

Answer to MTP_Final_Syllabus 2008_Jun2014_Set 2

Paper-17 - COST AUDIT & OPERATIONAL AUDIT

Time allowed-3 hrs.

Full Marks: 100

Section I (50 Marks) (Cost Audit)

Answer Question No. 1 (carrying 14 marks) which is compulsory and answer any two (carrying 18 marks each) from the rest in this Section.

Working Notes should form part of the answer.

“Wherever necessary, suitable assumptions should be made and indicated in answer by the candidates”

1.(a) State whether the following statements based on the quoted terms are “TRUE” or “FALSE” with justifications for your answer. No credit will be given for any answer without justifications.

[5×1=5]

- (i) Cost Audit is synonymous with efficiency audit.
- (ii) Cost Audit Order is product specific.
- (iii) Goodwill is to be deducted while computing Net Worth of the Company.
- (iv) Donations given to Charitable Institutions should not form part of Cost Accounts.
- (v) CAS 9 deals with indirect material cost.

Answer:

- (i) **True.** The Cost audit Report mainly comment on the efficiency of the company namely, utilization aspect of the factors of production.
- (ii) **True.** A company need not have Cost Audit for the product not specified in the order.
- (iii) **True.** All intangible assets needs to be deducted, and goodwill is an intangible asset.
- (iv) **True.** Expenses on account of donations are purely financial in nature, hence excluded from Cost Accounts.
- (v) **False.** CAS 9 deals with packing material cost.

1.(b) Choose the most correct answer among four alternatives:

[5×1=5]

- (i) A Cost Auditor should ‘qualify’ the Cost Audit Report where:
 - A. He is unable to form an opinion due to non availability of appropriate records/data.
 - B. He finds that items in the cost statements are mistated.
 - C. None of the above.
 - D. Both of the above.

(ii) CAS 11 deals in :

- A. Administrative Overheads.
- B. Factory Overheads.
- C. Selling and Distribution Overheads.
- D. Financial Costs.

(iii) According to CAS 2 on Capacity Determination , ‘Normal Capacity’ is :

- A. Practical capacity minus the loss of productive capacity due to external factors.
- B. Difference between installed capacity and the actual capacity utilization.
- C. Maximum productive capacity of a plant.
- D. Installed capacity minus the inevitable interruptions.

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- (iv) Each major materials for which details to be furnished as per Annexure to the Cost Audit Report Rules should constitute
- A. 10% of the raw material cost
 - B. 2% of the raw material cost
 - C. 5% of the raw material cost
 - D. 1% of the raw material cost
- (v) 'Significant influence' means:
- A. Participation in the financial policy decisions and control but not operating policy decisions and control of an enterprise.
 - B. Participation in the financial or operating policy decisions of an enterprise and control over those policies.
 - C. Participation in the financial or operating policy decisions of an enterprise but not control over those policies.
 - D. None of the above.

Answer:

- (i) - B
- (ii) - A
- (iii) - A
- (iv) - B
- (v) - C

- 1.(c) Fill in the blanks: [1x4]
- (i) The ceiling on number of Cost Audits to be undertaken by a Cost Auditor is laid down in Section ----- of Companies Act, 1956.
 - (ii) Cost Audit was initially introduced in the year-----.
 - (iii) Each Cost Accounting Record rule is given a ----- number and date of publication in the Gazette.
 - (iv) According to CAS 8 on Utilities the cost of maintaining stand-by utilities is ----- cost.

Answer:

- (i) 224(1-B)
- (ii) 1965
- (iii) GSR
- (iv) committed

2. (a) Explain the term 'full time employment' in respect to disqualifications of Cost Auditor. [5]

Answer:

As per Section 224(1)(B) of Companies (Amendment) Act, 1988 no person can be appointed as cost auditor of a company if he in full time employment.

However the Companies Act does not define the term 'full time employment.'

Thus the following guidelines could be helpful:

- (i) A whole time director of a company appointed under provisions of Section 269 of Companies Act, 1956 or Secretary under provisions of Section 383 A of Companies Act , 1956 may be considered to be in full time employment.

