Paper - 19 : Cost and Management Audit
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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 answers. (1 mark for correct choice, 1 mark for justification.)

(i) Cost Audit was initially introduced in India in the year ____________.
   (a) 1949
   (b) 1959
   (c) 1965
   (d) 1975

(ii) The Cost Auditor appointed has to render the cost audit report to the board of directors of the Company, as per the specified time limit, in Form ____________.
   (a) CRA – 1
   (b) CRA – 2
   (c) CRA – 3
   (d) CRA – 4

(iii) Cost Auditing Standard 104 deals with ______________.
   (a) knowledge of business, its Process and the Business Environment
   (b) planning an Audit of Cost Statements
   (c) Cost Audit Documentation
   (d) overall objectives of the Independent Cost Auditor

(iv) The Cost Accounting Standard 2 deals with ________.
   (a) Direct expenses
   (b) Packing material cost
   (c) Capacity determination
   (d) Classification of cost.
(v) Any casual vacancy in the office of a cost auditor, whether due to resignation, death or removal to be filled by the Board of Directors within _________days of occurrence of such vacancy.

(a) 30 days  
(b) 60 days  
(c) 90 days  
(d) 180 days

(vi) Once the instance document is successfully validated from the tool, the next step is to _______.

(a) download XBRL validation tool  
(b) pre-scrutinize the validated instance document  
(c) convert to PDF and verify the contents of the instance document  
(d) attach instance document to the Form CRA-4


(a) The Companies Act, 2013  
(b) The Energy Conservation Act, 2001  
(c) The Income Tax Act, 1961  
(d) None of the above

(viii) Which one of the following KPI is used to measure productivity & efficiency of a machine?

(a) % of idle time to total available time  
(b) Machine downtime ratio  
(c) Cost per of Break-Down Hour  
(d) Contribution per unit of material used.

(ix) Royalty paid on units produced ₹ 40,000, Hire Charges of equipment used for production ₹ 4,000, Design charges ₹ 20,000, Software development charges related to production ₹26,000. The Direct Expenses is:

(a) ₹ 40,000  
(b) ₹ 44,000  
(c) ₹ 64,000  
(d) ₹ 90,000
(x) The Cost Accounting Standard 21 deals with _______.

(a) Pollution Control cost
(b) Research and Development cost
(c) Manufacturing cost
(d) Quality Control.

Answer: 1.

(i) (c) 1965

Reason: Cost Audit was first introduced in India in the year 1965, with the introduction of Sec 233B of Companies Act 1956 for Cost Audit and Sec 209 (1) (d) for maintenance of Cost Records.

(ii) (c) CRA-3

Reason: Every cost auditor, who conducts an audit of the cost records of a company, shall submit the cost audit report along with his or its reservations or qualifications or observations or suggestions, if any, in form CRA-3.

(iii) (a) knowledge of business, its Process and the Business Environment

Reason: The objective of Cost Auditing Standard - 104 is to enable the cost auditor to have knowledge of the client’s business which is sufficient to identify and understand the events, transactions and practices that, in the cost auditor’s judgment may have a significant effect on the examination of cost statements or on the preparation of the cost audit report.

(iv) (c) Capacity determination

Reason: CAS-2 deals with the principles and methods of classification and determination of capacity of an entity for ascertainment of the cost of product or service and the presentation and disclosure in cost statements. The objective of this standard is to bring uniformity and consistency in the principles and methods of determination of capacity with reasonable accuracy.

(v) (a) 30 days

As per Rule-6 of the Companies (Cost Records and Audit) Rules, 2014, Any casual vacancy in the office of a cost auditor, whether due to resignation, death or removal to be filled by the Board of Directors within thirty days of occurrence of such vacancy and the company shall inform the Central Government in Form CRA-2 within thirty days of such appointment of cost auditor.

(vi) (b) pre-scrutinize the validated instance document

Reason: Once the instance document is successfully validated from the tool, the next step is to pre-scrutinize the validated instance document with the help of the same tool using a working internet connection.
(vii) (b) The Energy Conservation Act, 2001

**Reason:** The Bureau of Energy Efficiency formed under the Energy Conservation Act 2001. The agency’s function is to develop programs which will increase the conservation and efficient use of energy in India.

