

**FINAL EXAMINATION
[GROUP-IV]**

**SUGGESTED ANSWER TO QUESTIONS
DECEMBER 2011**

PAPER -17 : COST AUDIT & OPERATIONAL AUDIT

Time Allowed : 3 Hours

Full Marks: 100

The figures in the margin on the right side indicate full marks.

- Please :*
- (1) Answer all bits of a question at one place.*
 - (2) Open a new page for answer to a new question.*
 - (3) Attempt the required number of questions only.*

Answer Question No. 1 and Question No. 5 which is compulsory and answer any two each from the remaining questions of Section I and II.

**Section I (50 Marks)
(Cost Audit)**

Question :

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. [1×5=5]
- (i) Financial position and Ratio analysis are being dealt with under Para – 16 of the Cost Audit, Report Rules.
 - (ii) Cost Audit is to be conducted only when the shareholders of the company direct such an audit at the Annual General Meeting.
 - (iii) In case of appointment of Cost Auditor in Partnership firm's name, all the partners of the firm must be the Cost Accountants but the partners need not be the practicing Cost Accountants.
 - (iv) A Cost Accountant who has been appointed as Cost Auditor of the company can authenticate the Compliance Report of the same company.
 - (v) CAS -6 deals with determination of capacity of a unit.
- (b) In each of the cases / statements given below, one out of four alternatives is correct. Indicate the correct answer : [1×5=5]
- (i) The structuring of Cost Audit includes
 - A. Audit Programmes
 - B. Audit working papers
 - C. Checking including test checking
 - D. All of the above

- (ii) Time limit for submission of Compliance Report is within
- A. One hundred and twenty days
 - B. One hundred and eighty days
 - C. Forty five days
 - D. One hundred and thirty five days
- (iii) Under Para 23, cost of bought out services includes
- A. Raw Materials
 - B. Cost of Utilities
 - C. Indirect Material
 - D. All of the above
- (iv) CAS -4 deals with
- A. Determination of Cost of Production for Captive consumption
 - B. Determination of Average (equalized) Cost of Production
 - C. Determination of Capacity of a Unit
 - D. None of the above
- (v) The role of Cost Auditor in respect of non-moving stock is to review
- A. The causes explained by the company for non-movement of the items
 - B. How the company deals with the non-moving stock
 - C. The policy of the company regarding determination on non-moving items
 - D. All of the above
- (c) Fill in the blanks in the following sentences by using appropriate words / phrases: [1×4=4]
- (i) Section 209(i) (d) of the Companies Act, 1956 requires prima facie that the Cost Accounting records are to be maintained in theof the company.
- (ii) The annexure to the Cost Audit Report and Proforma should be signed by theandof the company.
- (iii) In view of e-filingis required to be submitted to the Cost Audit Branch.
- (iv) Form No.....is used for seeking the approval of the Central Government for appointment of a Cost Auditor.

Answer to Question No 1(a)

- (i) **FALSE:** Financial position and ratio analysis are being dealt with under PARA 24 of the Cost Audit Report Rules, 2001.
- (ii) **FALSE:** Cost Audit is conducted when Central Government directs / approves such an audit.
- (iii) **FALSE:** All the partners of the firm must be the Cost Accountants in practice.
- (iv) **TRUE :** A cost auditor can authenticate the Cost Audit Report and the Compliance Report of the same Company.
- (v) **FALSE:** CAS-6 deals with the principles and methods of determining the Material Cost.

Answer to Question No 1(b)

- (i) D. All of the above
- (ii) B. One Hundred and eighty days
- (iii) D. All of the above
- (iv) A. Determination of Cost of production for Captive Consumption.
- (v) D. All of the above

Answer to Question No 1(c)

- (i) Registered Office
- (ii) Secretary, a director
- (iii) No hard Copy
- (iv) 23 C

Question :

2. (a) How do you define a Service Cost Centre according to CAS-13? [2]
- (b) How is Cost Computed of Services in the following cases as per CAS-13?
- (i) In-house
 - (ii) By Contractor [2+2=4]
- (c) ASHLEEN SUGAR MILLS LTD., a sugar manufacturing company, located at Utter Pradesh has a boiler which is used for its own by-product, bagasse 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 31,2011:

Sugar produced	28,70,000 Quintals
Steam generated and consumed	14,65,000 Tonnes
Fuel (Bagasse) 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
Variable conversion cost of generation of power (excluding cost of steam)	₹ 4,22,18,000

- 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 as per Cost Accounting Record Rules.
 (ii) Compute the average Cost of Power as per PARA -7(A) of the Annexure to the Cost Audit Report Rules. [(5+4)+3=12]

Answer to Question No 2(a)

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 Centres 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.

