Paper 12- Company Accounts & Audit

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Full Marks: 100 **Time allowed: 3 hours**

Section – A

Question no. 1 is compulsory

I. Answer all the following questions:

1. (a) Answer the following questions: **[5×2=10]**

Foreign currency creditors at the end of the financial year are USD 10 Lakhs. Purchase were recorded at the exchange rate USD 1= ₹52. On the balance sheet date, the exchange rate is USD 1 = ₹54 which is not expected to be payable on the payment date. It has been estimated that around the payment time, the exchange rate will possibly be in the range of USD 1 - ₹55.00 to ₹56.50. At what value should the creditors be recorded in the balance sheet? What is the treatment of foreign exchange loss?

Answer:

Creditors should be recorded at the expected payable value, i.e. Average Expected Rate = (₹55.00 + ₹56.50) ÷ 2 = ₹55.75 per USD. The amount of creditors recognized in the Balance Sheet shall be ₹55.75 x 10 Lakhs USD = ₹557.50 Lakhs.

Treatment of foreign exchange loss –

The Exchange Loss of (₹55.75 – ₹52) x 10 Lakhs USD = ₹37.50 Lakhs should be recognized as loss in the Profit & Loss account.

(b)The share capital of M Ltd. consists of 1,00,000 equity shares of ₹10 each, and 25,000 preference shares of ₹100 each, fully called up. Besides, its securities premium account shows a balance of ₹40,000 and general reserve of ₹7,00,000. The company decides to buy-back 30,000 equity shares of ₹12 each. For this purpose, it utilises the securities premium in full and general reserve to the extent necessary.

Pass the necessary journal entries only showing the effects on the securities premium account and the general reserve account.

Answer:

Journal Entries

Particulars		Dr. (₹)	Cr.(₹)
Equity Share Capital A/c	Dr.	3,00,000	
Securities Premium A/c	Dr.	40,000	
General Reserve A/c	Dr.	20,000	
To, Equity Shareholders A/c			3,60,000
(Being the amount due to equity shareholders for buying-back of 30,000 equity shares)			
General Reserve A/c	Dr.	3,00,000	
To, Capital Redemption Reserve A/c			
(Being the nominal amount or equity shares bought back transferred)			3,00,000

(c) Income from operating Activities is ₹90 lakhs;
Fixed Asset sold for ₹120 lakhs;
Machinery purchased for ₹150 lakhs;
Income from Financing Activities is ₹(20) lakhs, copute the net effect on cash Flow.

Answer:

Particulars	₹ in lakhs	₹ in lakhs
Cash flow from operating Activities		90
Cash flow from Investing Activities		
Sale of fixed Asset	120	
Purchase of machinery	150	(30)
Cash flow from Financing Activities		(20)
Net increase Cash Flow		40

(d) Mugdha Ltd. purchased a machinery of ₹20,00,000 from Machinery Mart. The consideration was paid in the form of fully paid up equity shares of ₹10 each at 60% premium. Pass necessary journal entries in the books of Mugdha Ltd.

Answer:

Journal Entries
In the books of Mugdha Ltd.

Particulars		Dr. (₹)	Cr. (₹)
Machinery A/c	Dr.	20,00,000	
To Machinery Mart A/c			20,00,000
(Being Machinery purchased)		20,00,000	
Machinery Mart A/c	Dr.		12,50,000
To Equity Share Capital A/c			7,50,000
To Securities Premium A/c			
(Being Equity Shares issued as purchase consideration)			

(e) State the disclosure requirement of the following items as per schedule III:

- **Debit balance of Profit & Loss account**
- **Unsecured Bank loan**

Answer:

- **Debit balance of Profit & Loss account -** To be shown/ adjusted as a negative figure under "Reserves & Surplus".
- **Unsecured Bank loan -** If it is repayable after 12 months – to be sub-classified under "Long-term Borrowing" to be presented as a separate line item. Also state the terms of repayment, and if it is repayable within twelve months – to be sub – classified under "other current liabilities". To be shown as a separate line item.