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- (ii) Anyone receiving a salary and PF contribution from his employer or getting such other benefits like Bonus, HRA etc. may amount to be in full time employment.
- (iii) A person declaring income under the head 'Salaries' under Income Tax Act may be considered to be in full time employment.

2. (b) Under what conditions can a firm of Cost Accountants be appointed as Cost Auditors? [4]

Answer:

The Ministry of Corporate Affairs has decided to approve the appointment of cost auditors in firm's name under sub-Section (2) of Section 233-B of Companies Act, 1956 if such proposal is received from Board of Directors of any company subject to the following conditions:

- (i) 'All the partners are practicing Cost Accountants within the meaning of Sections 6 and 7 of the Cost Accountants Act, 1959' and
- (ii) 'The firm itself has been constituted with the previous approval of the Central Government /Institute as required under Regulation 113 of the Cost and Works Accountants Act, 1959 as amended from time to time.'

When a firm is appointed as Cost Auditors, authentication of Cost Audit Report is to be done by the signature of any one of the partners of the firm in his own hand for and on behalf of the firm. The report should not be signed by merely affixing firm name.

2. (c) What is the relevance of Cost Audit in India.

[9]

Answer:

Relevance of Cost Audit in India:

- (i) Liberalization and Globalization** – The liberalization of the economy has increased the relevance of Cost Audit in India more than ever before. In the present competitive scenario of globalization; the Cost Audit Reports have assumed greater importance and significance as the only source of reliable and authentic feedback to the government and its various departments and agencies. It has become very important that the product and services are made more competitive by constantly improving efficiency by reducing vital input costs and reduction of wastage. This constant exercise has to be monitored by Cost Audit only.
- (ii) For toning up efficiency and productivity** – Cost Audit is a powerful tool to highlight areas of inefficiency and improving performance. As such the need for Cost Audit is more in the present scenario than before.
- (iii) Antidumping** – The Cost Record and Cost Audit Report will play a good source document for the Indian exporters to substantiate their fair approach against any allegation of dumping. Further, for imposing Anti-dumping duties on the import into India, the expertise of Cost Auditors and certification by them will be useful.
- (iv) Transfer pricing issue** – Cost Audit Report Rules, 2001 have been amended to take care of the issue of 'Transfer Pricing' in right perspective in judging its impact on business activities.
- (v) Audit Committee** – The formation of Audit Committee is a big leap in ensuring good corporate governance. Cost Auditor plays as key role in the Audit Committee meetings.
- (vi) Major source of information for Direct & Indirect Tax authorities** – An independently audited Cost Records and the resultant Cost Audit Report become a major source of information, which can be effectively used by both the Direct & Indirect Tax authorities.

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- (vii) **Serves Central Excise authorities** – The Cost Audit Reports are used by Central Excise Authorities for verifying the claim of the companies relating to ex-factory prices of the excisable goods, especially in the case of Inter-unit transfer.
- (viii) **Fixation of Tariff by the Tariff commission** – The Tariff Commission relies on the authenticity of the Cost Audit Reports for fixing the tariff of the products, covered under Cost Accounting Records Rules.
- (ix) **Other relevant roles** – Cost Audit serves the interests of shareholders. It is also made use of by Income Tax Authorities. Further, the Banks and Financial Institution also find the report as useful. The Cost Audit Report is used as evidence by DGIR (Directorate General of Investigation and Registration) in pursuit of cases with the MRTP Commission.

3. (a) How do you define a Service Cost Centre according to CAS-13?

[2]

Answer:

The cost centre which primarily provides auxiliary services across the enterprise. The cost Centre which provides services to production, operation or other service Cost Centre but not directly engaged in manufacturing process or operation is a SERVICE COST CENTRE. A Service Cost Centre renders services to other Cost Centre / other units and in some cases to outside the parties.

Examples of Service Cost Centers are engineering, workshop, research & development, quality control, quality assurance, designing, laboratory, pollution control etc. However the definition excludes utilities and repairs & maintenance services dealt with in CAS-8 and CAS – 12 respectively.

(b) How is Cost Computed of Services in the following cases as per CAS-13?