Answer to Question No 2(b)

- (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.

Answer to Question No 2(c)**ASHLEEN SUGAR MILLS LTD**

<u>Cost of Steam</u>	₹
Cost of Fuel-Bagasse : 685000 Tonnes @ ₹ 1820	1246700000
Conversion Cost including Cost of Water	<u>64530000</u>
Total Cost	<u>1311230000</u>
Steam Generated (Tonnes)	1465000
Gross Cost of Steam per Tonne	
$1311230000 \div 1465000$	₹ 895.04
Steam directly used for Sugar Producti	₹
(1465000-620000) Tonnes X ₹ 895.04	756308800
Value of exhaust steam from Steam Turbine	
[At 82% of cost = (620000×895.04×0.82)] =	<u>455038336</u>
Total Cost of Steam used for Sugar Production	<u>1211347136</u>
Average Cost of Steam per Tonne	
$(1211347136 \div 1465000)$	₹ 826.86
For disclosure in Power & fuel to the Cost Audit Report :	
Steam Consumption per Quintal of Sugar:	0.51 Tonnes
$(1465000 \div 2870000)$	
Steam Cost per quintal of Sugar:	₹ 422.07
$(1211347136 \div 2870000)$	
<u>Cost of Power</u>	₹
Cost of high pressure steam sent to steam turbine	
$(620000 \text{ Tonnes} \times ₹ 895.04)$	554924800
Conversion cost for generation of Power	<u>42218000</u>
(excluding Cost of Steam)	597142800
Less : Cost of exhaust steam transferred	
to sugar manufacture	<u>455038336</u>
Net Cost of Power Generated	<u>142104464</u>
Power generated from steam Turbine	48525000 KWH
Cost of Power Generated per KWH	₹ 2.93

For disclosures in PARA 7(A) of the Annexure to the Cost Audit Report:

Quantity & Cost of Power	KWH	₹	₹ / KWH
(a) Own Generation	48525000	142104464	2.93
(b) Purchased (@ ₹ 5.40)	5270000	28458000	5.40
	53795000	170562464	3.17

Power consumed per quintal of sugar 18.74 KWH

(53795000 ÷ 2870000)

Power cost per quintal of Sugar ₹ 59.41

(18.74 × 3.17)

Question :

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

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

(c) You are the Cost Auditor of INDIA JUTE MILLS LTD .for the year ended March 31, 2011. The company had a strike from 15.9.2010. Although the company resumed working from 18.11.2010, normal production was achieved only from 12.12.2010. The expenses incurred during the year ended March 31, 2011 were:

	(Amount in ₹ lakh)
Salaries and wages (Direct)	450
Salaries and wages (Indirect)	220
Power (Variable)	160
Depreciation	140
Other fixed expenses	260

Detailed examination of the records revealed that of the above, the following relate to the period 15.9.2010 to 17.11.2010:

	(Amount in ₹ lakh)
Salaries & wages (Indirect)	80
Depreciation (Non- productive)	50
Other fixed expenses	110

Required :

As a Cost Auditor you are requested to calculate abnormal cost which will be excluded from the product cost. [3+2+2+2=9]

Answer to Question No 3(a)

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:

- a) A Member holding a part-time certificate of practice: or
- b) A Member who is in full time employment whose membership fees are in arrear; or
- c) 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.

Answer to Question No 3(b)

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.
- Channelising 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 mis-management if any for the benefit of shareholders, consumers and society in large.
- Hospitalisation, schooling, roads and transportation facilities to own employees as well as neighbouring people & cost benefit analysis.

