

**Paper - 19 : Cost and Management Audit**

## Paper – 19 : Cost and Management Audit

Full Marks : 100

Time allowed: 3 hours

Answer Question No. 1 which is compulsory and carries 20 marks and any five from Question No. 2 to 8.

### Section - A [20 marks]

1. Choose the correct option among four alternative answer. (1 mark for correct choice, 1 mark for justification.) [10\*2=20 marks]
- (i) In Cost Audit Report, auditor's observations and suggestions are given in:  
(A) Part A of the Annexure to Cost Audit Report  
(B) Part B of the Annexure to Cost Audit Report  
(C) Part C of the Annexure to Cost Audit Report  
(D) Form of the Cost Audit Report.
- (ii) Company has to upload Cost Audit Report electronically to the MCA through  
(A) Form CRA -1  
(B) Form CRA-2  
(C) Form CRA-3  
(D)Form CRA-4
- (iii) Financial Position and Ratio Analysis information in Annexure to Cost Audit Report to be provided for:  
(A) Current Year and Previous Year  
(B) Current Year and Previous 2 Years  
(C) Current Year and Previous 3 years  
(D) Current year only.
- (iv) CAS 13 deals with:  
(A) Pollution Control cost  
(B) Cost of Service Cost centre  
(C)Cost of Utilities  
(D)Direct Expenses.
- (v) CAS 5 deals with  
(A) Cost of production for captive consumption  
(B) Production and Operation Overheads  
(C)Average (Equalised Cost of Transportation)  
(D) Pollution Control Cost.
- (vi) The following is not professional misconduct as per The Second Schedule Part I of the Cost and Works Accountants Act, 1959  
(A) expresses his opinion on cost or pricing statements of any business or enterprise in which he, his firm or a partner in his firm has a substantial interest;  
(B) fails to report a material mis-statement known to him to appear in a cost or pricing statement with which he is concerned in a professional capacity;  
(C) contravenes any of the provisions of this Act or the regulations made there-under or any guidelines issued by the Council;  
(D) does not exercise due diligence, or is grossly negligent in the conduct of his professional duties;

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(vii)XBRL technical term for a table

- (A) Hypercube
- (B) Imputed Value
- (C)Fact
- (D)Item.

(viii)Internal Auditing is:

- (A)One time activity
- (B)Two Time activity
- (C)Bi-annual activity
- (D) Continuous process.

(ix) T.G Rose developed the concept of:

- (A)Cost Audit
- (B)Internal Audit
- (C)Management Audit
- (D)Financial Audit

(x) Audit Working Papers are property of:

- (A)Government
- (B)Company
- (C)Auditor
- (D)Public

**Answer:**

1. (i)- (D) Form of the Cost Audit Report.  
This is pursuant to Rule 6(4) of the Companies (Cost Records and Audit) Rules, 2014
- (ii)- (D) Form CRA-4  
This is pursuant to Rule 6(6) of the Companies (Cost Records and Audit) Rules, 2014
- (iii)- (A) Current Year and Previous Year  
This is pursuant to Rule 6(4) of the Companies (Cost Records and Audit) Rules, 2014
- (iv)- (B) Cost of Service Cost centre  
This standard deals with the principles and methods of classification, measurement and assignment of Cost of Service Cost Centre, for determination of the Cost of product or service, and the presentation and disclosure in cost statements.
- (v)- (C) Average (Equalised Cost of Transportation)  
The objective of the standard is to bring uniformity in the application of principles and methods used in the determination of averaged/ equalized transportation cost.
- (vi)- (C) Contravenes any of the provisions of this Act or the regulations made there-under or any guidelines issued by the Council;  
  
This is a professional misconduct as per The Second Schedule Part II of the Cost and Works Accountants Act, 1959 which deals with professional misconduct in relation to members of the Institute generally.
- (vii)- (A) Hypercube  
This is as per XBRL glossary of terms. Several technical terms are used, that have specific meanings, in the context of using XBRL.