2. Match the following: **[5×1=5]**

1.	**AS - 17**	**B**	**Premium on issue of shares**
2.	**Tax paid**	**D**	**Segmental Reporting**
3.	**Capital profit**	**A**	**Dividend unpaid**
4.	**Contingent Liability**	**E**	**Revenue expenditure**
5.	**Current Liability**	**C**	**Notes to account**

Answer:

1.	AS - 17	B	Segmental Reporting
2.	Tax paid	D	Revenue expenditure
3.	Capital profit	A	Premium on issue of shares
4.	Contingent Liability	E	Notes to account
5.	Current Liability	C	Dividend unpaid

3. Answer the following question: [5x2=10]

(a) List the essential features of auditing

Answer:

The essential features of auditing can thus be listed as

(i) It involves evaluation of the relevance, reliability and adequacy of evidence in support of verifiable information.
(ii) It is analytical, critical and investigative.
(iii) The information audited may be financial or non-financial.
(iv) There should be standards or criteria for evaluation of the information.
(v) The auditor should be competent and independent.
(vi) It ensures reliability of information and authenticity of assertions made in the financial statements relating to enterprises, whether profit-oriented or not and whether it is required by law or not, to enable the auditor to form his opinion on these statements with regard to true and fair view disclosed there in.

(b) State the significance of audit from legal point of view

Answer:

Significance of audit from legal point of view may be enumerated as follows:

(i) **Filing of income tax return** — Income Tax authorities generally accept the profit and loss account that has been prepared by a qualified auditor and they do not go into details of the accounts.
(ii) **Borrowing of money from external sources** — Money can be borrowed easily on the basis of audited balance sheet from the external sources. Most of the financial institution sanctions various loans on the basis of audited financial statements.
(iii) **Statement of insurance claim** — in case of flood, fire, other natural calamities and the like unexpected happenings the insurance company may settle the claim for loss or damages on the basis of audited accounts of the previous year.
(iv) **Sales tax payments** — The audited books of accounts may generally be accepted by the sales tax authorities.
(v) **Action against bankruptcy** — The audited accounts serve as a basis to determine action in bankruptcy and insolvency cases.

(c) Comment on Secretarial audit for bigger companies with reference to Companies Act, 2013.

Answer:

Secretarial Audit for bigger companies [Section 204 of Companies Act, 2013]

(i) Every listed company and a company belonging to other class of companies as may be prescribed shall annex with its Board's report made in terms of sub-section (3) of section 134, a secretarial audit report, given by a company secretary in practice, in such form as may be prescribed.

(ii) It shall be the duty of the company to give all assistance and facilities to the company secretary in practice, for auditing the secretarial and related records of the company.

(iii) The Board of Directors, in their report made in terms of sub-section (3) of section 134, shall explain in full any qualification or observation or other remarks made by the company secretary in practice in his report under sub-section (1).

(iv) If a company or any officer of the company or the company secretary in practice, contravenes the provisions of this section, the company, every officer of the company or the company secretary in practice, who is in default, shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

(d) List the contents of audit note book

Answer:

Contents of Audit Note Book

(i) Name of the business enterprise.
(ii) Organisation structure.
(iii) Important provisions of Memorandum and Articles of Association.
(iv) Communication with the previous auditor, if any.
(v) Management representations and instructions.
(vi) List of books of accounts maintained by the enterprise.
(vii) Accounting methods, internal control systems followed by the enterprise, applicable laws etc.
(viii) Key management personnel.
(ix) Errors and fraud discovered.
(x) Matters requiring explanations or clarifications.
(xi) Special points that need attention in the audit report and for subsequent audits.

(e) What are the objectives and functions of Auditing and Assurance Standard Board?

Answer:

(i) To review the existing and emerging auditing practices worldwide.
(ii) To formulate Engagement Standards, Standards on Quality Control and Statement on Auditing.
(iii) To review and revise the existing Standards and Statements on Auditing.
(iv) To develop Guidance Notes on issues arising out of any Standard, auditing issues pertaining to any specific industry and revise.
(v) To review and revise the existing Guidance Notes.
(vi) To formulate General Clarifications, where necessary, on issues arising from Standards.

