INTERMEDIATE EXAMINATION
GROUP II
(SYLLABUS 2012)

SUGGESTED ANSWERS TO QUESTIONS
JUNE 2017

Paper-12: COMPANY ACCOUNTS AND AUDIT

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

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

Where considered necessary, suitable assumptions may be made and

Clearly indicated in the answer.

Answer all bits of a question at one place.

Open a new page for answer to a new question.

SECTION – A

Answer all the following questions.

1. Answer the following questions: 2×5 =10

(a) ROLTA Ltd. had 10,00,000 equity shares (₹ 10 each) outstanding on 01.04.2016. The company issued one new share (right) for each five shares outstanding at ₹ 15 on 01.06.2016. The fair value of one Equity Share immediately before the right issue was ₹ 21. Calculate as per AS20, the theoretical ex-rights fair value per share of ROLTA Ltd.

(b) RENAN Ltd. finds at the end of financial year 2016-17 that there is a law suit outstanding. The possible outcome as estimated by the Board of Directors are as under:

	Probability	Amount of Loss (`)
Win	0.55	__
Loss-with high damages	0.20	1,50,00
Loss-with low damages	0.25	1,20,00

Compute the amount of contingent liability to be shown by way of a note to the financial statement as per AS – 29.

(c) What are the items taken into account while calculating segmental revenue?

(d) URASHI Ltd. acquired a patent at a cost of ₹ 60 lakh for a period of four years and the product life cycle is also four years. The company capitalized the cost and started amortizing at ₹15 lakh per annum. After three years, it was found that the product life cycle may continue for another 3 years from then. The net cash flow from the product during these 3 years are expected to be ₹ 20 lakh, ₹ 30 lakh and ₹ 25 lakh respectively.

Find out the amortization cost of the years as per AS-26.

(e) State the disclosure requirements under AS – 12.

Answer:

(a) According to AS-20, Theoretical Ex-right Fair Value per share
= [(₹21×10,00,000)+(₹15 × 2,00,000)]/(10,00,000 + 2,00,000) shares = ₹20.

(b) According to AS-29 for the purpose of disclosure of contingent liability by way of note, the amount will be:
0.20 × 1,50,000 = ₹30,000
0.25 × 1,20,000 = ₹30,000
60,000

The contingent liability to be shown in financial statement = ₹60,000.

(c) Segmental Revenue is the aggregate of
(i) the portion of enterprise revenue that is directly attributable to a segment;
(ii) the relevant portion of enterprise revenue that can be allocated on a reasonable basis to a segment; and
(iii) revenue from transactions with other segments of the enterprise.

(d) Total cost of the patent is ₹60 lakh.
The amortizations for first three years = 15 × 3 = ₹45 lakh
Unamortized amount of ₹(60 - 45) lakh = ₹15 lakh to be amortized for next three years in proportion of cash flows from the product in these years.

The amount to be amortized during next years calculated as follows:

Year	Net cash flow (₹ in lakh)	Amortization Amount (₹ in lakh)
4	20	15 × 20/75 =
5	30	15 × 30/75 =
6	25	15 × 25/75 =
	75	1

(e) The disclosures under AS-12 are as follows:

(i) The accounting policy adopted for Government grants including the method of presentation in the financial statements.
(ii) The nature and extent of Government grants recognized in the financial statements including grants of non-monetary assets given at a concessional rate or free of cost.
(iii) In the case of Companies, deferred government grants should be disclosed separately under the head non-current liabilities to the extent entity expects not to recognize the same within the next 12 months after the end of reporting period and the balance should be disclosed separately under the head current liabilities.

2. Match the following items in Column 'A' with items shown in Column 'B' **1×5=5**

	Column 'A'		Column 'B'
1.	Defined Contribution Plans	(a)	AS-20
2.	Amalgamation in the nature of merger	(b)	Unearned finance income
3.	Diluted Potential Equity Shares	(c)	AS-15
4.	AS-29	(d)	Pooling of Interest Method
5.	AS-19	(e)	Onerous Contract

Answer :

	Column 'A'		Column 'B'
1.	Defined Contribution Plans	(c)	AS-15
2.	Amalgamation in the nature of merger	(d)	Pooling of Interest Method
3.	Diluted Potential Equity Shares	(a)	AS-20
4.	AS-29	(e)	Onerous Contract
5.	AS-19	(b)	Unearned finance income

3. Answer any two questions: 5×2=10

(a) What do you understand by Audit Evidence?