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- (viii)- (D) Continuous process.  
It is a continuous and systematic process of examining and reporting the operations and records of a concern.
- (ix)- (C) Management Audit  
T.G Rose developed the concept of Management Audit as a logical system of evaluating the quality of Management.
- (x)- (C) Auditor  
Audit working papers are the documents which record all audit evidence obtained during audit. Such documents are used to support the audit work done in order to provide assurance that the audit was performed in accordance with the relevant Cost Auditing Standards. (Cost Auditing Standard 102 on Cost Audit documentation)

## Section - B [80 marks]

2. (a) (i) **A company is engaged in manufacturing products on its own as well as purchase the same products from other companies. The outsourced products are treated as trading activity in the financial accounts. Same products are also manufactured by supply of materials to converters. What would be treatment of such products for the purposes of maintenance of cost accounting records and cost audit?**
- (ii) **In the abridged cost statement, what are Industry specific operating expenses? When should this be used?**
- (b) **Explain whether the following amounts to professional misconduct by a CMA:**
- (i) **P, a practicing CMA Q is a practicing Advocate representing matters in courts of law. and Q agree to help each other in matters involving their professional expertise. Accordingly P recommends Q in all tax litigations in courts of law. Q consults P on all matters relating to costing and related matters, which come to him for arguing in various courts of law. They agree to 'share' the remuneration.**
- (ii) **R, a CMA, certifies a financial forecast of his client which was forwarded to the client's bank based on which the bank sanctioned a loan to the client. [8+8]**

### Answer:

2. (a) (i) Products manufactured by the company as well as conversion activity through third parties will be covered under the Companies (Cost Records and Audit) Rules 2014 and the company would be required to maintain cost accounting records and get cost audit conducted subject to threshold limits. The finished products bought from outside parties (treated as Trading Activity in Financial Accounts) would be reflected as "Cost of Finished Goods Purchased" in Abridged Cost Statement.
- (ii) Industry Specific operating expenses are those which are peculiar to a particular industry such as Telecommunication Industry which shows expenses such as Network Operating cost, License fee, Radio Spectrum charges, Microwave charges etc. which are peculiar to this Industry and should be disclosed separately in the cost statement. The Industry Specific operating expenses will vary from industry to industry depending upon the nature of operations. The industry specific operating expenses shall have to be identified and reported upon in the abridged cost statement.
- (b) (i) A CMA in practice shall be deemed to be guilty of professional misconduct if he either directly or indirectly shares commission or brokerage in the fees or profits of his professional business to any other than member of the Institute or accepts any part of the profits of the professional work of a lawyer, broker, etc. who is not a member of the Institute. Thus, as per Clauses 2 and 3 of Part I of the First Schedule to the Cost and Works Accountants Act, 1959 a member in practice can neither

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share fees or profits with a person who is not a member of the Institute nor he is permitted to receive and share the fees of other such as lawyers, engineers, etc.

P and Q therefore cannot "share" any remuneration. They may, however, remunerate each other for "professional" services rendered on any reasonable basis separately which would be on time basis at rates depending on the extent of expertise. It is, however, important that care should be taken by the member not to extend his service beyond the normal sphere of professional practice and any reports or recommendations should clearly delimit the responsibilities assumed and services rendered.

- (ii) Under Clause (3) of Part I of Second Schedule to the Cost and Works Accountants Act, 1959, a CMA in practice is deemed to be guilty of professional misconduct if he permits his name or the name of his firm to be used in connection with an estimate of cost or earnings contingent upon future transactions in a manner which may lead to the belief that he vouches for the accuracy of the forecast. Accuracy does not refer to arithmetical accuracy. All forecasts are estimates based on certain assumptions duly evaluated on a consideration of various relevant factors and cannot be ascertained with accuracy. But, first of all, he should clearly indicate in his report the sources of information, the basis of forecasts and also the major assumptions made in arriving at the forecasts and, secondly, he should not vouch for the accuracy of the forecasts. In the instant case, Mr. R is deemed to be guilty as it appears that he has certified the financial forecast without taking adequate safeguards.

Under Clause (3) of Part I of Second Schedule to the Cost and Works Accountants Act, 1959, a CMA in practice is deemed to be guilty of professional misconduct if he permits his name or the name of his firm to be used in connection with an estimate of cost or earnings contingent upon future transactions in a manner which may lead to the belief that he vouches for the accuracy of the forecast. Accuracy does not refer to arithmetical accuracy. All forecasts are estimates based on certain assumptions duly evaluated on a consideration of various relevant factors and cannot be ascertained with accuracy. But, first of all, he should clearly indicate in his report the sources of information, the basis of forecasts and also the major assumptions made in arriving at the forecasts and, secondly, he should not vouch for the accuracy of the forecasts. In the instant case, Mr. R is deemed to be guilty as it appears that he has certified the financial forecast without taking adequate safeguards.

**3. (a) How would you treat the following as per CAS-11 related to Administrative overheads?**

- (i) Leased Assets;
- (ii) Cost of Administrative Services procured from outside;
- (iii) Cost of Software.