(i) In-house

(ii) By Contractor

[2+2=4]

Answer:

- (i) Cost of In-house services shall include cost of materials, consumable stores, spares, manpower, equipment usage, utilities and other resources used in such services which includes related overheads.
- (ii) Cost of services rendered by contractors shall include charges payable to the contractor and cost of materials, consumables stores, spares, manpower, equipment usage, utilities and other resources provided to the contractors for such services.

(c) **ASHLEEN SUGAR MILLS LTD., a sugar manufacturing company, located at Uttar Pradesh has a boiler which is used for its own by-product, bagases as fuel. The steam generated is first used for generation of power and the exhaust steam is used in the process of sugar manufacture. The following details are extracted from the financial accounts and cost accounting records of ASHLEEN SUGAR MILLS LTD for the year ended March 31,2013:**

Sugar produced	28,70,000 Quintals
Steam generated and consumed	14,65,000 Tonnes
Fuel (Bagases) consumed for production of steam	6,85,000 Tonnes
Cost of generation of steam including cost of water (other than fuel cost)	₹ 6,45,30,000
Steam used for generation of power	6,20,000 Tonnes
Power purchased from Electricity Board @ ₹ 5.40 per KWH	52,70,000 KWH
Power generated from Steam Turbine	4,85,25,000 KWH

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Variable conversion cost of generation of power(excluding cost of steam)	₹ 4,22,18,000
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Notes: (1) The Sale Value of bagasse if sold in the open market is ₹ 1,820 per Tonne.
 (2) The exhaust steam (after generation of power) transferred to sugar manufacturing process is 82% of the cost of production of steam.

Required:

(i) Prepare two separate Cost Sheet for steam and power.

(ii) Compute the average Cost of Power.

[(5+4)+3=12]

Answer:

(i) ASHLEEN SUGAR MILLS LTD Cost Sheet

Particulars	Computation	₹
Cost of Steam		
Cost of Fuel-Bagasse	6,85,000 Tonnes @ ₹ 1,820	124,67,00,000
Conversion Cost including Cost of Water		6,45,30,000
Total Cost		131,12,30,000
Steam Generated (Tonnes)		14,65,000
Gross Cost of Steam per Tonne	$131,12,30,000 \div 14,65,000$	₹ 895.04
Steam directly used for Sugar Production	1465000-620000) Tonnes X ₹ 895.04	₹ 75,63,08,800
Value of exhaust steam from Steam Turbine	[At 82% of cost = $(620000 \times 895.04 \times 0.82)$]	45,50,38,336
Total Cost of Steam used for Sugar Production		<u>121,13,47,136</u>
Average Cost of Steam per Tonne	$(121,13,47,136 \div 14,65,000)$	₹ 826.86
For disclosure in Power & fuel to the Cost Audit Report :		
Steam Consumption per Quintal of Sugar:	$(14,65,000 \div 28,70,000)$	0.51 Tonnes
Steam Cost per quintal of Sugar:	$(121,13,47,136 \div 28,70,000)$	₹ 422.07

Particulars	Computation	₹
Cost of Power		
Cost of high pressure steam sent to steam turbine	$(620000 \text{ Tonnes} \times ₹ 895.04)$	55,49,24,800
Conversion cost for generation of Power (excluding Cost of Steam)		4,22,18,000
		59,71,42,800
Less : Cost of exhaust steam transferred to sugar manufacture		45,50,38,336
Net Cost of Power Generated		₹ 14,21,04,464
Power generated from steam Turbine		4,85,25,000 KWH
Cost of Power Generated per KWH		₹ 2.93

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(ii) Computation of average cost of power:

Quantity & Cost of Power	KWH	₹	₹ / KWH
(a) Own Generation	4,85,25,000	14,21,04,464	2.93
(b) Purchased (@ ₹ 5.40)	52,70,000	2,84,58,000	5.40
	5,37,95,000	17,05,62,464	3.17

Power consumed per quintal of sugar
(5,37,95,000 ÷ 28,70,000) 18.74 KWH

Power cost per quintal of Sugar
(18.74 x 3.17) ₹ 59.41

4. (a) Who can authenticate the Compliance Report as per the Companies (Cost Accounting Records) Rules,2011? [4]

Answer:

As per Rule 5, the Compliance Report and the annexure thereto is required to be certified by a "Cost Accountant" as defined under Rule 2(c).

