as shown in the table below. The RSI for the 14th day onwards shall then be calculated using the following formula:

$$RSI = 100 - \frac{100}{(1 + RS)}$$

$$\text{Where } RS = \frac{\text{Average Gain Per Day}}{\text{Average Loss Per Day}}$$

Further this updation in Avg Gain and Avg Loss columns for subsequent days shall be computed using following formula:

$$\frac{\text{Previous Day Avg Gain/Loss} \times 13}{14}$$

	Date	Closing Price	Change	Gain	Loss	Avg Gain	Avg Loss	RS	14-day RSI
1	14-12-20xx	334.54							
2	15-12-20xx	334.35	-0.19	0.00	0.19				
3	16-12-20xx	334.32	-0.03	0.00	0.03				
4	17-12-20xx	333.83	-0.49	0.00	0.49				
5	18-12-20xx	333.71	-0.12	0.00	0.12				
6	21-12-20xx	333.41	-0.30	0.00	0.30				
7	22-12-20xx	333.31	-0.10	0.00	0.10				
8	23-12-20xx	333.35	0.04	0.04	0.00				
9	24-12-20xx	333.02	-0.33	0.00	0.33				
10	28-12-20xx	332.59	-0.43	0.00	0.43				
11	29-12-20xx	332.52	-0.07	0.00	0.07				
12	30-12-20xx	332.86	0.34	0.34	0.00				
13	31-12-20xx	333.29	0.43	0.43	0.00				
14	04-01-20x1	332.84	-0.45	0.00	0.45				
15	05-01-20x1	332.99	0.15	0.15	0.00	0.07	0.18	0.39	28.06
16	06-01-20x1	333.25	0.26	0.26	0.00	0.08	0.17	0.47	31.97
17	07-01-20x1	333.30	0.05	0.05	0.00	0.08	0.16	0.50	34.21
18	08-01-20x1	333.20	-0.10	0.00	0.10	0.07	0.16	0.44	30.55
19	11-01-20x1	333.02	-0.18	0.00	0.18	0.07	0.16	0.44	30.50
20	12-01-20x1	333.20	0.18	0.18	0.00	0.08	0.15	0.53	34.64

Interpretation

The 14-day RSI on Day 20 is 34.64.

The conventional interpretation of RSI is:

- Above 70: Overbought
- 50–70: Bullish/positive momentum
- 30–50: Bearish/weak momentum
- Below 30: Oversold

Conclusion – Since the RSI is 34.64, it is below 50, indicating that the stock is experiencing bearish momentum. Although the RSI has recovered from 28.06 on Day 15 to 34.64 on Day 20, it remains below 50 and therefore does not yet provide confirmation of a bullish trend i.e. stock is still in bearish zone.

12. In post-pandemic time their role has been advanced in the following areas in addition to their traditional role:
- Risk Management:* Now a days the CFOs are expected to look after the overall functioning of the framework of Risk Management system of an organisation.
 - Supply Chain:* Post pandemic supply chain management system has been posing the challenge for the company to maintain the sustainable growth. Since CFOs are care takers of finance of the company, considering the financial viability of the Supply Chain Management their role has now become more critical.
 - Mergers, acquisitions, and Corporate Restructuring:* Since in recent period to maintain the growth and capture the market share there has been a spate of Mergers and Acquisitions and hence the role of CFOs has become more crucial because these are strategic decision and any error in them can lead to collapse of the whole business.
 - Environmental, Social and Governance (ESG) Financing:* With the evolving of the concept of ESG their role has been shifted from traditional financing to sustainability financing.
13. Political Risk is faced by and overseas investors, as the adverse action by the government of host country may lead to huge losses. This can be on any of the following form.
- Confiscation or destruction of overseas properties.
 - Rationing of remittance to home country.
 - Restriction on conversion of local currency of host country into foreign currency.
 - Restriction as to borrowings.

- Invalidation of Patents
- Price control of products

Though political risk is not a financial risk in direct sense but same can be included as any unexpected political change in any foreign country may lead to country risk which may ultimately may result in financial loss.

14. Market risks represent risks external to the transaction and include market-related factors that impact the performance of the securitization transaction. Some of these risks are as follows:

- (a) *Macroeconomic risks:* The performance of the underlying loan contracts depends on macroeconomic factors, such as industry downturns or adverse price movements of the underlying assets. For example, in the transportation industry a continuous decline in industrial production may lead to a downtrend in the use of services of the Commercial Vehicles (CVs) adversely impacting the cash flow of CVs operators. This in turn, may impact repayments on CV loans. Similarly, a fall in the prices of the CVs may increase chances of default as the borrower may wilfully default the loan and let the finance company repossess and sell the underlying vehicle instead of retaining it and continuing to pay instalments on time.
- (b) *Prepayment risks:* A change in the market interest rate represents a difficult situation for investors because it is a combination of prepayment risk and volatile interest rates. With a reduction in interest rates generally prepayment of retail loans increases, resulting in reinvestment risk for investors because investors may receive their monies ahead of schedule and may not be able to reinvest the amount at the same yield.
- (c) *Interest rate risks:* This risk is prominent where the loans in the pool are based on a floating rate and investor pay-outs are based on a fixed rate or vice versa. It results in an interest rate mismatch and can lead to a situation where the pool cash inflow, even at 100% collection efficiency, is not sufficient to meet investor pay-

outs. Interest rate swaps can be used to hedge this type of risk to some extent.

OR

As per Investopedia, Angel investors invest in small startups or entrepreneurs. Often, angel investors are among an entrepreneur's family and friends. The capital angel investors provide may be a one-time investment to help the business propel or an ongoing injection of money to support and carry the company through its difficult early stages.

Angel investors provide more favorable terms compared to other lenders, since they usually invest in the entrepreneur starting the business rather than the viability of the business. Angel investors are focused on helping startups take their first steps, rather than the possible profit they may get from the business. This makes their approach slightly different from venture capitalists.

Angel investors are also called informal investors, angel funders, private investors, seed investors or business angels. They are affluent individuals who inject capital for startups in exchange for ownership equity or convertible debt. Some angel investors invest through crowdfunding platforms online or build angel investor networks to pool in capital.

Angel investors typically use their own money, unlike venture capitalists who take care of pooled money from many other investors and place them in a strategically managed fund.

Though angel investors usually represent individuals, the entity that actually provides the fund may be a limited liability company, a business, a trust or an investment fund, among many other kinds of vehicles.

Angel investors who seed startups that fail during their early stages lose their investments completely. This is why professional angel investors look for opportunities for a defined exit strategy, acquisitions or initial public offerings (IPOs).



PAPER – 3: ADVANCED AUDITING, ASSURANCE AND PROFESSIONAL ETHICS

Part – I : Academic Update

**(Legislative Amendments / Notifications / Circulars / Rules / Guidelines
issued by Regulating Authority)**

Chapter 14 - Unit 2 - Special Features of Audit of Non-Banking Financial Companies

1. **Registration Exemption for Certain NBFCs – 2026 Amendment: On page no 14.90 following amendment may be read as an addendum to Chapter 14 and should be read along with the existing provisions.**

While the Registration Directions 2025 themselves introduced no substantive change from the SBR Directions 2023, a subsequent and significant amendment was introduced vide Reserve Bank of India (Non-Banking Financial Companies – Registration, Exemptions and Framework for Scale Based Regulation) Amendment Directions, 2026 (hereinafter referred to as the "Registration Amendment Directions 2026"), issued on April 29, 2026, effective from July 01, 2026. The Registration Amendment Directions 2026 introduced a three-category definitional framework:

- 1) **Unregistered (Type I – Exempt):** Non-deposit-taking NBFCs with no public funds, no customer interface, and asset size below ₹ 1,000 crore are exempted from the provisions of Sections 45IA and 45IC of the RBI Act. Such existing NBFCs, including those holding a Certificate of Registration as Type I NBFC, can apply for deregistration by December 31, 2026.
- 2) **Type I NBFC (Registered):** Non-deposit-taking NBFCs with no public funds and no customer interface, but with an asset size exceeding ₹ 1,000 crore, continue to require registration.