- (b) The profit as per Financial Accounts of JANARDHAN CEMENT LTD. for the year 2017-18 was ₹1,54,28,642.

The profit as per Cost Accounting Records for the same period was less.

The following details are collected from the Financial Accounting Schedules and Cost Accounting records:

Particulars	Financial Accounts(₹)	Cost Accounts(₹)
<b>Valuation of Stock :</b>		
<b>Opening: WIP</b>	<b>2562315</b>	<b>2265710</b>
<b>Finished Goods</b>	<b>26547520</b>	<b>29218950</b>
<b>Closing: WIP</b>	<b>4275640</b>	<b>3736346</b>
<b>Finished goods</b>	<b>37259430</b>	<b>43525149</b>

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Interest income from inter-corporate deposits	615340	
Donations given	485560	
Loss on Sale of Fixed Assets	122546	
Value of cement taken for own consumption	382960	365426
Cost of power drawn from own Wind Mill		
-At EB Tariff		4956325
-At cost	3620370	
Non opening income	4536770	
Voluntary retirement compensation	1676540	
Insurance claim relating to previous year received during the year	1435620	

You are required to prepare a Reconciliation Statement and arrive at the Profit as per Cost Records. [6+10]

Answer:

3. (a) (i) In case of Leased Assets, if the Lease is an operating lease, the entire rentals shall be included in the administrative overheads. If the lease is a financial lease, the finance cost portion shall be segregated and treated as part of finance costs.
- (ii) Cost of administrative services procure from outside shall be determined at invoice or agreed price including duties and taxes, and other expenditure directly attributable thereto net of discounts (other than cash discount), taxes and duties refundable or to be credited.
- (iii) The Cost of Software (developed in house, purchased, licensed or customized) including upgradation Cost shall be amortised over its estimated useful life.

(b)

### JANARDHAN CEMENT LTD.

#### Reconciliation of Financial profit and Costing Profit for the year 2017-2018.

Profit as per Financial Accounts		1,54,28,642
Add : Difference in Stock Valuation	33,51,600	
Loss on Sale of Fixed Assets	1,22,546	
Donation not considered in Cost Accounts Voluntary retirement compensation not included in cost Accounts	4,85,560	
Less : Interest income from inter-corporate deposit	16,76,540	
Difference in value of cement taken for own Consumption	6,15,340	56,36,246
		2,10,64,888
Difference in valuation of windmill power	17,534	
Non-operating Income	13,35,955	
Insurance claim relating to previous year	45,36,770	
Profit as per Cost Accounts	14,35,620	79,41,219
		1,31,23,669

Working:

Figure in ₹

Computation in difference in Valuation of Stock

	Financial Accounts	Cost Accounts
Opening WIP and FG	2,91,09,835	3,14,84,660
Closing WIP and FG	4,15,35,070	4,72,61,495
	1,24,25,235	1,57,76,835

The increase is higher in Cost Accounts and hence Cost Accounts profit would be more than the financial accounts profit by (₹1,57,76,835 - ₹ 1,24,25,235) i.e. ₹ 33,51,600.

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4. (a) What is meant by 'Social Responsibility Management'? Briefly list the different types of Pollution for which a manufacturing Company is responsible.
- (b) What do you understand by 'Corporate Image' and 'Branding'? Are they inter-related? What are the possible approaches to evaluate Corporate Image? [8+8]

**Answer:**

4. (a) Social responsibility describes the duty of care that corporations, governments, charities and institutions all have to their stakeholders.

To keep the confidence of customers, employees, shareholders and a growing array of other organizational stakeholders management need to establish a meaningful framework embedding responsible decision making into all of activities.

Social responsibility is an ethical or ideological theory that an entity whether it is a government, corporation, organization or individual has a responsibility to society at large. This responsibility can be "negative", meaning there is exemption from blame or liability, or it can be "positive," meaning there is a responsibility to act beneficently (proactive stance).

The term "corporate social responsibility" came into common use in the late 1960s and early 1970s after many multinational corporations formed the term stakeholder, meaning those on whom an organization's activities have an impact. Development business ethics is one of the forms of applied ethics that examines ethical principles and moral or ethical problems that can arise in a business environment. Although the Government have enacted legislations for prevention of pollution and provision of safety measures, the company on its own should take measures for community development besides protection of environment.

