

INTERMEDIATE EXAMINATION

GROUP I

(SYLLABUS 2008)

SUGGESTED ANSWERS TO QUESTIONS

DECEMBER 2014

Paper- 6 : COMMERCIAL & INDUSTRIAL LAWS AND AUDITING

Time Allowed : 3 Hours

Full Marks : 100

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

- Please : (i) Answer all bits of a question at one place
(ii) Open a new page for answer to a new question
(iii) Attempt the required number of questions only.

Answer Question No. 1 and Question No. 5 which are compulsory and attempt any two from the rest in Section-I and any two from the rest in Section-II.

Section-I (50 Marks)
(Commercial and Industrial Laws)

1. Comment on the following based on legal provisions (no mark for wrong reasons or justification) 2×7 =14
- (i) Mr. Rabin tells Miss Rekha that Mr. Rajib expressed his willingness to marry Miss Rekha on 25th December, 2014. This is a valid contract.
 - (ii) Employers are liable to contribute @ 10% of wages to EPF in respect of its members.
 - (iii) (a) The maximum ceiling of gratuity amount is ₹ 3,50,000.
(b) Ashim calculated bonus taking $15/30 \times \text{No. of year of service}$.
 - (iv) Worker is punishable with fine which may extend to INR-250 if he contravenes any provisions of Factories Act, 1948.
 - (v) An unpaid seller cannot exercise his right of lien when he is in possession of goods as agent for the buyer.
 - (vi) A limited liability partnership is bound by any act done by a partner in dealing with a person.
 - (vii) The employer is not liable to pay compensation in few cases under Workers Compensation Act, 1923.

Answer:

1. (i) This is not a valid agreement nor a contract.
As the essential element or condition of communication of offer by one Party and its acceptance of Other Party are missing.
- (ii) False
Employers contributes to Member of EPF @ 12%. However in case of sick company, any establishment having accumulated loss equal to its entire paid up capital and any

Suggested Answer_Syl2008_Dec2014_Paper_6

establishment in Jute Industry, Beedi Industry, Brick Industry, Coir Industry, and Gour Gum Factories Employers are to contribute 10% instead of 12%.

- (iii) (a) INR 10 lakhs
(b) 15/26 days x No. of years of Service
- (iv) False
Fine may extend to INR 500 and not 250
- (v) False
See 47 of Sales of Goods Act 1930, provided that the seller may exercise his right of lien notwithstanding that he is in possession of the goods as agent or bailee for the buyer.
- (vi) False
In following cases, an LLP is not bound by anything done by a Partner in dealing with a person (Sec 27(1)).
(a) The Partner in fact has no authority to act for the LLP in doing a particular act and
(b) The person knows that he has no authority or does not know or believe him to be Partner of the LLP.
- (vii) According to the workmen's Compensation Act 1923 the Employer shall not be liable when:
(i) The employee under the influence of drugs/ alcohol at the time of accident.
(ii) Employee will fully disobeys any safety rules
(iii) Employee will fully removes/disregards any safety guard/equipments.
(iv) Employee has filed a civil suit for claim of compensation.
(v) Employee has refused to get himself medically examined, cost of which is borne by the employer.

2. (a) State with reasons in brief, if the followings are correct. Give correct answer.