As per Rule 7, the annexure to the Compliance Report is to be duly approved by the Board of Directors. A "Cost Accountant" within the definition of these Rules does not include:

- (i) A Member holding a part-time certificate of practice: or
- (ii) A Member who is in full time employment whose membership fees are in arrear; or
- (iii) A Member of ICWAI who has been admitted as a member through reciprocal arrangement of membership by virtue of being a member of Institute of Management Accountants, USA.

4. (b) Write a note on 'Social objectives' of Cost Audit. [5]

Answer:

The social objectives of Cost Audit are enumerated below:

- Facilitation in fixation of reasonable prices for goods and services produced by the enterprise.
- Improvement in productivity of human, physical and financial resources of the enterprise.
- Channelizing of the enterprise resources to most optimum, productive and profitable areas.
- Availability of Audited Cost data as regards Contracts containing escalation clauses.
- Facilitation in settlement of bills in the case of Cost-plus contracts entered into by the Government.
- Pinpointing areas of inefficiency and miss-management if any for the benefit of shareholders, consumers and society in large.
- Hospitalization, schooling, roads and transportation facilities to own employees as well as neighboring people & cost benefit analysis.

4 (c) Opening stock of raw materials (10,000 units) ₹ 1,80,000; Purchase of Raw Materials (35,000 units) ₹ 7,00,000; Closing Stock of Raw Materials 7,000 units; Freight Inward ₹ 85,000; Self-manufactured packing material for purchased raw materials only ₹ 60,000 (including share of administrative overheads related to marketing sales ₹ 8,000); Demurrage charges levied by transporter for delay in collection ₹ 11,000; Normal Loss due to shrinkage 1% of materials ; Abnormal Loss due to absorption of moisture before receipt of

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materials 100 units.

[9]

Answer :

Computation of value of closing stock of raw materials [Average Cost Method]

	Particulars	Quantity (Units)	Amount (₹)
	Opening Stock of Raw Materials	10,000	1,80,000
Add	Purchase of raw materials	35,000	7,00,000
Add	Freight inwards		85,000
Add	Demurrage Charges levied by transporter for delay in collection		11,000
			9,76,000
Less	Abnormal Loss of raw materials (due to absorption of moisture before receipt of materials) = $[(7,00,000 + 85,000 + 11000) \times 100] / 35,000$	(100)	(2,274)
Less	Normal loss of materials due to shrinkage during transit [1% of 35,000 units]	(350)	----
Add	Cost of self-manufactured packing materials for purchased raw materials only (60,000 – 8,000)		52,000
	Cost of raw materials	44,450	10,25,726
Less:	Value of Closing Stock = Total Cost / (Total units – Units of Normal Loss) [10,25,726 / (10,000 + 35,000 – 350)] x 7,000	(7,000)	(1,61,169)
	Cost of Raw Materials Consumed	37,450	8,64,557

Note:

- (i) Units of normal loss adjusted in quantity only and not in cost, as it is an includible item
- (ii) Cost of self-manufactured packing materials does not include any share of administrative overheads or finance cost or marketing overheads. Hence, marketing overheads excluded.
- (iii) Abnormal loss of materials arised before the receipt of the raw materials, hence, valuation done on the basis of costs related to purchases only. Value of opening stock is not considered for arriving at the valuation of abnormal loss.
- (iv) Demurrage charges paid to transporter is an includible item. Since this was paid to the transporter, hence considered before estimating the value of abnormal loss

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ALTERNATIVELY, SOLVING THE ABOVE QUESTION BASED ON FIFO METHOD

Computation of value of closing stock of raw materials [FIFO Method]