(vii) To formulate and issue Technical Guides, Practice Manuals, Studies and other papers.

Section – B

II. Answer any three of the following: [3×15=45]

4. (a) On January 1, 2004 Vardhaman Ltd. allotted 20,000, 9% Debentures of ₹ 100 each at par, the total amount having been received along with applications.

(1) On 1st Feb., 2005 the Company purchased in the open market 2,000 of its own debentures @ ₹ 102 each and cancelled them immediately.

(2) On 1st January, 2008 the Company redeemed at par debentures for ₹ 3,00,000 by draw of a lot.

(3) On 1st June, 2010 the Company purchased debentures of the face value of ₹ 2,00,000 for ₹ 1,97,800 in the open market, held them as investments for one year and then cancelled them.

(4) Finally, as per resolution of the Board of Directors, the remaining debentures were redeemed at a premium of 3% on 1st Feb., 2014 when Securities Premium Account in the company's ledger showed a balance of ₹ 50,000.

Pass journal entries for the above mentioned transactions ignoring debentures redemption reserve, debenture-interest and interest on own debentures. [12]

Answer:

Journal Entries

Date	Particulars		Debit (₹)	Credit (₹)
1.1.04	Bank A/c	Dr.	20,00,000	
	To Debenture Application and Allotment A/c			20,00,000
	(Being amount received on issue of ₹ 20,000, 9% debentures @ ₹ 100 each).			
1.1.04	Debenture Application and Allotment A/c	Dr.	20,00,000	
	To 9% Debentures A/c			20,00,000
	(Being Allotment of 20,000, 9% Debentures ₹ 100 each)			
1.2.05	Investment in Own 9% Debenture A/c	Dr.	2,04,000	
	To Bank A/c			2,04,000
	(Being, own debenture purchased)			
"	9% Debenture A/c	Dr.	2,00,000	
	Loss on Cancellation A/c	Dr.	4,000	
	To Investment in Own 9% Debenture A/c			2,04,000
	(Being , own debenture cancelled)			
1.1.08	9% Debenture A/c	Dr.	3,00,000	
	To Debenture Redemption A/c			3,00,000
	(Being, Amount due on redemption of debentures of ₹3,00,000)			
"	Debenture Redemption A/c	Dr.	3,00,000	
	To Bank A/c			3,00,000
	(Being, Amount paid on redemption of debentures of ₹3,00,000)			
1.6.10	Investment in Own 9% Debenture A/c	Dr.	1,97,800	
	To Bank A/c			1,97,800
	(Being, own debenture purchased, of the face value of ₹ 2,00,000 for ₹ 1,97,800)			
"	9% Debentures A/c	Dr.	2,00,000	
	To Investment in Own 9% Debenture A/c			1,97,800

	To Profit on Cancellation of own Debenture A/c (Being cancellation of own debenture)		2,200
"	Profit on cancellation of Own Debenture A/c Dr. To Capital Reserve A/c (Being, transfer of profit on cancellation of own debentures to capital reserves)	2,200	 2,200
1.2.14	9% Debenture A/c Dr. Premium on Redemption A/c Dr. To Debenture Redemption A/c (Being the amount due on redemption of 9% Debenture at a premium of 3%)	13,00,000 39,000	 13,39,000
"	Debenture Redemption A/c Dr. To Bank A/c (Being, Payment on redemption of debentures)	13,39,000	 13,39,000
"	Securities Premium A/c Dr. To Premium on Redemption A/c (Being, utilization of a part of Securities Premium A/c to write off premium paid on redemption of debentures)	39,000	 39,000

[No. of remaining debentures = 20,000 – 2,000 – 3,000 – 2,000= 13,000].

