Paper – 12: Company Accounts and Audit

The following table lists the learning objectives and the verbs that appear in the syllabus learning aims and examination questions:

	Learning objectives	Verbs used	Definition
LEVEL B	KNOWLEDGE What you are expected to know	List	Make a list of
		State	Express, fully or clearly, the details/facts
		Define	Give the exact meaning of
	COMPREHENSION What you are expected to understand	Describe	Communicate the key features of
		Distinguish	Highlight the differences between
		Explain	Make clear or intelligible/ state the meaning or purpose of
		Identity	Recognize, establish or select after consideration
		Illustrate	Use an example to describe or explain something
	APPLICATION How you are expected to apply your knowledge	Apply	Put to practical use
		Calculate	Ascertain or reckon mathematically
		Demonstrate	Prove with certainty or exhibit by practical means
		Prepare	Make or get ready for use
		Reconcile	Make or prove consistent/ compatible
		Solve	Find an answer to
		Tabulate	Arrange in a table
	ANALYSIS How you are expected to analyse the detail of what you have learned	Analyse	Examine in detail the structure of
		Categorise	Place into a defined class or division
		Compare and contrast	Show the similarities and/or differences between
		Construct	Build up or compile
		Prioritise	Place in order of priority or sequence for action
		Produce	Create or bring into existence

Paper – 12: Company Accounts and Audit

Full Marks: 100 **Time Allowed: 3 Hours**

This paper contains 4 questions. All questions are compulsory, subject to instruction provided against each question. All workings must form part of your answer. Assumptions, if any, must be clearly indicated.

1. Answer all questions: **[2×10=20]**

(i) Anu Ltd. provides the following information. Compute basic EPS as per AS – 20. Number of Equity shares outstanding as at beginning of the period = 5,00,000. Bonus Issue on 1st July of current year = 3 Shares for every 1 share held. Net Profit for current year and previous reporting period (assume calendar year) = ₹160 lakhs and ₹100 lakhs.

Answer:

Since the Bonus Issue is an issue without consideration, the issue is treated as if it had occurred prior to the beginning of the previous reporting period, i.e. the earliest period reported, The computation is as under-

Step	Procedure
1	Number of Equity Shares Outstanding at the beginning of the current period = 5,00,000
2	Total Number of Equity Shares Outstanding, i.e. Step 1 + Bonus $= 5,00,000 + \left(5,00,000 \times \frac{3}{1}\right) = 20,00000$
3	Basic EPS for Current Year $= \frac{\text{Net Profit for the year}}{\text{Total shares as per step 2}} = \frac{₹1,60,00,000}{20,00,000 \text{ Shares}} = ₹\mathbf{8.00}$
4	Adjusted Basic EPS for the previous year $\frac{\text{Net Profit for the year}}{\text{Total shares as per step 2}}$ $= \frac{₹1,00,00,000}{20,00,000 \text{ Shares}} = ₹5.00.$

(ii) Vidhata Ltd. acquired Patents on 1st April 1988 for ₹ 40 Lakhs and has not amortised the same. AS - 26 is applicable to the Company from 1st April 2003 on which date the Patents appeared in the Balance Sheet at ₹40 Lakhs. Give the accounting treatment.

Answer:

Amortisation Period for the Patents = 10 years from 1st April 1988. (as per Para 63 of AS - 26). The amortisation period expires in 1997 - 1998 itself, i.e. before AS - 26 is applicable for the Enterprise.

The Carrying Amount of Patents (₹40 Lakhs) should be eliminated by the following empty:

Profit and Loss A/c or Revenue Reserve Dr.	₹40 lakhs	
To Patents A/c		₹40 Lakhs

(iii) B Ltd. Purchase the assets of ₹10,80,000 from C Ltd. The consideration was payable in fully paid equity shares of ₹100 each.