(viii) (b) Machine downtime ratio

**Reason:** It is a ratio which indicates the efficiency and productivity of a machine. So, it is a key performance indicator to measure performance of a machine.

(ix) (d) ₹ 90,000/-

**Reason:** Direct expenses = Royalty paid on units produced + Hire Charges of equipment used for production + Design charges + Software development charges related to production = ₹ 40,000 + ₹ 4,000 + ₹ 20,000 + ₹ 26,000 = ₹ 90,000/-. 

(x) (d) Quality Control.

**Reason:** CAS-21 deals with the principles and methods of measurement and assignment of Quality Control cost and the presentation and disclosure in cost statement. The objective of this standard is to bring uniformity, consistency in the principles, methods of determining and assigning Quality Control cost with reasonable accuracy.

Section – B

[80 marks]

2. (a) (i) Which Companies are required to maintain Cost Records?

(ii) Discuss about the applicability of Cost Audit.

(b) What is Cost audit Documentation? Indicate the matters to be included in the Cost Audit Documentation with respect to smaller entities. 

[(2+6)+(2+6)]

**Answer:**

2. (a)

(i) Under section 148 of the Companies Act, 2013, any domestic or foreign company, falling under regulated or non-regulated sectors and engaged in production of goods or provision of services with overall turnover from all its products or services is equal or more than ₹ 35 crores in preceding financial year is required to maintain Cost Records.

(ii) Applicability of cost audit:

(1) Every company specified in item (A) of rule 3 shall get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is rupees fifty crore or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under rule 3 is rupees twenty five crore or more.
(2) Every company specified in item (B) of rule 3 shall get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is rupees one hundred crore or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under rule 3 is rupees thirty five crore or more.

(3) The requirement for cost audit under these rules shall not apply to a company which is covered in rule 3; and

(i) whose revenue from exports, in foreign exchange, exceeds seventy five per cent of its total revenue; or

(ii) which is operating from a special economic zone;

(iii) which is engaged in generation of electricity for captive consumption through Captive Generating Plant. For this purpose, the term “Captive Generating Plant” shall have the same meaning as assigned in rule 3 of the Electricity Rules, 2005.

2. (b)
Audit helps to detect errors and frauds and provides suggestions to improve them which intern, help the management to take corrective action. To complete the audit process one need to gather the documents related to audit process. Cost Audit Documentation means the material including working papers prepared by and for, or obtained and retained by the cost auditor in connection with the performance of the audit. Cost Auditing Standard – 102 deals with Cost Audit Documentation.

The following matters should be included in the Cost Audit Documentation in respect of smaller entities:

(i) A description of the entity, the products produced, services provided and other activities

(ii) An organization Chart showing the responsibility centres and the person responsible

(iii) A description, preferably a flow chart of the manufacturing process

(iv) Internal controls over material cost, labour cost and expenses

(v) The risks of material misstatement assessed, for example, in respect of scrap recovery and disposal

(vi) Tests of materiality used

(vii) The overall audit strategy and audit plan

(viii) Significant matters noted during the audit, and conclusions reached

3. (a) From the following figures extracted from the financial and cost accounting records, you are required to compute:

   (i) Value Added.

   (ii) Ratio of Operating Profit to Sales.