(b) The Following data apply to a company's defined benefit pension plan for the year:

Particulars	Amount (₹)
Fair market value of plan assets (begnning of year)	**4,00,000**
Fair market value of plan assets	**5,70,000**
Employer Contribution	**1,40,000**
Benefit Paid	**1,00,000**

Calculate the actual return on plan assets. **[3]**

Answer:

The actual return is computed as follows:

Particulars		Amount (₹)
Fair market value of plan assets (end of year)		5,70,000
Fair market value of plan assets (benning of year)		4,00,000
Change in plan assets		1,70,000
Adjusted for		
Employer contributions	1,40,000	
Less: Benefit Paid	1,00,000	40,000
Actual return on plan assets		1,30,000

5. (a) The Balance Sheets ZEET Ltd. and ASTAR Ltd. as on 31st March, 2015 were as follows:

Liabilities	ZEET Ltd.	ASTAR Ltd.
Equity Share Capital (fully paid shares of ₹20 each)	**30,000**	**12,000**
Securities Premium	**6,000**	**------**
General Reserve	**19,000**	**7,020**
Profit and Loss Account	**5,740**	**1,650**
12% Debentures	**------**	**2,000**
Bills Payable	**240**	**------**
Sundry Creditors	**5,820**	**2,330**
	66,800	**25,000**
Assets		

Land & Buildings		
Plant and Machinery	**12,000**	**------**
Furniture & Fixtures	**28,000**	**10,000**
Stock	**4,608**	**3,400**
Debtors	**15,724**	**8,082**
Cash at Bank	**4,240**	**2,040**
Bills Receivable	**2,228**	**1,218**
Cost of Issue of Debentures	**------**	**160**
	------	**100**
	66,800	**25,000**

All the bills receivable held by ASTAR Ltd. were ZEET Ltd.'s acceptances.

On 1st April, 2016 ZEET Ltd. took over ASTAR Ltd. in an amalgamation in the nature of merger. It was agreed that in discharge of consideration for the business ZEET Ltd. would allot three fully paid equity shares of ₹20 each at par for every two shares held in ASTAR Ltd. It was also agreed that 12% debentures in ASTAR Ltd. would be converted into 13% debentures in ZEET Ltd. of the same amount and denomination. Expenses of amalgamation amounting to ₹ 2,00,000 were borne by ZEET Ltd. Pass necessary journal entries in the books of ZEET Ltd. **[10]**

Answer:

Books of ZEET Ltd.
Journal Entries

Particulars	Dr.(₹)	Cr. (₹)
1. Business Purchase A/c Dr. To Liquidators of ASTAR Ltd. (Being Business of ASTAR Ltd. taken over for consideration settled as per agreement)	18,000	 18,000
2. Plant and Machinery A/c Dr. Furniture & Fixtures A/c Dr. Stock A/c Dr. Debtors A/c Dr. Cash at Bank A/c Dr. Bills Receivable A/c Dr. To General Reserve A/c(7,020 – 6,000) To Profit & Loss A/c (1,650 – 100) To 12% Debentures A/c To Sundry Creditors A/c To Business Purchase A/c (Being Assets and Liabilities taken over from ASTAR ltd.)	10,000 3,400 8,082 2,040 1,218 160	 1,020 1,550 2,000 2,330 18,000
3. Liquidator of ASTAR Ltd. A/c Dr. To Equity Share capital A/c (Being discharge of consideration)	18,000	 18,000
4. General Reserve A/c** Dr. To Bank A/c (Liquidation expenses paid by ZEET Ltd.)	2,00,000	 2,00,000
5. 12% Debentures A/c Dr. To 13% Debentures A/c (Being 12% Debentures discharged)	2,000	 2,000
6. Bills Payable A/c Dr. To Bills Receivable A/c (Being adjustment for mutual owing on account of bills)	160	 160

**** It can be adjusted against Profit and Loss Account also.**

(b) X Ltd. has leased equipment over its useful life that costs ₹7,46,55,100 for a three year lease period. After the lease term the asset would revert to the Lessor. You are informed that:

(i) The estimated unguaranteed residual value would be ₹ 1 lakh only.
(ii) The annual lease payments have been structured in such a way that the sum of their present values together with that of the residual value of the asset will equal the cost thereof.
(iii) Implicit interest rate is 10%.