Answer to Question No 3(c)

INDIA JUTE MILLS

Calculation of fixed expenses incurred during the period : 18.11.2010 to 11.12.2010:

(Amount in ₹Lakh)

Total Expenses for 2010-2011	1230
Less : Variable Expenses (Electricity)	<u>160</u>
Fixed Expenses for 2010-11	1070
Less : Fixed expenses during strike period	<u>240</u>
Fixed Expenses during non strike period	<u>830</u>

Since strike period was for 64 days (15.9.2010 to 17.11.2010)
the non-strike period is 301 days .

Hence Fixed expenses attributed to 24 days i.e.

18.11.2010 to 11.12.2010 is 7.97% ($24 \div 301 \times 100$) of ₹830 lakh = ₹66.15 lakh

(Amount in ₹ Lakh)

Expenses incurred during the period of 15.9.2010 to 17.11.2010	240.00
Expenses incurred during the period of 18.11.2010 to 11.12.2010	<u>66.15</u>
Total	<u>306.15</u>

Hence ₹ 306.15 lakh is to be treated as Abnormal Cost and should be excluded from Product Cost.

Question :

4. (a) State whether the following companies are covered by Cost Accounting Records Rules, with reasons for your conclusions:
- A small scale industrial unit manufacturing formulations which is subject to Statutory Price Control under Drug Price Control Order.
 - A construction company which runs a mini cement plant to manufacture cement for its own use. [2+2=4]
- (b) How would you compute the cost of utilities as per CAS-8 in the following circumstances?
- Utilities generated for the purpose of inter unit transfer.
 - Utilities generated for the purpose of inter company transfer.
 - Utilities generated for the sale to outside parties. [2×3=6]
- (c) (i) What are “Waste Multipliers” in textile costing?
- (ii) The following details of the process-wise wastages on inputs are taken from the Cost Accounting Records of ANUSUA COTTON MILLS LTD., a yarn manufacturing company, for the year ended March 31, 2011:

PROCESS	% of Wastages on Input
Mixing and Blow Room	8.85
Carding	6.95
Drawing	1.22
Roving (Simplex)	1.10
Ring frame (Spinning)	6.90
Reeling and Winding	1.50

Required:

Calculate the process-wise Waste Multiplier factors for the year ended March 31, 2011. [2+6=8]

Answer to Question No 4(a)

- (i) Normally, Small Scale Companies are exempted from maintenance of Cost Accounting records and their Cost audit. However, as per explanation to the application clause of Cost accounting Records (Formulations) Rules, 1988, such companies will not be exempted from the operation of these rules if these companies are subject to Price Control under Drugs Price Control order as amended from time to time.
- (ii) Any Company manufacturing cement (whether for Sale or Captive Consumption) is covered by Cost Accounting Records (Cement) Rules. Thus, a Construction Company manufacturing cement for its own use is covered by the said rules.

Answer to Question No 4(b)

- (i) Cost of utilities generated for the purpose of inter unit transfers shall comprise of direct material cost, direct employee cost, direct expenses, factory overheads and the distribution cost incurred for such transfers.
- (ii) Cost of utilities generated for the inter company transfers shall comprise of direct material cost, direct employee cost, direct expenses, factory overheads, distribution cost and share of administrative overheads.
- (iii) Cost of utilities generated for the sale to outside parties shall comprise of direct material cost, direct employee cost, direct expenses, factory overheads, distribution cost share of administrative overheads and marketing overheads. The sale value of such utilities will also include the margin, and share of research and development cost incurred for development and improvement of existing process or product.

Answer to Question No 4(c)

(i) Waste Multipliers:

Under the Section 209(1)(d) Rules for the textile industry, the process wise cost /kg of output is being worked out at first. Then these costs are aggregated to arrive at the total yarn cost. As there are wastes at each process, the final aggregation of processes to arrive at the finished yarn has to take into account all such process wise wastages. This is done by using a factor known as a Waste Multiplier. Accordingly Waste Multiplier is that quantity of output from any process which will be needed to get one unit of final output.