   (iii) Ratio of Operating Profit to Value Added.
<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹ in lakhs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Sales</td>
<td>25,000</td>
</tr>
<tr>
<td>Increase in Stock of finished goods</td>
<td>500</td>
</tr>
<tr>
<td>Expenses:</td>
<td></td>
</tr>
<tr>
<td>Raw Materials consumed</td>
<td>4,000</td>
</tr>
<tr>
<td>Packing materials consumed</td>
<td>1,800</td>
</tr>
<tr>
<td>Stores and spares consumed</td>
<td>600</td>
</tr>
<tr>
<td>Power and fuel</td>
<td>5,000</td>
</tr>
<tr>
<td>Repairs and maintenance</td>
<td>250</td>
</tr>
<tr>
<td>Insurance</td>
<td>150</td>
</tr>
<tr>
<td>Direct salaries and wages</td>
<td>500</td>
</tr>
<tr>
<td>Depreciation</td>
<td>900</td>
</tr>
<tr>
<td>Interest paid</td>
<td>1,500</td>
</tr>
<tr>
<td>Factory overhead:</td>
<td></td>
</tr>
<tr>
<td>Salaries and wages</td>
<td>250</td>
</tr>
<tr>
<td>Others</td>
<td>300</td>
</tr>
<tr>
<td>Selling and distribution expenses:</td>
<td></td>
</tr>
<tr>
<td>Salaries and wages</td>
<td>150</td>
</tr>
<tr>
<td>Others</td>
<td>1,800</td>
</tr>
<tr>
<td>Administration overheads:</td>
<td></td>
</tr>
<tr>
<td>Salaries and wages</td>
<td>150</td>
</tr>
<tr>
<td>Others</td>
<td>100</td>
</tr>
</tbody>
</table>

(b) Write a short note on Risk of Material misstatement.  

Answer:

3. (a) (i)

<table>
<thead>
<tr>
<th>Computation of Value Added</th>
<th>₹ in lakhs</th>
<th>₹ in lakhs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Sales + Increase in Stock of Finished Goods</td>
<td></td>
<td>25,500</td>
</tr>
<tr>
<td>Less:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of bought out materials and services:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Raw Materials</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>Packing materials</td>
<td>1,800</td>
<td></td>
</tr>
<tr>
<td>Stores and spares</td>
<td>600</td>
<td></td>
</tr>
<tr>
<td>Power and fuel</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Repairs and maintenance</td>
<td>250</td>
<td></td>
</tr>
<tr>
<td>Insurance</td>
<td>150</td>
<td></td>
</tr>
</tbody>
</table>
Other factory overhead | 300
---|---
Other Selling & distribution overhead | 1,800
Other Administration overhead | 100 | 14,000

**Value Added** | **11,500**

**Composition of Value Added:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Depreciation</td>
<td>900</td>
</tr>
<tr>
<td>Interest</td>
<td>1,500</td>
</tr>
<tr>
<td>Salaries and wages (500+250+150+150)</td>
<td>1,050</td>
</tr>
</tbody>
</table>

**Profit before tax (balancing figure)** | **8,050**

**Operating Profit:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>PBT</td>
<td>8,050</td>
</tr>
<tr>
<td>Interest paid</td>
<td>1,500</td>
</tr>
</tbody>
</table>

**9,550**

(ii) Ratio of operating profit to net sales = Operating profit/ Net sale = 9,550/25,000 x 100 = 38.20%

(iii) Ratio of operating profit to value added = Operating profit/ Value Added = 9,550/11,500 x 100 = 83.04%

3. (b) Risk of material misstatement:

Audit risk is a function of the risk of material misstatement and detection risk. The risk of material misstatement has two components viz. Inherent Risk and Control risk.

(1) **Inherent risk:** the susceptibility of an assertion about the measurement, assignment or disclosure of cost to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.

(2) **Control risk:** the risk that a misstatement that could occur in an assertion about the measurement, assignment or disclosure of cost and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entities internal, operational and management control.

The cost auditor shall identify and assess the risks of material misstatement at the cost statement level; and at the assertion level including items of cost, cost heads and disclosures thereof.

For this purpose, the cost auditor shall:

(1) Identify risks including relevant controls that relate to the risk of material misstatements or a risk of fraud;

(2) Assess whether the risk is related to recent significant economic, accounting or other developments and, therefore, requires specific attention;

(3) Assess whether the risk involves significant transactions with related parties;

(4) Assess the degree of subjectivity in the measurement of information related to the risk.

(5) Assess whether there arises a need for revising the assessment of risk based on additional audit evidence obtained.
4. (a) (i) Discuss about the requirements of Cost Auditing Standard – 103.