	Particulars	Quantity (Units)	Amount (₹)
	Opening Stock of Raw Materials	10,000	1,80,000
Add	Purchase of raw materials	35,000	7,00,000
Add	Freight inwards		85,000
Add	Demurrage Charges levied by transporter for delay in collection		11,000
			9,76,000
Less	Abnormal Loss of raw materials (due to absorption of moisture before receipt of materials) = $[(7,00,000 + 85,000 + 11,000) \times 100] / 35,000$	(100)	(2,274)
Less	Normal loss of materials due to shrinkage during transit = [1% of 35,000 units]	(350)	----
Add	Cost of self-manufactured packing materials for purchased raw materials only (60,000 – 8,000)		52,000
	Cost of Raw Materials	44,550	10,25,726
Less:	Value of Closing Stock = Total Cost / (Total units – Units of Normal Loss) Where Total Cost = = $[7,00,000 + 85,000 + 11,000 - 2,274 + 52,000] = 8,45,726$ And Total Units = $[35,000 - 1\% \text{ of } 35,000] = 34,650$ units Value of Closing Stock = $[8,45,726 \times 7,000] / 34,650$	(7,000)	(1,70,854)
	Cost of Raw Materials Consumed	37,550	8,54,872

Note:

- (i) Since FIFO method is followed, hence for the purpose of estimating the units sold/used/consumed, it is presumed that there is no units left out of units in opening stock.
- (ii) Since normal loss is in transit, hence it is calculated on units purchased only.

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Section II (50 Marks) (Operational Audit)

Answer Question No. 5 (carrying 14 marks) which is compulsory and Answer any two (carrying 18 marks each) from the rest in this Section.

5. (a) State whether the following statements are TRUE or FALSE with justification for your answer. No credit will be given for merely answering TRUE or FALSE — without giving any justification/reasoning : [1×4=4]

- (i) Dumping is an 'illegal' practice.
- (ii) Productivity is defined as ratio of production and sales.
- (iii) There are no fixed items of evidence to be checked by Management Auditor.
- (iv) Three-fourths of the members of the Audit Committee shall be independent directors.

Answer:

- (i) **False.** 'Dumping' is an 'unfair' practice.
- (ii) **False.** Productivity is defined as ratio of output to input.
- (iii) **True.** A Management Auditor has to rely more on his experience and acumen to identify areas of review.
- (iv) **False.** 2/3rd of the members of the Audit Committee shall be independent Directors.

(b) What do the following abbreviations stand for? [1×5=5]

- (i) OECD;
- (ii) MTA;
- (iii) TPRM.
- (iv) CFC
- (v) TPRB

Answer:

- (i) OECD: Organization for Economic Co-operation and Development
- (ii) MTA : Multilateral Trade Agreements
- (iii) TPRM: Trade Policy Review Mechanism
- (iv) CFC : Certified Facilitation Centre
- (v) TPRB : Trade Policy Review Body

(c) Fill in the blanks in the following sentences by using appropriate word(s)/ phrase (s) number(s) : [1×5=5]

- (i) _____ is the evaluation of every resources declared in the industry.
- (ii) Management Audit can be a _____ for managerial control and reduction of cost.
- (iii) _____ Audits are concerned with objectives of efficiency and effectiveness.
- (iv) _____ services have been defined as independent professional services that improve the quality of information for decision makers.
- (v) _____ is a movement protecting interest of the consumers.

Answer:

- (i) Productivity Analysis
- (ii) Potent tool

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- (iii) Operational
- (iv) Assurance
- (v) Consumerism

6. (a) You are required to look into, as a Management Auditor, the production functions of a manufacturing units. How would you proceed and what areas would look into. [8]

Answer:

Management Auditor is not a technical expert on production methods.

At the same time his experience and background make him look at operations in an unbiased way.

Preparation for Production audit should cover the following areas :

- (i) Study of the process in detail.
- (ii) Gathering of comparative data from publisher secondary sources in process technology; industry standards, theoretical/achievable norms of capacity, input/output from technical literature.
- (iii) Internal data from Industrial Engineering Studies, Reports of Technical Consultants, Project Reports, Manufacturers specification and guarantees, returns furnished to Govt. agencies etc.
- (iv) List of machines/Depts. Operations carried out, numbers of operatives in each station with their duties.
- (v) List of records maintained in respect of production operation how it is compiled who checks them and how it is utilised.
- (vi) Collection of all input/output data in regard to major materials, wastages, scrap re-work etc. for different batches/days.
- (vii) Data on availability of man/machine hours loss of production hours, reasons thereof under specific causes.