(b) What are the objectives of Operational Audit?

(c) 'Management audit is useful for society at large'.—Comment.

(d) Write a short note on Defined Contribution Plan?

(e) State the two components of Audit risk.

Answer:

(a) Audit evidence may be defined as the information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information.

(b) The Objectives of operational audit are as given below:

1. To ensure that the operational activities are as per objectives of the company.
2. To assure management that MIS has been functioning properly to attain organizational objectives.
3. To assure management that the management control system is functioning efficiently and effectively.

(c) The management audit is very useful for society at large. It is intended to review all managerial aspects of the company so as to enhance efficiency and efficacy of the entire system which has a social advantage as well. It serves the interest of different segments of society like customers, creditors, stakeholders, government and people at large.

(d) Defined Contribution plans (DCP)

1. Retirement benefit is determined by contribution at agreed /specified rate to the fund together with earnings thereof.
2. Contribution (e.g.PF) whether paid or payable for the reporting period is charged to P/L statement.
3. Excess if any is treated as prepayment.

(e) Components of audit risks:

- Inherent risk (risk that material errors will occur)
- Control risk (risk that the client's system of internal control will not prevent or correct such errors); and
- Detection risk (risk that any remaining material errors will not detected by the auditor).

SECTION – B

Answer any three questions from Q no 4,5,6 and 7. **15×3=45**

4. (a) A company had 16,000, 12% Debentures of 100 each outstanding as on 1st April, 2015, redeemable on 31st March, 2016. On that day, Sinking fund was ₹ 14,98,000 represented by 2000 own debentures purchased at the average price of ₹ 99 and 9% stocks face value of ₹13,20,000. The annual installment was ₹ 56,800.

On 31st March, 2016 the investments were realized at ₹ 98 and the debentures were redeemed.
You are required to prepare 12% Debentures Account and Debenture Redemption Sinking Fund.
Account for the year ending 31st March 2016. **9**

(b) Goods purchased on 24.2.2016 of US $1,000 for which payment was made on 05.06.2016. Exchange Rate on 24.2.2016 ₹ 61.60 per US $, on 31.3.2016 ₹ 62.00 per US $, 05.06.2016 ₹62.50 per US $.State the Accounting Treatment at the date of transaction, reporting date and settlement date as per AS-11. **6**

Answer :

(a) Dr. (I) 12% DEBENTURES ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Own Debentures A/c	2,00,000	By Balance b/d	16,00,000
To Bank A/c	14,00,000		
	16,00,000		**16,00,000**

Dr. (II) DEBENTURES REDEMPTION SINKING FUND ACCOUNT Cr.

Particulars	₹	Particulars	₹
To 9% Stock A/c (loss)	6,400	By Balance b/d	14,98,000
To General Reserve A/c (b.f)	16,93,200	By Profit and loss A/c	56,800
		By Interest on Sinking Fund A/c	1,42,800
		By Own Debentures A/c	2,000
	16,99,600		**16,99,600**

Working Note:

(i) Amount of 9% Stock as on 1st April, 2015 Sinking Fund Balance as on 1st April, 2015 Less: Own debentures	 ₹14,98,000 ₹(1,98,000) ₹13,00,000
(ii) Sales value of 9% Stock = (₹13,20,000/₹100) × ₹98	₹12,93,600
(iii) Interest credited to Sinking Fund = (₹13,20,000 × 9%) + (₹2,00,000 × 12%)	₹1,42,800

Dr. (III) OWN DEBENTURES ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance b/d	198,000	By 12% Debentures A/c	2,00,000
To Sinking Fund A/c	2,000		
	2,00,000		**2,00,000**

Dr. (IV) 9% Stock ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance (Face value 13,20,000)	13,00,000	By Bank A/c	12,93,600
		By Sinking Fund A/c (loss on sales)	6,400
	13,00,000		**13,00,000**

(b) Accounting Treatment at the Date of Transaction:

As per para 9 of AS 11 on 'The Effects of Changes in foreign Exchange Rates'., a foreign currency transaction should be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate at the date of the transaction.
Accordingly, Goods purchased and corresponding Creditors would be recorded at ₹ 61,600 [i. e. 1,000 × ₹ 61.60]

Accounting Treatment at the Reporting Date

As per para 11 of AS 11, at balance sheet date all monetary items should be reported using the Closing Rate.
Accordingly,
1. Closing Creditors will be reported at ₹ 62,000 i.e. [1,000 x ₹ 62.00]
2. Exchange Loss of ₹ 400 i.e. [₹ 62,000 - ₹ 61,600] should be debited in Profit and Loss Account for the year 2 015 - 2016.