(ii) How would you treat the Idle Time Cost as per the CAS 7 related to Employee Cost?

(b) The Financial Profit and Loss of M/s. PIRON Manufacturing Company Ltd. for the year is ₹32,50,000. During the course of cost audit, it is noticed the followings:

(i) Some Old assets sold off which fetched a profit of ₹1,50,000

(ii) Interest was received amounting to ₹60,000 from outside the business investment.

(iii) Work-in-progress valuation for financial accounts does not as a practice take into account factory overhead. Factory overhead is ₹2,50,000 in opening W.I.P and ₹2,80,000 in closing W.I.P.

(iv) The Company was engaged in Trading activity by purchasing goods of ₹12,30,000 and selling at ₹14,50,000 after incurring ₹60,000 as expenditure.

(v) A major overhaul of machinery was carried out at a cost of ₹6,00,000 and next such overhaul will be done only after five years.

(vi) Opening stock of Raw material and finished good was overvalued for ₹2,50,000 and closing stock was overvalued ₹2,00,000 in financial records.

Work out the profit as per Cost Accounts. 

[(8+2) +6]

Answer:

4. (a) (i)

The Cost Auditing Standard – 103 deals with the overall objectives of the independent cost auditor, the nature and scope of a cost audit, the independent auditor’s overall responsibilities when conducting an audit of cost statements in accordance with Cost Auditing Standards. It also explains the requirements establishing the general responsibilities of the independent auditor applicable in all audits, including the obligation to comply with the Cost Auditing Standards.

The requirements of Cost Auditing Standard – 103 are given below:

(a) The cost auditor shall comply with the relevant ethical requirements including those pertaining to independence in respect of cost audit engagements.

(b) While conducting an audit, the cost auditor shall comply with each of the Cost Auditing Standards relevant to the audit.

(c) The cost auditor shall have an understanding of the entire text of the Cost Auditing Standard, including its application and other explanatory material, to understand its objectives and to apply its requirements properly.

(d) The cost auditor shall plan and perform an audit with an attitude of professional scepticism recognizing that circumstances may exist that cause the Cost Statements to be materially misstated.

(e) The auditor shall obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor’s opinion.
(f) The cost auditor shall determine whether the Cost Reporting Framework followed by management in preparing cost statements is in line with the Companies Act and the Rules prescribed there under.

(g) The cost auditor shall not be required to perform audit procedures regarding the entity's compliance with laws and regulations governing cost audit in the absence of identified or suspected non-compliance.

(h) If an objective in a relevant Cost Auditing Standard cannot be achieved, the auditor shall evaluate whether this prevents the auditor from achieving the overall objectives of the auditor and thereby requires the auditor, in accordance with the Cost Auditing Standards, to modify the auditor's opinion.

(ii) Idle Time Cost shall be assigned direct to the cost object or treated as overheads depending on the economic feasibility and the specific circumstances causing such idle time. Cost of idle time for reasons anticipated like normal lunchtime, holidays etc is normally loaded in the employee cost while arriving at the cost per hour of an employee/a group of employees whose time is attributed direct to the cost objects.

4. (b) Reconciliation of Profit between Cost Accounts and Financial Accounts of M/s. PIRON Manufacturing Company Ltd.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (₹)</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit as per Financial Accounts</td>
<td></td>
<td>32,50,000</td>
</tr>
<tr>
<td>Add: Difference in valuation of W-I-P</td>
<td></td>
<td>30,000</td>
</tr>
<tr>
<td>Proportionate charge i.e. four-fifth for overhaul of machinery</td>
<td></td>
<td>4,80,000</td>
</tr>
<tr>
<td>Overvaluation of Opening Stock in the financial records</td>
<td>2,50,000</td>
<td>7,60,000</td>
</tr>
<tr>
<td>Less: Profit on sale of old assets not included in Cost A/cs.</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>Interest received from outside investment</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Trading profit not included in cost accounts</td>
<td>1,60,000</td>
<td></td>
</tr>
<tr>
<td>Overvaluation of closing stock in the financial records</td>
<td>2,00,000</td>
<td>(-) 5,70,000</td>
</tr>
<tr>
<td>Profit as per Cost Accounts</td>
<td></td>
<td>34,40,000</td>
</tr>
</tbody>
</table>

5. (a) The management of a very big Public Sector Company suspects on the existence of “ghost workers”. You, as an Internal Auditor of the company are required to formulate a system of Internal Control for payment of wages and salaries.