The level of pollution varies with the density of population and per capita income and inversely with the extent of recycling, technology and waste treatment. The different types, cause and effects of environmental pollution may be as follows:-

(a) **Air pollution:**

Air pollution is the human introduction into the atmosphere of chemicals, particulates or biological materials that cause harm or discomfort to humans or other living organisms or damage the environment. Air pollution is caused by burning coal or crude oil like naphtha in power stations, smoke from factories, exhaust fumes from automobiles, solvent losses and agricultural chemicals, etc. Air pollution leads to deaths and respiratory diseases.

(b) **Water pollution:**

Water pollution is the contamination of water bodies such as lakes, rivers and/or oceans caused by effluents from breweries and tanneries, coal washeries, chemical plants, discharge of coolants from nuclear power plants, pesticides and agricultural chemicals. Water pollution affects public health and safety, causes damage to property and leads to many economic losses.

(c) **Noise pollution:**

Noise pollution is a type of energy pollution in which distracting, irritating or damaging sounds are freely audible and is caused by noise due to running of heavy machines, big aircrafts, drilling machines, etc. Noise pollution may lead to loss of efficiency at work, loss of hearing and causes psychological disorders, even insanity.

(d) **Smell pollution:**

Discharge of industrial products, unclear garbage dumps, open sewers, etc. It affects physical well being and even causes psychological disorders.

(e) **Thermal pollution:**

Large inputs of heated water from a single plant or a number of plants using the same lake or slow-moving stream can have harmful effects on aquatic life. Thermal pollution is radiation of heat generated by plants in industries. Warmer temperatures lower dissolved oxygen content and cause aquatic organisms to increase their respiration rates consume oxygen faster and increases their susceptibility to disease, parasites, and toxic chemicals. Thermal pollution affects ecological balance and thereby the inhabitants.

(f) **Visual pollution:**

Effluents from chemical plants and washeries are discharged into the waterways causing reduced visibility. Industrial fumes and dust causing loss of landscape attractiveness and strain to vision of pedestrians and motorists, may cause more road accidents and traffic deaths.

(g) **Climate pollution:**

Radiation of heat in highly industrial centres leading to "micro climate zones" causing deforestation, shortening plants growth and affecting surroundings. It affects ecological balance and causes damages to plant and surroundings.

(h) **Radiation pollution:**

Radioactive fallouts, leakage from nuclear reactors and prolonged exposures to small doses of radiation results in a bio-accumulative process, causes a significant chronic affect by increasing the rate of genetic mutation.

(i) **Soil/land pollution:**

Indiscriminate use of fertilizers and pesticides, pollution of soil with man-made chemicals, indiscriminate disposal of solid waste etc. Due to pollution the quality of soil deteriorates to the extent that they fail to support vegetation. It affects the global climate also.

(b) **Corporate Image:**

The term "Image" indicates an idea or procure formed in the mind of a person about an individual or an institution. Corporations, like individuals, consciously build up images in the minds of the people with whom they come into contract. In developing a "Corporate Image", an enterprise has to ensure an overall consistency, as regards the quality of the products, the ethics of its management, employee relations, attitudes towards customers, quality and service to customers etc. The Public have different perceptions of "Corporate Image".

Customers measure it by the product quality, prompt and courteous after sales service, regularity in maintaining supplies; etc.

Shareholders, measure it by the consistency in financial performance and prospects of growth.

Supplier measure it by the company's liquidity and ability to honour commitments. Banks and Financial Institutions measure it by the financial health, net worth and history of servicing debts.

Government looks at it from the point of view of revenue generation and as an honest tax payer.

Employees look for steady career growth and smooth Industrial Relations.

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## **Corporate Branding:**

Corporate branding is the process of creating and maintaining a favourable reputation of the company and its constituent elements. It is an important organizational resource that enable to create, strengthen and sustain competitive advantage. It is a strategic asset that creates competitive advantage and favourable climate for survival and development of an organization.

The purpose of corporate branding is to:

Make the organization known as unique, distinct and creditable in the mind of potential customers.

Facilitate the building of relationships and trust.

Portray the benefits of the organization to the customer

Both Corporate Image and Branding are interrelated concepts. The factors which contribute to build up a "corporate image" also substantially help in building a "corporate branding".

## **Evaluation of Corporate Image**

Evaluation of Corporate Image is a very complex process and it involves a critical examination of events and trends concerning business environment – both internal as well as external.

The following are the steps to evaluate Corporate Image.

Prepare a list of desirable attributes.

Group them functionally and specify the qualifications

Assign weights to each attribute based on their relative importance.

Involve experts in the respective fields in rating the qualifications and attributes – based on facts, judgments and interpretations.

