

Paper 12- Company Accounts & Audit

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Full Marks:100

Time allowed: 3 hours

Section A

I. Answer all the following questions.

1. Answer the following questions:

[5 × 2 = 10]

(a) As per AS – 12 Accounting for Government Grants related to non-depreciable assets should be credited to Capital Reserve

In the Books of P Ltd.

Particulars	Dr.(₹)	Cr.(₹)
On purchase of land		
Land A/c Dr.	60,00,000	
To, Bank A/c		60,00,000
On receipt of Government Grant		
Bank A/c Dr.	30,00,000	
To, Capital Reserve A/c		30,00,000

- (b) (i) Recognition of events and transactions in the financial statements.
(ii) Measurement of their transactions and events.
(iii) Presentation of these transactions and events in the financial statements in a manner that is meaningful and understandable to the reader.
(iv) Disclosure requirements which should be there to enable the public at large and the share holders and the potential investors in particular to get an insight into what these financial statements are trying to reflect and facilitating them to take prudent and informed business decisions.

(c)

Journal Entries

	Particulars	Dr.(₹)	Cr.(₹)
31.03.2012	Investment in Debenture A/c Dr.	94,500	
	Interest A/c (1,00,000 × 6% × 1/12) Dr.	500	
	To, Bank A/c		95,000
	(Being the purchase of 1,000 6% debentures of ₹100 each at ₹95 each cum interest)		

(d) It is duty to perform in a particular manner, for example to Interest of a loan at the end of every quarter and repay the principle on a specific date.

It may be legally enforceable but that not a necessary condition.

Obligation also arises, however from normal business practice custom and a desire to maintain good business relating or act in a equitable manner. An announcement to pay bonus to employee becomes an obligation because of normal business practice (or) although there is no legally enforceable agreement.

(e) It is an option which is managed and financed in such a manner that any change in the exchange rate has almost immediate effects on the cash flow of the reporting enterprise. Further they are also seem as an extension of the operation of the reporting enterprise.

Example: Foreign branch

2. Match the following:

[5×1=5]

Answer to MTP_Intermediate_Syllabus 2012_June2016_Set 1

1.	AS 2	C	Valuation of Inventory
2.	AS 6	D	Depreciation Accounting
3.	AS 7	A	Construction Contract
4.	AS 9	E	Revenue Recognition
5.	AS 10	B	Accounting for Fixed Assets

3. Answer the following:

[5×2=10]

(a) The act of examining all documentary evidence is referred to as vouching. Its basic objective is to establish the authenticity of the transactions recorded in the primary books of accounts. Vouching is said to be "the essence of auditing (or) may be termed as the backbone of auditing; It serves as evidence, assurance, preliminary for verification, establisher's authenticity.

(b) Three component of audit risk:

Inherent risk (risk that material error will occur).

Control risk (risk that the clients system of internal control will not prevent (or) correct such error).

Detection risk (risk that any remaining material error will not be detected by the auditor).

(c) Debentures may be issued to creditors, bankers (or) any other persons without receiving any cash thereon. Here its acts as a Co-lateral Security and becomes real debentures in the event of the default of the loan.

Auditor's duty:

He should see that such debentures do not appear in the liabilities side of the B/S, but are shown by way of note under the head loan.

He should ensure that necessary entries made in the register of mortgages and that the necessary papers are filed with the register of companies.

He should also examine the loan agreement and conform that it has been approved by the board.

(d) While auditing the auditor came across various assertions of the management. The auditor has to evaluate these accessories so that he would be able to express his opinion on the financial statements. This evaluation can be made in the light of same facts and reasons. These facts and reasons are called audit evidence. The auditor should evaluate whether he has obtained sufficient appropriate audit evidence. So that reasonable conclusions can be drawn there from.

(e) Any reserve not appearing on the Balance Sheet is called as a Secret reserve. The existence of the reserve may infer from an intelligent Verification of the accounts by the auditor even though the amount cannot be ascertained. Generally such type of reserve appears in financial Institution and Insurance Companies.