- (i) An agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others is a "void contract". 1
- (ii) An offer may contain a term, the non-compliance of which would amount to acceptance. 2
- (iii) Mr. Shyamal learnt from Mr. Anil that Mr. Bhabesh would be director of XYZ Ltd. to be formed. Mr. Shyamal told this to Krishna in order to induce him to purchase shares of XYZ Ltd. Mr. Krishna did so. This is a case of fraud by Mr. Shyamal. 3
- (b) (i) Pledging of goods obtained on "sale or return" basis will complete the sale. Offer your views. 2
- (ii) Against Amal's tender, Bimal agrees to sale and deliver 1000 kgs. of potato @ INR 10/- per kg. Bimal delivered 700 kgs. of potato and agrees to deliver balance 300 kgs. next month. Amal accepted 700 kgs. sent by Bimal. Later on, Bimal failed to deliver the balance quantity. Amal refuses to pay the price for 700 kg. which he accepted on the ground that Bimal failed to execute the sale contract. Can Amal refuse to pay? 2
- (c) State the provision of annual leave with wages in respect of workers under Factories Act, 1948. 2
- (d) State the correct answer with reason if the following statement are wrong. 2
- (i) Wage period cannot exceed 60 days.
- (ii) Deduction on account of payment to co-operative societies cannot be more than 50% of wages.
- (iii) No fine can be recovered on installments from the worker or after the expiry of 30 days from the day on which it was imposed.
- (iv) Deduction for damages or loss cannot exceed double the amount of loss.
- (e) Barun's salary per month is INR 9,500/- whether Barun is entitled to bonus. 2
- (f) Examine with reference to the relevant provisions of the Competition Act, 2002, whether a

Suggested Answer_Syl2008_Dec2014_Paper_6

person purchasing goods not for personal use but for resale can be considered as "consumer".

2

Answer:

2. (a) (i) Incorrect

According to Sec 2(i) of the Contract Act 1872, an agreement which is enforceable by Law at the option of one or more of the parties but not at the option of the other or others is a "voidable contract" not a "Void" Contract.

(ii) Wrong

The offer should not impose on the offeree an obligation to reply, while making the offer, the offerer cannot say that if the offer is not accepted before a certain date it will be presumed to have been accepted, unless the offeree sends his reply, no contract will arise.

(iii) This is not a Case of Fraud but misrepresentation.

Misrepresentation is incorrect or false statement but the falsity or inaccuracy is not due to any desire to deceive or defraud the other party, it is innocent. The Party making it believes it to be true.

Therefore, it is misrepresentation by Mr. Shyamal though he believed in the truthfulness of the statement and there was no intention to deceive as the information was derived not from Mr. Bhabesh but from Anil and was hearsay.

(b) (i) This statement is correct. As per Section 24 of Sale of Goods Act, 1930, the pledging of goods obtained on "Sale or Return" basis amounts to an act adopting the transaction and therefore will complete the Sale.

(ii) As per provisions of Sec 37(i) of Sale of Goods Act, where the seller delivers to the buyer a quantity of goods less than the quantity which was agreed to by seller, the Buyer can refuse to accept and reject 700 kgs. of potato. But when the buyer accepts the potato so delivered he shall be required to pay the contracted price for the potato already received.

(c) Every worker who had worked for a period of 240 days or more in a factory during a calendar year shall be allowed during subsequent calendar year, leave with wages for a number of days calculated at the rate of

(i) If an adult, one day for every twenty days of work performed by him during the previous Calendar year.

(ii) If a child, one day for every fifteen days work formed by him during the previous calendar year.

(d) (i) One month

(ii) 75%

(iii) 90 days

(iv) Exceed the amount of loss or damage.

(e) Bonus payable to Employees getting upto INR 10000 per month but Bonus will be calculated on INR 3500 only.

Where the salary or wages of an employee exceeds INR 3500 per month, the Bonus payable to such employee under sec 10 or as the case may be under Sec 11, shall be calculated as if his salary or wages were INR 3500 per month.

Hence Barun is entitled to bonus subject to the above.

(f) Yes, he can be considered as "Consumer" because the term "Consumer" is defined in Sec 2 (f) of Competition Act 2002. As per said Act "Consumer" means any person who buys any goods for a consideration which has been paid or promised or partly paid and partly promised, whether such purchase of goods is for resale or for any Commercial purpose or for personal use.

Hence it is not necessary that a person must purchase the goods for personal use in

Suggested Answer_Syl2008_Dec2014_Paper_6

order to be considered as a consumer under the Competition Act 2002. Even a person purchasing goods for resale or for any Commercial purpose will also be considered as a "consumer" within the meaning of Sec 2(f) of Competition Act 2002.