Accounting Treatment at the Settlement Date

Exchange Differences on settlement of monetary items should be transferred to Profit and Loss Account as gain or loss, Accordingly, Exchange Difference of ₹ 500 i.e [₹62,500 - ₹62,000] should be debited in Profit and Loss Account for the year 2016-2017.

5. (a) The following particulars relate to VIEN Ltd. which has gone into voluntary liquidation on 31st December, 2015:

Liabilities	Amount (₹)	Assets	Amount (₹)
Share capital:		**Assets:**	
5000, 10% Cumulative preference shares of ₹ 100 each fully paid-up.	**5,00,000**	**Non-current assets**	
2500 Equity shares of ₹ 100 each 75 paid up.	**1,87,500**	**Land & Building**	**2,50,000**
7,500 Equity shares of ₹100 each, 60 paid up.	**4,50,000**	**Plant & Machinery**	**6,25,000**
Non-current Liabilities		**Furniture & Fixtures**	**1,00,000**
15% Debentures secured by a floating charge	**2,50,000**	**Current assets**	
Current Liabilities		**Stock**	**1,37,500**
Trade payables	**3,18,750**	**Trade receivables**	**2,75,000**
Outstanding interest on debentures	**37,500**	**Cash and bank balance**	**75,000**
		Profit & Loss Account	**2,81,250**
	17,43,750		**17,43,750**

Other Information:

(i) The assets were sold and realized as follows:

	₹
Land & Building	3,00,000
Plant & Machinery	5,00,000
Furniture & Fixtures	75,000
Stock	1,50,000
Trade Receivables	2,00,000
Expenses of liquidation were	27,250

(ii) Preference shares dividends are in arrears for the last 2 years.

(iii) Trade payables include preferential creditors of ₹38,000.

(iv) Liquidator is entitled to receive commission of 3% on assets realized except cash.

(v) Preference shareholders have right to dividend at the time of liquidation.

(vi) The final payment including those on debentures is made on 30th June, 2016.

You are required to prepare liquidator's final statement of account. 9

(b) From the following information, prepare Cash Flow Statement:

BALANCE SHEET AS AT 31.03.2016			
Particulars	Note	31.03.2016 ₹	31.03.2015 ₹
I. EQUITY AND LIABILITIES			
(1) Shareholder's Funds			
(a) Share Capital		12,50,000	10,00,000
(b) Reserves and Surplus	1	4,90,000	4,00,000
(2) Non-Current Liabilities [Long Term Loan]		4,00,000	5,00,000
(3) Current Liabilities			
Trade payables		4,00,000	5,00,000
Short-term Provisions (Provision for tax)		60,000	50,000
Total		26,00,000	24,50,000
II. ASSETS			
(1) Non-Current Assets			
Tangible Fixed Assets	2	13,00,000	11,50,000
Non-Current Investments		50,000	1,00,000
(2) Current Assets			
Inventories		2,80,000	3,00,000
Trade Receivables		4,20,000	4,00,000
Cash & Cash Equivalents		5,50,000	5,00,000
Total		26,00,000	24,50,000

NOTE 1: RESERVES AND SURPLUS		
Particulars	31.03.2016 ₹	31.03.2015 ₹
Profit and Loss A/c	4,80,000	4,00,000
Capital Reserve	10,000	—
Total	4,90,000	4,00,000

NOTE 2: TANGIBLE FIXED ASSETS		
Particulars	31.03.2016 ₹	31.03.2015 ₹
Land Building	3,80,000	4,00,000
Machinery	9,20,000	7,50,000

Total	**13,00,000**	**11,50,000**

Additional information:

(1) Depreciation written off on land and building ₹20,000.