Required: Show the necessary journal entries in books of B Ltd. assuming that –
- **Such shares are issued at premium of 20%**

Answer:

Journal

Particulars	L.F.	Dr. Amount (₹)	Cr. Amount (₹)
Sundry Assets A/c Dr. To C Ltd. A/c [Being the purchase of assets from C Ltd. as per agreement dated…)		10,80,000	10,80,000
C Ltd. A/c Dr. To Equity Share Capital A/c To Securities Premium A/c (Being the issue of 9,000 shares at 20% premium to C Ltd. as per Board's Resolution no ……dated….)		10,80,000	9,00,000 1,80,000

Working Note: calculation of no. of Shares to be issued in different cases

	At a Premium
A. Amount to be paid (₹)	10,80,000
B. Issue price per share (₹)	120
C. No. of Shares to be issued (A/B)	9,000

(iv) A Company issued 1,00,000 debentures of ₹100 each redeemable at the end of 10th year, but reserves the right to redeem earlier from the end of 5th year. The company decides at the end of 5th year to redeem 25,000 debentures out of profits it has made.
Pass necessary journal entries relating to redemption.

Answer:

Date	Particulars	Dr. ₹'000	Cr. ₹'000
5th year end	Debentures A/c Dr. To Debenture Redemption A/c	2,500	2,500
	Debenture Redemption A/c Dr. To Bank Account	2,500	2,500
	Profit/loss appropriation A/c Dr. To Debenture Redemption Reserve A/c	2,500	2,500

(v) Income from Operating Activities is ₹70 lakhs;
Fixed Asset sold for ₹100 lakhs;
Machinery Sold for ₹130 lakhs;
Income from Financing Activities is ₹20 lakhs, compute the net effect on Cash Flow.

Answer:

Particulars	₹ in lakhs	₹ in lakhs
A. Cash flow from Operating Activities		70
B. Cash flow from Investing Activities Sale of Fixed Asset Purchase of Machinery	 100 130	 230
C. Cash flow from Financing Activities		20
Net increase Cash Flow (A+B+C)		320

(vi) Vikas Ltd. took over assets of ₹ 460 Lakh and liabilities of ₹ 60 Lakh of Prakash Ltd. for a purchase consideration of ₹ 440 Lakh. The Vikas Ltd. paid the purchase consideration issuing 8% Preference Share of ₹ 100 each at 10% premium. Give journal entries in the books of the Vikas Ltd.

Answer:

Particulars		Dr. (₹)	Cr. (₹)
Sundry Assets A/c	Dr.	460	
Goodwill A/c	Dr.	40	
To, Liabilities A/c			60
To, Prakash Ltd. A/c			440
(Being purchase of assets and liabilities of Prakash Ltd.)			
Prakash Ltd. A/c	Dr.	440	
To, 8% Preference Share A/c			400
To Securities Premium A/c			40
(Being issue of debenture at 10% premium)			

(vii)Discuss the term Final Audit.

Answer:

A final audit is also known as Completed Audit or Periodical Audit. Final audit is done after the close of the financial year, i.e. after the books of accounts have been closed and the final accounts are drawn up. In this type of audit, the client gives the possession of books of accounts to the auditor for audit and routine checking and other audit procedures begin only after that.

(viii) Vouch foreign travelling expenditure of a Director and list any two issues.

Answer:

Following are the two issues related to the vouching of foreign travelling expenditure of a Director:

- Visa for travel — which shows the purpose of travel.
- Amount of Foreign exchange — Sanctioned for the travel including the authenticity/jurisdiction of the sanctioning authority. Sanction given by the board , if any

(ix) List the importance of Verification.

Answer:

Importance of Verification – Verification is very important function from the view point of both, the auditor and the client as it gives clear idea as to true and fair view of balance sheet.

The importance of verification may be described as under –

(a) True and fair view of Balance Sheet – verification of assets and liabilities enables the auditor to comment on true and fair state of affairs of the business.
(b) Valuation – verification enables the auditor to determine whether the assets or liabilities are overstated or under stated.

(c) Omissions – verification facilitates the act of confirming the omission of any asset or liability in the balance sheet.

(x) Discuss what partial audit is.

Answer:

A partial audit is a non statutory audit, which restricts the scope of the auditor to checking of certain specific aspects only. The auditor's powers to enquiry are restricted by his terms of engagement. He may not be allowed to obtain information which falls outside the purview of the scope defined for him. E.g. an auditor may be appointed to check the accuracy of recording of transactions relating to cash sales, or he may be appointed to conduct an audit for the month of Diwali only.