3. (a) Goods of ABC Ltd. seized by customs authorities in Kolkata Port after payment of customs duty. The seized goods were subsequently lost from the custom's custody. Hence customs authorize are responsible for loss. Offer your views on the basis of legal provisions. 2
- (b) Mr. A is employed as cashier on a monthly salary of INR 20,000 by PQR Bank for last three years. Mr. B gave surety for Mr. 'A'. After twelve months, the financial position of the bank deteriorated. All the employees agreed to accept a lower salary with 20% reduction. Mr. A's salary was reduced to INR 16,000 per month. Six months later, it was revealed that Mr. A misappropriated cash since the time of his appointment. Whether surety can be held liable if Mr. A fails to repay. 2
- (c) Mere silence as to facts likely to affect the willingness of a person to enter into a contract is fraud. – Offer your views. 2
- (d) Sona bought Refrigerator from manufacture's authorized dealer for INR 30,000. This Refrigerator was defective right from beginning and it did not work inspite of repairs by the manufacture's authorized engineers. Can Sona return the Refrigerator and claim refund? 2
- (e) When lien is terminated (Sale of Goods Act, 1930)? 2
- (f) Give correct number of workers based on Factories Act, 1948, in respect of following: 2
- (i) In every factory wherein more than 100 workers are ordinarily employed, adequate shelters or Rest Rooms and suitable Lunch Room shall be provided.
- (ii) In every factory where more than 250 workers are ordinarily employed, there shall be Ambulance Room.
- (iii) In every factory wherein 1000 or more workers are ordinarily employed, there shall be Welfare Officer.
- (iv) In every factory where in 50 workers are employed, the factory shall provide First Aid Box/First Aid Appliances.
- (g) What are the items being related to "collective disputes" under Ind. Disputes Act? 2
- (h) As per payment of Gratuity Act, 1972, Mr. J. K. Roy makes his wife his nominee, but wife predeceased Mr. J. K. Roy. In such case the amount of gratuity has been transferred to company's benevolent fund – State the correct position. 2
- (i) A cheque is drawn payable to Mr. Binay or order. It is stolen and the thief forges Mr. Binay's endorsement and endorsed it to Mr. Kashi. The banker pays the cheque in due course. Can Mr. Binay recover the amount from Bank? 2

Answer:

3. (a) This is a case of bailment and bailment exist u/s 148 of the Contract Act 1972 because in this case possession of goods is transferred to the Customs Authority.

This is Case of non-gratuitous bailment and Customs Authority is bailee whereas ABC Ltd. is bailor. Since the goods were lost from the custody of Bailee i.e., Customs Authority, the Custom Authority is responsible.

- (b) Yes Surety can be held responsible because:

Sec 133 of Contract Act 1872 says that any variance made without Surety's consent, in the terms of the contract between the principal (Debtor) and the creditor discharges the Surety as to transactions subsequent to the variance.

Suggested Answer_Syl2008_Dec2014_Paper_6

In the instant case Surety is liable for the loss suffered by the Bank due to misappropriation of cash by Mr. A (Cashier) during the first twelve months but not for the period after reduction of salary and variation of contract between the cashier & Bank.

- (c) **False:** Mere silence as to facts likely to affect the willingness of a person to enter into contract is not fraud unless the circumstances of the case are such that regard being had to them, it is the duty of the person keeping silence to speak or unless his silence is, in itself equivalent to speech.
- (d) Sona shall be entitled to return the Refrigerator and claim refund According to Sec 16 of the Sale of Goods Act, unless otherwise agreed upon, every contract of sale of goods is subject to the implied conditions as to Merchantability, i.e. the goods must be capable of being used as the goods of that description. Besides there is an implied condition as to quality & fitness. Thus a refrigerator is expected to function as a refrigerator. Where it fails to, as in the present case, there is deemed to be breach of that condition and as such, return of price shall have to be made.
- (e) Sec 49 of Sale of Goods Act 1930 provides that the unpaid seller of goods loses his lien thereon
- (i) When he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without receiving the right of disposal of the goods.
 - (ii) When the buyer or his agent lawfully obtains possession of the goods.
 - (iii) By waiver thereof.

The unpaid seller of goods, having a lien thereon, not lose his lien by reason only that he has obtained a decree for the price of the goods.

