

Paper 12- Company Accounts and Audit

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Full Marks: 100

Time allowed: 3 hours

Section – A (Company Accounts)

Answer Question No. 1 and any three from Question Nos. 2,3,4 and 5.

1. (a) Choose the correct answer from the given four alternatives: [6x1=6]
- (i) A _____ is a business segment or a geographical segment identified on the basis of foregoing definitions for which segment information is required to be disclosed by this Statement.
- (A) Reportable Segment
(B) geographical segment
(C) Business Segment
(D) None of the above
- (ii) Issue of Application Forms for Securities is covered under section _____ of Companies Act,2013
- (A) Sec 53
(B) Sec 63
(C) Sec 39
(D) Sec 33
- (iii) Before entering into an agreement with the company, the underwriters assess which of the following?
- (A) worth of the public issue
(B) Market response to the issue
(C) Own ability of the issue to get the issue fully subscribed
(D) All of the above
- (iv) General Insurance consists of _____, _____ and _____.
- (A) Fire, Marine, Accidental Insurance
(B) Fire, Life, Accidental Insurance
(C) Property, Marine, Accidental Insurance
(D) None of the above
- (v) As per AS 11, _____ is the currency of the primary economic environment in which the entity operates.
- (A) Functional currency
(B) Foreign currency
(C) Exchange rate
(D) Reporting currency
- (vi) Cash receipts from disposal of shares, warrants or debt instruments of other enterprises will be classified as Cash Flow from _____ activity.
- (A) Investment
(B) Operating
(C) Financing
(D) Both A and B

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Answer:

- (i) (A)
- (ii) (D)
- (iii) (D)
- (iv) (A)
- (v) (D)
- (vi) (A)

(b) Match the following:

[4×1=4]

	Column 'A'		Column 'B'
1.	Section 70	A.	An issuance of stock following a company's Initial Public Offer
2.	Section 55	B.	created out of profits for the purpose of redemption of debentures
3.	DRR	C.	Prohibition for Buy-Back in Certain Circumstances
4.	Follow on public offer	D.	Issue and Redemption of Preference Shares

Answer:

	Column 'A'		Column 'B'
1.	Section 70	C.	Prohibition for Buy-Back in Certain Circumstances
2.	Section 55	D.	Issue and Redemption of Preference Shares
3.	DRR	B.	created out of profits for the purpose of redemption of debentures
4.	Follow on public offer	A.	An issuance of stock following a company's Initial Public Offer

(c) State whether the following statements are True (or) False.

[4×1=4]

- (i) Service Line cum Development Charges can be accounted for as Reserves and disclosed under the head Reserves and Surplus without transferring any proportionate amount to Income Statement during the expected life of the Asset.
- (ii) Initial Public Offer is made when company seeks to raise capital via public investment while Follow on Public Offer is subsequent public contribution.;
- (iii) Free Reserves mean such reserves which, as per the latest audited balance sheet of a company, are restricted to be distributed as dividend.
- (iv) Post-employment benefits (other than termination benefits and short-term employee benefits) payable after the completion of employment.

Answer:

- (i) True;
- (ii) True;
- (iii) False;
- (iv) True.

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Answer any three questions out of the following four questions

[3×12=36]

2. (a) Give journal entries for the following:

- (i) KP Ltd. forfeited 20,000 equity shares of ₹10 each for nonpayment of first call of ₹2 and final call of ₹3 per share. These shares were reissued at a discount of ₹3.50 per share.
- (ii) KP Ltd. forfeited 40,000 equity shares of ₹15 each (including ₹5 per share as premium), for non-payment of final call of ₹3 per share. Out of these 20,000 shares were reissued at a discount of ₹4 per share.
- (iii) KP Ltd. forfeited 30,000 equity shares of ₹15 each (including ₹5 per share as premium), for non-payment of allotment money ₹8 (including premium money) and first & final call of ₹5 per share. Out of these 20,000 shares were reissued at ₹14 per share. [9]

Answer:

Book of KP Ltd.