(2) The company sold some investment at a profit of ₹ 10,000, which was credited to Capital Reserve.

(3) Income-tax provided during the year ₹55,000.

(4) During the year the company purchased a machinery for ₹ 2,25,000. They paid ₹1,25,000 in cash and issued 10000 equity shares of ₹ 10 each at par.

You are required to prepare a Cash Flow Statement for the year ended 31st March 2016 as per AS3 by using indirect method. 6

Answer :

(a) Liquidator's Final Statement of Account

Dr. **Cr.**

Receipts	Amount (₹)	Payments	Amount (₹)
To Assets Realised:		By Liquidation Exp.	27,250
Cash at Bank	75,000	By Liquidator's Remuneration	36,750
Land & Building	3,00,000	By Preferential Creditors	38,000
Plant & Machinery	5,00,000	By Debenture Holders	3,06,250
Furniture & Fixtures	75,000	W.N.-1	
Stock	1,50,000	By Unsecured Creditors	2,80,750
Trade Receivables	2,00,000	(3,18,750 - 38,000)	
Call on equity shares		By Preference Shareholders	6,00,000
(₹ 2.65 × 7,500)	19,875	(5,00,000 +1,00,000)	
		By Equity Shareholders W.N.-2(₹12.35 × 2,500)	30,875
	13,19,875		13,19,875

Workings:

1. Payment to Debenture Holders

	(₹)
15% Debentures secured by floating charge	2,50,000
Add: Outstanding debenture interest	37,500
Add: Interest from 01.01.16 to 30.06.16	18,750
(since the company is solvent)	3,06,250

2. Total paid up value of equity shares ₹(1,87,500 + 4,50,000) = ₹6,37,500

Less: Net assets available for equity shareholders ₹ (13,00,000 – 12,89,000) = ₹11,000

Total loss to be borne by the equity shareholders 6,26,500

	₹	₹
Paid up value of shares	75.00	60.00
Less: Net loss per share	62.65	62.65
To be paid per share	12.35	___
To be taken per share	___	(2.65)

(b) CASH FLOW STATEMENT FOR THE YEAR ENDING 31ST March , 2016

Particulars	₹	₹	₹
(i) Cash flows from Operating Activities:			
Net Profit before tax tor the year [80,000 + 55,000]	1,35,000		
Add: Depreciation on machinery	55,000		
Depreciation on land & building	20,000		

Operating profit before change in working capital Add: Decrease in Inventories Less: Increase in Trade Receivables Less: Decrease in Trade Payables Cash generated from Operations Less: Income tax paid **Net Cash generated from operating activities**	2,10,000 20,000 (20,000) (1,00,000) 1,10,000 (45,000)	**65,000**	
(ii) Cash flow from Investing Activities: Purchase of machinery (2,25,000 - 1,00,000) Sale of investment **Net Cash used in investing activities**	(1,25,000) 60,000	**(65,000)**	
(iii) Cash flow from Financing Activities Issue of equity shares (2,50,000 - 1,00,000) Repayment of long term loan **Net Cash generated from Financing Activities**	1,50,000 (1,00,00)	**50,000**	
Net Increase in Cash and Cash Equivalents			**50,000**
Cash and Cash Equivalents at the beginning			**5,00,000**
Cash and Cash Equivalents at the end (5,00,000 – 50,000)			**5,50,000**

Working Notes:

Dr. (I) MACHINERY ACCOUNT Cr.

Particulars	₹	**Particulars**	₹
To Balance b/d	7,50,000	By Depreciation (bal.fig)	55,000
To Bank A/c	1,25,000	By Balance c/d	9,20,000
To Equity Share Capital A/c	1,00,000		
	9,75,000		9,75,000

Dr. (II) PROVISION FOR TAXATION ACCOUNT Cr.

Particulars	₹	**Particulars**	₹
To Bank A/c (Bal.fig)	45,000	By Balance b/d	50,000
To Balance c/d	60,000	By Profit and Loss A/c	55,000
	1,05,000		1,05,000

Dr. (III) INVESTMENT ACCOUNT Cr.