- (f) (i) 150
(ii) 500
(iii) 500
(iv) In every factory First Aid Boxes or Cupboards equipped with prescribed contents shall be provided as per Sec 45.
The number of boxes and cupboards to be provided and maintained shall not be less than one for every one hundred and fifty workers ordinarily employed.
- (g) Collective disputes may relate to the following:
- (i) Bonus, wages, gratuity & other allowances.
 - (ii) Duration of working hours, leave holidays etc.
 - (iii) Rules Governing discipline, retrenchment, closure, rationalization.
- All collective disputes are Industrial disputes.
- (h) This is wrong.
When the nominee predeceased the Employee (Mr. J. K. Roy), the interest of the nominee shall revert to the employee who shall make a fresh nomination in the prescribed form in respect of such interest.
- (i) According to Sec 85 of Negotiable Instrument Act 1881, the drawee banker is discharged when he pays a cheque payable to order, when it is purported to be endorsed by or on behalf of the payee. Even though the endorsement of Binay is forged, the banker is protected and he is discharged. Mr. Binay, the true owner cannot recover the money from the drawee Bank.

Suggested Answer_Syl2008_Dec2014_Paper_6

4. (a) (i) Ranabir sold 2500 kgs. of potato to Sunder who paid by cheque which was dishonoured. Ranabir gave a delivery order to Sunder. Sunder resold the whole lot of potatoes to Singh (who bought in good faith for valid consideration) and endorsed the delivery order to Singh. Ranabir refused to deliver the potato against that delivery order to Singh on the plea of non-payment. Advise Singh. 2
- (ii) Akhilesh entered into an agreement with Sekhar to deliver Sekhar 5000 bags to be manufactured. The bags could not be manufactured and supplied because of strike by the workers. Decide whether Akhilesh is liable under the provisions of Contract Act, 1872. 4
- (b) (i) Mr. Amit is the owner of a writing table but he does not know that he is the owner of table. Mr. Sumit pretends to be the owner of that table and sells to Mr. Amit. Whether this is a sale as per the Sale of Goods Act, 1930? 2
- (ii) M/s. XYZ Ltd. supplied milk to Mr. Jacob who consumed the milk was infected and died. Laboratory test report indicated that the milk contained typhoid germs. State the liability of M/s. XYZ Ltd on the basis of sale of Goods Act, 1930. 2
- (c) (i) Mr. Ram Chandra is a member of EPF and PF statement as on 31.03.2013 shows that he has the following balance.
- | | | |
|------------------|----|--------------|
| Employer's Share | .. | INR 1,50,000 |
| Employee's Share | .. | INR 2,00,000 |
- Whether Ram Chandra can take non-refundable loan from EPF balance for marriage of his daughter? 2
- (ii) Fill in the blanks 2
- An employer who intends to close down an undertaking of an Industrial Establishment shall in the prescribed manner apply for prior permission at least _____ days before the date on which the intended closure is to become effective to the appropriate Government. If the appropriate Government does not communicate the order granting or refusing grant permission to the Employer within _____ days from the date on which such application is made, the permission applied for shall be deemed to have been granted on the expiration of said _____ days.
- (iii) Answer based on Consumer Protection Act, 1986. 2
- On admission of a complaint by the District Forum, a copy of complaint is to be referred to Opposite Party, within 3 days directing him to give his version within _____ days. This period may be extended by another _____ days.
- Any person aggrieved by an order made by the District Forum may prefer appeal to _____ within _____ days from the date of order.
- (d) Mr. Mukesh did not get certain information about his provident fund contributions. He wants to proceed under RTI Act for obtaining the same. Advise him what he should do. 2

Answer:

4. (a) (i) Mr. Singh cannot claim delivery of potato. The rule of law is Nemo dat quod non-habet i.e. one cannot give what one does not have. Sunder's title having become defective by dishonor of the cheque, he cannot confer a good title to Mr. Singh. The only exception to the aforesaid rule is the possession of a "holder-in-due course" in respect of negotiable instrument. But delivery order is not a negotiable instrument.
- (ii) According to Sec 56 of Contract Act 1872 when the performance of a contract becomes impossible or unlawful subsequent to its formation, the contract becomes

Suggested Answer_Syl2008_Dec2014_Paper_6

void i.e. "Supervening Impossibility.