(b) Opening stock of raw materials (5,000 units) ₹ 1,80,000; Purchase of Raw Materials (17,500 units) ₹ 7,00,000; Closing Stock of Raw Materials 3,500 units; Freight Inward ₹ 85,000; Self-manufactured packing material for purchased raw materials only ₹ 60,000 (including
share of administrative overheads related to marketing sales ₹ 8,000); Demurrage charges levied by transporter for delay in collection ₹ 11,000; Normal Loss due to shrinkage 1% of materials; Abnormal Loss due to absorption of moisture before receipt of materials 100 units. Calculate the value of Closing Stock (as per Average Cost Method).

Answer:

5. (a)

The following system of Internal Control is suggested, to prevent frauds and payment made to “Ghost Workers”, if any:

(i) Every employee should be issued an identity card, containing such particulars as Name, Employee No., Department with Photo affixed.

Every employee should be told to have their identity card always with them and they should be able to show that on demand at any time for verification/ checking. One employee particulars register must be maintained by the Personnel Department with signature of the Departmental Head and Head of the institution.

At the time of marking attendance and at the time of wage payment, he should show this card.

(ii) A Bio-metric attendance system may be implemented for recording/checking of proper attendance.

(iii) A comparison should be made between the attendance time and time booked to the jobs and this will reveal detection of a dummy worker easily, since there would be no booking in the job card for the dummy worker.

(iv) The system of internal checks should exist for preparation of wages sheets, such that work of each person is checked by another person. All the calculations and entries should then be checked by a responsible person.

(v) Payment of wages should be made in presence of some responsible officers. Shop-floor Foreman should also be present for identification of workmen. In cases, where possible, payment should be directly credited to the bank accounts of the employee concerned.

(b) Computation of value of closing stock of raw materials [Average Cost Method]

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Quantity (Units)</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Stock of Raw Materials</td>
<td>5,000</td>
<td>1,80,000</td>
</tr>
<tr>
<td>Add : Purchase of raw materials</td>
<td>17,500</td>
<td>7,00,000</td>
</tr>
<tr>
<td>Add : Freight inwards</td>
<td></td>
<td>85,000</td>
</tr>
<tr>
<td>Add : Demurrage Charges levied by transporter for delay in collection</td>
<td></td>
<td>11,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>9,76,000</td>
</tr>
<tr>
<td>Less: Abnormal Loss of raw materials (due to absorption of moisture before receipt of materials)</td>
<td>(100)</td>
<td>(4,549)</td>
</tr>
</tbody>
</table>
\[
\text{Value of Closing Stock} = \frac{\text{Total Cost}}{(\text{Total units} - \text{Units of Normal Loss})} \\
= \frac{10,23,451}{(5,000 + 17,500 - 175)} \times 3,500
\]

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of raw materials</td>
<td>22,225</td>
</tr>
<tr>
<td>Value of Closing Stock</td>
<td>(3,500)</td>
</tr>
<tr>
<td>Cost of Raw Materials Consumed</td>
<td>18,725</td>
</tr>
</tbody>
</table>

Note:

(i) Units of normal loss adjusted in quantity only and not in cost, as it is an includible item.
(ii) Cost of self-manufactured packing materials does not include any share of administrative overheads or finance cost or marketing overheads. Hence, marketing overheads excluded.
(iii) Abnormal loss of materials arose before the receipt of the raw materials, hence, valuation done on the basis of costs related to purchases only. Value of opening stock is not considered for arriving at the valuation of abnormal loss.
(iv) Demurrage charges paid to transporter is an includible item. Since this was paid to the transporter, hence considered before estimating the value of abnormal loss.