You are required to ascertain the annual lease payment and the unearned finance income. P. V. factor @ 10% for years 1 to 3 are 0.909, 0.826 and 0.751 respectively. [5]

Answer:

(I) Calculation of Annual Lease Payment

Cost of the equipment	₹7,46,55,100
Unguaranteed Residual Value	₹1,00,000
PV of unguaranteed residual value (₹1,00,000 × 0.751)	₹75,100
Fair value to be recovered from Lease Payment (₹7,46,55,100 - ₹ 75,100)	₹7,45,80,000
PV factor for 3 years @ 10%	2.486
Annual Lease Payment (₹7,45,80,000 / PV Factor for 3 years @ 10% i.e. 2.486) -	₹3,00,00,000

(II) Calculation of Unearned Finance Income

	₹
Total lease payments [₹3,00,00,000 × 3]	9,00,00,000
Add: Residual value	1,00,000
Gross Investments	9,01,00,000
Less: Present value of Investments (₹7,45,80,000 + ₹75,100)	(7,46,55,100)
Unearned Finance Income	1,54,44,900

6. (a) Kachari Limited granted 25,000 employees stock options (face value ₹10) on 1st April, 2012 at ₹100, when the market price was ₹425. The options were to be exercised between 16th October, 2012 and 15th March, 2014. The employees exercised their options for 22,500 shares only. The remaining options lapsed. The company closes its books on 31st March every year. Pass Journal entries. [7]

Answer:

Date	Particulars	Dr. (₹)	Cr. (₹)
01/4/12	Employee Compensation Expense A/c Dr. To Employee Stock Options Outstanding A/c (Being grant of 25000 stock options to employees at ₹100 when market price is ₹ 425)	81,25,000	 81,25,000
(16/10/12 to 15/3/14)	Bank A/c Dr. Employee stock options outstanding A/c Dr. To Equity share capital A/c To Security premium A/c (Being allotment to employees of 22500 equity shares of ₹10 each at a premium of ₹415 per share in exercise of stock options by employees)	22,50,000 73,12,500	 2,25,000 93,37,500
16/3/14	Employee stock options outstanding A/c Dr. To Employee compensation expense A/c	8,12,500	 8,12,500

	(Being entry for lapse of stock options for 2500 Shares)		
31/3/14	Profit & Loss A/c Dr. To Employee compensation expense A/c (Being transfer of employee compensation Expense to profit and loss account)	73,12,500	 73,12,500
Note: Employee stock options outstanding will appear in the Balance Sheet as part of Net Worth or Shareholders' Equity.			

(b) Mogari Limited has 10% Redeemable Preference share capital of ₹30,00,000 consisting of ₹10 shares fully paid up. The company wants to redeem these shares at 25% premium.
The ledger accounts show the following balances:
Securities premium ₹1,00,000;
General Reserve ₹13,00,000 and
Profit & Loss Account (Cr.) ₹7,00,000
In order to facilitate the redemption of preference shares, the company decided the following:
1. 1,20,000 Equity shares of ₹10 each were issued at 50% premium.
2. 10,000, 12% Debenture of ₹100 each were issued at par.
3. Investments of book value ₹5,00,000 were sold at ₹5,60,000.
Pass the necessary journal entries to record above transactions and redemption of preference shares. [8]

Answer:

Particulars	Dr. (₹)	Cr. (₹)
Bank A/c Dr. To E. S. Application A/c To Debenture A/c (Being, Application money received on 120,000 equity shares @₹15 per share and on 10,000 debentures @ ₹ 10 each)	28,00,000	 18,00,000 10,00,000
Bank A/c Dr. To Profit & Loss A/c To Investment A/c (being, Profit on sale of Investments)	5,60,000	 60,000 5,00,000
E. S. Application A/c Dr. To E. S. Capital A/c To Securities Premium A/c (Being, Application money transferred)	18,00,000	 12,00,000 6,00,000
Debenture Application A/c Dr. To 12% Debenture A/c (Being, Application money transferred)	10,00,000	 10,00,000
Security Premium A/c Dr. General Reserve A/c Dr. To Premium on Redemption of Pref. Shares A/c	7,00,000 50,000	 7,50,000
General Reserve A/c Dr. Profit & Loss A/c Dr. To Capital Redemption Reserve A/c	12,50,000 5,50,000	 18,00,000
10% Redeemable P. S. Capital A/c Dr. Premium on Redemption of Pref. Shares A/c Dr. To Bank A/c	30,00,000 7,50,000	 37,50,000

Note: Preference shares are redeemed either out of distributable profits or proceeds from fresh issue of shares or both. Hence, Preference shares of ₹12,00,000 redeemed through fresh issue of equity shares and remaining of ₹18,00,000 redeemed out of profits.