Section B

II. Answer any three of the following

[3×15=45]

4. (a) AS-11 Exchange difference arising on the settlement of monetary items or on reporting an enterprises monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements. Should be recognized as income (or) as expenses in the period in which they arise. Exchange difference arising on repayment of liabilities incurred for the purpose of acquiring fixed assets are recognized as incomes (or) expenses.

Exchange:

Answer to MTP_Intermediate_Syllabus 2012_June2016_Set 1

Foreign exchange loan = $6000 / 40 = \text{US\$ } 150 \text{ Lakhs}$
 Exchange difference = $\text{US\$ } 150 \text{ Lacks} \times (45-40) = \text{₹}75,000,000$

Treatment:

Loss due to exchange difference amounting to ₹750 lacks should be charged to P/L A/c for the year ended 31-3-2013, depreciation of ₹1200 lacks (20% of ₹6000 lacks) should be provided in the financial statements for the year ended 31-3-2013.

(b) Computation of EPS

Particulars	Earnings	Shares	EPS
Net profit for the year 2013-14	₹30,00,000	-	-
No. of shares outstanding during 2013-14	-	12,00,000	-
Basic EPS [₹30,00,000/12,00,000]	-	-	₹2.50
No. of shares under option	-	2,00,000	-
No of shares that would have been issued at fair value [2,00,000 shares × 15/25]	-	(1,20,000)	-
Diluted EPS [₹30,00,000 / 12,80,000]	-	-	₹2.34
	₹30,00,000	12,80,000	₹2.34

5. (a) Shares outstanding test:

Maximum no. of shares that can be brought back 25% of 33 ⇒ 8.25 crores

Resource test:

25% of (paid up capital + free reserve)
 25% of ₹(330+420) / ₹30 ⇒ 6.25 crores

Debit equity ratio test:

1. Loan funds	₹1,000
2. Maximum equity to be maintained after buy back is 2:1	₹500
3. Present share holders funds	750
4. II – III	Nil
5. Maximum no. of share that can brought back @ 30	Nil

The company is not eligible to buy back shares.

(b)

Journal Entries

Particulars	Dr.(₹)	Cr.(₹)
Bank A/c To Share application & allotment A/c (Being money received in respect of 8000 shares at 115 each).	Dr. 9,20,000	9,20,000
Share application & allotment A/c To Share capital A/c To Securities premium A/c (Being T.V. of money received on 8000 shares to Capital A/c and Securities premium A/c @100 and 15 respectively).	Dr. 9,20,000	8,00,000 1,20,000

Answer to MTP_Intermediate_Syllabus 2012_June2016_Set 1

A A/c To Share capital A/c To Securities premium A/c (Being the amount due on 1800 shares taken up in terms of underwriting agreement by A).	Dr.	2,07,000	1,80,000 27,000
Underwriting commission A/c To A A/c (Being Commission @1% on 9000 shares at 100 each)	Dr.	9,000	9,000
Bank A/c To A A/c (Being the money received from the broker is settlement of A/c)	Dr.	1,98,000	1,98,000

Working note:

Particulars	A	Company
Gross liability	9000 shares	1000 shares
(-) Application received allotted in the ratio of 9:1	7200 shares	800 shares
	1800 shares	200 shares

Note: (It has been assumed that the receiving 10% of the shares are undertaken by the company itself).

6. (a) Calculation of finance charges for each year

Year	Finance charges (₹)	Payments (₹)	Reduction in o/s liability (₹)	Outstanding liability (₹)
1st year beginning	-	-	-	6,99,054
1st ending	1,04,858	3,00,000	1,95,142	5,03,912
II year ending	75,587	3,00,000	2,24,413	2,79,499
III year ending	41,925	3,00,000	2,58,075	21,424

Present value of minimum lease payment

Annual lease × p.v. factor + present value of guaranteed residual value

$$₹ 3,00,000 \times (0.869+0.756+0.657) + ₹ 22,000 \times 0.657$$

$$₹ 6,84,600 + ₹ 14,454 \Rightarrow ₹ 6,99,054$$

Value of machinery:

Fair value of machinery is ₹ 7,00,000; the N.P value of minimum lease payment is ₹ 6,99,054.