- 3) **Type II NBFC (Registered):** NBFCs that avail public funds or have a customer interface, regardless of asset size, continue to require registration.

This is a material departure from the position under the SBR Directions 2023, which did not provide for any such statutory exemption from registration for non-public fund, non-customer-facing NBFCs below the ₹ 1,000 crore threshold.

This deregulation specifically targets micro-NBFCs, private investment vehicles, holding companies, and family offices that previously bore the disproportionate administrative and financial compliance burden of maintaining a CoR simply because their balance sheets mathematically satisfied the 50-50 Test. The new three-tier registration model summary:

Classification Category	Customer Interface Requirement	Acceptance of Public Funds	Asset Size Threshold	RBI Registration Status
Unregistered Type I NBFC	Strictly None	Strictly None (Direct or Indirect)	Less than ₹ 1,000 crore	Exempt from Section 45-IA
Type I NBFC	Strictly None	Strictly None (Direct or Indirect)	Greater than ₹ 1,000 crore	Mandatory (CoR Required)
Type II NBFC	Permitted	Permitted	Any Asset Size	Mandatory (CoR Required)

2. As per the circular DoR.FIN.REC.25/03.10.038/2025-26 dated June 06, 2025, if an NBFC-MFI fails to maintain the criteria specified in following para for four consecutive quarters, it shall approach the Reserve Bank with a remediation plan for taking a view in the matter.

“NBFC-MFI” means a non-deposit taking NBFC which has a minimum of 60 percent of its total assets (netted off by intangible assets), on an ongoing basis, deployed towards “microfinance loans” as defined under

Reserve Bank of India (Regulatory Framework for Microfinance Loans) Directions, 2022.

3. Capital Requirements on page no. 14.92 to be read as:

Every applicable NBFC as defined in the Master Direction – Reserve Bank of India (Non-Banking Financial Company – Scale Based Regulation) Directions, 2023 shall maintain the minimum capital ratios given below, depending on the layer in which it is placed under the Scale Based Regulation (SBR) framework.

With effect from November 28, 2025 (as updated up to July 01, 2026), the RBI (Non-Banking Financial Companies – Prudential Norms on Capital Adequacy) Directions, 2025 prescribe the capital adequacy requirement on a layer-wise basis under the Scale Based Regulation (SBR) framework, summarised below.

- (a) NBFC primarily engaged in lending against gold jewellery (such loans comprising 50 percent or more of its financial assets), irrespective of layer: minimum Tier 1 capital 12 percent and minimum CRAR 15 percent of aggregate risk weighted assets (Tier 2 capital shall not, at any time, exceed 100 percent of Tier 1 capital);
- (b) NBFC – Middle Layer (NBFC-ML) and above (other than gold-jewellery lending NBFCs covered in (a) above): minimum Tier 1 capital 10 percent and minimum CRAR 15 percent of aggregate RWAs (Tier 2 capital $\leq$ 100 percent of Tier 1 capital);
- (c) NBFC – Upper Layer (NBFC-UL): all the requirements at (b) above PLUS a minimum Common Equity Tier 1 (CET1) capital of 9 percent of aggregate RWAs. CET1 is the highest-quality slice of Tier 1 capital – broadly, paid-up equity capital, share premium, statutory/capital/other free reserves and retained earnings, less specified regulatory deductions (e.g. goodwill, intangibles, certain DTAs);
- (d) NBFC – Top Layer: all the requirements at (c) above, PLUS a higher capital charge specifically communicated by the RBI to the NBFC at the time of its classification in the Top Layer; and

- (e) NBFC – Base Layer (other than gold-jewellery lending NBFCs): no specific CRAR/Tier 1 ratio is prescribed under Chapter II of the Directions; however, its Leverage Ratio (Total Outside Liabilities ÷ Owned Fund) shall not exceed 7 at any point of time.

CRAR = (Tier 1 Capital + Tier 2 Capital) ÷ Risk Weighted Assets (RWAs);
Tier 1 Capital Ratio = Tier 1 Capital ÷ RWAs; CET1 Capital Ratio = CET1 Capital ÷ RWAs.

“Tier 1 capital” for NBFCs (except NBFCs-BL) is the sum of

- (i) Owned fund as reduced by investment in shares of other NBFCs and in shares, debentures, bonds, outstanding loans and advances including hire purchase and lease finance made to and deposits with subsidiaries and companies in the same group exceeding, in aggregate, ten percent of the owned fund; and
- (ii) Perpetual debt instruments issued by a non-deposit taking NBFCs in each year to the extent it does not exceed 15 percent of the aggregate Tier 1 capital of such company as on March 31 of the previous financial year.

Notes:

1. NBFCs-BL are not eligible to include perpetual debt instruments in their Tier 1 capital.
2. Common Equity Tier 1 (CET1) capital: CET1 is Tier 1 capital as computed above, further reduced by items such as Perpetual Debt Instruments (PDI) included in Tier 1, goodwill and other intangible assets, specified deferred tax assets, and other regulatory deductions. An NBFC-UL and an NBFC in the Top Layer must additionally maintain CET1 of at least 9 percent of aggregate RWAs [see (c) and (d) above]; this requirement does not apply to NBFC-BL and NBFC-ML.

“Tier 2 capital” for NBFCs (except NBFCs-BL) is the sum of

- (i) Preference shares other than those which are compulsorily convertible into equity;
- (ii) Revaluation reserves at discounted rate of 55 percent;

- (iii) General provisions (including that for Standard Assets) and loss reserves to the extent these are not attributable to actual diminution in value or identifiable potential loss in any specific asset and are available to meet unexpected losses, to the extent of one and 1.25% of risk weighted assets;
- (iv) Hybrid debt capital instruments;
- (v) Subordinated debt; and

Provided that book value of subordinated debt shall be subject to discounting as provided under

Remaining Maturity of the instruments	Rate of discount
Up to one year	100%
More than one year but up to two years	80%
More than two years but up to three years	60%
More than three years but up to four years	40%
More than four years but up to five years	20%

to the extent such discounted value does not exceed fifty percent of Tier 1 capital; and

- (vi) Perpetual debt instruments issued by a non-deposit taking NBFC which is in excess of what qualifies for Tier 1 capital;

to the extent the aggregate does not exceed Tier 1 capital.

Note – NBFCs-BL are not eligible to include perpetual debt instruments in their Tier 2 capital. For in-depth understanding student may refer the detailed Directions issued by RBI available on https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12959

4. Addition of ROU Assets to Other Assets definition in Weighted risk assets - On-Balance Sheet items table given on page no 14.94

S. No.	Weighted risk assets – On Balance Sheet Items	Percentage weight
(ii)	(e)(i) Loans to 'High-quality infrastructure projects' as defined in the Reserve Bank of India (Non-Banking Financial Companies - Concentration Risk	75

	Management) Directions, 2026 and where the borrower has repaid at least 2 per cent of the sanctioned project debt:	
	(ii) Loans to 'High-quality infrastructure projects' as defined in the Reserve Bank of India (Non-Banking Financial Companies - Concentration Risk Management) Directions, 2026 and where the borrower has repaid at least 5 per cent of the sanctioned project debt: Provided that, for Sl. no.(e)(i) and (e)(ii) above, in the event the projects that qualify as High-quality infrastructure projects subsequently fail to meet these conditions, they shall be subject to risk weights prescribed under Sr. no.3(e) or (g), as applicable, of this table. Provided further that for Sl. no.(e)(i) and (e)(ii) above the repayment threshold should be determined based on the sanctioned project debt. Additional debt, if any, sanctioned as a part of takeover of the loan or otherwise should be clubbed with previous loan(s) sanctioned against the project assets and/or cash flows to determine the repayment threshold. Provided further that, in case of exposures attracting a lower risk weight under the guidelines applicable up to March 31, 2026, but will be subject to higher risk weights in terms of Sl. no. (e)(i) and (e)(ii) above, NBFCs can continue to maintain the extant risk weights till the next review / renewal or March 31, 2027, whichever is earlier.	50
(v)	Other assets: (d) Others (to be specified) including ROU assets	100

5. On page no. 14.99, Standard asset provisioning to be read as

Standard Asset Provisioning – NBFC-ML: NBFC-ML shall make provisions for standard assets at 0.40 percent of the outstanding (including microfinance loans), which shall not be reckoned for arriving at net NPAs.