(ii)

ANUSUA COTTON MILL LTD

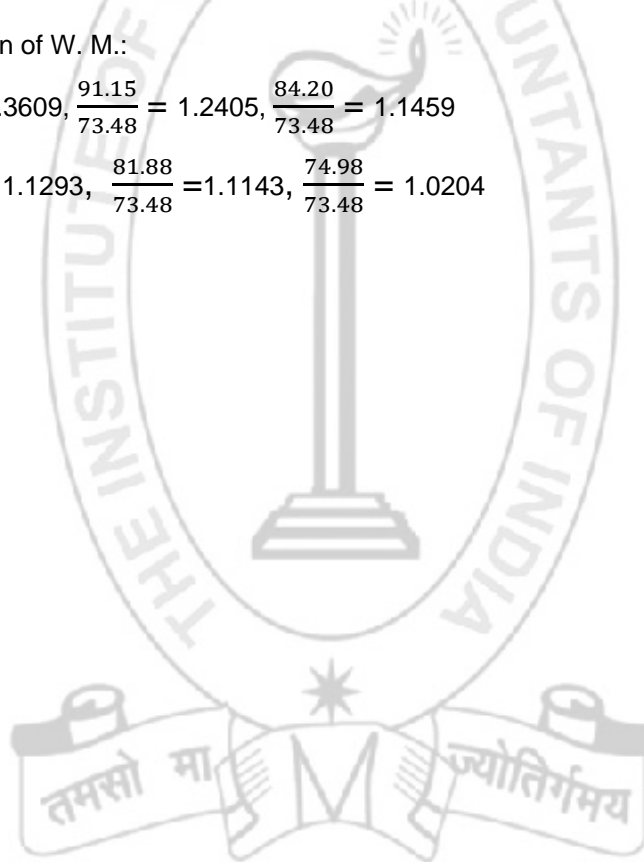
CALCULATION OF PROCESS WISE WASTE MULTIPLIER FACTOR

Process	% of wastages on Input	Net output for 100 units of input	Waste multiplier
Total		100.00	1.3609
Mixing and Blow Room	8.85	100-8.85=91.15	1.2405
Carding	6.95	91.15-6.95=84.20	1.1459
Drawing	1.22	84.20-1.22=82.98	1.1293
Roving(Simplex)	1.10	82.98-1.10=81.88	1.1143
Ring frame (spinning)	6.90	81.88-6.90=74.98	1.0204
Reeling and Winding	1.50	74.98-1.50=73.48	1.0000

Note: Calculation of W. M.:

$$\frac{100}{73.48} = 1.3609, \frac{91.15}{73.48} = 1.2405, \frac{84.20}{73.48} = 1.1459$$

$$\frac{82.98}{73.48} = 1.1293, \frac{81.88}{73.48} = 1.1143, \frac{74.98}{73.48} = 1.0204$$



Section II (50 Marks)
(Operational Audit)

Question :

5. (a) Fill in the blanks in the following sentences by using appropriate words / phrases:

- (i) Management Audit requiresapproach.
- (ii)is needed to create corporate culture of transparency.
- (iii) ISO 9000 certification is anservice.
- (iv) Salvage is considered asby insurer against what is owed under the policy for an insured loss.
- (v) Theis the highest body of the structure of the WTO. [1×5=5]

(b) 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:

- (i) The Managing Director of a company can be appointed as Chairman of Audit Committee.
- (ii) Corporate image of a company is built up exclusively by its product quality but is not affected by its attitude towards its other stakeholders.
- (iii) Productivity is defined as ratio of production and sales.
- (iv) Energy Audit means monitoring the energy efficiency of different equipment and process. [1×4=4]

(c) What do the following abbreviations stand for?

- (i) IAASB
- (ii) CEGAT
- (iii) TRAI
- (iv) GATT
- (v) OECD [1×5=5]

Answer to Question No 5(a)

- i. Inter-disciplinary
- ii. Corporate Governance
- iii. Assurance
- iv. Credit
- v. Ministerial Conference

Answer to Question No 5(b)

- i. False: The chairman of the Audit committee must be an independent Director. SEBI requires the setting up of a qualified and independent Audit Committee.

- ii. False: Corporate image is not confined to its product quality only, but it extends to all its field of business.
- iii. False: Productivity is defined as ratio of output to input.
- iv. True: Energy Audit gives suggestion how energy consumed can be cut down without affecting production.

Answer to Question No 5(c)

- i. IAASB- International Auditing & Assurance Standards Board.
- ii. CEGAT- Central Excise and Gold Control Appellate Tribunal.
- iii. TRAI- Telecom Regulatory Authority of India.
- iv. GATT- General Agreement on Tariffs and Trade.
- v. OECD – Organization for Economic Co-operation and Development.