As the present value of the machine is less than the fair value of the machine. The machinery will be recovered at the value of ₹ 6,99,054.

(b) According to AS-17 segment reporting a business segment (or) geographical segment should be identified as a reportable segment. If —

- (a) Its revenue from sales to external customers and from transactions with other segment is 10% (or) more of the total revenue external and internal of all segments (or)
- (b) Its segment result whether profit (or) loss is 10% (or) more of the combined result of all segments in profit (or) the combined result of all segments in loss. Whichever is greater in absolute amount (or)
- (c) Its segment assets are 10% (or) more of the total assets of all segments.

Answer to MTP_Intermediate_Syllabus 2012_June2016_Set 1

If total external revenue attributable to reportable segment constitute less than 75% of the total enterprise revenue, additional segments should be identified as reportable segments, even if they do not meet the 10% threshold until at least 75% to total enterprise revenue is included in reportable segment.

Following segments are reportable segments.

Basic	Reportable segment
Segment revenue	A & B
Segment result	A, B & F
Segment assets	A, B, C, D & E

Hence the contention of the finance Director that only segment A and B need reporting is not correct as all the six segments are reportable segments.

7. (a) Liquidator's Statement of Account

Receipts	Amount(₹)	Payments	Amount(₹)
Assets realized	3,95,000	Liquidator's remuneration	1,000
Call on Contributor's On 2000 shares @ ₹4 On 1000 shares @ ₹11	8,000 11,000	Unsecured creditors	99,000
		Preferential share holders	3,00,000
		Equity share holders (500 E.S @ ₹28)	14,000
	4,14,000		4,14,000

Working Note:

Calculations of % of deficiency.

a. Total paid up share capital	₹1,75,000
b. (+) cash deficit	₹5,000
c. Total deficiency to be borne (a+b) ⇒	₹1,80,000
d. Total nominal share capital	₹2,50,000
e. Deficiency = (c/d x 100)	72%

Calculation of Net amount returnable/receivable per share

	A	B	C
Paid up value per share	₹100	₹50	₹25
b. deficiency @72% on nominal value	₹72	₹54	₹36
c. Net amount receivable/returnable	₹28	(₹4)	(₹11)

(b)

Journal entries in the books of X Ltd.

Particulars	Dr.(₹)	Cr.(₹)
Equity share capital A/c To Share surrender A/c To Equity share capital A/c (Being the sub-division of 10,000 E.S @100 in to 1,00,000 E.S of 10 each and 50% of shares are surrendered by share holders)	Dr. 10,00,000	 5,00,000 5,00,000
15% Debentures A/c Accrued Interest A/c To Capital reduction A/c (Being 50% of debentures are converted into 10% pref. share and 50% of debenture are transfer to capital reduction A/c)	Dr. Dr. 1,50,000 22,500	 1,72,500

Answer to MTP_Intermediate_Syllabus 2012_June2016_Set 1

Creditors A/c To Capital reduction A/c (TV of claims of the creditors to capital reduction A/c 25% of which is reduction and equity share are issued in consideration of the balance amount)	Dr.	52,000	52,000
Share surrender A/c To 10% Preference share capital A/c To Equity share capital A/c To Capital reduction A/c (Being the balance in share surrender A/c is transferred to Capital reduction A/c)	Dr.	5,00,000	1,00,000 39,000 3,61,000
Capital reduction A/c To P/L A/c To Capital reduction A/c (Being the Capital reduction A/c balance is used to write off Debit balance of P/L A/c).	Dr.	5,85,000	5,80,000 5,500