But impossibility of performance is, as a rule, not an excuse from performance, whether a promise becomes absolutely impossible depends upon the facts of each case.

The performance does not become absolute impossible on account of strike, lock out and civil disturbance and the contract in such a case is not discharged unless otherwise agreed by the parties to the contract (Budget V Bennington, Jacobs V Credit Lyonnais).

In this case, this difficulty in performance cannot be considered as impossible of performance and hence Akhilesh is liable to Mr. Sekhar for non-performance of contract unless otherwise there is specific clause in the agreement entered into between Sekhar & Akhilesh.

- (b) (i) In the case of sale there must be at least two parties because the property in goods has to pass from one person to another. Its first essential, therefore, is that the seller and buyer must be different persons. A person cannot buy his own goods.

In this case there is no Sale because Amit cannot buy the Table which is already his own (Bell V Lever Bros Ltd. 1932 act 161).

- (ii) In case of food article, there is an implied condition that the item is fit for human consumption. One of the conditions as to quality & fitness.

Hence there was a breach of condition as to fitness and XYZ & CO. was liable to pay damages (Frost V Avlesbury Dairy Co. Ltd. 1905 1 KB 608.)

- (c) (i) Sec 68K of E.P.F. & Misc Provisions Act. 1952 provides that a member can take non-refundable loan for marriage of his daughter upto 50% of his share of contribution with interest thereon standing to his credit in the fund on the date of approval/authorization provided he has completed seven years of membership of the fund. Hence he is entitled for ₹1,00,000/-

Alternate Answer:

Provides "member can withdraw from his accumulations to cater the financial exigencies in life and no need to refund unless misused".

- (ii) Factories Act 1948 provides that (Sec 40A)

90 days
60 days
60 days

- (iii) 21 days

30 days
15 days
30 days

- (d) As per section 6 of RTI Act, A person, who desires to obtain any information under this Act, shall make a request in writing or through electronic means in English or Hindi or

Suggested Answer_Syl2008_Dec2014_Paper_6

in the official language of the area in which the application is being made, accompanying such fee as may be prescribed, to the Central Public Information Officer or State Public Information Officer, as the case may be, of Provident Fund, specifying the particulars of the information sought by him.

SECTION II (50 Marks) (Auditing)

5. **Comment on the following based on legal provisions (No mark for wrong reasons or justification):** **2x7=14**
- (a) **Inventory turnover ratio is calculated by the auditor to obtain evidence concerning managements' ascertainment about valuation of inventory.**
 - (b) **Auditor is not bound to attend the Annual General Meeting of the company.**
 - (c) **Auditor advised to amend the faulty Profit & Loss A/c. but the director (finance) of the company disagreed. Hence auditor has no action to take.**
 - (d) **It is an accepted fact that internal auditing function to be effective, must be independent of the activities to be audited.**
 - (e) **According to the Institute of internal auditors, internal audit involves five areas of operations (only give four names without explanation).**
 - (f) **When it is an Information Technology audit, the Auditor is to know the meaning of "system"—What is it?**
 - (g) **The Society at large also feels the need of Management Audit.**

Answer:

5. (a) This ratio is used by the management to ascertain the Profitability. Higher inventory ratio suggest efficient business whereas lower ratio suggest dull business for improvement of which some steps shall be taken.
Calculation of Inventory turnover ratio and its comparison with those of previous years ratio will provide an evidence on correct valuation of slow moving defective and obsolete items included in the inventories.
- (b) The auditor has right to attend the General Meetings of the company. As well as he can participate in the discussions relating to Accounts and Audit of the Company.

Notice of General Meeting is required to be given to Auditor also.

He may attend the General Meeting and shall have right to be heard at such meeting on any part of the business which connects him as the Auditor.