7. (a) As on 31.03.2014, the Equity share Capital of AB Ltd. is ₹10 Crores divided into Shares of ₹10 each. During the financial year 2014-2015, it has issued Bonus Shares in the ratio of 1:1. The Net Profit after Tax for the years 31.03.2014 and 31.03.2015 are ₹8.50 Crores and ₹11.50 Crores respectively. EPS disclosed in the accounts for two years in ₹8.50 and ₹5.75 respectively. Comment on the above. [5]

Answer:

Step	Particulars
1	Number of Shares at period beginning, on 31.03.2014 = ₹10 Crores ÷ ₹10 = 1 Crore Shares = 100 Lakh Shares
2	Bonus Shares in the ratio 1:1 = 100 Lakh Shares. So, Total Number of Equity Shares Outstanding, i.e. Step 1 + Bonus = Given 100 Lakh + Bonus 100 Lakh = 200 Lakh Shares.
3	Basic EPS for Current Year = $\frac{\text{Net Profit for the year}}{\text{Total Shares as per Step 2}} = \frac{₹1{,}150 \text{ Lakhs}}{200 \text{ Lakh Shares}}$ =₹5.75
4	Adjusted Basic EPS for the previous year $= \frac{\text{Net Profit for the previous year}}{\text{Total Shares as per Step 2}} = \frac{₹850 \text{ Lakhs}}{200 \text{ Lakh Shares}}$ =₹4.25

(b) Tiptop Ltd. came out with an issue of 45 lakh equity shares of ₹ 10 each at a premium of ₹ 2 per share. The promoters took 20% of the issue and the balance was offered to the public. The issue was equally underwritten by P, Q and R respectively.
Each underwriter took firm underwriting of 1,00,000 shares each. Subscriptions for 31,00,000 equity shares were received with marked forms for the underwriters as given below:

P	**7,25,000 shares**
Q	**8,40,000 shares**
R	**13,10,000 shares**
	28,75,000 shares

The underwriters are eligible for a commission of 5% on face value of shares. The entire amount towards shares subscription has to be paid along with application. You are required to:
(1) Compute the underwriters" liability (number of shares);
(2) Compute the amount payable as due to underwriters; and
(3) Pass necessary Journal Entries in the books of Tiptop Ltd. relating to underwriters. [10]

(Note: As per contract, the underwriters are to be given credit for "firm" applications and that credit for unmarked applications be given in proportion to the shares underwritten.)

Answer:

(1) Computation of Liabilities of Underwriters (No. of Shares)

Particulars	P	Q	R
Gross Liability	12,00,000	12,00,000	12,00,000
Less: Firm Underwriting	1,00,000	1,00,000	1,00,000
	11,00,000	**11,00,000**	**11,00,000**
Less: Marked Application	7,25,000	8,40,000	13,10,000
	3,75,000	**2,60,000**	**(2,10,000)**
Less: Unmarked Application distributed in equal ratio among P & Q	1,12,500	1,12,500	NIL
	2,62,500	**1,47,500**	**(2,10,000)**

Less: Surplus of R distributed to P & Q	1,05,000	1,05,000	2,10,000
Net Liability (excluding firm underwriting)	**1,57,500**	**42,500**	**NIL**
Add: Firm Underwriting	**1,00,000**	**1,00,000**	**1,00,000**
Total Liability (No. of Shares)	**2,57,500**	**1,42,500**	**1,00,000**

(2) Computation of amount payable by underwriters

Particulars	P	Q	R
Liability towards shares to be subscribed @ 12 per share	30,90,000	17,10,000	12,00,000
Less: Commission (5% on 12 lakhs @ ₹ 10 each)	6,00,000	6,00,000	6,00,000
Net Amount to be paid by underwriters	**24,90,000**	**11,10,000**	**6,00,000**

(3) In the Books of Massod Ltd.