Balance sheet of X Ltd and reduced as at 31-3-2013

Particulars	Note No.	Amount (₹)
(I) Equity & Liabilities		
(i) <u>Share holder funds:</u>		
(a) Share capital	1	6,39,000
(b) Reserves & Surplus		5,500
(ii) <u>Long term Borrowings:</u>		
15% Debentures	-	1,50,000
(iii) <u>Current Liabilities:</u>		
(a) Trade payable	-	-
(b) Short term provisions	-	36,000
(c) Other current liabilities (outstanding interest)	-	22,500
Total		8,53,000
(II) Assets		
(i) <u>Non – Current assets</u>		
(a) Fixed assets:		
Tangible assets	-	3,50,000
(ii) <u>Current assets:</u>		
(a) Inventory	-	2,53,000
(b) Trade receivables	-	2,30,000
(c) Cash & cash equivalents	-	20,000
Total		8,53,000

Note: 1

Share Capital

53,900 E.S @ 10 each =	5,39,000
10,000 10% P.S @ 10 each	<u>1,00,000</u>
	<u>6,39,000</u>

- 8. (a)** Cash sales are generally open to a wide scope for commission of frauds and these may be prevented only by an effective system of Internal checks and controls.

After ascertaining the efficiency of the Internal check system of cash controls as detailed above, the auditor should vouch cash sales as follows:

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Sl. No.	Evidences Relevant	Audit Procedures
(I)	Compliance of accounting manual or laid down control systems.	To Evaluate that the system laid down is proper and the same is being adhered to.
(II)	Separate authority to deliver goods and collect cash.	To ensure that the sales man have no authority to deliver the goods to, or receive cash from, the customers.
(III)	Three copies of cash memo.	To verify that there should be at least three copies, preferably in different colors and clearly marked on it the purpose "Original for customers" and the second copy for the Delivery Counter are to be delivered to the customer. The third (book copy) remains with the respective sales man.
(IV)	Stamp-marking by cashier as "paid".	To ensure that the Customer present both the copies to the Cashier who, upon receiving the payment and stamp-marking the copies as "paid" returns the same to the customer.
(V)	One copy retained by Delivery Counter.	To verify that the second copy with "paid" stamp is handed over to, and retained by the delivery clerk for his own record of out go.
(VI)	Daily cash sales summary for Reconciliation.	To verify that the pre-numbered Cash memos are reconciled with Daily Cash summary and that any mission number is vouched for to be recorded in it.
(VII)	<ul style="list-style-type: none"> • Bank pay-in-slips • Cash Book • Bank Book • Bank statement 	To check daily deposit of cash as per cash sales summary.

(b) Objectives of Internal Control:

Each Organisation must have a system of Internal Control in place for achieving the present goals. Other than accomplishing the desired goals and objectives of the organization, this system plays a very important role in any organization. The main objectives of Internal Control are as follows:

(i) Compliance:

To have compliance with law and the accounting practices generally accepted and followed in the country. The accounting process also needs to be in compliance with these.

(ii) Reliance

To Increase the reliance on the Internal Systems People and accounting practices followed by the organization, so that chances of frauds are reduced.

(iii) Safeguarding:

To safeguard the Organisation's accounts, employees and assets by formation of fool-proof policies, rules and regulations.

(iv) Security:

To provide security to customers, employees and property of the organization. physical security system like security guards, locks and anti-theft devices are used for providing protection.

(v) Increased Efficiency:

To assist in human resources and performance management, and to keep proper controls over business activities to achieve maximum levels of efficiency.

(vi) Evaluation:

To evaluate the accounting system for proper authorization of transactions.

Answer to MTP _Intermediate_ Syllabus 2012_ June2016_ Set 1

(vii) Review and Correction:

To review the working of the business, locate weak points in operations and to take Corrective measures for proper working.

(viii) Authorisation:

To provide proper authority for purchase, sale, valuation and possession of assets.

9. (a) Procedure for appointing the auditor of a company is as follows.

First Auditor:

- First auditor of the company, other than a government company, shall be appointed by the BOD within 30 days from the date of registration of the company.
- If BOD fails to appoint, by the member of the company within 90 days at an extraordinary general meeting appoint the first auditor.
- In case of Government company, first auditor shall be appointed by CAG within 60 days from the of registration.
- If CAG fails to appoint, by the BOD of the company within next 30 days.
- If again BOD fails to appoint the first auditor of the company by the member of the company within 60 days at an extraordinary general meeting.
- Tenure of the fist auditor of the company both above cases till the conclusion of the first annual general meeting.