Standard asset provisioning – NBFC-UL (category-wise): Individual housing loans / loans to SMEs – 0.25%; housing loans at teaser rates – 2.00% (decreasing to 0.40% one year after reset, if still 'standard'); advances to CRE-RH – 0.75%; advances to CRE (other than CRE-RH) – 1.00%; restructured advances – as per the Resolution of Stressed Assets Directions, 2025; all other loans/advances (incl. Medium Enterprises) – 0.40%.

Illustration: An NBFC-UL has the following 'standard' assets outstanding: individual housing loans ₹ 200 crore; CRE (other than CRE-RH) advances ₹ 50 crore; and other loans ₹100 crore. Standard asset provision = $(200 \times 0.25\%) + (50 \times 1.00\%) + (100 \times 0.40\%) = ₹ 0.50 \text{ crore} + ₹ 0.50 \text{ crore} + ₹ 0.40 \text{ crore} = ₹ 1.40 \text{ crore}$.

The above regulatory requirements are to be amended in a phased manner under the Scale- Based Regulation prescribed by RBI for NBFCs.

Students may note that (a) an NBFC may factor in Default Loss Guarantee (DLG) cover while computing Ind AS Expected Credit Loss provisions, subject to conditions; and (b) on implementation of a resolution plan under Chapter VI-A of the Resolution of Stressed Assets Directions, 2025, an additional specific provision of 5% of the outstanding debt is required per instance of restructuring (capped at 100%), written back once the borrower repays at least 20% without slipping back into NPA.

[Students may refer Master Direction – Reserve Bank of India (Non-Banking Financial Companies – Income Recognition, Asset Classification and Provisioning) Directions, 2025 for detailed guidelines on prudential norms relating to Non-Banking Financial Companies covered in these Directions.]

Chapter 19- Professional Ethics & Liabilities of Auditors**1. On page no. 19.68 amendment in Clause (9) of Part I of First Schedule**

Clause (9) accepts an appointment as auditor of a company without first ascertaining from it whether the requirements of Section 225 of the Companies Act, 1956 (1 of 1956), or sections 139 to 141 of the Companies Act, 2013 or any other law pertaining to appointment of auditors for the time being in force, in respect of such appointment have been duly complied with;

2. On page no. 19.109 insertion of Clause (5) in Part II of Second Schedule

Clause (5) acts as an auditor of the company in contravention of the provisions of the Companies Act, 2013.

3. On Page no 19.111, Chapter VI to be read as

In order to ensure the quality of tax audit, the Council of the Institute has decided the limit on the number of tax audits, to be effected by issuance of new guidelines, as follows –

- (i) the existing limit of 60 tax audit assignments per member to be retained, but the same shall be in respect of tax audit assignments in a particular financial year.
- (ii) the said limit of 60 would be the aggregate limit in respect of all tax audits accepted and signed by a member, both in his individual capacity and as a partner of a firm(s). In other words, an individual member cannot sign more than 60 tax audit reports in a financial year.
- (iii) the limit on number of tax audit assignments per partner in a CA Firm cannot be distributed/or shared between the partners.
- (iv) the limit of 60 would, however, not apply to tax audit assignments arising out of the requirements under clause (c), clause (d) and clause (e) of section 44AB, in relation to persons covered under section 44AE, 44ADA and 44AD, respectively.
- (v) in the case of revision of tax audit report, the revised tax audit report shall not be taken into account for the purpose of reckoning the said limit of 60.

Part – II: Questions and Answers**QUESTIONS****PART A: Multiple Choice Questions****Integrated Case Scenarios**

PNBM & Associates, Chartered Accountants, is a firm comprising four partners. Chetan, one of its partners, had accepted and signed 68 tax audit reports under Section 44AB of the Income-tax Act, 1961, excluding tax audits covered under Sections 44AD, 44ADA and 44AE. When this came to light, Chetan justified his action by stating that since the firm had 4 partners, the firm's aggregate ceiling was 240 tax audits, and therefore any partner could sign more than 60 reports if the firm's overall ceiling was not exceeded.

PNBM & Associates also serves as the statutory auditor of Solaris Renewables Ltd., a listed company, for the year ended March 31, 2026. During the course of the audit, the engagement team observed the following matters:

- (i) CA Priya is employed as the Chief Financial Officer of Solaris Renewables Ltd. During assessment proceedings, she appeared before the Income-tax authorities as the company's authorised representative. Subsequently, a fellow employee of the company, Mr. Karan, asked Priya to represent him in his personal income-tax assessment, and she agreed to do so.
- (ii) During the audit, the audit team observed that Solaris Renewables Ltd. had early adopted a new Ind AS, which would otherwise become mandatory from April 1, 2027. Such early adoption was permitted under the applicable regulatory framework. The early adoption had a material effect on the financial statements and was adequately disclosed in the notes to accounts. The audit team performed appropriate procedures and concluded that the accounting treatment adopted was appropriate.
- (iii) As part of the audit of accounts receivable, the firm sent positive confirmation requests to Solaris Renewables Ltd.'s top 60 customers, whose balances represent 70% of total receivables. Positive confirmation requests were also sent to banks to confirm balances held and

outstanding loans. In addition, negative confirmation requests were sent to 180 small suppliers with low-value account balances.

The following events occurred during the confirmation process:

- (1) Out of the 60 positive confirmation requests, 15 responses confirmed agreement with the stated balances, 5 responses reported discrepancies, and 40 customers did not respond at all.
- (2) One of the responses to a positive confirmation appears unreliable due to discrepancies in the customer's letterhead and inconsistent information that did not match the customer's usual correspondence.
- (3) 120 negative confirmation requests receive no responses.
- (4) In the case of non-response, the audit team examined subsequent cash receipts/payments, correspondence, and goods received/dispatch records as alternative evidence.

Based on the above facts, answer the following MCQs:

1. With reference to the provisions of the Chartered Accountants Act, 1949 and the applicable ceiling on tax audit assignments, whether Chetan is guilty of professional misconduct?
 - (a) No, Chetan is not guilty, as the aggregate limit for the firm is 240 tax audits, and any partner may sign beyond 60 reports if the firm's overall limit is not exceeded.
 - (b) Yes, Chetan is guilty of professional misconduct, as the ceiling of 60 tax audit reports is applicable individually to each member, irrespective of the number of partners in the firm.
 - (c) No, Chetan is not guilty, as corporate and non-corporate tax audits are counted separately for determining the ceiling applicable to a member.
 - (d) No, Chetan is not guilty, as the ceiling is determined with reference to the tax audit assignments undertaken by the firm and the number of partners associated with the firm.

2. In relation to Priya's representation before the Income-tax authorities, which of the following is correct?
- (a) Priya is permitted to represent both Solaris Renewables Ltd. and Karan, since both are connected with the same employer and the representation arises in the course of their employment.
 - (b) Priya is permitted to represent Karan in his personal income-tax proceedings, since a Chartered Accountant in employment may undertake such representation for another employee without affecting her employment with the company.
 - (c) Priya is permitted to appear as the tax representative of her employer, Solaris Renewables Ltd., but is not permitted to represent Karan in his personal income-tax proceedings; such representation would amount to professional misconduct.
 - (d) Priya is not permitted to appear before the Income-tax authorities even on behalf of Solaris Renewables Ltd., since a Chartered Accountant in service is prohibited from acting as a tax representative.
3. Considering the circumstances relating to the early adoption of Ind AS, how should the matter be dealt with in the auditor's report?
- (a) The matter should be included under Other Information, as the early adoption relates to information that is relevant to users of the financial statements but does not form part of the financial statements.
 - (b) The matter should be reported as a Key Audit Matter, as the early adoption had a material effect on the financial statements and required significant attention from the audit team.
 - (c) The matter should be reported in Other Matter paragraph, since early adoption of an accounting standard represents information that is fundamental to users' understanding of the financial statements.
 - (d) The matter may be highlighted through an Emphasis of Matter paragraph, since the early adoption has a material effect, is

appropriately accounted for and is adequately disclosed in the financial statements.