6. (a) Which points are to be considered while conducting audit of Hospital.

(b) Define Local Bodies. What is the basic objective of Local Body and discuss about the audit programme of the same.

[10 + 6]

Answer:

6. (a)

The following points are to be considered necessary for conducting an audit of Hospital:

(i) Check the letter of appointment to ascertain the scope of responsibilities.
(ii) Study the Charter or Trust Deed under which the hospital has been set up and take a special note of the provisions affecting the accounts.
(iii) Examine, evaluate and verify the system of internal check, internal control and determine the nature, timing and the extent of the audit procedures.
(iv) Vouch the entries in the Patient’s Bill Register with a copies of bill issued. Test check the selected bills to see that these have been correctly prepared taking into consideration the period of stay of each patient as recorded in the Attendance Schedule.
(v) Vouch the entries in the Patient’s Bill Register with a copies of bill issued. Test check the selected bills to see that these have been correctly prepared taking into consideration the period of stay of each patient as recorded in the Attendance Schedule.
(vi) Vouch the collection from patients with copies of bills and entries in Bills Register. Arrears of dues should be properly carried forward and where these are deemed to be irrecoverable, they should be written off under due authorizations.

(vii) Interest and/or dividend income should be vouched with reference to the Investment Register and Interest and Dividend warrants.

(viii) In case of legacies and donations which are received for specific purposes, it should be ensured that any income there from is not utilized for any other purposes.

(ix) Where receipts of subscription show significant deviations from budgeted figures, it should be thoroughly.

(x) Inquired into and the matter be brought to the notice of the trustees or the Managing Committee.

(xi) Government grants or grants from local bodies should be verified with the reference to the correspondence with the concerned authorities.

(xii) Clear distinction should be made between the items of capital and revenue nature.

(xiii) The capital expenditure should be incurred under proper authorization by a valid resolution of the trustee for the Managing Committee.

(xiv) Verify the system of internal check as regards purchases and issue of stores, medicines etc.

(xv) Examine that the appointment of the staff, payment of salaries etc. are duly authorized.

(xvi) Physically verify the investments, fixed assets and inventories.

(xvii) Check that adequate depreciation has been provided on all the depreciable assets.

6. (b)

Local bodies are institutions of the local self governance, which look after the administration of an area or small community such as villages, towns, or cities. The Local bodies in India are broadly classified into two categories. The local bodies constituted for local planning, development and administration in the rural areas are referred as Rural Local Bodies (Panchayats) and the local bodies, which are constituted for local planning, development and administration in the urban areas, are referred as Urban Local Bodies (Municipalities).

The objectives of Local Bodies are:

- To report the content and presentation of financial statements are true and fair
- Detection and prevention of error fraud, misuse of funds
- To ascertain that full value received for money spent
- Legal and administrative requirements fulfilled

The audit programme for Local Bodies includes the following:

- All sanctions are accorded by competent authority
- Expenditure incurred is according to provisions and as per regulations framed by competent authority

Different schemes, programmes, and projects are running economically and the purpose such programme is achieved.
7. (a) Supreme Ltd., a manufacturing unit, provides the following extracts from its records for the year ended March 31, 2019:

<table>
<thead>
<tr>
<th>The Company’s specifications capacity for a machine per hour</th>
<th>1,600 units</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of shifts (each shift of 8 hours) per day</td>
<td>3 shifts</td>
</tr>
<tr>
<td>Paid Holidays in a year (365 days):</td>
<td></td>
</tr>
<tr>
<td>(i) Sunday</td>
<td>52 days</td>
</tr>
<tr>
<td>(ii) Other holidays</td>
<td>12 days</td>
</tr>
<tr>
<td>Annual maintenance is done within these holidays</td>
<td>-</td>
</tr>
<tr>
<td>Preventive weekly maintenance for the machine is carried on during Sundays</td>
<td></td>
</tr>
<tr>
<td>Normal idle capacity due to lunchtime, shift changes etc. per shift</td>
<td>1 hour</td>
</tr>
<tr>
<td>Production based on sales expectancy in past 5 years (units in Lakh):</td>
<td></td>
</tr>
<tr>
<td></td>
<td>82.50</td>
</tr>
<tr>
<td></td>
<td>89.80</td>
</tr>
<tr>
<td></td>
<td>76.40</td>
</tr>
<tr>
<td></td>
<td>84.30</td>
</tr>
<tr>
<td></td>
<td>83.60</td>
</tr>
<tr>
<td>Actual Production for the year (units in lakh)</td>
<td>86.50</td>
</tr>
</tbody>
</table>