Particulars	₹	**Particulars**	₹
To Balance b/d	1,00,000	By Bank A/c (bal. fig)	60,000
To Capital reserve (Profit on Sale of investments)	10,000	By Balance c/d	50,000
	1,10,000		1,10,000

6. (a) Crystal Company Limited decided to reconstruct its business as it has accumulated huge losses. The following is the Balance Sheet of the company as on 31.03.2016 before reconstruction:

BALANCE SHEET AS ON 31.03.2016			
Liabilities	**₹**	**Assets**	**₹**
300000 Equity shares of ₹ 10 each fully	**30,00,000**	**Goodwill**	**5,20,000**

paid up			
160000, 6% Preference shares of ₹ 10 each fully paid up	16,00,000	Patents	1,50,000
6% Debentures (Secured against Land & Building)	15,00,000	Land & Building	17,00,000
Bank overdraft	5,80,000	Plant & Machinery	2,00,000
Trade Payables	12,00,000	Investments (at cost)	2,20,000
Provision for Income Tax	2,00,000	Trade Receivables	17,40,000
		Inventories	17,00,000
		Profit & Loss A/c	18,50,000
	80,80,000		80,80,000

Following scheme of reconstruction has been approved by all interested parties:

(i) All equity shares are reduced to ₹ 3 each and preference shares to ₹ 7 each.

(ii) Debenture holders agree to take over a part of land and building, book value of which is ₹ 7,00,000 towards their 50% claim. Rate of interest of balance 50% debentures increased to 9%.

(iii) Goodwill and patent will be written off.

(iv) 10% of Trade Receivables to be provided for bad debts.

(v) Inventories to be written off by ₹ 2,60,000.

(vi) 50% of balance land & building sold for ₹6,00,000 and remaining land & building valued at ₹ 6,00,000.

(vii) Investments to be sold for ₹ 2,00,000.

(viii) There are pending contracts amounting to ₹70,00,000. These contracts are to be cancelled on payment of penalty @ 5% of pending contract amount.

(ix) The income tax liability of the company is settled at ₹3,06,000. Provision for income tax will be raised accordingly.

(x) 1/3 of Trade Payables decided to forgo their claim.

(xi) After making all the above adjustments, balance amount available through scheme, will be utilized to write off the value of plant & machinery to that extent.

Required: Pass the necessary journal entries. 10

(b) Write short note on: Managerial Remuneration. 5

Answer:

(a) JOURNAL OF CRYSTAL COMPANY LIMITED

Date	Particulars	Dr. (₹)	Cr. (₹)
1.	Equity Share Capital A/c (₹ 10) Dr. To Equity Share Capital A/c (₹ 3) To Reconstruction A/c (Being reduction of equity share of ₹10 each to shares of ₹3 each as per the reconstruction scheme)	30,00,000	 9,00,000 21,00,000
2.	6% Preference Share Capital A/c (₹ 10) Dr. To 6% Preference Share Capital A/c (₹ 7) To Reconstruction A/c (Being reduction of preference shares of ₹ 10 each to shares of ₹7 each as per the reconstruction scheme)	16,00,000	 11,20,000 4,80,000
3.	6% Debentures A/c Dr. To Land & Building A/c To 9% Debentures A/c To Reconstruction A/c (Being 50% claim of debenture holders discharged by transfer of a part of land & building having book value ₹ 7,00,000 and rate	15,00,000	 7,00,000 7,50,000 50,000

	of interest of balance 50% debentures increased to 9% as per the reconstruction scheme)		
4.	Bank A/c Dr. To Land & building A/c To Reconstruction A/c (Being 50% of balance land & building having book value of ₹ 5,00,000 sold for ₹ 6,00,000 as per the reconstruction scheme)	6,00,000	 5,00,000 1,00,000
5.	Land & building A/c Dr. To Reconstruction A/c (Being 50% of balance land & building having book value ₹ 5,00,000, valued at ₹ 6,00,000, as per the reconstruction scheme)	1,00,000	 1,00,000
6.	Bank A/c Dr. Reconstruction A/c To Investment A/c (Being all the investments sold as per the reconstruction scheme)	2,00,000 20,000	 2,20,000
7.	Sundry creditors A/c Dr. To Reconstruction A/c (Being 1/3 of sundry creditors decided to forgo their claim as per the reconstruction scheme)	4,00,000	 4,00,000
8.	Reconstruction A/c Dr. Bank overdraft A/c Dr. To, Goodwill A/c To, Patents A/c To, Provision for doubtful debts A/c To, Stock A/c To, Bank A/c To, Provision for income tax A/c To, Profit and Loss A/c (Being goodwill, patent, profit and loss, part value of stock, plant and machinery, penalty paid tor cancellation of contracts written off and provisions made for doubtful debts and income tax, as per the reconstruction scheme)	32,10,000 2,00,000	 5,20,000 1,50,000 1,74,000 2,60,000 3,50,000 1,06,000 18,50,000