But he is not bound to attend the meeting.
- (c) Auditor has right to take action.
If the Auditor's advice to amend faulty profit & loss account and/or Balance Sheet not followed by the Directors, he can report it to shareholder by way of qualified report.
- (d) Yes but it cannot be a fully independent department for various reasons. A proper organizational status for the Internal Auditing department ensures its relative independence so that it can carry out its work freely and objectively and render impartial and unbiased service.

Suggested Answer_Syl2008_Dec2014_Paper_6

- (e) Areas of operations are:
 - (i) Reliability and integrity of financial and operating information.
 - (ii) Economical and efficient use of Resources.
 - (iii) Compliance with Laws, Policies, Plans, Procedures & Regulations.
 - (iv) Accomplishment of Established Goals for operations.
 - (v) Safeguarding of assets.
- (f) System means the instrumentality that combines inter related interacting artifact designed to work as a coherent entity.
- (g) Society at large likes to be assured that the top and middle management discharges their functions efficiently and to the best advantage to the society. The management audit satisfy the different interest of Groups like customers, employees, Citizens, Government & others of the society and also guide the management in the application of scientific methods in business management for social well being.

- 6. (a) What is audit evidence? 2
- (b) Information system Auditor is concerned with certain objectives — What are those objectives? 2
- (c) What are the internal control aspect in relation to Bank Reconciliation Statements? 2
- (d) An Audit Firm comprising of two partners hold office as Auditor of 41 Private Companies. Out of which paid up share capital of 20 companies exceed INR 50 lakhs. Senior Partner said, their present holding are permitted as per companies Act, 1956. (or Answer be based on Companies Act, 2013) 2
- (e) A company's receivable turnover rate decreased from 7.3 to 4.3 over the last three years. Amal opined, this is due to stringent credit policy. Answer with workings. 2
- (f) The company Auditor has right to receive notice for Annual General Meeting only—Offer your views. 2
- (g) As an internal auditor, how you will verify the "Idle Facilities"? 2
- (h) Auditors specific objectives shall change due to processing the accounting data manually and by computer — Offer your views. 2
- (i) Is it correct that some of the appraisal areas cannot be covered in a Management Audit System? 2

Answer:

- 6. (a) Audit evidence refers to information used by the Auditor in arriving at the conclusions on which the Auditors opinion is based. Concept of evidence is fundamental to accounting. All auditing techniques and procedures are determined from it.

Audit evidence includes both information contained in the Accounting Records underlying the Financial Statement and other informations.

- (b) Information system Auditor is concerned with following objectives -
 - (i) Asset safeguarding
 - (ii) Data integrity
 - (iii) System effectiveness
 - (iv) System efficiency

To achieve these objectives, Auditor may fail to detect real material losses or errors due

Suggested Answer_Syl2008_Dec2014_Paper_6

to the nature of verification etc. Hence there are some Audit risk. To reduce the risk, the appropriate Audit approach is selected and designed accordingly.

- (c) Internal control aspects in relations to bank reconciliation statement are as follow :
- (i) Receipt of bank Statement.
 - (ii) Frequency of Reconciliation Statement.
 - (iii) Authorization.

Special attention to be given for long outstanding, un-presented cheques, stop payment notices, examination of the sequence of cheque numbers and comparison of cheque details with detail records in the cash book.

- (d) As per section 224 (1B) of the Companies Act, 1956, private companies have been exempted from the provisions with respect to ceiling on number of audits. As per the section, an audit firm is entitled to 20 audits per partner that is 40 audits in the given case out of which not more than 10 companies per partner should be having paid-up share capital of ₹25 Lakhs or more. The firm can do audit of any number of private companies. Thus, there is no problem in audit firm holding office of 41 private companies.

Alternate Answer:

As per companies act 2013

SEC 141 (3) (g) of Companies Act 2013 provides that a person (i.e. A chartered accountant in practice) shall not be eligible for appointment as an auditor of a company if such person or a partner is at the date of such appointment or reappointment holding appointment as auditor of more than 20 (twenty) companies. That means an auditor cannot audit more than 20 companies.

Hence two partners can audit only 40 companies in this case.