Question :

6. (a) Explain whether the following activities amount to Professional Misconduct on the part of a Cost Accountant:
- (i) Mr. S. JAIN, a practicing Cost Accountant takes up job as full time lecturer in XBL Management Institute at Jamshedpur affiliated to Ranchi University.
 - (ii) Mr. P. DHAR, a practicing Cost Accountant uses a visiting card in which he designates himself besides as Cost Accountant, as “ Tax Consultant”.
 - (iii) Mr. P. NADKARNI, a Cost Accountant practicing in India enter into partnership with MR R.D. HONES, CMA, USA. [2×3=6]
- (b) Explain in brief the basic differences between Internal Audit and Operational Audit. [4]
- (c) “To-day’s customer is the more demanding than the customer of yesterday”- In view of this how would you evaluate, as a Management Auditor, the performance of “ Customer Services Department”. [8]

Answer to Question No 6(a)

- (i) Clause- 10 of Part 1 of the First schedule to the Cost & Works Accountants Act, 1959 prohibits a member in practice to engage in any business or occupation other than the profession of Cost Accountant unless permitted by the Council so to engage. Such prohibition has been introduced

as it would not be in keeping with the dignity of the profession and may also enable the member to secure an unfair advantage in his professional practice. In the instant case, Mr S Jain has accepted the appointment of Lectureship without obtaining specific and prior approval of the Council. Accordingly Mr S Jain would be guilty of Professional Misconduct.

- (ii) Section 7 of the Cost & Works Accountants Act 1959 read with clause of Part 1 of the Schedule of the said Act prohibits advertising of Professional attainments of services of a member. Thus it is improper to use designation "Tax Consultant" since neither a degree of a university established by laws or recognised by the Central Government nor it is a recognised professional membership by the Central Government or the Council. So Mr. P. Dhar is guilty of Professional misconduct under clause-7 of Part 1 of First schedule to the Cost & Works Accountants Act 1959.
- (iii) As per MOU with IMA USA a member of ICWAI can get enrolled as a member of IMA USA and
- (iv) vice-versa. However, an IMA member enrolling as member of ICWAI will not be allowed to hold a certificate of Practice to undertake any statutory work in India.
- (v) Mr. P.Nadkarni, a Cost Accountant practicing in India and entering into Partnership with Mr. R.D. hones CMA, USA amounts to professional misconduct.

Answer to Question No 6(b)

Internal audit is a continuous and systematic process of examining and reporting the operation and records of a concern by its employees or external agencies specially assigned for this purpose.

Internal Auditing is an independent appraisal activity within an organisation for review of operations as a service to Management.

As Operational Audit (or value for money) has been defined as an organized search for ways of improving efficiency and effectiveness. Operational Audit concentrates on seeking out aspects of operations in which waste, inefficiency and excessive costs would be subject to reduction by introduction of improvement of operating controls. It is audit of the performance at mainly operating level is supervisory level.

The differences between Internal audit and Operational Audit can be summarized as follows:

Internal Audit	Operational Audit
1. Compliance Objective	Risk identification, process improvement objective.
2. Financial Accounts Focus	Business Focus
3. Audit Focus	Efficiency and improvement Focus
4. Transaction Based	Process Based
5. Policies and procedures Focus	Risk Management Focus

6. Cost centre wise budget Monitoring	Accountability for Performance Improvement results.
7. Focus on policies transactions and compliance	Focus on goals strategies and risk management process.

Answer to Question No 6(c)

A customer is the most important person for business because it is he who provides the profit. Therefore, the starting point in any marketing strategy is identifying the customers, their needs and organizing the efforts of the company towards satisfying such needs.

In order to create and retains customers, certain services are to be provided by properly attending to their needs and supplying right quality goods at the right price. Such services would not only stimulate the demand for the products of the company but also will help to establish product acceptability and widen the scope of potential customers.