- (viii) Chart of administration of factory indicating lines of control, responsibility.

Analysis : The analysis of this data, wherever necessary using statistical techniques would be directed in assessing productivity.

- (i) Capacity utilisation of equipments
- (ii) Input/output relationships
- (iii) Control and supervision
- (iv) Management reporting

The analysis would focus the areas of weakness and shortcomings in regard to each function of production, bottlenecks, imbalances, constraints, possible areas of improvement in productivity cost reduction, supervision and control.

After a detailed discussion with concerned individuals, the Management auditor after taking the views expressed into consideration, put forward an objective assessment of the situation indicating both long and short term measures, the level at which action is to be initiated the quantified results that can be expected, the scales of investments or resources that may be required as well as the control systems that need to be installed/modified/changed.

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- (b) In the conducting of a Management Audit, a controversy often arises on identifying the criteria or standards against which performance should be judged. Discuss. [6]**

Answer:

The causes for the difficulties in setting standard, in management Audit work arise from :

- (i) The variety of functions covered is quite wide
- (ii) Environmental variable are many
- (iii) Individuals are very different from one another
- (iv) Organisational culture varies
- (v) Management performance cannot always be measured in quantitative terms
- (vi) Limitations of familiarity with the audited organisations nature of business, people dealt with etc.

The possible remedies could be :

- (i) Constitution of a competent management audit team drawn from different disciplines
- (ii) Familiarisation with the firm's business
- (iii) Formal listing of peculiarities of the business
- (iv) identifying the corporate culture
- (v) Proper selection of methods for carrying out the management audit
- (vi) Proper careful and scientific designing of questionnaires to be administrated.
- (vii) Wherever necessary encouraging transparency in actions.

- (c) Write a short note on Professional Ethics. [4]**

Answer:

Essentially a person is recognised as a professional only when he combines skill, knowledge and ethics. While the first two can be acquired by practice and study, the last one is dependent on the attitude of the individual. Every professional organization of international repute, including ICAI, is therefore keen that high standards of ethics are to be maintained by its members. Many of the rules provided as part of the schedules to the Cost and Works Accountants Act, 1959 try to emphasise this principle. Basically they require that if there be a conflict of interest, particularly personal interest and professional duties, the cost accountant should avoid accepting such assignments. Similarly they require that no work should be grabbed from another member by undercutting or without informing the other member.

- 7. (a) "Operating auditing is an extension of internal audit in operational areas, but with different approach". Examine this statement in the light of the objectives of operational audit. [6]**

Answer:

Operational auditing is review of operational methods and procedures. To that extent it is no more than internal audit extended to operational areas. However as applied to operational areas the attempt must be not only to evaluate controls, but also to assess the effectiveness of existing procedures to meet the objectives and plans of the department which is being audited.

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The objectives of operational audit may be briefly listed as appraisal of the relevant departments.

Objectives and plans;

Controls;

Existing procedures to achieve the objectives and plans;

Quantitative measures to monitor performance;

Productivity.

Since operating departments would be structuring their methods and procedures based on their objectives and plans, such objectives and plans have to be appraised. Restatement or changes in definitions of the objectives could have an impact on the plans and similar change in plans may make it advisable to redefine the objectives. Hence appraisal of plans and objectives becomes essential and the first step in operational audit.

The procedure in the department have to be reviewed and appraised to assess their effectiveness in achieving the objectives and plans with the given resources.

It is necessary that every department should develop a few quantitative measures to monitor their performance. Such measures may be in simple or composite units. The trend of such measures, the usefulness of such indicators as well as their reliability may have to be appraised as part of operational auditing. Appraisal of productivity could be complex as the term 'Productivity' is all embracing and covers the effectiveness of entire operations of the concerned department.

(b) What do you mean by the term "Due Diligence"? What are the areas Due Diligence ought to investigate? [3+5=8]

Answer:

Due Diligence: The term 'Due Diligence' is generally used for a number of concepts involving the performance of an act with a certain standard of care and caution.