Sub-sequent Auditor:

- At the first annual general meeting, appoint an Individual or firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting.
- Before such appointment, the written consent of the auditor to such appointment and a certificate from him shall be in accordance with the condition as may be prescribed.
- Within 15 days of the meeting the company shall file a notice of such appointment with the registration.
- No listed company or a company belonging to such class or classes of companies as may be prescribed shall appoint or re-appoint.
 - a. An Individual as auditor for more than one term of five consecutive years; and
 - b. An audit firm as auditor for more than two term of five consecutive years.

(b) An auditor appointed under that act shall provide to the company only such other services as are approved by the board of director or the audit committee, as the case may be. But which shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company, namely:

- a. Accounting and book keeping services
- b. Internal audit
- c. Design and Implementation of any financial information system
- d. Actual services
- e. Investment advisory services
- f. Investment banking services
- g. Rendering of outsourced financial services
- h. Management services; and
- i. Any other kind of services as may be prescribed.

Answer to MTP_Intermediate_Syllabus 2012_June2016_Set 1

Provided that an auditor firm who or which has been performing any non-audit services on or before the commencement of this Act shall comply with the provisions of this section before the closure of the first financial year after the date of such commencement.

10. (a) Declaration of dividend [Section 123]

Final dividend is declared in the general meeting. Board of directors has to recommend a dividend. Declaration of dividend is "Ordinary Business" in general meeting.

No dividend shall be declared or paid by a company for any financial year except –

- a) Out of the profits of the company for that year arrived at after providing for depreciation in accordance with the provisions of Sub Section (2), or out of the profits of the company for any previous year or years arrived at after providing for depreciation in accordance with the provisions of that sub-section and remaining undistributed, or out of both; or
- b) Out of money provided by the Central Government or State Government for the payment of dividend by the company in pursuance of a guarantee given by the Government.

Provided that a company may, before the declaration of any financial year, transfer such percentage of its profits for that financial year as it may consider appropriate to the reserves of the company.

Interim dividend:

The Board of Directors of a company may declare Interim dividend during the any financial year out of the surplus in the profit and loss account and out of profits of the financial year in which such Interim dividend is sought to be declared.

Declaration of Interim dividend if the company has Incurred losses in Current financial year:

In case the company has Incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of Interim dividend shall not be declared at a rate higher than the average dividend declared by the company during the Immediately preceding three financial years.

Legal provisions applicable to Interim dividend:

The amount of the dividend, including Interim dividend, shall be deposited in a scheduled bank in a separate account within five days from the date of declaration of such dividend.

Unpaid Dividend Account [Section 124]

Transfer of unpaid dividend to separate account:

Where a dividend has been declared by a company but has been paid or claimed within thirty days from the date of the declaration to any share holders entitled to the payment of the dividend, the company shall, within seven days from the date of expiry of the said period of thirty days, transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in that behalf in any scheduled bank to be called the "Unpaid Dividend Account".

(b) The following steps would be required to conduct an audit from incomplete records:

- (i) Ascertain that the balance sheet or statement of affairs as at the beginning of the year should be prepared and all the relevant accounts should be opened in the

ledger. Normally under the single entry system, cash, bank and personal accounts are maintained.

- (ii) Confirming that all entries on receipts side of the cash book are posted in the ledger, even by opening new accounts (s) wherever necessary.
- (iii) Check that all entries on the payment side of cash book are posted in the ledger.
- (iv) Confirming that all entries appearing in bank account is posted in the ledger.
- (v) Analyse personal accounts of debtors. This will provide vital Information regarding credit sales, Sales returns, Discount allowed, bill received, bill dishonoured, etc. It would be necessary to post such items to relevant account, to complete the double entry from the debtors accounts.

Similarly, It would be necessary to analyse the creditors accounts and post entries relating to credit purchase made, discounts earned, Purchase returns, bills payable issued to suppliers, bill payable dishonoured etc. to relevant accounts.