2. (Answer any 2 questions)

(a) Amit purchased a computer for ₹44,000 and leased out it to Sumit for four years on leases basis, after the lease period , value of the computer was estimated to be ₹ 3,000; which he realized after selling it in the second hand market. Lease amount payable at the beginning of each year is ₹ 22,000; ₹13,640;₹6,820 & ₹3,410. Depreciation was charged @ 40% p.a. You are required to pass the necessary journal entries in the books of Sumit. [8]

Answer:

Journal Entries
In the books of Sumit

Date	Particulars	Dr.(₹)	Cr.(₹)
?	**Purchase of Computer:**	**No Entry**	
	Payment of First Year's Lease: Lease Rent A/c Dr. To, Bank A/c	22,000	22,000
	Depreciation for First Year:	**No Entry**	
?	**Transfer to Profit & Loss Account:** Profit and Loss A/c Dr. To, Lease Rent A/c	22,000	22,000
?	**Payment of Second Year's Lease:** Lease Rent A/c Dr. To, Bank A/c	13,640	13,640
	Depreciation for Second Year:	**No Entry**	
?	**Transfer to Profit & Loss Account:** Profit and Loss A/c Dr. To, Lease Rent A/c	13,640	13,640
?	**Payment of Third Year's Lease:** Lease Rent A/c Dr. To, Bank A/c	6,820	6,820
	Depreciation for Third Year:	**No Entry**	
?	**Transfer to Profit & Loss Account:** Profit and Loss A/c Dr. To, Lease Rent A/c	6,820	6,820
?	**Payment of Fourth Year's Lease:** Lease Rent A/c Dr. To, Bank A/c	3,410	3,410
	Depreciation for Fourth Year:	**No Entry**	
?	**Transfer to Profit & Loss Account:**		

	Profit and Loss A/c Dr. To, Lease Rent A/c	3,410	 3,410
	Sale of Lease Assets:	**No Entry**	

(b) (i) In the context of relevant Accounting Standards, give your comment on the following matter for the financial year ending 31st March, 2015:
"Increase in pension liability on account of wage revision in 2014-15 is being provided for in 5 instalments commencing from that year. The remaining liability of ₹ 600 lakhs as redetermined in actuarial valuation will be provided for in the next 2 years". [4]

Answer:

As per AS-15, the costs arising from an alteration in the retirement benefits to employees should be treated as follows:

(i) The cost may relate to the current year of service or to the past years of service.
(ii) In case of costs relating to the current year, the same may be charged to Profit and Loss Account.
(iii) Where the cost relates to the past years of service these should be charged to Profit and Loss Account as 'prior period' items in accordance with AS-5.
(iv) Where retirement benefit scheme is amended in a manner which results in additional benefits being provided to retired employees, the cost of the additional benefits should be taken as " Prior Period and Extraordinary Items" as per AS-5.
In view of the above, the method adopted for accounting the increase in pension liability is not in consonance to the provisions mentioned in AS-15.

(b) (ii)As at the end of a financial year, on 31st March, Vidisha Ltd. has 5,000 Shares of Face Value ₹10 each. The Stock Options outstanding at that date are for 1,000 Shares. Net Loss for the year is ₹90,000. Fair Value of the Shares on the date of grant and the Exercise Price are ₹8.10 and ₹ 6 per Share respectively. Compute the Basic and Diluted EPS. [4]

Answer:

Basic EPS = $\frac{\text{Net Loss attributable to Equity Shareholders}}{\text{Weighted Average Number of Shares}} = \frac{(₹90{,}000)}{5{,}000 \text{ Shares}} = (₹18.00)$ per share (negative).

As per AS - 20, Basic and Diluted EPS should be presented with equal prominence for all periods presented, irrespective of a loss per Share, i.e. even if the amounts disclosed are negative.

Diluted EPS = (₹18.00) per Share (negative). Anti-dilutive effect of Potential Equity Shares, i.e. Stock Options will be ignored, (since this will reduce the Loss per Share).