- (e) False
The decrease in receivable turnover rate from 7.3 to 4.3 over last three years is due to more liberal credit policy. Customers would be taking longer time to pay [$365/4.3 = 85$ days] compared to [$365/7.3 = 50$ days].
- (f) Wrong
The Auditor of the company has a right to receive all notices to any General Meeting of the Company.
- (g) Following areas /items are required to be checked/verified -
- (i) Find out the reasons for idle facilities.
 - (ii) Review the plans, procedures for control of idle facilities.
 - (iii) Examine the scope for utilization of the idle facilities. Can the facilities be leased out?
 - (iv) See whether any review report is made periodically for facilities remaining idle etc.
- (h) Auditors specific objectives do not change whether accounting data is processed manually or by computer. However methods of applying audit procedure together evidence may be influenced by the methods of computing process. The auditor can use manual Audit procedure or computer assisted techniques or a combination of both to obtain sufficient application. It may be difficult or impossible for the auditor to obtain certain data for inspection, inquiry or confirmation without computer assistance.

Suggested Answer_Syl2008_Dec2014_Paper_6

- (i) Yes - this is one of the limitations of management audit.
In a Management Audit Scheme, the areas of investigation should fruitfully cover the entire management system and so the situation demands the audit team to complete the studies under a time constraint which may result in not covering some of the important appraisal areas.

7. (a) Is it correct that "Intangible Assets" are prepared as per AS 18 whereas "Related Party" are dealt with AS 20? State the correct Answer if incorrect. 2
(b) How you will verify the "Bad Debts" written off but has been recovered? 2
(c) A firm of Cost Accountants having 3 practicing Cost Accountants and one partner appearing for final examination of Institute of Cost Accountants have been appointed as Cost Auditor by ABC Ltd. This is not a valid appointment—Offer your opinion. 2
(d) How an auditor shall report to comply with CARO in respect of 2+2
(i) "Default in repayment of dues".
(ii) "Guarantees of loan taken by others".
(e) How you will verify the "sales return"? 2
(f) What are the areas shall be verified by an auditor is respect of 2+2
(i) "System & Applications".
(ii) Information processing facilities.
(g) State any four advantages of management audit. 2

Answer:

7. (a) "Intangible Assets" are dealt with AS 26 and "Related Party" is dealt with AS 18.
- (b) (i) To see that the amount has been properly recorded in cash/bank Book.
(ii) To see that recovery of old Bad debts already written off is treated as other revenue instead of crediting to the concerned Debtors A/c.
(iii) To see the amount of such Bad Debts recovered has been verified from the letter of the client or collecting agency or notification from the court.
- (c) This is not a valid appointment. A firm shall be qualified to be appointed as Cost Auditor if all the partners of the firm are practicing Cost Accountants within the meaning of Cost and Works Accountants Act 1959 (Sec. 233B of the Companies Act, 1956).
- (d) (i) Default in Repayment of dues -
Whether the company has defaulted in repayment of dues to a financial institutions or bank or debenture holders? If yes the period, amount of default to be reported.
(ii) Whether the company has given any guarantee for loans taken by others from Bank, or Financial Institutions, the terms and conditions which are prejudicial to the interest of the company.
- (e) Sales Return: Auditor or internal auditor shall take following steps, to examine and review the -
(i) Procedure adopted in receiving and recording of sales return.
(ii) Compare the sales return with total sales. If the amount of sales return is considered high, ascertain the reasons there for and suggest remedial actions.
(iii) To see whether freight charges incurred in returning the sales are borne by the customer. Examine whether there is clear policy in this regard.
(iv) Whether Sales return are properly recorded & adjusted.
(v) Whether there is system for issue of credit notes.