4. Assume, contrary to the facts given, that the early adoption of the new Ind AS was not adequately disclosed in the notes to accounts, even though the auditors still regarded the accounting treatment itself as appropriate. How would this change the reporting requirement?
 - (a) The auditor would issue a qualified or adverse opinion for material misstatement, since an Emphasis of Matter paragraph can only be used for a matter that is already adequately disclosed, inadequate disclosure is itself a misstatement, not a basis for such a paragraph.
 - (b) The auditor would still issue an Emphasis of Matter paragraph, since its purpose is precisely to draw attention to matters that have not been adequately disclosed by management.
 - (c) The auditor would issue an Emphasis of Matter paragraph and separately note within it that the related disclosure was inadequate, without any change to the opinion.
 - (d) The auditor would instead report the matter as a Key Audit Matter, since inadequate disclosure automatically elevates any matter into one of most significance in the audit.
5. Which of the following is the most appropriate for PNBM & Associates in response to the events that occurred when performing external confirmation procedures to obtain relevant and reliable audit evidence in accordance with relevant Standard on Auditing?
 - (a) The failure to receive a response to a negative confirmation request explicitly indicate receipt by the intended confirming party of the confirmation request or verification of the accuracy of the information contained in the request.
 - (b) Confirming parties also may be more likely to respond indicating their disagreement with a confirmation request when the information in the request is in their favour, and less likely to respond otherwise.

- (c) Non-response for negative confirmation does not mean that there is some misstatement as negative confirmation request itself is to respond to the auditor only if the confirming party disagrees with the information provided in the request.
- (d) The auditor shall use negative confirmation requests as the sole substantive audit procedure when he is not aware of circumstances or conditions that would cause recipients of negative confirmation requests to disregard such requests.

Independent MCQs

6. A large infrastructure company, Vikas Constructions Ltd., is developing an industrial corridor project in a semi-rural area. The project involves land acquisition, construction activities, and possible relocation of a small local settlement. The company aims to align its actions with Principle 8 – Promote Inclusive Growth and Equitable Development.

During the ESG compliance and CSR strategy meeting, the sustainability director proposes several actions to align the project with Principle 8. However, the internal audit team observes that one of the proposed actions is not consistent with the core elements of this principle.

Which of the following actions is not aligned with Principle 8?

- (a) The entity should have systems in place to identify and address impacts of its activities on the social, cultural, and economic aspects of the people, including issues like land acquisition and construction activities for new facilities.
- (b) The entity should review, measure, and track the adverse impacts of its activities on society and environment and make action plans to mitigate them adequately.
- (c) The entity should ensure that business decisions primarily focus on maximising economic efficiency even if it results in business induced displacement or relocation of communities, without requiring participative or informed negotiations.
- (d) The entity should make efforts to bring up creative products, technologies, and business concerns that help marginalized communities to have well-being and a better quality of life.

7. A bank proposes to shift certain Government securities from the "Available for Sale" (AFS) category to the "Held to Maturity" (HTM) category. The securities satisfy the conditions for classification as HTM, and the ALCO has approved the proposed shift. However, no approval of the Board of Directors has been obtained. The management contends that the absence of Board approval should not affect the classification since the securities otherwise qualify for HTM. Which of the following is the most appropriate treatment?
- (a) The securities may be classified as HTM, since compliance with the eligibility conditions for HTM is the primary requirement and the approval of ALCO provides adequate internal authorisation for the transfer.
 - (b) The securities cannot be transferred to HTM merely on the basis of ALCO approval, since the prescribed approval requirements for such transfer must be complied with in addition to the eligibility conditions for HTM classification.
 - (c) The securities may be classified as HTM if the bank discloses the absence of Board approval and demonstrates that its intention to hold the securities until maturity existed at the time of their original acquisition.
 - (d) The securities should continue to be classified as AFS only for the year of transfer and may thereafter be classified as HTM once the Board subsequently approves the transfer.
8. During the statutory audit of Kavya Industries Ltd. for the year ended March 31, 2026, the auditor completed the audit of the financial statements and was in the process of finalising the auditor's report. The company's annual report also contained a Directors' Report, which was not part of the audited financial statements.

Before the date of the auditor's report, while reading the Directors' Report, the auditor noted that it stated that the company's revenue had increased by 22% during the year, whereas the audited financial statements showed that revenue had increased by only 9% over the previous year. The auditor confirmed that the figures and disclosures in

the audited financial statements were correct and that the difference arose solely from an incorrect statement in the Directors' Report.

In the above circumstances, which of the following is the most appropriate course of action for the auditor?

- (a) Modify the audit opinion on the financial statements, since the inconsistency between the Directors' Report and the audited financial statements represents a material misstatement affecting the annual report.
- (b) Request management to correct the Directors' Report and, if management refuses and the auditor concludes that the other information is materially misstated, communicate the matter to those charged with governance and consider the implications for the auditor's report in accordance with SA 720.
- (c) Take no further action, since the Directors' Report is outside the financial statements and the auditor's responsibility under SA 720 does not extend to information contained in the annual report other than the financial statements.
- (d) Withdraw from the audit engagement, since management's refusal to correct a material misstatement in the Directors' Report constitutes a scope limitation that prevents the auditor from expressing an opinion on the financial statements.

PART B: DESCRIPTIVE QUESTIONS

Standards on Auditing, Statements and Guidance Notes

Audit Planning, Strategy & Execution

9. During the statutory audit of KPK Manufacturing Ltd., the engagement partner noted that the company has a well-established and effective internal audit function. The internal auditors have recently completed the following assignments:
- Testing of the operating effectiveness of internal controls over the purchase and payment cycle.
 - Observed the year end physical inventory count at various warehouses.

- Determined the materiality for the audit of the financial statements.
- Verified compliance with applicable environmental and labour regulations.
- Evaluated the appropriateness of management's assumptions used in estimating the provision for pending litigation.
- Reviewed the financial information of a small overseas subsidiary that is not a significant component of the group.
- Decided the nature, timing and extent of substantive audit procedures to be performed for revenue recognition and drafted the proposed audit opinion on the financial statements.

The engagement partner proposes to use the work of the internal audit function extensively with a view to reduce the extent of external audit procedure. As the statutory auditor, analyse each of the above areas and identify which assignments can be used and which cannot be used by the external auditor as per relevant Standard on Auditing.

Completion and Review

10. While conducting the audit of LML Ltd., the auditor, CA Hema, observed a continuous decline in revenues, significant operating losses, and delays in repayment of bank dues during the year. The company is also facing difficulty in obtaining further financing, and a major portion of its customers have shifted to competitors. Management has prepared cash flow forecasts and is confident of turning around the business through cost-cutting measures and proposed funding arrangements.

However, the auditor has concerns regarding the reliability of the assumptions used in the forecasts and the feasibility of management's plans. The financial statements include a note disclosing these circumstances.

The auditor is in the process of concluding the audit and forming an opinion on the financial statements.

Analyse the matters that the auditor should consider in the above situation and discuss the implications for the auditor's report, with reference to relevant auditing standards.

Reporting

11. CA Ravi is the Statutory Auditor of Rajhans Textiles Ltd., a listed company, for the financial year 2025-26. During the audit, the following matters came to the auditor's attention:
- (i) The company has granted a loan of ₹5 crore to its subsidiary. No repayment schedule has been stipulated and no repayment has been received during the year.
 - (ii) The company had availed a term loan of ₹ 50 crore from a consortium of banks. During the year, the company defaulted in repayment of instalments aggregating to ₹ 6 crore for a period of 95 days. However, the default was subsequently cleared before the balance sheet date.
 - (iii) The company has an outstanding Income-tax demand of ₹ 2 crore, which is disputed before the appellate authority. The amount has been appropriately disclosed in the financial statements.