(c) (i) UK International Ltd is developing a new production process. During the Financial Year ended 31st March 2014, the total expenditure incurred was ₹50 Lakhs. This process met the criteria for recognition as an Intangible Asset on 1st December 2013. Expenditure incurred till this date was ₹22 Lakhs. Further expenditure incurred on the process for the Financial Year ending 31st March 2015 was ₹80 Lakhs. As at 31st March 2015, the Recoverable Amount of Know-how embodied in the process is estimated to be ₹72 Lakhs. This includes estimates of future cash outflows as well as inflows. Calculate the amount to be charged to Profit and Loss A/c and Carrying Value of Intangibles as on the closing date in respect of Financial Year ending - 31st March 2014 and 31st March 2015. Ignore depreciation. [4]

Answer:

Expenditure charged to P&L A/c for 2013-2014: ₹22 Lakhs will be recognized as an Expense because the recognition criteria were not met until 1st December 2011. This expenditure will not form part of the cost of the Production Process recognized in the Balance Sheet.

Carrying Value of Intangibles as on 31.03.2014: The Production Process will be recognized (i.e. Carrying Amount) as an Intangible Asset at a cost of ₹28 Lakhs (expenditure incurred since the date the recognition criteria were met, i.e. on 1st December 2010).

Expenditure charged to P&L A/c for 2014-2015:

Particulars	**₹ Lakhs**
Book value on 31.03.2015 = Carrying amt. 31.03.2014 + Expenditure in 2014 – 2015 = 28 + 80	108
Less: Recoverable Amount	72
Impairment Loss to be charged to P & L A/c	**36**

Carrying Value of Intangibles as on 31.03.2015: The Production Process will be shown at Book Value ₹108 Lakhs, or Recoverable Amount ₹72 Lakhs, whichever is less, hence at ₹**72 Lakhs.**

(c) (ii) What are the accounting principles in respect of a Contingent Liability? [4]

Answer:

1. **No Recognition [Para 26]:** An Enterprise **should not recognise** a Contingent Liability.
   [Students may note the difference between Recognition & Disclosure. A Provision should be recognised and also disclosed. However, a Contingent Liability should not be recognized, but only disclosed.]
2. **Disclosure [Para 27]:** A Contingent Liability should be disclosed under Para 68, unless the possibility of an outflow of resources is remote.
3. **Joint and Several Liability for an obligation [Para 28]:** In respect of a Joint and Several Liability for an obligation -
   (a) **Other Parties' Share**: The part of the obligation that is expected to be met by other patties is treated as a Contingent Liability.
   (b) **Enterprise's Share**: The balance portion of the obligation related to the Entity should be recognized as Provision, except when no reliable estimate can be made.
4. **Periodical Review [Para 29]:** Contingent Liability should be periodically reviewed. On such review, if the character of the Contingent Liability is found to be changed and there is a probable outflow resources, then it will be recognized as a Provision and treated accordingly.

3. (Answer any 2 questions)

(a) The draft balance sheet of H Ltd. as on 31.03.15: (Figures in ₹ Lakhs)

Liabilities	Amount	Assets	Amount
Equity Share Capital (in equity shares of ₹ 10 each)	4.00	Fixed Assets less depreciation to date	6.00
10% Preference Share Capital	3.00	Stock and debtors	5.30
General Reserve	1.00	Cash and Bank	0.70
Profit & Loss Account	1.00		
Creditors	3.00		
	12.00		12.00

M Ltd. another existing company holds 25% of equity Share capital of H Ltd. purchased at ₹10 per share.

It was agreed that M. Ltd. should take over the entire undertaking of H Ltd. on 30.9.15 on which date the position of Current assets (except cash and bank balances) and creditors was as follows.

Stock and debtors	**4 lakhs**
Creditors	**2 lakhs**

Profits earned for half year ended 30.9.15 by H Ltd. was ₹ 90,000 after charging depreciation of ₹ 32,500 on fixed assets. H Ltd. declared 10% dividend for 2014-15 on 30.8.15 and the same was paid within a week.

Goodwill of H Ltd. was valued at ₹ 80,000 and block assets were valued at 10% over their book value as on 31.3.15 for purposes of take over. Preference shareholders of H Ltd. will be allotted 10% preference shares of ₹ 10 each by M Ltd. Equity share holders of H Ltd. will receive requisite number of equity shares of ₹ 10 each from M Ltd. valued at ₹ 10 per share.