Summarise the rating under the selected groups and present a composite evaluation to the management.

The summary should throw light on what the company has been able to do for itself and for the public in general.

5. (a) Mr . X, newly appointed CEO of ABC Ltd. engages you as a Management Auditor to give him a factual report , as to causes of demoralization of his staff .
- (b) (i) State which one of the following companies is required to appoint Internal Auditor as per the Companies Act, 2013, and the Rules made thereunder:

Figures are in ₹ crore and correspond to the previous year.

Name	Nature	Equity Capital	Turnover	Loan from Bank/PFI	Public Deposit
LMN Ltd.	LISTED	100	190	50	24
PQR Ltd.	UNLISTED PUBLIC	60	190	50	24
XYZ Ltd.	UNLISTED PRIVATE	60	190	50	-

- (ii) Can the Chief Cost Accounts Officer of the company be given additional charge as Internal Auditor? [8+8]

**Answer:**

**5. (a) Report on demoralization of Employees:**

The investigation reveals that by and large the employees of the organization are demoralized and dispirited. There is total absence of commitment and initiative on the part of employees. There is a growing discontentment among the employees. The factors responsible for grave demoralization amongst the employees are as follows:

- i) Insufficient promotion opportunities: There is no system of 'Individual career growth plan'. Some employees are stagnant and are not getting promotion for long stretch of time. Such employees are totally frustrated and demoralized. A statement of employees stagnating for more than 6 years in the same post may be compiled and reason may be looked for.
- ii) Preference is given to Direct Recruitment over Internal Promotion. There is no management succession system and no system of 'potential spotting' amongst employees. Neither the company is serious about training its Human Resources in their functional areas. Direct recruitment to senior staff position is resented to by the employees.
- iii) There is considerable imbalance in workload and in overtime opportunities.
- iv) There is a system of assignment of personnel to tasks that do not interest/encourage them.
- v) There is no 'Employee Participation' in management.
- vi) The application of management concepts like 'job rotation', 'job evaluation', 'merit rating' are totally absent in the organization.
- vii) There is no scientific appraisal system. There is favourism and nepotism by the management.
- viii) Apart from the above, the human aspects of personnel development viz. the programme of informal education, recreation and culture, community development etc. to enhance the quality of work life are totally neglected.
- ix) There is no transfer policy and employees are transferred at the whims and fancies of the management.

So it can be concluded that company is pursuing wrong personnel policies and procedures, leading dissatisfied and demoralized employees.

- (b) Every private company having (i) turnover of two hundred crore rupees or more during the preceding financial year or (ii) outstanding loans or borrowing from banks or public financial institutions exceeding rupees one hundred crore or more at any point of time during the preceding financial year Shall be required to appoint an Internal Auditor or Firm of Internal Auditor.

Here,

- (1) LMN Ltd. Being listed company has to appoint Internal Auditor in either case.
- (2) PQR Ltd. An unlisted company exceeds capital limit of rupees 50 crore though the minimum turnover, minimum loan and public deposit are not met. The company has to appoint an Internal Auditor.
- (3) XYZ Ltd. An unlisted private company need not appoint Internal Auditor as the limits of appointment of Internal Auditor are not met.

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6. (a) SRIZONI LTD. of Gandhi Nagar producing industrial alcohol generates Bio-gas from the waste wash of alcohol in its Bio-gas Plant. The said Bio-gas is used as a fuel in generating steam along with conventional fuel oil. The high pressure steam is first sent to the STEAM TURBINE and the exhaust steam is used in the process of manufacturing Alcohol.

The following details are extracted from the financial accounts and cost accounting records of SRIZONI LTD. for the year ended March 31, 2018:

	Boiler (₹)	Steam Turbine (₹)
Cost of water	10,48,000	—
Fuel oil	918,85,000	—
Bio-gas Plant Expenses	258,02,000	—
Stores and Chemicals	2,57,000	66,000
Salaries and Wages	29,58,000	7,33,000
Repairs and Maintenance	65,64,000	2,58,000
Depreciation	17,25,000	6,50,000
Other Expenses	39,95,000	1,21,000
<b>High Pressure Steam generated</b>	<b>34950 MT</b>	
<b>Power generated</b>		<b>2550200 KWH</b>

Note: The fall in the enthalpic value of the steam is 10%

Required:

Prepare two separate cost sheets for steam and power as per the Companies (Cost Records and Audit) Rules 2014 for the year ended March 31, 2018.