Examine each of the above situations and state how CA Ravi should report the same under CARO 2020.

Specialised Areas

12. JKL Ltd. has published a set of condensed financial information for its shareholders, summarizing its audited financial statements for the year. The summary financial statements have been circulated independently and are not accompanied by the complete audited financial statements. The management has stated that the full financial statements are available upon request at the company's registered office.

The auditor has been engaged to report on these summary financial statements. While reviewing the same, the auditor noted that the level of aggregation appears quite high, certain disclosures regarding the basis of preparation are unclear, and there is limited reference to the audited financial statements.

In the given circumstances, discuss the procedures that the auditor should consider while forming an opinion on such financial information.

Review of Financial Information

13. Luck & Associates, a firm of Chartered Accountants, was approached by Best Ltd. to undertake a review of its financial statements. During initial discussions, the engagement partner observed certain issues such as possible limitations on the scope of work, concerns regarding availability and reliability of information, and doubts about management's integrity. Further, the engagement was proposed to meet certain regulatory expectations, though it was unclear whether a review would be appropriate in the given circumstances. The firm also needs to evaluate its ability to comply with ethical requirements, including independence.

Discuss the considerations that the practitioner should evaluate in the above situation before accepting/proceeding with the engagement.

Prospective Financial Information and Other Assurance Services

14. Mr. B, a Chartered Accountant in practice, has been approached by ABC Ltd. to examine and report on its prospective financial information prepared for the purpose of raising finance from investors. The management intends to circulate the information widely.

During initial discussion, CA B notices that certain assumptions used in the preparation of such information appear to be unrealistic. He is also uncertain about the reliability of historical financial data and the exact purpose and scope of circulation of such information.

CA B is considering whether to accept the engagement and, if so, what are the factors he should evaluate before doing so?

Digital Auditing and Assurance

15. CA Jiya was conducting a remote audit of Nova Ltd. using an online document-sharing platform. To expedite the audit process, the company granted unrestricted access to all employees and auditors on the platform. During the audit, CA Jiya downloaded several documents and retained them on the shared platform even after completing her review.

While discussing audit observations through a video conference, she took screenshots of employees appearing on the screen as evidence of discussions without obtaining prior consent. She also captured screenshots of certain confidential company records without seeking

authorization from the auditee. Further, while accessing the company's ERP system from her home office, she logged in through a public internet connection without using a Virtual Private Network (VPN).

The management of Nova Ltd. later raised concerns regarding confidentiality, security, and data protection practices followed during the audit.

Discuss the security, confidentiality, and data protection concerns arising from the above situation. What safeguards and controls should an auditor implement while conducting a remote or digital audit to ensure protection of client information and compliance with applicable regulations?

Group Audits

16. CA Ananya has been appointed as the statutory auditor of PQR Ltd. (the parent company) as well as of every subsidiary, wholly owned and partly owned, within the PQR group. While finalising the audit of the Consolidated Financial Statements (CFS) for the year ended March 31, 2026, she notices that although the CFS are broadly compliant with the applicable consolidation Accounting Standards, one subsidiary's figures have not been adjusted in the manner required by the standard. This omission constitutes a material departure from the prescribed consolidation principles.

CA Ananya brought the matter to the attention of management and requested the necessary adjustments. However, management refused to revise the CFS (i.e., Consolidated Balance Sheet, Consolidated Statement of Profit and Loss and Consolidated Cash Flow Statement) stating that the impact was limited to a single subsidiary and did not affect the overall presentation significantly.

Discuss the responsibilities of CA Ananya as auditor of the CFS in the given situation, and the course of action she must adopt while framing her audit opinion.

Special Features of Audit of Banks & Non-Banking Financial Companies

17. XYZ Investments Pvt. Ltd. is a company incorporated under the Companies Act, 2013, engaged solely in acquiring and holding shares and debentures of group companies as an investment activity. It does

not accept public deposits, does not avail public funds, has no customer interface and does not intend to avail public funds or have customer interface as part of its business model. Its total asset size as per the latest audited balance sheet is ₹ 850 crore. The company had earlier obtained a Certificate of Registration (CoR) from the RBI as a NBFC-BL under the SBR Directions, 2023, since its financial assets and financial income satisfied the 50-50 Test.

The statutory auditor of XYZ Investments Pvt. Ltd., while planning the audit for FY 2026-27, is examining the applicability of the Non-Banking Financial Companies – Registration, Exemptions and Framework for Scale Based Regulation Amendment Directions, 2026 to the company.

Examine, with reasons, whether XYZ Investments Pvt. Ltd. is required to continue holding a Certificate of Registration under the RBI Act, 1934, in light of the Non-Banking Financial Companies – Registration, Exemptions and Framework for Scale Based Regulation Amendment Directions, 2026. What compliance requirements and exit option, if any, are available to XYZ Investments Pvt. Ltd.?

Overview of Audit of Public Sector Undertakings

18. The Comptroller and Auditor General has initiated a performance audit of a large government programme aimed at rural infrastructure development. The audit team has been assigned the task of planning the audit. During initial discussions, it was observed that the programme is implemented across multiple ministries and has been operational for several years. The scheme has also attracted attention in parliamentary discussions and media reports due to concerns about its efficiency and outcomes.

The audit team is considering various sources such as internal records of the implementing agencies, legislative discussions, reports of committees, prior audit findings, independent research studies, and inputs from stakeholders to develop a comprehensive understanding of the programme before finalising the audit plan.

Identify the stage of the performance audit process represented in the above scenario. Further discuss how the various sources of information

referred to above assist the audit team in developing an in-depth understanding of the entity/programme for effective audit planning.

Sustainable Development Goals (SDG) & Environment, Social and Governance (ESG) Assurance

19. Green Limited, engaged in electric vehicle manufacturing has recently expanded its operations in multiple states. During the audit, the auditor noted the following:

- The company faces litigation for alleged environmental violations.
- Management has highlighted sustainability achievements through press releases and investor presentations.
- Certain climate-related risks have been disclosed in the Board's Report, but similar disclosures are absent from the financial statements.

Discuss the auditor's responsibilities in evaluating the above matters while completing the audit of the financial statements.

Professional Ethics & Liabilities of Auditors

20. Comment with reference to the provisions of the Chartered Accountants Act, 1949 and Schedules thereto in the following situation:

- (a) CA Anshul is appointed as the statutory auditor of Rise Ltd. During the audit, he obtained details of significant litigation, regulatory investigations, and tax disputes of the company. The Managing Director of the company requested him to share certain audit working papers and internal findings with the company for the purpose of internal restructuring.
- (b) Mr. Raman is a Chartered Accountant in practice holding a Certificate of Practice. He is also enrolled as an advocate after obtaining the requisite permission from the Bar Council. While appearing before the High Court in a tax litigation matter, he files the vakalatnama and appears using the designation "CA Raman, Chartered Accountant & Advocate." He also uses both designations on his visiting card and letterhead for his advocacy practice.

**SUGGESTED ANSWERS****PART A: Answers to Multiple Choice Questions**

Question No.	Answer
1.	(b)
2.	(c)
3.	(d)
4.	(a)
5.	(c)
6.	(c)
7.	(b)
8.	(b)

PART B: Answers to Descriptive Questions

9. As per SA 610, "Using the Work of Internal Auditors", work of the internal audit function that can be used by the external auditor include the following:
- Testing of the operating effectiveness of controls.
 - Substantive procedures involving limited judgment.
 - Observations of inventory counts.
 - Tracing transactions through the information system relevant to financial reporting.
 - Testing of compliance with regulatory requirements.
 - In some circumstances, audits or reviews of the financial information of subsidiaries that are not significant components to the group (where this does not conflict with the requirements of SA 600).