- **Compute the purchase consideration.**
- **Explain, how the Capital reserve or goodwill, if any, will appear in the balance sheet of M Ltd. after absorption. [16]**

Answer:

Draft balance sheet of H Ltd. as at 30.09.15

Liabilities	Amount ₹	Assets		Amount ₹
Equity Share capital		Block Assets	6,00,000	
(40,000 equity shares of ₹ 10 each)	4,00,000	Less: Depreciation	(32,500)	5,67,500
10% Preference Share capital	3,00,000	Stock and Debtors		4,00,000
Reserves and surplus		Cash and Bank (balancing figure)		1,52,500
General Reserve	1,00,000			
Profit and Loss A/c*	1,20,000			
Creditors	2,00,000			
	11,20,000			**11,20,000**

Profit & Loss Account (draft)

Particulars	Amount
Opening Balance	1,00,000
Add: Half year profit	90,000
Less: Preference dividend @ 10%	(30,000)
Less: Equity dividend @ 10%	(40,000)
Closing balance	1,20,000

Purchase Consideration - Net Assets Method

Particulars	Amount	Amount
Fixed assets	6,60,000	
Stock and Debtors	4,00,000	
Cash and Bank	1,52,500	
Goodwill	80,000	12,92,500
Less: Creditors		(2,00,000)
Net Assets Taken over		**10,92,500**

Net Assets ₹ 10,92,500

Preference Shareholders ₹ 3,00,000 → Satisfied by issuing 10% preference share at par

Net Assets pertaining to Equity shareholders ₹7,92,500 → Proportionate net assets for the outside shareholders (75%) → 5,94,375

Total Purchase Consideration

	Particulars	Amount ₹
a.	10% Preference Share Capital	3,00,000
b.	Equity Share Capital (Outsiders)	5,94,375
c.	**Total**	8,94,375

Calculation of Capital Reserve

	Particulars		Amount ₹
a.	Net Assets takenover		10,92,500
b.	Less:		
	i) Preference shares to be alloted	3,00,000	
	ii) Equity shares to be allotted	5,94,375	

	iii) Cost of Investments	1,00,000	(9,94,375)
c.	**Capital Reserve**		**98,125**

Balance sheet of M Ltd. as on 30th September 2015 (Extracts)

Liabilities	₹	Assets	₹
		Intangible Assets	
		Capital Reserve	98,125
		Less: Goodwill	80,000
			18,125

(b) (i) TQM Ltd. group has three divisions T, Q, M. details of their turnover, results and net assets are given below:

	(₹ in lakhs)
Division T	
Sale to Q	**3,050**
Other sales (Home)	**60**
Export sales	**4,090**
	7,200
Division Q	
Sale to M	**30**
Export sales to Europe	**200**
	230
Division M	
Export sales to America	**180**

		Division		
	Head Office	**T**	**Q**	**M**
	(₹ in lakhs)	**(₹ in lakhs)**	**(₹ in lakhs)**	**(₹ in lakhs)**
Operating Profit or loss before tax		**160**	**20**	**(8)**
Re-allocated cost from Head Office		**48**	**24**	**24**
Interest cost		**4**	**5**	**1**
Fixed assets	**50**	**200**	**40**	**120**
Net current assets	**48**	**120**	**40**	**90**
Long-term liabilities	**38**	**20**	**10**	**120**

Prepare a Segmental Report for publication in TQM Ltd. Group. **[10]**

Answer:

TQM Ltd.
Segment Report **(₹ in Lakhs)**

	Divisions				
	T	**Q**	**M**	**Inter segment Elimination**	**Consolidated Total**
Segment Revenue Sales:					
Domestic	60	-	-	-	60
Export	4,090	200	180	-	4,470
External Sales	4,150	200	180	-	4,530
Inter-segment sales	3,050	30	-	3,080	-
Total Revenue	7,200	230	180	3,080	4,530

Segment result (given)	160	20	(8)	-	172
Head office expenses					(96)
Operating profit					76
Interest expense					10
Profit before tax					66
Other information					
Fixed Assets	200	40	120	-	360
Net current assets	120	40	90	-	250
Segment Assets	320	80	210	-	610
Unallocated corporate assets					98
Segment Liabilities	20	10	120		150
Unallocated corporate liabilities					38