At its simplest, due diligence means care and precaution. In this sense, due diligence in workplace means taking every precaution to protect the health, safety and welfare of all workers and staff.

Due Diligence primarily means 'background checking' or the intense examination of a target asset for an acquisition by a prospective buyer. It is done to ensure that the buyer has all the information to take the necessary decision.

The main objective of Due Diligence is to verify the assertions made by the seller and to identify caveats, if any that may not have been disclosed by the seller. It can also be described as the task of carefully confirming all critical assumptions and facts presented by a buyer or borrower and to ensure that no material facts are omitted.

In other words, it is a reasonable investigation about the state of affairs of the business to be acquired, especially focusing on matters which may have a critical bearing on the future of the business. In short, the Buyer determines through Due Diligence that the proposed bought out acquisition contains all the assets and liabilities that have been paid for.

Areas to be investigated :

The due diligence process (framework) can be divided into nine distinct areas :

- **Compatibility audit** deals with the strategic components of the transaction and in particular the need to add shareholder value.

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- **Financial audit** is the verification of the financial statements of a legal entity, with a view to express an audit opinion.
- **Macro-environmental audit** examines six main areas, the detail depending on the involvement of the business and involvement required by the Industry-Demographics, Economic, Environmental, Technology, Political and Cultural.
- **Legal-environmental audit**- Environmental law governs any environmental issues regarding individuals, businesses, and government entities. Environment law includes regulations and cleanup regarding hazardous or chemical materials and the consequences of individuals who violate environment statutes.
- **Marketing Audit**- Carrying out the marketing audit provides the opportunity to review and appraise the whole marketing activity, enabling the company to assess past and present performance as well as to provide the basis for evaluating possible future courses of action.
- **Production Audit**- The main objective of production audit is to verify whether the company is to turn out finished goods of requisite quality by making an optimum use of men, machine, and services.
- **Management audit** - is analysis and assessment of competencies and capabilities of a company's management in order to evaluate their effectiveness, especially with regard to the strategic objectives and policies of the business. The objective of a management audit is not to appraise individual executive performance, but to evaluate the management team in relation to their competition.
- **Information systems audit** - An information system (IS) audit or information technology(IT) audit is an examination of the controls within an entity's Information technology infrastructure. These reviews may be performed in conjunction with a financial statement audit, internal audit, or other form of attestation engagement.
- **Reconciliation audit** which links/consolidates other audit areas together via a formal valuation in order to test whether shareholder value will be added.

(c) Explain whether the following activities amount to professional misconduct on the part of a Cost Accountant: **[2x2=4]**

(i) CMA Mitra, a Cost Accountant in practice published a book and gave her personal as an author. These details also mentioned her professional experiences and her association as partner with MKR and Associates, a firm of Cost Accountants.

(ii) M/s. K. Bhatt & Associates, a firm of Cost Accountants in practice, develops a website "bhatt.com". The colour chosen for website was very bright yellow where the names of the partners of the firm along with their various professional attainments and the major clients were to be displayed on the website.

Answer:

(i) A Cost Accountant in practice shall be deemed to be guilty of professional misconduct, if he solicits clients or professional work either directly or indirectly, by circular, advertisement, personal communication or interview or by any other means.

CMA, Mitra being a Cost Accountant in practice has committed a professional misconduct by mentioning that at present she is a partner of M/s MKR & Associates, a firm of Cost Accountants (Clause 6 of part I of First Schedule to the Cost and Works Accountants Act, 1959)

(ii) The Council of the Institute of Cost Accountants of India had approved posting of particular on website by Cost Accountants in practice under clause (6) of Part-I of First Schedule to the Cost and Works Accountants Act, 1959 subject to the prescribed guidelines. The relevant guidelines are:

- No restriction on the colours used in the website.

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- Names of clients and fees charged not to be given.

Clause (7) of Part-I of First Schedule to the Cost and Works Accountants Act, 1959 prohibits a member not to advertise his professional attainments or services other than Cost Accountant on professional documents, visiting cards, letter heads or sign boards.

In view of the above, M/s K. Bhatt & Associates would have no restriction on the colours used in the website but failed to satisfy other guidelines.