Suggested Answer_Syl2008_Dec2014_Paper_6

- (f) (i) **Systems & Application**
An auditor to verify whether systems and applications are appropriate, efficient and adequately controlled ensure valid, reliable, timely and secure input processing and output at all levels of a system activity.
- (ii) **Information Processing Facilities**
An auditor should verify whether this processing facility is controlled to ensure timely accurate and efficient processing of applications under normal and potentially disruptive conditions.
- (g) Advantages of Management Audit
- (i) The company's personnel know the organizational policies, plans, personnel operations, personalities and working relationships, the political climate, the functional importance, and some of the problems themselves.
- (ii) The audit team need not spend an unduly long time for familiarizing themselves with the background information for study.
- (iii) It may be easier to get the support of the higher management, because such audit in the form of self appraisal apparently involves no extra cost.
- (iv) The acceptance of the findings may be comparatively easier because the concerned personnel may readily accept the recommendations from the internal management audit team (consisting of co-workers) than from the external management auditors (or consultants).
- (v) The implementation of the new method of operation or organizational arrangement may be easier because the personnel who designed and advised it are on the premises. The constant co-operation necessary in the implementation phase are greatly facilitated.
- (vi) The experience and expertise gained by the company personnel in the conduct of management by self appraisal could be gainfully utilized for subsequent audits.
8. (a) **How you will verify livestock?** 4
- (b) **What are the liabilities of Auditor? Give only the names without details.** 2
- (c) (i) **CARO is not applicable to Government Companies as their Auditors are appointed by Comptroller & Auditor General of India.** 2
- (ii) **How an Auditor shall report in his audit report to comply with CARO in respect of "maintenance of Cost Records"?** 2
- (d) **How you can reduce the sample errors?** 2
- (e) **What is Computer Auditing?** 4
- (f) **Out of company's talent (i.e. "Audit Committee", "Officer on special Duty") and outside management consultants, who will be the best for conducting the management audit?** 2

Answer:

8. (a) Live Stock
- (i) See the live Stock Register and note down carefully the particulars like breed, year of purchases, purchase price, depreciation etc. for various categories of animals.
- (ii) See that some identification number is given to identify the animals.
- (iii) Examine the basis of valuation of animals. In case the animals are purchased at the age of maturity, the cost will include Purchase Price plus freight. If the animal is reared from its conception and then brought to Maturity, the cost includes cost of calving, cost of fodder etc. consumed, till maturity and the suitable share of overheads.
- (iv) See that the cost up to the maturity stage of animal has been written off once the

Suggested Answer_Syl2008_Dec2014_Paper_6

- earning capacity of the animals starts declining over the remaining life.
- (v) Ensure that disposal value at the end of the life of the assets has been adjusted properly.
- (b) Liabilities of Auditor
Auditors liability are subject to change from time to time. Auditors are liable to different Authorities including third parties. Auditors liability can be classified as under -
- Liabilities for –
- (i) Negligence
 - (ii) Misfeasance
 - (iii) Liabilities to third parties
- Liabilities under –
- (i) Companies act 1956 & 2013
 - (ii) Penal Code
 - (iii) Income Tax Act 1961
 - (iv) Chartered Accountant Act 1949 & Cost and Works Accountants Act 1956, Company Secretaries Act other Act and rules.
- (c) (i) Not Correct
In case of Government companies, CARO is also applicable and this is in addition to the directions of Comptroller and Auditor General of India.
- (ii) Where Maintenance of cost records has been prescribed by the Central Government under Companies Act, whether such accounts and records have been made and maintained.
- (d) Method of Reducing Sample Errors
The Simplest way of increasing the accuracy of a sample is to increase the sample size i.e. the number of units in the sample. Sampling error decreases with the increase in sample size. The bigger the sample size -the lesser the chances of sample errors.
- (e) Computer Auditing
In information processed on computers the one way of auditing is to get the printouts of all records, accounts and information and then check it as usual, but this is very time consuming and cannot evaluate the system of internal controls and certain errors etc. remains undetected. The other more acceptable way is to evaluate the controls in the computer information system and then decide the nature of timing and extent of the substantive procedure to be followed and make use of computer in conducting compliance tests as well as substantive test, but the auditor must have sufficient knowledge of computer system even in certain cases specialized skills in operations of computer system.
- (f) Considering the prevailing circumstances in a company a combination of company talent and outside management consultants would be a best team to conduct the management audit. The advantages of each compliment the other.