Sales Revenue by Geographical Market

	Home Sales	Export Sales (by division T)	Export to Europe	Export to America	Consolidated Total
External Sales	60	4,090	200	180	4,530

(b) (ii) The BBK Co. Ltd. resolved by a special resolution to buy – back 1,50,000 of its equity shares of the face value of ₹10 each on which ₹8 has been paid up. The general reserve balance of the company stood at ₹40,00,000 and no fresh issue of shares was made.
Journalize the transactions. [6]

Answer:

In the Books of BBK Co. Ltd.
Journal Entries

Date	Particulars	Debit ₹	Credit ₹
	Equity share Final Call A/c Dr. To Equity Share Capital A/c (Final call of ₹2 per share due on 1,50,000 equity shares as per Board resolution)	3,00,000	 3,00,000
	Bank A/c Dr. To Equity Share Final call A/c (Final call money on 2,00,000 shares received)	3,00,000	 3,00,000
	Equity Share capital A/c Dr. To Equity Shareholders A/c (Amount due to Equity shareholders transferred to their account for Buy Back)	15,00,000	 15,00,000
	Equity Shareholders A/c Dr. To Bank A/c (Payment to shareholders towards buy-back)	15,00,000	 15,00,000
	General Reserve A/c Dr. To Capital redemption reserve A/c (Transfer of nominal value of shares bought- back.)	15,00,000	 15,00,000

(c) (i) Following information relates to Ping-Pong Ltd. State under which heads these items will appear in the Balance Sheet as per Schedule III ?

- **2,00,000 8% Preference Share of ₹100 each.**
- **Investment of ₹45,00,000 in 40,000 12% Debenture of ₹100 each of Amrit Ltd.**
- **License of ₹18,00,000 for Mining Right.**
- **Provision for taxation of ₹88,000. [4]**

Answer:

As per Schedule III —

- 2,00,000 8% Prefence Shares of ₹100 each will come under : Equity and Liabilities – Shareholders' funds - Share Capital.
- Investment of ₹45,00,000 in 40,000 12% Debenture of ₹100 each of Amrit Ltd. will come under: Assets - Non-current Assets – Non-current Investments.
- License of ₹18,00,000 for Mining Right : Assets - Non-current Assets – Intangible assets.
- Provision for taxation of ₹88,000 will come under: Equity and Liabilities – Current Liabilities – Short-term Provision.

(c) (ii) Banana Ltd. has furnished that the net profit before tax and managing director's remunerations is ₹5,85,60,000, after adjusting the Depreciation as per books of ₹71,00,000 (Depreciation as per schedule II is ₹80,00,000), provision for doubtful debts of ₹80,000. The managing director's remuneration is at 5% of Net Profit as per law subject to maximum of ₹2,40,000 p.a. Compute the Managing Director's remuneration. [6]

Answer:

Computation of managing director's remuneration

Particulars	₹000's
Net profit before tax and managing director's remuneration	58,560
Add: Depreciation as per books	7,100
Provision for doubtful debts	80
	65,740
Less: Depreciation as per schedule II to Companies Act, 2013	(8,000)
Net profit for the purpose of Managerial remuneration	57,740
Maximum managerial remuneration at 5% of net profit	2,887
Restricted to actual under the agreement	240

(c) (iii) Discuss the three types of Cash Flows in the context of AS - 3. [6]

Answer:

Cash Flow Statement explains cash movements under three different heads, namely

- Cash flow from operating activities;
- Cash flow from investing activities;
- Cash flow from financing activities.

Sum of these three types of cash flow reflects net increase or decrease of cash and cash equivalents.

Operating activities are the principal revenue - producing activities of the enterprise and other activities that are not investing and financing. Operating activities include all transactions that are not defined as investing or financing. Operating activities generally involve producing and delivering goods and providing services.

Investment activities are the acquisition and disposal of long term assets and other investments not included in cash equivalents.

Financing activities are activities that result in changes in the size and composition of the owners' capital (including preference share capital in the case of a company) and borrowings of the enterprise.