Thus M/s K.Bhatt & Associates would be held guilty of professional misconduct under clause (6) and clause (7) of Part-I of First Schedule to the Cost and Works Accountants Act,1959.

8. Write a short note on any three of the following:

[6×3=18]

- (a) Functions of the WTO**
- (b) Environmental Pollution**
- (c) SWOT Analysis**
- (d) Productivity audit**

Answer:

(a) Functions of the WTO:

The main functions of WTO are —

(i) Facilitate the management of the Multilateral Trade Agreements (MTA) and the Plurilateral Trade Agreements (PTA) for the fulfillment of their obligations.

(ii) All Multilateral Trade Relations concerning the above agreements will be negotiated by the Members in this forum.

(iii) WTO will also facilitate implementation of the results of the negotiations as decided by the Ministerial Conference.

(iv) The WTO shall administer the Understanding on Rules and Procedures Governing the Settlement of Disputes, forming part of the Agreements (MTAs and PTAs)

(v) The WTO is responsible for administration of the Trade Policy Review Mechanism (TPRM) forming part of the Agreement.

(vi) WTO is also the organ for establishing coordination with other wings of the UNO such as the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD) and its affiliated agencies.

(b) Environmental Pollution:

Environmental Pollution means smoke from industries, effluents from chemical plants, noise from heavy machines and vehicles, unclear garbage dumps etc. The concept of pollution embraces environmental problems-such as air and water pollution, noise and loss of open space as nuisances that contribute to the deterioration of the quality of life-both human and other living organisms.

Pollution is a kind of interference to the environment and causes environmental degradation. The problems of environmental de-gradation-air, water, noise and visual pollution, solid wastes, radiation hazards, thermal pollution, threats to wild-life, depletion and destruction of natural resources, etc., are all "Environmental crisis" and "threats to the delicate balance" .

Environmental Pollution, now constitutes one of the biggest hazards. It is the biggest hazards not only to human existence of all the gifts that nature has so kindly bestowed on mankind. Rapid industrialization and ever-increasing urbanization have resulted in the environmental problems, assuming alarming proportions.

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The problems of environmental pollution are extremely acute in the developed and developing countries. Even with the availability of improved methods and stringent laws, the problems are far from being solved. Thus, protection and preservation of environment has to be looked at, encouraged and developed as a people's movement world over.

(c) SWOT Analysis:

SWOT analysis refers to the identification of a company's Strength, Weakness, Opportunities and Threats. While the first two are internal to the organization, the other two are external environment. The following is an indicative list of Questions for which answers must be obtained to make an objective SWOT analysis as follows:

A. Strength/Weakness

- (a) Financial
- (b) Marketing
- (c) Personnel

B. Opportunities/Threats

- (a) Power requirement and availability
- (b) International competition
- (c) Export potential
- (d) Opportunities available in the country
- (e) Govt. policy regarding the industry
- (f) Product obsolescence

(d) Productivity audit

The Productivity audit is basically an analysis of the productivity of the resources deployed by any organization. It is generally done to generate information about the status of productivity in the organization for the purpose of determining the scale of efficiency and effectiveness of 'resource utilization'. The term 'resources' here would include not only "money" but also "men", "machines", "materials" and "methods".

In other words, the objectives of productivity audit is –

- (a) to attain optimum result, and
- (b) to improve on the benchmarks.

This audit would generally comprise –

- (a) comparison of expected returns on utilization of the resources vis-à-vis the actual returns;
- (b) comparison of optimum returns on utilization of the resources vis-à-vis the actual returns;
- and
- (c) the steps taken to improve benchmarks of returns and the utilization.

The term 'Productivity' is normally attributed only to the "productivity of labour" or "efficiency of labour" alone. But productivity audit is actually "productivity of every resource employed".

Productivity audit is done by –

- (a) Ratio analysis
 - Return on capital employed
 - Return on sales

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- Turnover ratios of fixed assets, current assets, inventories, category-wise debtors etc.
- (b) Capacity utilization of plant, machinery and equipments against available capacity.
- (c) Productivity analysis of man (labour) hours in time and cost.
- (d) Material consumption against norms and benchmarks, etc.