Work performed by Internal Audit Function	Can the External Auditor Use the Work?
Tested the operating effectiveness of internal controls over the purchase and payment cycle.	Yes
Observed the year end physical inventory count at various warehouses.	Yes
Determined the materiality for the audit of the financial statements.	No
Verified compliance with applicable environmental and labour regulations.	Yes
Evaluated the appropriateness of management's assumptions used in estimating the provision for pending litigation	No
Reviewed the financial information of a small overseas subsidiary that is not a significant component of the group.	Yes
Decided the nature, timing and extent of substantive audit procedures to be performed for revenue recognition and drafted the proposed audit opinion on the financial statements.	No

Accordingly, the engagement partner's proposal to rely extensively on all the work of the internal audit function is not appropriate. The external auditor must independently perform and conclude on areas involving significant professional judgment and remain solely responsible for expressing the audit opinion.

- 10.** As per SA 570, "Going Concern", if events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern, the auditor shall obtain sufficient appropriate audit evidence to determine whether or not a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern

through performing additional audit procedures, including consideration of mitigating factors. These procedures shall include:

- (a) Where management has not yet performed an assessment of the entity's ability to continue as a going concern, requesting management to make its assessment.
- (b) Evaluating management's plans for future actions in relation to its going concern assessment, whether the outcome of these plans is likely to improve the situation and whether management's plans are feasible in the circumstances.
- (c) Where the entity has prepared a cash flow forecast, and analysis of the forecast is a significant factor in considering the future outcome of events or conditions in the evaluation of management's plans for future actions:
 - (i) Evaluating the reliability of the underlying data generated to prepare the forecast; and
 - (ii) Determining whether there is adequate support for the assumptions underlying the forecast.
- (d) Considering whether any additional facts or information have become available since the date on which management made its assessment.
- (e) Requesting written representations from management and, where appropriate, those charged with governance, regarding their plans for future actions and the feasibility of these plans.

In the given case, CA Hema has observed such points that may cast significant doubt on the entity's ability to continue as a going concern. Therefore, CA Hema should follow audit procedures such as:

- Review of management's assessment of the company's ability to continue as a going concern.
- Examine and challenge the reasonableness of the company's cash flow forecasts and key assumptions.

- Review events after the reporting period that might affect the going concern assumption, such as further financial deterioration or inability to secure financing.
- Analysis of the company's key financial ratios and compliance with loan agreements to assess liquidity and solvency.
- Review of the company's challenges and efforts to secure additional financing and the reasons for the bank's reluctance to provide further credit.
- Assess the impact of declining customer base, delayed payments, and other operational challenges on the company's ability to continue as a going concern.

Further, as per SA 570 if adequate disclosure about the material uncertainty is made in the financial statements, the auditor shall express an unmodified opinion and the auditor's report shall include a separate section under the heading "Material Uncertainty Related to Going Concern" to:

- (a) Draw attention to the note in the financial statements that discloses the matters set out in above; and
- (b) State that these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the auditor's opinion is not modified in respect of the matter.

- 11. (i) Loan granted to Subsidiary:** As per Clause (iii)(a)(A) of Paragraph 3 of CARO 2020, the auditor is required to report, inter alia, whether during the year the company has provided loans or provided advances in the nature of loans, or stood guarantee, or provided security to any other entity [not applicable to companies whose principal business is to give loans], if so, indicate the aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to subsidiaries, joint ventures and associates;

Further, as per Clause (iii)(c) of Paragraph 3 of CARO 2020, the auditor is required to report in respect of loans and advances in

the nature of loans, whether the schedule of repayment of principal and payment of interest has been stipulated and whether the repayments or receipts are regular;

Furthermore, as per Clause (iii)(f) of Paragraph 3 of CARO 2020, the auditor is required to report, whether the company has granted any loans or advances in the nature of loans either repayable on demand or without specifying any terms or period of repayment, if so, specify the aggregate amount, percentage thereof to the total loans granted, aggregate amount of loans granted to Promoters, related parties as defined in clause (76) of section 2 of the Companies Act, 2013.

In the given case, the company has granted a loan of ₹ 5 crore to its subsidiary, for which no repayment schedule has been stipulated and no repayment has been received during the year. Accordingly, CA Ravi should make appropriate reporting under Clause (iii)(a)(A), Clause (iii)(c), Clause (iii)(f) of Paragraph 3 of CARO 2020.

- (ii) **Default in repayment of Loans/Borrowings:** As per Clause (ix)(a) of Paragraph 3 of CARO 2020, where the company has defaulted in repayment of loans or other borrowings, the auditor is required to report the amount of default and the period of default, along with lender-wise details.

In the given case, the company had availed a term loan of ₹ 50 crore from a consortium of banks and defaulted in repayment of instalments aggregating to ₹6 crore for a period of 95 days. Although the default was subsequently cleared before the balance sheet date, the default had occurred during the year. Accordingly, CA Ravi should report the amount of default of ₹ 6 crore and the period of default of 95 days, lender-wise, under Clause (ix)(a) of Paragraph 3 of CARO 2020.

- (iii) **Disputed Income-tax Demand:** As per Clause (vii)(b) of Paragraph 3 of CARO 2020, the auditor is required to report the amounts of statutory dues not deposited on account of disputes, along with the nature of the dues and the forum where the dispute is pending.

In the given case, the company has an outstanding Income-tax demand of ₹ 2 crore, which is disputed before the appellate authority and has been appropriately disclosed in the financial statements. Accordingly, CA Ravi should report the amount of ₹ 2 crore, nature of the dues and the forum where the dispute is pending under Clause (vii)(b) of Paragraph 3 of CARO 2020.

- 12.** As per SA 810, "Engagements to Report on Summary Financial Statements", the auditor shall perform the following procedures, and any other procedures that the auditor may consider necessary, as the basis for the auditor's opinion on the summary financial statements:
- (a) Evaluate whether the summary financial statements adequately disclose their summarised nature and identify the audited financial statements.
 - (b) When summary financial statements are not accompanied by the audited financial statements, evaluate whether they describe clearly:
 - (i) From whom or where the audited financial statements are available; or
 - (ii) The law or regulation that specifies that the audited financial statements need not be made available to the intended users of the summary financial statements and establishes the criteria for the preparation of the summary financial statements.
 - (c) Evaluate whether the summary financial statements adequately disclose the applied criteria.
 - (d) Compare the summary financial statements with the related information in the audited financial statements to determine whether the summary financial statements agree with or can be re-calculated from the related information in the audited financial statements.
 - (e) Evaluate whether the summary financial statements are prepared in accordance with the applied criteria.
 - (f) Evaluate, in view of the purpose of the summary financial statements, whether the summary financial statements contain the

information necessary, and are at an appropriate level of aggregation, so as not to be misleading in the circumstances.

- (g) Evaluate whether the audited financial statements are available to the intended users of the summary financial statements without undue difficulty, unless law or regulation provides that they need not be made available and establishes the criteria for the preparation of the summary financial statements as discussed already.

13. As per SRE 2400, "Engagements to Review Historical Financial Statements", factors affecting Acceptance and Continuance of Client Relationships and Review Engagements: Unless required by law or regulation, the practitioner shall not accept a review engagement if:

- (a) The practitioner is not satisfied:

- (i) That there is a rational purpose for the engagement. Assurance engagements may only be accepted when the engagement exhibits certain characteristics that are conducive to achieving the practitioner's objectives specified for the engagement.

It may be unlikely that there is a rational purpose for the engagement if, for example, there is a significant limitation on the scope of work or the practitioner suspects association of the practitioner's name with the financial statements in an inappropriate manner. Similarly, when the engagement is intended to meet compliance requirements of relevant law or regulation and such law or regulation requires the financial statements to be audited, there is no rational purpose for such a review engagement.

- (ii) That a review engagement would be appropriate in the circumstances. When the practitioner's preliminary understanding of the engagement circumstances indicates that accepting a review engagement would not be appropriate, the practitioner may consider recommending that another type of engagement be undertaken. Depending on the circumstances, the practitioner may, for example,

believe that performance of an audit engagement would be more appropriate than a review. In other cases, if the engagement circumstances preclude the performance of an assurance engagement, the practitioner may recommend a compilation engagement, or other accounting services engagement, as appropriate.