(b) Managerial remuneration:

Companies Act has not defined managerial personnel. As per Schedule V, it appears that managerial personnel mean MD/Whole time director and manager. Computation of managerial remuneration is based on profit and is to be computed as per the provisions of Section 198 just before computing the provision for taxation as follows:

Profit as per books		xxxx
Add: Depreciation as per books	xxxx	
Provision for Doubtful debts	xxxx	
Misc. Exp. Written back	<u>xxxx</u>	<u>xxxx</u>
		xxxx
Less: Depreciation as per sec 198		<u>xxxx</u>

Profit available for Managerial Remuneration xxxxx

Managerial Remuneration is to be computed on the above figure at the specific percentage given in the question. If it is not given in the question then managerial remuneration shall be calculated as per the maximum limit as given in Schedule V.

Managerial Remuneration maximum limits

(A) For companies having profits :

(i) Overall	11% of net profit
(ii) If there is one managerial person	5 % of net profit
(iii) If there are more than one managerial person	10 % of net profit

Remuneration payable to directors who are neither MD nor whole-time directors shall not exceed —

(a) 1% of net profit of the company if there is a managing director/ whole-time director/ manager;

(b) 3% of net profit in any other case.

Note: Managerial person include MD, Whole time director and Manager
For companies having no profits or inadequate profits: in the event of loss or inadequacy of profits Managerial Remuneration is to be limited as per the rules specified in Schedule V depending on the effective capital of the company.

7. (a) The following is summarized balance Sheet of JEEL Ltd. as on 31st March, 2017:

Liabilities	Amount (₹)	Amount (₹)	Assets	Amount (₹)	Amount (₹)
Share capital			**Fixed Assets Cost:**	**15,00,000**	
Authorized capital:		**25,00,000**			
Issued and subscribed			**Less: Provisions for depreciation**	**1,25,000**	
					13,75,000
Capital:					
1,50,000 equity shares of ₹10 each fully paid	**15,00,000**		**Non-current investments at cost**		**25,00,000**
1,00,000 9% Preference share of ₹100 each (issued 2 months back for the purpose of buy back)	**10,00,000**	**25,00,000**	**Current Assets, loans and Advances including cash and bank balance**		**20,00,000**
Reserve and surplus :					
Capital reserve	**5,000**				
Revenue reserve	**20,00,000**				
Securities premium	**2,50,000**				
Profit & Loss account	**9,00,000**	**31,55,000**			
Non- current liabilities:					
10% Debentures		**2,00,000**			
Current liabilities and provisions		**20,000**			
		58,75,000			**58,75,000**

(i) The company passed a resolution to buy back 20% of its equity capital @ ₹ 15 per share. For this purpose, it sold its investments of ₹ 30 lakhs for ₹ 25 lakhs.
(ii) The company redeemed the preference share at a premium of 10% on 1st April, 2017.
(iii) Included in its investments were investments in own debentures costing ₹ 1,50,000 (face value ₹ 1,65,000). These debentures were cancelled on 1st April, 2017.

You are required to pass necessary journal entries on 01.04.17. 10

(b) Write short note on Contingent Liability. 5

Answer: (a)