You are required to calculate:

(i) Installed Capacity
(ii) Practical Capacity
(iii) Actual Capacity (%)
(iv) Normal Capacity
(v) Idle Capacity (%)
(vi) Abnormal Idle Capacity

Keeping in view of the relevant Cost Accounting Standard (CAS-2).

(b) Write a short note on Corporate Development Audit. (10 + 6)

Answer:

7. (a)

Calculation of different capacities of Supreme Ltd.

(i) Installed Capacity: days in year x working hours per day x unit per hour
   = 365 x 8 x 3 x 1,600
   = 140.16 lakh units
(ii) Practical capacity: days available × available hour per shift × shifts × units per hour

\[= (365 - 52 - 12) \times (8 - 1) \times 3 \times 1600\]

\[= 101.136 \text{ lakh units}\]

(iii) Actual capacity Utilization: Current production / Installed capacity

\[= (86.50 / 140.16) \times 100 = 61.72\% \text{ (approx)}\]

(iii) Normal capacity: \((82.50 + 89.80 + 76.40 + 84.30 + 83.60) / 5\)

\[= 83.32 \text{ lakh units}\]

(v) Idle Capacity: Installed capacity – Actual capacity

\[= 140.16 - 86.50 = (53.66 / 140.16) \times 100 = 38.29\% \text{ (approx)}\]

(vi) Abnormal Idle capacity: \((101.136 - 86.50) = 14.636 \text{ lakh units}\)

7. (b)

A Corporate Development Audit is an independent objective study of an organization’s capabilities. It aims at identifying strengths and weaknesses and moving toward state-of-the-art performance. A Corporate Development Audit gives a comprehensive picture of the status of corporate development effectiveness and highlights developmental needs. Many organizations use the Corporate Development Audit to identify the state-of-the-art in business development in their industry and determine exactly how much they differ from that ideal. The resulting feedback report highlights all key findings, with specific recommendations for course correction or improvement.

Corporate Development Audit is a comprehensive task to assist the corporate management in various aspects of development through a process of systematic review and evaluation of long-term strategies of the company. Such corporate development audit assures that –

(a) The various factors and forces constituting a corporate enterprise are the right kind and quality.

(b) Communication remains the key to the functioning of an enterprise.

(c) The pattern of departmentalization in an enterprise adopted in the past and proposed for the future for dealing with multidirectional responsibilities is fully responsive to circumstances and business environment.

(d) The personnel problems are handled appropriately considering the overall objectives of development of the corporate enterprise.

(e) The responsibilities of planning, coordination, motivation and control at functional management levels are discharged in proper spirit.

A Corporate Development Audit is best performed by a team consisting of different experts of different disciplines as it requires multi-disciplinary approach. Large scale corporate enterprises offer opportunities to the conduct of Corporate Development Audit.

As the Corporate Development Audit is more of an introspective nature, necessary initiation and support should come from a firm decision taken by the Board of Directors and its chairman. Moreover, as this audit highlights the corporate strengths and weakness, especially failures, inefficiencies and bottlenecks, it should be undertaken by a high-powered team with the corporation and acceptability of all those concerned with it.
8. Answer any four.  

(a) Mention at least 4 Professional misconduct in relation to members in practice in terms of second schedule.

(b) “Management Audit team should be multidimensional.” — Discuss.

(c) Distinguish between Continuous Audit and Final Audit.