- (b) The practitioner has reason to believe that relevant ethical requirements, including independence, will not be satisfied.
 - (c) The practitioner's preliminary understanding of the engagement circumstances indicates that information needed to perform the review engagement is likely to be unavailable or unreliable.
 - (d) The practitioner has cause to doubt management's integrity such that it is likely to affect proper performance of the review or
 - (e) Management or those charged with governance impose a limitation on the scope of the practitioner's work in the terms of a proposed review engagement such that the practitioner believes that the limitation will result in the practitioner disclaiming a conclusion on the financial statements.
- 14.** As per SAE 3400, "The Examination of Prospective Financial Information", before accepting an engagement to examine prospective financial information, CA B, the auditor would consider, amongst other things:
- The intended use of the information;
 - Whether the information will be for general or limited distribution;
 - The nature of the assumptions, that is, whether they are best estimates or hypothetical Assumptions;
 - The elements to be included in the information; and
 - The period covered by the information.

Further, the auditor should not accept, or should withdraw from, an engagement when the assumptions are clearly unrealistic or when the auditor believes that the prospective financial information will be inappropriate for its intended use. The auditor should consider the extent to which reliance on the entity's historical financial information is justified.

Like in other engagements, it is necessary that terms of engagements should be agreed with client by sending an engagement letter.

- 15. Confidentiality, Security and Data Protection:** To ensure data security and confidentiality, access to document sharing platform should be sufficiently restricted and secured by encrypting the data that is sent across the network. The information, once reviewed and documented by auditor, is removed from the platform, and stored according to applicable archiving standards and data protection requirements.

Auditors should take into consideration legislation and regulations, which may require additional agreements from both sides (e.g., there will be no recording of sound and images, or authorizations to using people's images). Auditors should not take screenshots of auditees as audit evidence. Any screenshots of documents or records or other kind of evidence should be previously authorized by the audited organization. In case of accessing the auditee's IT system auditor should use VPN (Virtual private network). VPN is a service which creates safe and encrypted online connections. It prevents unauthorized users to enter into network and allows the users to perform work remotely.

In the given case, CA Jiya failed to adhere to several important requirements relating to confidentiality, security, and data protection during a digital audit.

Therefore, the auditor's actions of using an unsecured platform, retaining reviewed information on the platform, taking unauthorized screenshots, and accessing the auditee's systems without a VPN are inconsistent with the principles of confidentiality, security, and data protection applicable to digital audits.

- 16. When the Parent's Auditor is also the Auditor of all its Components:**

In the given case, CA Ananya is the statutory auditor of both the parent company, PQR Ltd., and all its subsidiaries. Accordingly, she needs to consider the following:

- While drafting the audit report, the auditor should report whether principles and procedures for preparation and presentation of consolidated financial statements as laid down in the relevant accounting standards have been followed.

In case of any departure or deviation, the auditor should consider the requirements given in SA 705, "Modifications to the Opinion in the Independent Auditor's Report" in the audit report so that users of the consolidated financial statements are aware of such deviation.

- Auditor should issue an audit report expressing an opinion whether the consolidated financial statements give a true and fair view of the state of affairs of the Group as on balance sheet date and as to whether consolidated profit and loss statement gives true and fair view of the results of consolidated profit or losses of the Group for the period under audit.
- Where the consolidated financial statements also include a cash flow statement, the auditor should also give his opinion on the true and fair view of the cash flows presented by the consolidated cash flow statements.

In view of above, being an auditor of PQR the parent company and all its subsidiaries, CA Ananya is required to consider whether the principles and procedures prescribed for the preparation and presentation of the CFS under the applicable Accounting Standards have been followed. In the given case, the required consolidation adjustments relating to one subsidiary have not been incorporated, resulting in a material departure from the applicable accounting principles. Since management has refused to make the necessary adjustments, CA Ananya should consider the effect of the resulting misstatement on the CFS and apply the requirements of SA 705, Modifications to the Opinion in the Independent Auditor's Report, as appropriate.

The fact that the departure relates to only one subsidiary does not, by itself, relieve the auditor of the responsibility to report its effect on the CFS. The auditor should evaluate the materiality and pervasiveness of the resulting misstatement to determine the appropriate modification of opinion.

Accordingly, CA Ananya should:

- evaluate the effect of the unadjusted consolidation adjustment on the CFS;

- consider the requirements of SA 705 and determine the appropriate modified opinion, wherever required;
- clearly state the nature of the departure and its effect in the audit report, as applicable; and
- express an opinion on whether the CFS give a true and fair view of the state of affairs of the Group as at the balance sheet date and of its consolidated profit or loss for the period.

Further, she should also express an opinion on whether the consolidated cash flows give a true and fair view in accordance with the applicable framework considering the fact that the CFS also include a Consolidated Cash Flow Statement.

Thus, CA Ananya cannot ignore the material departure merely because it relates to a single subsidiary. She must assess its materiality and pervasiveness and modify her opinion in accordance with SA 705, if the uncorrected misstatement warrants such modification.

- 17. Registration status of XYZ Investments Pvt. Ltd.:** Section 45-IA of the Reserve Bank of India Act, 1934 provides, inter alia, that an NBFC is required to obtain a Certificate of Registration (CoR) from the RBI for carrying on the business of a non-banking financial institution, subject to the exemptions provided under the applicable regulatory framework.

The Reserve Bank of India (Non-Banking Financial Companies – Registration, Exemptions and Framework for Scale Based Regulation) Amendment Directions, 2026 introduced the framework for an “Unregistered Type 1 NBFC”.

An NBFC which, subject to fulfilment of the prescribed conditions:

- does not avail public funds;
- does not have any customer interface;
- has an asset size of less than ₹1,000 crore; and
- operates on this basis as a conscious and long-term business model,

is eligible for exemption from the requirement of registration under Sections 45-IA and 45-IC of the RBI Act, 1934.

The prescribed conditions also include, inter alia, passing an annual Board resolution confirming that the NBFC will not avail public funds and will not have customer interface during the financial year and making the prescribed disclosure in the Notes to Accounts.

In the present case, XYZ Investments Pvt. Ltd.:

- does not avail public funds;
- has no customer interface;
- does not intend to avail public funds or have customer interface as part of its business model; and
- has an asset size of ₹850 crore, which is below ₹1,000 crore.

Accordingly, subject to fulfilment of the prescribed conditions, XYZ is eligible to fall within the category of Unregistered Type 1 NBFC and avail the exemption from registration.

However, XYZ Investments Pvt. Ltd. already holds a CoR. Its CoR does not automatically cease to be effective merely because it satisfies the conditions for exemption.

The Amendment Directions provide an exit mechanism for existing NBFCs which become eligible for the exemption. Accordingly, XYZ Investments Pvt. Ltd. may apply to the RBI for deregistration/surrender of its CoR within the prescribed timeline, i.e., by December 31, 2026, subject to the applicable conditions and RBI's approval.

Therefore, XYZ Investments Pvt. Ltd. should:

- ensure that it satisfies the conditions prescribed for an Unregistered Type 1 NBFC;
- pass the prescribed annual Board resolution;
- make the prescribed disclosure in the Notes to Accounts; and
- if it wishes to exit the regulatory registration framework, apply to the RBI for deregistration/surrender of its CoR within the prescribed timeline.

Thus, XYZ Investments Pvt. Ltd. is eligible to avail the exemption applicable to an Unregistered Type 1 NBFC, subject to fulfilment of the prescribed conditions. However, its existing CoR does not automatically lapse. It may avail the prescribed deregistration mechanism to surrender the CoR.

- 18.** The activities described in the case represent the initial stage of planning a performance audit, commonly referred to as understanding the entity/programme. It is the starting point for planning individual performance audit.