In the books of JEEL Ltd.
Journal Entries

Date	Particulars		Dr. (₹)	Cr.(₹)
	Bank A/c Profit & Loss A/c To Investment A/c (Being investment sold for the purpose of buy-back)	Dr. Dr.	25,00,000 5,00,000	 30,00,000
	Preference Share Capital A/c Premium on Redemption of Preference Shares A/c To Preference Shareholders A/c (Being Redemption of Preference Share Capital at premium of 10%)	Dr. Dr.	10,00,000 1,00,000	 11,00,000
	Preference Shareholders A/c To Bank A/c (Being payment made to Preference Shareholders)	Dr.	11,00,000	 11,00,000
	Revenue Reserve A/c To Capital Redemption Reserve A/c (Being creation of Capital Redemption Reserve to the extent of nominal value of Preference Sares redeemed)	Dr.	10,00,000	 10,00,000
	Equity Share Capital A/c Securities Premium A/c (Premium payable on buy-back) To Equity Shares buy-back A/c (Being the amount due on buy-back)	Dr. Dr.	3,00,000 1,50,000	 4,50,000
	Equity Shares Buy-back A/c To Bank A/c (Being payment made for buy-back)	Dr.	4,50,000	 4,50,000
	10% Debentures A/c To Own Debentures A/c To Capital Reserve A/c (Profit on cancellation) (Being Own Debentures cancelled at profit)	Dr.	1,65,000	 1,50,000 15,000
	Securities Premium A/c To Premium on Redemption of Preference Shares A/c (Being premium on Redemption of Preference Shares adjusted through securities premium)	Dr.	1,00,000	 1,00,000

(b) Contingent liability can be termed as an obligation relating to an existing condition or situation which may arise in future depending on the occurrence or non-occurrence of one or more uncertain future events, Example: a company may have certain pending litigation, assessments made by tax authorities which are being contested etc., in all such cases, the amounts involved are shown as Contingent liability. Contingent liabilities are classified under the following head:

(i) Claims against the company not acknowledged as debts;
(ii) Unclaimed liability on shares partly paid;
(iii) Arrears of fixed cumulative dividend;
(iv) Estimated amount of contracts remaining unexecuted on capital account not provided for; and
(v) Other money for which the company is liable contingently.

SECTION - C

Answer any two questions from Q no 8, 9 and 10. 15×2=30

8. (a) State the general guidelines for preparing audit working papers. 6

(b) What are the services which cannot be rendered by a statutory auditor of a company under section 144 of the Companies Act, 2013? 4

(c) Highlight the principles in SA 299 on Division of work among joint auditors. 5

Answer: 8 (a)

1. **Clarity and Understanding:**

   As a preparer of audit documentation, step back and read your work of objectively. Would it be clear to another work? Working papers should be clear and understandable without supplementary oral explanations. With the information the working papers reveal, a reviewer should be able to readily determine their purpose, the nature and scope of the work done and the preparer's conclusions.

2. **Completeness and Accuracy:**

   As a reviewer of documentation, if you have to ask the audit staff basic questions about the audit, the documentation probably does not really serve the purpose. Work papers should be complete, accurate and support observations, testing, conclusions, and recommendations.

3. **Logical arrangement:**

   File the working papers in a logical order.

4. **Pertinence:**

   Limit the information in working papers to matters that are important and necessary to support the objectives and scope established for the assignment.

5. **Safety:**

   Keep your work papers safe and retrievable.

6. **Legibility and Neatness:**

   Working papers should be legible and as neat as practical.

7. **Initial and Date:**

   Put your initials and date on every working paper.

8. Summary of Conclusions:

Summarize the results of work performed and identify the overall significance of any weakness or exceptions found.

(b) Auditor not Render Certain Services (Prohibited Services)-as per section 144:

An auditor shall provide to the company only such other services as are approved by the Board of directors/ the Audit Committee, but which shall not include any of the following services whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company, namely:

I) Accounting and book keeping services;
II) Internal audit;
III) Design and implementation of any financial information system;
IV) Actuarial services;
V) Investment advisory services;
VI) Investment banking services;
VII) Rendering of outsourced financial services;
VIII) Management services; and
IX) Any other kind of services as may be prescribed.

(c) Where joint auditors are appointed, they should, by mutual discussion, divide the audit work among themselves. The division of work would usually be in terms of audit of identifiable units or specified areas. In some cases, due to the nature of the business of the entity under audit, such a division of work may not be possible. In such situations, the division of work may be with reference to items of assets or liabilities or income or expenditure or with reference to periods of time. Certain areas of work, owing to their importance or owing to the nature of the work involved, would often not be divided and would be covered by all the joint auditors.

The division of work among joint auditors as well as the areas of work to be covered by all of them should be adequately documented and preferably communicated to the entity.