(d) Briefly discuss about the contribution of Internal Audit.

(e) Write a short note on creation of XBRL Instance document.

Answer:

(a) A cost accountant in practice shall be deemed to be guilty of professional misconduct, if he—

(i) discloses information acquired in the course of his professional engagement to any person other than his client so engaging him, without the consent of his client, or otherwise than as required by any law for the time being in force;

(ii) certifies or submits in his name, or in the name of his firm, a report of an examination of cost accounting and related statements unless the examination of such statements has been made by him or by a partner or an employee in his firm or by another cost accountant in practice;

(iii) 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;

(iv) fails to report a material misstatement known to him to appear in a cost or pricing statement with which he is concerned in a professional capacity;

(v) does not exercise due diligence, or is grossly negligent in the conduct of his professional duties.

(b) A management auditor handling a large organisation on a continuous basis or a number of audits at the same time has to build up a competent team of people, who possess the qualifications attributed to a management auditor.

As a management auditor, he/she is concerned with all aspects of the business and the organisation, ranging from manufacture, to marketing and finance, the management audit team should be multi-disciplinary to make multi-dimensional approach to audit function.

A competent management audit team, internal to an organisation, could effectively be represented by the heads of various departments’ viz., production, materials management, maintenance, personnel, marketing, finance, industrial engineering, quality control, etc. Such a team can competently lead and direct the audit to attain the organisational objectives.

(c) Continuous Audit:

Continuous audit involves the detailed examination of all the transactions by the auditor continuously throughout the year or at regular intervals, say fortnightly or monthly. A continuous audit is one which is commenced and carried on before the close of the
financial year to which it relates. It involves the constant engagement of auditor’s staff at the client office throughout the period under review. Continuous audit is suitable in cases where the final accounts are desired to be presented soon after the close of the financial year or there is great volume of transactions or the system of internal check is weak.

Final audit:

A final audit is also called as Completed Audit or Periodical Audit. Final audit is done after the close of the financial year, i.e. after the books of accounts have been closed and the final accounts are drawn up. In this type of audit, the client gives the possession of books of accounts to the auditor for audit and routine checking and other audit procedures begin only after that.

(d) Internal Audit is an independent, objective assurance and consulting activity designed to add value and improve an organization’s operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

The internal audit may contribute in the following areas:

(i) Independent review and appraisal of control systems across the organization (both financial control systems and operational areas where the organization may reap benefits)

(ii) Ascertaining of the extent of compliance of policies, procedures, regulations and legislations, checking compliance management systems of an organization.

(iii) Facilitate good practices in management of risk. This requires systems for ascertaining, measuring, managing and where possible mitigation or dispersion of the risk.

(iv) Achieve savings by identifying waste, inefficiency and duplication of effort across the organization

(v) Structuring programs and activities such that company assets are safeguarded and there are internal check systems which minimize the possibility for reducing fraud / early warning signals for identifying fraud.

(e) The first step for creating the instance document is tagging of the XBRL taxonomy elements with the information in the Cost audit report of the company by means of mapping of the taxonomy elements with the Cost audit report. This converts the report into XBRL form. We need to have a tool to create and xml file and convert it into an instance document. There are several vendors, who provide sell this application, which has to be acquired for the purpose.

Mapping is the process of comparing the concepts in the Cost audit report to the elements in the published taxonomy, assigning a taxonomy element to each costing concept published by the company. Once the tagging of Cost audit report/ compliance report elements with the published taxonomy elements is done, the next step is to create the instance document. An instance document is a XML file that contains business reporting information and represents a collection of costing information and report-specific information using tags from the XBRL taxonomy. It is to be noted that no extensions to the
core Taxonomy will be allowed. Separate instance documents need to be created for the Cost Audit report, for the periods prior to and beginning after 1.04.2014.

Once the instance document has been prepared, it needs to be ensured that the instance document is a valid instance document and all the information has been correctly captured in the instance document. MCA Validation Tool provides for ‘human readable’ PDF printable form as well as a view of the instance document.