- (b) The following figures relate to usage of power for a product:

	2014 -15	2015-16	2016 -17
Total power consumed to KWH	2402474	2494872	2175677
Rate KWH ₹	2.29	2.12	1.90
Total production in million kgs.	337.73	333.084	300.865

Compute necessary productivity measures and compare the efficiency of power usage during the three years. [8+8]

Answer:

6. (a) (i)

Statement showing Cost of Steam

	Total amount (₹)	Cost/Mt (₹)
		Quantity produced: 34950 mt
Water	10,48,000	29.98
Fuel oil	9,18,85,000	2629.04
Bio-gas plant expenses	2,58,02,000	738.25
Stores and chemicals	2,57,000	7.35
Salaries and wages	29,58,000	84.64
Repairs and maintenance	65,64,000	187.81
Depreciation	17,25,000	49.36
Other expenses	39,95,000	114.31
	13,42,34,000	3840.74

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(ii)

Statement showing Cost of Power generated by Steam Turbine

Power Generated: 2550200 KWH

	Total amount (₹)	Cost/Kwh (₹)
Steam	13,42,34,000	52.64
Stores and chemicals	66,000	0.02
Salaries and wages	7,33,000	0.29
Repairs and maintenance	2,58,000	0.10
Depreciation	6,50,000	0.25
Other expenses	1,21,000	0.05
	13,60,62,000	53.35
Less: Credit for exhaust steam (90%)	12,24,55,800	48.02
Cost of Power used in alcohol manufacture	1,36,06,200	5.33

(b)

	2014-15	2015-16	2016-17
Power consumed in Kwh	24,02,474	24,94,872	21,75,677
Rate per Kwh (₹)	2.29	2.12	1.90
Total Power cost (₹)	55,01,665	52,89,129	41,33,786
Production (in million kgs)	337.730	333.084	300.865
	(337730 MT)	(333084 MT)	(300865 MT)
Power cost/MT (₹)	16.29	15.88	13.74
Power usage MT (KWH)	7.11	7.49	7.23

**Variances over previous year:**

Rate (₹)	4,24,128 (F)	4,78,649 (F)
Volume (₹)	75,683 (F)	5,11,638 (F)
Usage (₹)	2,87,275 (A)	1,65,056 (F)
	2,12,536 (F)	11,55,343 (F)

**Calculation of variances:**

**Rate variance:**

	2014-15	2015-16	2016-17
Total power consumed (Kwh)	24,02,474	24,94,872	21,75,677
Rate per Kwh (₹)	2.29	2.12	1.90
Rate variance		24,94,872 × (2.29 - 2.12)	21,75,677 × (2.12 - 1.90)
		= ₹4,24,128 (F)	= ₹4,78,649 (F)
Production in Million Kgs	337.730	333.084	300.865

**Volume variance:**

2016-17 & 2015-16  $(333084 - 300865) \times 15.88 = ₹5,11,638 (F)$

2015-16 & 2014-15  $(337730 - 333084) \times 16.29 = ₹75,683 (F)$

**Usage variance:**

2016-17 & 2015-16  $11,55,343 - 4,78,649 - 5,11,638 = ₹1,65,056 (F)$

2015-16 & 2014-15  $2,12,536 - 4,24,128 - 75,683 = ₹2,87,275 (A)$

**Total variance:**

2016-17 & 2015-16  $52,89,129 - 41,33,786 = ₹11,55,343 (F)$

2015-16 & 2014-15  $55,01,665 - 52,89,129 = ₹2,12,536 (F)$

7. (a) ABC Ltd. has received an enquiry for supply of 2,50,000 numbers of special type of auto components. The Company can execute the assignment provided a capital investment of ₹ 3,00,000 and working capital to the extent of 3 months' cost of sales are made available. The costs estimated are as follows:

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Raw Materials - @ ₹ 3.25 per unit  
 Direct Labour Hours - 8,000  
 Labour Rate - ₹ 4.50 per hour  
 Factory Overheads - ₹ 4 per direct labour hour  
 Selling and Distribution expenses - ₹ 30,000

Borrowed funds will be available @11.5% on additional capital outlay. The Company expects a net Return of 25% on Sales. The Managing Director wants a Cost and Price statement, indicating the price which should be quoted to the customer.