Journal Entries

Particulars		Dr.	Cr.
Underwriting Commission A/c	Dr.	18,00,000	
To, P Ltd			6,00,000
To, Q Ltd			6,00,000
To, R Ltd			6,00,000
(Being underwriting Commission on the shares underwritten)			
P Ltd	Dr.	30,90,000	
Q Ltd	Dr.	17,10,000	
R Ltd	Dr.	12,00,000	
To, Equity Share Capital A/c			50,00,000
To, Share Premium A/c			10,00,000
(Being shares incl. firm underwritten shares allotted to underwriters)			
Bank A/c	Dr.	42,00,000	
To, P Ltd			24,90,000
To, Q Ltd			11,10,000
To, R Ltd			6,00,000
(Being the amount received towards shares allotted to underwriters, less underwriting commission due to them)			

Section – C
Answer any two questions

8. (a) Mr. Raghav, who is a chartered accountant, wants to conduct the audit of Ram-Shyam Limited. State the disqualifications that would make him ineligible for the post.

(b) Should an auditor sign his audit report? [10+5 = 15]

Answer:

(a) Appointment of Mr. Raghav as an Auditor.

The following persons shall not be eligible for appointment as an auditor of a company, namely:—

(a) a body corporate other than a limited liability partnership registered under the Limited Liability Partnership Act, 2008;

(b) an officer or employee of the company;

(c) a person who is a partner, or who is in the employment, of an officer or employee of the company;

(d) a person who, or his relative or partner—

(i) is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company.

(ii) Provided that the relative may hold security or interest in the company of face value not exceeding one thousand rupees or such sum as may be prescribed;
(iii) is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of such amount as may be prescribed; or
(iv) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for such amount as may be prescribed;

(e) a person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed;
(f) a person whose relative is a director or is in the employment of the company as a director or key managerial personnel;
(g) a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies;
(h) a person who has been convicted by a court of an offence involving fraud and a period of ten years has not elapsed from the date of such conviction;
(i) any person whose subsidiary or associate company or any other form of entity, is engaged as on the date f appointment in consulting and specialised services as provided in section 144.

If Mr. Raghav possess any of the above disqualifications he would not be eligible for the post of an auditor in Ram-Shyam Ltd.

(b) Auditor to sign audit reports [Section 145]

The person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company in accordance with the provisions of sub-section (2) of section 141, and the qualifications, observations or comments on financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

9. (a) What is Audit Programme? State its advantages.
(b) Distinguish between clean audit report and qualified audit report. [8+7 = 15]

Answer:

(a) Audit Programme

An audit programme is a detailed plan of the auditing work to be performed, specifying the procedures to be followed in verification of each item and the financial statements and the estimated time required. To be more comprehensive, an audit programme is written plan containing exact details with regard to the conduct of a particular audit. It is a description or memorandum of the work to be done during an audit. Audit programme serves as a guide in arranging and distributing the audit work as well as checking against the possibility of the omissions.

The main **advantages** of an audit programme are as follows:
(i) It serves as a ready check list of audit procedures to be performed.
(ii) The audit work can be properly allocated to the audit assistants or the article clerks.
(iii) The auditor may easily know the extent of work done at any point of time. Thus, the progress of work done can be under the supervision and control of the auditor.

(iv) Audit programme would not only be useful for the audit assistants in carrying the audit work but for the principal too as he would be in a position to account for the individual responsibilities.
(v) A uniformity of the work can be attained as the same programme would be followed from time to time.
(vi) It is a useful basis for planning the programme for the following year.
(vii) It may be used as evidence by the auditor in the event when any charge is brought against him. He can prove that there has been no negligence on his part and he exercised reasonable care and skill while performing the task.