Where, in the course of his work, a joint auditor comes across matters which are relevant to the areas of responsibility of other joint auditors and which deserve their attention, or which require disclosure or require discussion with, or application of judgment by, other joint auditors, he should communicate the same to all the other joint auditors in writing. This should be done by the submission of a report or note prior to the finalization of the audit.

9. (a) "Auditor's assessment of materiality may be different at the time of planning the engagement than at the time of evaluating the results of his audit procedures". Comment. 8

(b) Who is responsible for preparation and presentation of financial statements? 7

Answer: 9 (a)

Planning the audit solely to detect individually material misstatements overlooks the fact that the aggregate of individually immaterial misstatements may cause the financial statements to be materially misstated, and leaves no margin for possible undetected misstatements. Performance materiality (which, as defined, is one or more amounts) is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in the financial statements exceeds materiality for the financial statements as a whole. Similarly, performance materiality relating to a materiality level determined for a particular class of transactions, account balance or disclosure is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in that particular class of transactions, account balance or disclosure exceeds the materiality level for that particular class of transactions, account balance or disclosure. The determination of performance materiality is not a simple mechanical calculation and involves the exercise of professional judgment. It is affected by the auditor's understanding of the entity, updated during the performance of the risk assessment procedures; and the nature and extent of misstatements identified in previous audits and thereby the auditor's expectations in relation to misstatements in the current period.

(b) The Management and where appropriate those charged with Governance are responsible for preparation and presentation of financial statement. An audit in accordance with SAs is conducted on the premise that management and, where appropriate, those charged with governance have responsibility:

(1) For the preparation and presentation of the financial statements in accordance with the applicable financial reporting framework; this includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of financial statements that are free from material misstatement, whether due to fraud or error; and

(2) To provide the auditor with:
- (i) All information, such as records and documentation, and other matters that are relevant to the preparation and presentation of the financial statements;
- (ii) Any additional information that the auditor may request from management and, where appropriate, those charged with governance; and
- (iii) Unrestricted access to those within the entity from whom the auditor determines it necessary to obtain audit evidence.

10. (a) As an Auditor state how will you verify 'Loans and Advances' appearing in the financial statement of the company. 8

(b) Mention the special steps involved in audit of Cinema Hall. 7

Answer: 10 (a)

Loans and advances may be different types like-

(1) Loans against the security of Land & Building.

(2) Loans against the security of goods.

(3) Loans against the security of stocks & shares.

(4) Loans against the security of Insurance Policies.

(5) Loans against the personal security of the borrower.

Therefore, in each case the duty of auditor in general is as under:

- (i) Examine whether a proper loan ledger has been maintained upto date or not.
- (ii) Examination of the Security ledger against each loan.
- (iii) Examine the loan agreement and find out the rate of interest, due dates of installments, penalty, interest etc.
- (iv) Ascertain whether any loan is doubtful of recovery. In case it is doubtful, a provision for the expected loss is to be made.
- (v) Verify that loans have got proper sanction from the authority.
- (vi) Obtain a letter of confirmation from the parties to whom loans are advanced. In case of loans to directors, prior approval of the Central Government is obtained.

(b)

1. Ensure that entrance to the cinema hall is only through, printed tickets;
2. Ensure that tickets are serially numbered and bound into books;
3. Ensure that the number of tickets issues tor each show and class are different;
4. Ensure that tor advance booking a separate series of tickets is issued; and
5. Ensure that inventory of tickets is kept in proper custody;
6. Ensure the reliability and authenticity of tickets issued through computer;
7. Ensure that at the end of each show a proper statement is prepared and cash collected is tallied.
8. Ensure that Cash collected is deposited in banks partly on the same day and rest on the next day - depending upon the banking facility available.
9. Verify that proper record is kept tor tree passes issued and the same are issued under proper authority.
10. Cross check the entertainment tax deposited.
11. Verify the income from advertisements and slides showed before the show.
12. Vouch the expenditure incurred on publicity of picture, maintenance of hall, electricity expenses etc.
13. Vouch recoveries of advertisement expenses etc from film distributors.
14. Vouch payment of film hire with reference to agreement with distributor or producer.
15. Verify the basis of other incomes earned like restaurant, car and scooter parking and display windows etc.
16. Confirm that depreciation on machinery and furniture has been charged at appropriate rates which are higher, as compared to those admissible in the case of other businesses, in respect of similar assets.