(b) The following is a summary of the Profit and Loss Account of M/s. Straw Berry Company Limited for the year ended 31.03.2018 (₹ in lakh):

Sales		13,540
Cost of Sales: Raw Materials, Stores, Spares	5,600	
Excise Duty	830	
Salaries, Wages	1,400	
Power and Fuel	470	
Repairs: Major Breakdown	35	
Regular Maintenance	94	
Selling and Distribution Cost	1,040	
Insurance	56	
Rent, Rates and Taxes	97	
Printing, Stationery, etc.	437	
Travelling	776	
Other Administrative expenses	426	
Depreciation	391	
Interest	1,494	
Total expenses		13,146
Profit		394

There was a major breakdown of machinery, resulting in loss of production for 42 days in June and July, 2017 and there was a labour strike of 97 days from 14.02.2018 to 21.05.2018. The company produced a single product (Steel-Billet) and the production during the year was 9,42,000 kgs. You are required to compute the amount of abnormal cost on account of the breakdown and strike and the impact on cost per unit of output. Where, do these figures find a place in the Cost Audit Report? [8+8]

Answer:

7. (a)

Special type Auto Components: 2,50,000 Nos.	(₹) in'000	(₹) in '000
Materials (250,000 @ ₹ 3.25)	812,500	
Labour 8000 Hrs @ ₹ 4.50	36,000	
Prime Costs		848,500
Factory Over Heads (8000 × 4)	32,000	
Factory Cost		8,80,500
Selling and Distribution Cost	30,000	
Cost of Sales		9,10,500
Interest @11.5% on 300000 +0.25 × 910,500)	60,677	
Total Cost		9,71,177
Profit		323,726
Sales		12,94,903

**Working Notes :** Calculation of Sales

Sales = Total Cost × (1.00-0.25%)=971177/0.75 = ₹ 12,94,903

Profit = Sales - Cost = 1294903- 971177 = ₹ 323726

Quote Per Unit = 12,94,903 /250000 = ₹ 5.18

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- (b) Loss of working days due to abnormal situation are:  
 Breakdown 42 days -Salary Paid  
 Strike 46 Days (up to 31<sup>st</sup>March, 2018) - No Salary Paid  
 Total 88 Days

₹ in Lakh

Income	13,450
Variable Exp : Raw Materials stores 5,600	
Excise Duty 830	
Power Fuel 470	6,900
Margin	6,640
Fixed Cost (13,146 -6900)	6,246

Salaries amounting to ₹ 1,400 Lakh is for (365-46) = 319 Days

Abnormal cost comes to

Fixed Cost on PRODUCTION	Total (₹)	Abnormal (₹)	Normal (₹)
Breakdown Repairs	35	35	00
Salaries Wages (in the ratio 42:319)	1400	184	1216
Interest	1494	00	00
Selling Distribution Cost	1040	00	00
Production Fixed Cost (Balance figure in the ratio 88:365)	2277	549	1728
<b>Total</b>	<b>6246</b>	<b>768</b>	<b>2944</b>
Production Cost Per Kg :(942000 Kg)	Variable = 6900/9.42 = ₹732.48	Fixed Cost = 2944/9.42 = ₹312.52	Abnormal Cost= 768/9.42 = ₹81.52

**Note :**

1. Interest, Selling charges are not included in the Cost of Production.
2. Abnormal Cost is excluded from Cost of Sales and charged to Profit & Loss Account
3. In the Cost Accounting Policy declared in Annexure to Cost Audit Report 'A', the treatment of abnormal or non-recurring cost has to be declared
4. The analysis of value addition and distribution of Earnings show extra ordinary expenses as post Value Addition.

**8. Answer any 4 questions**

**[4×4=16 marks]**

- (a) How would you treat the following as per CAS-9 related to Packing Material Cost?

- (i) Primary and Secondary packing material cost.
- (ii) Self manufactured packing material.

- (b) Audit of Commercial Accounts with respect to Government.

- (c) Objectives of Operational Audit

- (d) The following are the process wise wastages on inputs in the year

Process	%age of wastage on input
Blow Room	9.18
Carding	7.17
Drawing	1.1
Roving (Simplex)	0.3
Ring Frame (Shinning) Reeling and Winding	7.21
	1.5

Calculate waste multiplier.

- (e) ABC Stores is a departmental store, selling goods on retail basis. It makes a gross profit of 20% on net sales. The following figures for the year-end are available: Opening Stock ₹62,000, Purchases ₹4,46,000, Purchase Returns ₹12,500, Freight Inwards ₹15,000, Gross Sales ₹5,60,000, Sales Returns ₹14,000 and Carriage Outwards ₹8,000. Calculate the estimated cost of the Inventory on the closing date.