The auditor may use the following sources for understanding the entity:

- (i) Documents of the entity: Documents on administration and functions of the entity, policy files, annual reports, budget documents, accounts, minutes of meetings, information on the website, internal audit reports, electronic databases and MIS reports, RTI material etc.
- (ii) Legislative documents: Legislation, parliamentary questions and debates, reports of the Public Accounts Committee, the Committee on Public Undertakings, the Estimates Committee and letters from Members of Parliament.
- (iii) Policy documents: Documents of Planning Commission, Ministry of Finance etc.
- (iv) Academic or special research: Independent evaluations on the entity, academic research and similar work done by other governments and other SAs.
- (v) Past audits: Past financial and performance audits of the entity provide a major source of information and understanding.
- (vi) Media coverage: Print and electronic media - their systematic documentation on regular basis in a transparent manner.
- (vii) Special focus groups: Audit Advisory Committee concerns, annual and special reports of World Bank, Reserve Bank of India, reports by special interest groups, NGOs, etc.

- 19.** The role of the auditor is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, to enable auditor to report whether the financial statements are prepared and presented fairly, in all material respects, in accordance with the applicable financial reporting framework.

In developing the understanding of an entity, the auditor should include the consideration of climate-related risks and how these risks may be relevant to the audits. The climate-related risks could be more relevant in certain sectors or industries, e.g., banks and insurance, energy, transportation, materials and buildings, agriculture, food, and forestry products.

Many investors and stakeholders are seeking information from auditor's reports about how climate-related risks were addressed in the audit. With this increased user focus on climate change, auditor need to be aware of, and may face, increasing pressure for transparency about climate matters in our auditor's reports. However, the auditor's reports must follow the requirements of applicable auditing standards.

The auditor's report is a key mechanism of communication to users about the audit that was performed. In addition to the audit opinion, it provides information about auditor's responsibilities and, when required, an understanding of the matters of most significance in our audit and how they were addressed.

In some circumstances, it may warrant inclusion of an Emphasis of matter paragraph to draw attention to disclosures that are of fundamental importance to users' understanding of the financial statements. The auditor should also determine whether the entity has appropriately disclosed relevant climate-related information in the financial statements in accordance with the applicable financial reporting framework e.g., Indian Accounting Standards or Accounting Standards, when relevant before considering climate-related matters in the auditor's report.

The auditor should also read the other information for consistency with information disclosed in the financial statements and information that may be publicly communicated to stakeholders outside the financial

statements, such as management report narratives in the annual report, press releases, or investor updates. This is a requirement under ISA 720 and SA 720, The Auditor's Responsibilities Relating to Other Information.

- 20. (a)** As per Clause (1) of Part I of the Second Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he discloses information acquired in the course of his professional engagement to any person other than his client so engaging him without the consent of his client or otherwise than as required by any law for the time being in force.

An accountant in public practice has access to a great deal of information of his client, which is of a highly confidential character. It is important that he should treat such information as having been provided to him only to facilitate the performance of his professional duties. To divulge such information would be a breach of professional confidence. The accountant's duty not to disclose continues even after completion of his assignment.

If disclosure is required as a part of performance of professional duty, the fact that such performance is required by the client would itself amount to the client consenting to such disclosure. In all cases, the request or initiative must come from the client. In case of a company, consent is required to be obtained from a competent authority such as the Managing Director if duly authorised, otherwise by a resolution of the Board of Directors.

An auditor is not required to provide the client or other auditors of the same enterprise or its related enterprise such as a parent or subsidiary, access to his audit working papers. The main auditor does not have a right of access to the audit working papers of branch auditors. However, the auditor may, at his discretion, make portions of or extracts from his working papers available to the client. There is a difference between sharing of working papers and sharing of information, and information may be provided only after obtaining consent of the client.

In the given case, during the audit CA Anshul acquired certain confidential information and is requested by the Managing Director of Rise Ltd. to share audit working papers and internal findings.

In view of above, CA Anshul must not share the audit working papers or any confidential information relating to the litigation, investigations or tax disputes with the Managing Director, or discuss it with anyone other than the client, without the client's proper consent obtained through a competent authority.

- (b) As per Clause (7) of Part I of First Schedule to the Chartered Accountants Act, 1949, a CA in practice is deemed to be guilty of professional misconduct if he (i) advertises his professional attainments or services or (ii) uses any designation or expressions other than 'Chartered Accountant' on professional documents, visiting cards, letter heads or sign boards unless it be a degree of a university established by law in India or recognized by the Central Government or a title indicating membership of the ICAI or of any other institution that has been recognized by the Central Government or may be recognized by the council.

Further, members of the Institute in practice who are otherwise eligible may practise as advocates subject to the permission of the Bar Council but in such case, they should not use designation 'Chartered Accountant' in respect of the matters involving the practice as an advocate. In respect of other matters, they should use the designation 'Chartered Accountant' but they should not use the designation 'Chartered Accountant' and 'Advocate' simultaneously.

In the present case, CA Raman, by appearing before the High Court and filing the vakalatnama as "CA Raman, Chartered Accountant & Advocate," and by printing both designations together on his visiting card and letterhead, has used a designation other than "Chartered Accountant" in a matter of his advocacy practice, and has combined both titles impermissibly. He is therefore guilty of professional misconduct under Clause (7) of Part I of the First Schedule to the Chartered Accountants Act, 1949.

**Applicability of Standards / Guidance Notes / Legislative Amendments
etc. for November, 2026 Examination**

Final Course

Paper 1: Financial Reporting

(I) List of topic-wise exclusions from the syllabus

(1)	(2)	(3)
S. No. in the syllabus	Topics of the syllabus	Exclusions
3.	Application of Indian Accounting Standards (Ind AS) with reference to General Purpose Financial Statements	Indian Accounting Standard (Ind AS) 16 'Property, Plant and Equipment' Appendix B- Stripping Costs in the Production Phase of a Surface Mine
	(iv) Ind AS on Assets and Liabilities of the Financial Statements	Indian Accounting Standard (Ind AS) 37 'Provisions, Contingent Liabilities and Contingent Assets' - Appendix A: Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds - Appendix B: Liabilities arising from Participating in a Specific Market — Waste Electrical and Electronic Equipment
	(vii) Other Ind AS	- Indian Accounting Standard (Ind AS) 29: Financial Reporting in Hyperinflationary Economies - Indian Accounting Standard (Ind AS) 106: Exploration for

		and Evaluation of Mineral Resources • Indian Accounting Standard (Ind AS) 114: Regulatory Deferral Accounts • Indian Accounting Standard (Ind AS) 117: Insurance Contracts
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(II) Important Points for Consideration

- (1) November, 2024 edition and Reprint August, 2025 and onwards of the Study Material is relevant for November, 2026 examination.
- (2) The relevant Amendments / Notifications / Circulars / Rules issued by the Companies Act, 2013 and Limited Revisions in existing standards, issued up to 30th April, 2026 will be applicable for November, 2026 Examination. Accordingly, limited revisions in Ind AS issued by MCA in the year 2025 i.e. on 7th May, 2025 and 13th August, 2025 are applicable for November, 2026 examination
- (3) Newly notified Ind AS becomes applicable only one year after its notification. However, though Ind AS 117: Insurance Contracts has been notified on 12th August, 2024, yet being an industry specific standard, it has been excluded for November, 2026 Examination. However, limited revisions in the existing applicable Ind AS consequent to notification of Ind AS 117 will be applicable in November, 2026 examination.
- (4) Limited discussion of Accounting Standards has been given at relevant places in the form of differences of particular provision in Ind AS vis-à-vis AS. Accounting standards do not form part of the syllabus. However, with respect to AS 7, AS 9, AS 19 and AS 22 where there are significant differences between Ind AS and AS, questions on these Accounting Standards (i.e. AS 7, AS 9, AS 19 and AS 22) testing differential treatments in both the set of standards (i.e. Ind AS and AS) may be asked in the examination.

Paper 3: Advanced Auditing, Assurance and Professional Ethics

Applicability of the Legislative Amendments for November 2026 Examination: Students are expected to be updated with the notifications, circulars and other legislative amendments made up to 6 months prior to the examination. Accordingly, the relevant notified Sections and legislative amendments including relevant Notifications / Circulars / Rules / Guidelines issued by Regulating Authority up to April 30th, 2026 will be applicable for November 2026 Examination.