4. (Answer any 2 questions)

(a) (i) Difference between Statutory Audit and Government Audit. [6]

Answer:

The following are the differences between Statutory Audit and Government Audit:

SL. No.	Statutory Audit	Government Audit
i.	Applicable to (a) All private companies (b) All co-operative societies (c)Proprietorship and partnership concerns in some cases. E.g. Tax audit under Income Tax Act.	Applicable to (a) Government departments (b) Statutory corporations (c) Government companies
ii.	(a) In case of private companies: shareholders. (b) In case of sole proprietor and partnership: proprietor or partners. (c) In case of trust: trustee or Managing Committee. (d) In case of co-operative societies: Managing Committee with prior approval of the Registrar.	(a) In case of government departments: Comptroller and Auditor General (b) In case of statutory corporation: as per the provisions of the special statute for that corporation. (c) In case of government company: Company Law Board, on the advice of the Comptroller and Auditor General.
iii.	Report is submitted to the owners/ shareholders in a format prescribed by the Companies Act, in the case of Companies.	Report is submitted to the shareholders and a copy is given to the Comptroller and Auditor General in a format prescribed by the CAG.

(ii) Write a note on — Adverse or Negative Audit Report. [4]

Answer:

Adverse or Negative Audit Report —

An Adverse or Negative Report is given when the Auditor concludes that based on his examination, he does not agree with the affirmations made in the Financial Statements / Financial Report. The Auditor states that the Financial Statements do not present a true and fair view of the state of affairs and the working results of the organisation. The Auditor should state the reasons for issuing such a report.

An Adverse Opinion should be expressed when the effect of a disagreement is so material and pervasive to the Financial Statements, that the Auditor concludes that a qualification of the report is not adequate to disclose the misleading or incomplete nature of the Financial Statements.

(iii) "Teeming & Leading is a commonly followed method of misappropriation of cash" — Discuss. [6]

Answer:

Teeming & Leading is a commonly followed method of misappropriation of cash by concealing cash shortages and covering them through recoveries from another customer. It is not uncommon in case of cash collections if the internal check and internal control on cash transactions are not proper. E.g., a salesman recovers ₹10,000 from customer C and misappropriates the same, but to conceal the misappropriation, he declares ₹10,000 received later from another customer D as received from C so that the balance of C confirms to the client's debtor list, and so on for recovery from E of same amount declared as from D.

Teeming and leading may not amount to fraud, but negligence on the part of the management and weaknesses in internal checks or controls may lead to substantial amounts being misappropriated by the cashier. This may result in a huge loss if he is not in a position to clear the debts when caught.

The auditor has to follow the following procedure for timely detection of teeming and leading:

i. Ascertain if the Cash Memos are consecutively numbered, and the dates, name and amount as per the Daily Summary reconcile with relevant cash receipt records.
ii. Reconcile individual cash amounts as per receipts with records in the Rough Cash Book.
iii. Reconcile the receipts as recorded in the Rough Cash Book, main Cash Book, pre-numbered Cash Memos, with counterfoils of the pay-in-slips.
iv. Ensure whether cash receipts are deposited in the bank on a timely basis.
v. Examine the Debtors Ledger, especially entries showing part payments, to satisfy that the debtors concerned have indeed made part payments.
vi. Confirmations may be obtained from the debtors from time to time.

(b)(i) State the meaning of Continuous Audit and the advantages of Continuous Audit. [3+5=8]

Answer:

Continuous audit involves the detailed examination of all the transactions by the auditor continuously throughout the year or at regular intervals, say fortnightly or monthly. A continuous audit is one which is commenced and carried on before the close of the financial year to which it relates. It involves the constant engagement of auditor's staff at the client office throughout the period under review.

Continuous audit is suitable in cases where the final accounts are desired to be presented soon after the close of the financial year or there is great volume of transactions or the system of internal check is weak.

Advantages of Continuous Audit are:

- A close and extensive examination of accounts is possible as the auditor gets a full year for this purpose.
- The errors and frauds can be detected and rectified soon.
- A regular supervision by the auditor brings increased efficiency and accuracy in the accounts of the enterprise.
- Better MIS system because of availability of updated and accurate accounts.
- Continuous audit create more check on the client's staff.
- The auditor can have much better understanding of the client's business and thus he can suggest the client the ways to improve operational efficiency.
- The final accounts can be prepared and reported upon soon after the end of the financial year.
- It also facilitates auditor to schedule his work in convenient manner and avoid the pressure that may mount at the close of financial year.