Customers services may be evaluated on the following lines:

- Do the products manufactured by the company meet the needs of the customers of different purchasing power and different tastes?
- Are the prices of the products reasonable, considering the product quality?
- Are the prices competitive to similar other products available in the market?
- Are the customers given prompt and personal attention?
- Does the company guarantee the quality of its products?
- Does the company provide after-sales services?
- Are the customers complaints carefully and promptly attended to?
- Are spare parts of the products easily available in the company offices and in the open market?
- Are the product properly packed to avoid any damage to its products?
- Is there any provision for home-delivery services?
- Does the company undertake marketing research in regard to customer behaviour and customer services?
- Does the company make use of marketing research data to improve customer services?
- Does the company's product bear ISI Mark / AGMARK?
- Are the company's products easily available at various retail outlets?
- How effective are the various channels of distribution used by the company?
- Does the company educate the customers about the use of the products through printed material and other means?

- Are the sales man retailers continuously motivated to provide the best attention and services while selling company's products?

Question :

7. (a) Enumerate the main areas to be covered by the Auditor in the case of Environment Audit of an Industrial unit. [6]
- (b) What is Corporate Governance?
State any 8 of the 14 key aspects of the CII (Confederation of Indian Industries) code which should be shared by the Board. [2+6=8]
- (c) Some of the risks covered by General Insurance are : fire, marine (transit), loss of profit, malicious damage, SRCC (Strike, Riots and Civil Commotion) etc.
- What are the risks for which a Cost Accountant as Surveyor can effectively use the methods and techniques of Cost Accounting for assessing the loss? [4]

Answer to Question No 7(a)

Main areas to be covered in the case of environment audit of an Industrial unit are enumerated below:

- Layout and design of the factory to provide for the installation pollution control devices with provision for up gradation of Pollution Control measures to meet regulatory authorities' requirement. Areas of deficiency to be included in the report.
- The use of all resources such as air, water, land, energy, raw material and human resources with minimum waste and interlinking for best results to be looked into and reported.
- It has to be reported whether all pollution Control measures in vogue are effective with reference to the type of industry, nature of working and grade of polluting the environment.
- Availability of adequate trained staff and safety amenities with provision for constant up gradation to be verified.
- Availability of adequate health care provisions and medical facilities for the workers to be looked into.
- Availability of proper system to eliminate industrial unhygienic state.
- Availability of adequate safeguard against occupational health hazards depending upon the nature of industry to be verified.
- Existence of adequate information system and reporting of compliance of statutory legal provisions to the board at regular intervals to be verified.
- Compliance of regularly mechanism by way of updating the existing environment system with the latest changes in the regulations to be looked into.

- It has to be verified as to how social aspects are addressed by the industry as they have as obligation to protect the society from pollution hazards of the industry.

Answer to Question No 7(b)

Corporate Governance is a system by which companies are directed and collected by the management in the best interest of the shareholders as well as others with greater transparency and better and timely reporting.

Corporate Governance is key to survival in the competitive business environment and the corporate governance codes all over the world are directed to achieve good Corporate Governance through Non-executive Directors.

The following key aspects of CII code which should be shared by the board are as follows:

1. Annual operating plan and budgets together with updated long term plans.
2. Capital Budgets, man-power and overhead budgets.
3. Quarterly results for the company as a whole and its operating division for business segments.
4. Internal audit reports, including cases of theft and dishonesty of a material nature.
5. Details of any joint venture or collaboration agreement.
6. Transactions that involve substantial payment towards goodwill, brand equity or intellectual property.
7. Labour problem and their proposed solutions.
8. Fatal or serious accidents, dangerous occurrences and any effluent or pollution problems.
9. Default in payment of interest or non payment of the principal on any public deposit, and / or to any secured creditors or financial institutions.
10. Recruitment and remuneration of Senior Officers just below the Board level, including appointment or removal of the Chief Financial Officer and the Company Secretary.
11. Show Cause, demand and prosecution notices received from the revenue authorities which are considered to be materially important.
12. Quarterly details of foreign exchange exposure and the steps taken by management to limit the risk of adverse exchange rate movement, if material.
13. Defaults such as non payment of inter corporate deposits by or to the company or materially substantial non-payments for goods sold by the company.
14. Any issue which involves possible public or product liability claims of a substantial nature, including any judgement or order which may have either passed, strictures on the conduct of the company, or taken an adverse view regarding another enterprise that can have negative implications for the company.