**Answer:**

10. (a) (i) As per CAS-9, the cost of primary materials shall form part of the cost of production. Cost of secondary packing materials shall form part of distribution overheads.

(ii) Self manufactured packing materials shall be valued including direct material cost, direct employee cost, direct expenses, job charges, factory overheads including share of administrative overheads comprising factory management and administrative and share of research and development cost incurred for development and improvement of existing process or product.

(b) The government also engages in commercial activities and for the purpose it may incorporate following types of entities:

(i) Departmental enterprises engaged in commercial and trading operations, which are governed by the same regulations as other Government departments such as defense factories, mints, etc.

(ii) Statutory corporations created by specific statutes such as LIC, Air India, etc.

(iii) Government companies, set up under the Companies Act, 2013. All aforesaid entities are required to maintain accounts on commercial basis. The audit of departmental entities is done in the same manner as any Government department, where commercial accounts are kept. Audit of statutory corporations depends on the nature of the statute governing the corporation. In respect of government companies, the relevant provisions of Companies Act, 2013 are applicable.

**(c) Objectives of Operational Audit :**

The scope and quality of operational auditing is predominantly dependent upon management attitudes. An open minded management with broad vision, can appreciate the need of operational auditing and to give it the necessary freedom and sanction to perform what it is capable of performing. Also, the qualities and the sense of perspectives of the operational auditor can mould operational audit in the right shape. Therefore, there is a possibility of operational auditing having different objectives to fulfill in different considerations. Generally, operational audit objectives include :

(i) **Appraisal of controls:** The most significant gain an organization can derive from operational auditing is probably in the area of appraisal of controls. Internal controls, because of their unobtrusive omnipresence in the organization, provide the essential hinges to ensure proper performance in each functional or organizational area for accomplishing the desired organizational objective.

(ii) **Evaluation of performance:** In performance appraisal, the operational auditor is basically concerned not so much with how well technically the operations are going on, but with accumulating information and evidence to measure the effectiveness, efficiency and economy with which the operations are being carried on. The principal basis of performance evaluation can be productivity, personnel, workload, cost and quality. In the area of productivity, the operational auditor can undertake such tests as input-output ratios for materials and labour in quantitative terms.

(iii) **Appraisal of objectives and plans:** Everything in an organization is the product of basic plans and objectives set by the management. If the management policy favours installation of controls or specifies the extent of controls whether satisfactory or not, control would have to stay within the policy frame. Therefore, the basic thing that should be evaluated is management policies, plans and objectives. Operational auditor may look into the aspects like whether objectives are clearly spelt out and properly communicated to the personnel responsible for implementation and whether the personnel have understood the objectives in the sense meant by the management. Also, he can take note of any apparent conflict in the objectives for its effect on operations.

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(iv) **Appraisal of organizational structure:** Organizational structure provides the line of relationship and delegation of authority and tasks. This is an important element of the internal control design. Therefore, this is also another important area for appraisal by the operational auditor. In evaluating organizational structure, the aspects that may be considered by the operational auditor whether the organizational structure is in conformity with management objectives and is drawn up on the basis of matching of responsibility and authority.

(d)

Process	% of wastage on input	Net output for 100 units of input	Waste multiplier
Total			1.3161
Blow room	9.18	$100 - 9.18 = 90.82$	1.1953
Carding	7.17	$90.82 - 7.17 / 100 \times 90.82 = 84.31$	1.1096
Drawing	1.10	$84.31 - 1.10 / 100 \times 84.31 = 83.38$	1.0974
Roving (Simplex)	0.30	$83.38 - 0.30 / 100 \times 83.38 = 83.13$	1.0941
Ring Frame (Spinning)	7.21	$83.13 - 7.21 / 100 \times 83.13 = 77.14$	1.0152
Reeling and winding	1.50	$77.14 - 1.50 / 100 \times 77.14 = 75.98$	1.0000

(e) Stores has the following inventory at the end of the year: (figures in ₹ '000)

1	Opening Stock	62,000
2	Purchases	4,46,000
3	Less Returns	12,500
4	Net Purchases	4,33,500
5	Freight Inwards	15,000
6	Cost of Materials Purchased	4,48,500
7	Total Cost of Materials (1)+(6)	5,10,500
8	Sales	5,60,000
9	Less Returns	14,000
10	Net Sales	5,46,000
11	Profit @ 20%	1,09,200
12	Cost of Sales	4,36,800
13	Carriage Outwards	8,000
14	Closing Stock=(7)-(12)-(13)	65,700