(ii) Discuss the types of analysis that are covered by analytical procedures. [5]

Answer:

Analytical procedures include the analysis of comparisons of the entity's financial information with, for example:
• Comparable information for prior periods.
• Anticipated results of the entity, such as budgets or forecasts, or expectations of the auditor, such as an estimation of depreciation.
• Similar industry information, such as a comparison of the entity's ratio of sales to accounts receivable with industry averages or with other entities of comparable size in the same industry.

Analytical procedures also include the analysis of relationships, for example:
• Among elements of financial information that would be expected to conform to a predictable pattern based on the entity's experience, such as gross margin percentages.
• Between financial information and relevant non-financial information, such as payroll costs to number of employees.

(iii) Discuss the features of Internal Audit. [3]

Answer:

Following are the features of an Internal Audit —

- It is an independent appraisal activity within the organization.
- It can be conducted by the staff of the entity or by an independent professional appointed for that purpose.
- It is conducted for review of accounting, financial and other operations and controls established within an organization.
- It is conducted as a service to the organization and is not a part of the organization.
- It intends to furnish the analysis, appraisals, suggestions and information concerning the activities reviewed to the management.
- Internal auditing functions as a continuous effort for promoting effective control at cost reasonable cost

(c) (i) Discuss the reasons for conducting Information Systems Audit. [6]

Answer:

According to Ron Weber, "Information systems auditing is an organizational function that evaluates asset safeguarding, data integrity, system effectiveness, and system efficiency in computer based information systems. It has arisen for seven major reasons:

i. The consequences of losing the data resource;

The possibility of misallocating resources because of decision based on incorrect data or decision rules;

ii. The possibility of computer abuse if computer systems are not controlled;

iii. The high value of computer hardware, software, and personnel;

iv. The high costs of computer error;

v. The need to maintain the privacy of individual persons; and

vi. The need to control the evolutionary use of computers."

(c) (ii) List the areas to be covered while auditing the payment for acquisition of an asset. [4]

Answer:

Following are the areas to be covered while auditing the payment for acquisition of an asset —

i. The payment for acquisition of assets should be made under proper authorization and be duly supported by receipt for amount paid.

ii. Check the title deeds in case of purchase of immovable properties. Also ensure that the ownership in case of the moveable asset has been registered in the name the purchaser.

iii. The auditor should also verify the existence, value and the title of the assets acquired.

iv. In case of a company, ensure that the provisions of section 179 of the Companies Act, 2013 have been complied with.

v. Check that the cost of the asset purchased has been properly capitalized in the books of account. Thus, the amounts paid to bring the asset to their present condition or location and, incurred upto the asset being put into use should be capitalized. Further such taxes (e.g. CENVAT) which are recoverable from the authorities shall not form the part of cost of the asset.

(c) (iii) Write a note on Internal Audit Documentation as per Standards on Internal Audit (SIA) – 3. [6]

Answer:

Internal Audit Documentation as per Standards on Internal Audit (SIA) – 3:

i. Internal audit documentation should be designed and properly organized to meet the requirements and circumstances of each audit. To formulate policies for standardization of internal audit documentation.

ii. It should be sufficiently complete and detailed for an internal auditor to obtain an overall understanding of the audit.

iii. All significant matters which require exercise of judgment, together with internal auditor's conclusion thereon should be included in the internal audit documentation. Documentation prepared by internal auditor should enable reviewer to understand:

- the nature, timing and extent of audit procedures performed to comply with SIAs and applicable legal and regulatory requirements;

- the results of audit procedures and audit evidence obtained;
- significant matters arising during the audit and conclusions reached thereon; and
- terms and conditions of an internal audit engagement/requirements of internal audit charter, scope of work, reporting requirements, any other special conditions, affecting the internal audit.

iv. It should cover all the important aspects of an engagement viz., engagement acceptance, engagement planning, risk assessment and assessment of internal controls, evidence obtained and examination/evaluation carried out, review of the findings, communication and reporting and follow up.

v. The internal audit file should be assembled within sixty days after the signing of the internal audit report.

vi. To formulate policies as to the custody and retention of the internal audit documentation within the framework of the overall policy of the entity in relation to the retention of documents.