Answer to Question No 7(c)

All risk covered General Insurance can be quantified in one way or the other, and there are clear rules for computation of the loss suffered by the insured. However, the following areas in particular give maximum scope for a Cost Accountant to use his skills in evaluating the loss:

- (i) Fire: In correctly working out the value of goods lost (raw materials, work-in-progress or finished goods special in the latter cases)
- (i) Loss of Profit : In identifying the period costs and product cost.
- (ii) Transit damages or losses: In estimating the costs of repair or the value of goods lost.

Risks such as SRCC or malicious damages involve more legal issues than pure accounting statements.

Question :

8. Write short notes on *any three* out of the following:

- (a) Assurance Services
- (b) Professional Behaviour
- (c) The major characteristics of ERP systems necessitating change in Audit Approach
- (d) Functions of the WTO.

[6×3=18]

Answer to Question No 8(a)

Assurance Services

It is defined as “independent professional services that improve the quality of information, or its context, for decision makers”. This broad concept includes audit & attestation services.

Advances in information technology, have dramatically increased companies’ reliance on computerized information systems to conduct operations and together and report performance information both internally and externally. So reliability of information requires assurances. The Cost and Management Accounting profession in India is committed to provide services of high quality in the public interest as per international standard. So, the standards are being developed and promulgated by one Standard board as per International Auditing and Assurance Standard Board (IAASB) called as Cost Audit & Assurance Board (CAAB). Assurance services focus primarily on improving the information rather than on providing advice or installing system. It includes all types of informations. Assurance Services includes:

- (1) Assessment of ethics-related risk and vulnerability
- (2) Controls over and risk related investment
- (3) Adequacy of controls and policies for derivatives
- (4) Fairness of Inventory Valuation
- (5) Valuation of intangible assts
- (6) Optimum product mix and maximization of profit
- (7) Information systems security reviews

- (8) Fraud and illegal act risk assessment
- (9) Scope of Cost Reduction
- (10) After Sales service for Customer satisfaction
- (11) Identification of key factors to monitor and ISO-9000 certification
- (12) Assurance that systems are designed and operated in a manner that provides reliability of information and so on.

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Answer to Question No 8(b)

Professional behaviour

The principle of Professional Behaviour imposes an obligation on Professional Accountants to comply with relevant laws and regulations and avoid any action that may bring discredit to the profession. This includes actions which are reasonable and informed third party, having knowledge of all relevant information, would conclude negatively affects the good reputation of the profession. In marketing and promoting themselves and their work, professional Accountants should not bring the profession into disrepute. Professional Accountants should be honest and truthful and should not

- (i) Make exaggerated claim for the services they are able to offer the qualifications they possess or experience they have gained or
- (ii) Make disparaging references or unsubstantiated comparisons to the work of others.

The conceptual framework requires a Professional Accountant to identify, evaluate and address threats to comply with the fundamental principles, rather than merely complying with a set of specific rules which may be arbitrary. If threats to ethics are not clearly insignificant, a Professional Accountant should apply safeguards to eliminate the threats or reduce them to an acceptable level.

Answer to Question No 8(c)

The major characteristics of ERP systems necessitating change in Audit Approach:

The major characteristics of ERP systems necessitating change in the Audit approach are as follows:

- (i) On-line real time processing
- (ii) All transactions are stored in one common database
- (iii) System usually resides on multiple computers
- (iv) Optimum coordination is a challenge
- (v) Traditional 'batch' controls and audit trails not available
- (vi) Data bases can be accessed by any module
- (vii) System modules are transparent to the users
- (viii) Significant increase in number of users
- (ix) Network and data base access security is critical.

The audit of an ERP system requires specific knowledge and an understanding of the integrated complex features required for the successful implementation. The auditors require not only specialized skills but also capability to use unique methodologies to deal with various risks involved. Audit and review guidelines should also be developed providing management oriented frame work and proactive control self assessment.

Answer to Question No 8(d)

Functions of the WTO

The World Trade Organization (WTO) is the main organ of implementation of the Multilateral Trade Agreements (MTA). It is the forum for negotiation among its members. It is also the forum for negotiations on terms of the Plurilateral Trade Agreement (PTA).

The main functions of the WTO are as follows:

- (i) Facilitate the management of the Multilateral Trade Agreement (MTA) and the Plurilateral Trade Agreement (PTA) for the fulfilment of their obligations.
- (ii) All Multilateral Trade Relations concerning the above agreements will be negotiable 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 a 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 co-ordination 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.