(b) Distinctions between Clean Audit Report and Qualified Audit Report

A clean report which is otherwise known as unconditional opinion is issued by the auditor when he does not have any reservation with regard to the matters contained in the financial statements. In such a case the audit report may state that the financial statements give a true and fair view of the state of affairs and profit and loss account for the period. Under the following circumstances an auditor is justified, in issuing a clean report:
(i) the financial information has been prepared using acceptable accounting policies, which have been consistently applied;
(ii) the financial information complies with relevant regulations and statutory requirements; and
(iii) there is adequate disclosure of all material matters relevant to the proper presentation of
(iv) the financial information, subject to statutory requirements, where applicable.

Qualified audit report, on the other hand, is one which does not give a clear chit about the truth and fairness of the financial statements but makes certain reservations. The gravity of such reservations will vary depending upon the circumstances. In majority of cases, items which are the subject matter of qualification are not so material as to affect the truth and fairness of the whole accounts but merely create uncertainty about a particular item. In such cases, it is possible for the auditors to report that in their opinion but subject to specific qualifications mentioned, the accounts present a true and fair view. Thus, an auditor may give his particular objection or reservation in the audit report and state "subject to the above, we report that balance sheet shows a true and fair view........". The auditor must clearly express the nature of qualification in the report. The auditor should also give reasons for qualification.

According to 'Statement on Qualifications in Auditor's Report' issued by the ICAI. All qualifications should be contained in the auditor's report. The words "subject to" are essential to state any qualification. It is also necessary that the auditors should quantify, wherever possible the effect of these qualifications on the financial statements in clear and unambiguous manner if the same is material and state aggregate impact of qualifications. Thus, it is clear from the above, that in case of a clean report, the auditor has no reservation in respect of various matters contained in the financial statements but a qualified report may involve certain matters involving difference of opinion between the auditor and the management.

10. (a) State the objectives of cost audit from the point of view of Government.
(b) Discuss briefly the scope of Audit Committee in public limited company. [7+8 = 15]

Answer:

(a) The objective of Cost audit from the point of view of government:

(i) To ensure whether the national resources are prudently and optimally used.
(ii) To reduce cost of production of commodities and regularize their distribution.

(iii) To determine whether particular industry should be given subsidy/grants.
(iv) To determine whether particular industry should be protected from external competition.
(v) To make comparisons of cost parameters of different firms manufacturing same product.
(vi) To assess the costs of the same product on different regions so as to decide to grant incentives etc.
(vii) To fix the maximum price of a commodity.
(viii) To devise, apply and evaluate cost control measures.

(b) Scope of audit committee

An Audit Committee consists of three to five members formed to serve as communication link among various departments. Audit Committee has a fourfold relationship and therefore has to interact with management, internal auditor, statutory auditor and the public.

The Scope of Audit Committee can be discussed as follows: -
(i) Review of annual financial statements before submission to the Board of Directors.
(ii) Selection of the Statutory Auditor
(iii) Act as lies on between the Statutory Auditor and Board of Directors
(iv) Administrative control of the internal control functions through the feedback between the Internal Auditor and the Audit Committee.
(v) Over seeing internal control operation.
(vi) Over seeing internal audit operations and feedback between internal audit committee and developing the internal auditing authority through broad based internal audit programming.
(vii) Review and approval of financial information for publication
(viii) Review proposed changes in accounting system and procedures.
(ix) Help resolve differences between management, internal and statutory auditor.
(x) Report on the audit committee acting in the Annual Reports of Board of Directors.
(xi) Ensure reliability of organisation's financial statements and operational activities.

To be effective and purposeful, the audit committee should maintain the following:-

(1) Audit Committee should have the independence of management, Statutory Auditor and Internal Auditor. The Board of Directors allows full freedom to the audit committee to investigate into any areas of operation.
(2) The relation between the audit committee and management should be cordial and congenial towards optimum efficiency and healthy growth of the organization.
(3) There should be a regular line of communication through occasional meetings with the management.
(4) There should be good communication relationship interwoven among management, internal auditor and statutory auditor.