Journal

Date	Particulars	L. F.	Dr. Amount (₹)	Cr. Amount (₹)
(i)	Equity Share Capital A/c To Calls in Arrear A/c To Forfeited Share A/c (20,000 shares forfeited for non-payment of first and final call money)	Dr.	2,00,000	1,00,000 1,00,000
	Bank A/c Forfeited Share A/c To Equity Share A/c (Reissue of 20,000 sh. @ ₹6.50 each)	Dr. Dr.	1,30,000 70,000	2,00,000
	Forfeited Share A/c To Capital Reserve A/c (Balance of Forfeited share Account transferred)	Dr.	30,000	30,000
(ii)	Equity Share Capital A/c To Calls in Arrear A/c To Forfeited share A/c (20,000 shares forfeited for non-payment of final call money)	Dr.	4,00,000	1,20,000 2,80,000
	Bank A/c Forfeited Share A/c To Equity Share Capital A/c (Reissue of 20,000 sh. @ ₹6 each)	Dr. Dr.	1,20,000 80,000	2,00,000
	Forfeited Share A/c To Capital Reserve A/c (Balance of Forfeited share A/c relating to 20,000 shares transferred)[20,000 × ₹ (7- 4)]	Dr.	60,000	60,000

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(iii)	Equity Share Capital A/c Securities Premium A/c To Calls in Arrear A/c To Forfeited share A/c (30,000 shares forfeited for non-payment of allotment and first and final call money)	Dr. Dr.	3,00,000 1,50,000	3,90,000 60,000
	Bank A/c To Security Premium A/c To Equity Share Capital A/c (Reissue of 10,000 sh. @ ₹15 each)	Dr.	2,80,000	80,000 2,00,000
	Forfeited Share A/c To Capital Reserve A/c (Balance of Forfeited share A/c on 20,000 shares transferred)(20,000 × ₹2)	Dr.	40,000	40,000

(b) On 1st April 2019 VV Limited received Government Grant of ₹750 lakhs for acquisition of a machinery costing ₹3,750 lacs.

The grant was credited to the cost of the asset.

The life of the machinery is 5 years.

The machinery is depreciated at 20% on written down value basis.

The company had to refund the grant in May 2022 due to non-fulfillment of certain conditions.

How you would deal with the refund of grant in the books of Hero Limited. [3]

Answer:

Date	Particulars	₹ in Lakhs
01.04.2019	Cost of machine (adjusting grant) ₹3,750 - ₹750	3,000
31.03.2020	Depreciation	600
	Written Down Value	2,400
31.03.2021	Depreciation	480
	Written Down Value	1,920
31.03.2022	Depreciation	384
	Revised book value	1,536

Note 1: Depreciation on revised book value will be provided prospectively over the residual life of the asset.

Note 2: The company can also debit the refund amount of ₹750 lakhs to DGG A/c if the same account was credited at the time of receipt of the grant.

- 3. (a) The life insurance fund of PP Life Insurance Co. Ltd. was ₹17,00,000 on 31st March, 2022. Its actuarial valuation on 31st March, 2022 disclosed a net liability of ₹14,40,000. An interim bonus of ₹20,000 was paid to the policyholders during the previous two years. It is now proposed to carry forward ₹55,000 and to divide the balance between the policyholders and the shareholders.**

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Show –

- (i) the Valuation Balance Sheet,
- (ii) the net profit for the two-year period, and
- (iii) the distribution of the profits.

[2+2+3=7]

Answer:

**In the Books of PP Life Insurance Co. Ltd. Valuation
Balance Sheet as on 31st March, 2021**

Liabilities	Amount (₹)	Assets	Amount (₹)
To Net liability	14,40,000	By Life Assurance Fund	17,00,000
To Net Profit	2,60,000		
	17,00,000		17,00,000

Particulars	Amount (₹)
Net profit for the two-year period	
Profit as per Valuation Balance Sheet	2,60,000
Add: Interim Bonus paid during the previous two years	20,000
Net Profit	2,80,000
Distribution of the profits	
Net Profit	2,80,000
Less: Amount proposed to be carried forward	55,000
Balance	2,25,000
Share of policyholders (95% of ₹ 2,25,000)	2,13,750
Less: Interim bonus paid	20,000
Amount due to policyholders	1,93,750
Share of Shareholders (5% of ₹2,25,000)	11,250

- (b) The books of a bank include a loan of ₹5,00,000 advanced on 30.09.2020, interest changeable @ 16% p.a. compounded quarterly. The security for the loan being 7,000 shares of ₹100 each in a public limited company valued @ ₹90 each. There is no repayment till 31.12.2021. On 31.12.2021, the value of shares declined to ₹80 per share. How would you classify the loan as secured or unsecured in the Balance Sheet? [5]

Answer:

Date	Particulars	Amount (₹)
31.12.2021	Balance of Loan (Principal)	5,00,000
	Add: Outstanding Interest	1,08,326*
	Total claim	6,08,326
	Less: Value of security at that date 7,000 shares × ₹ 80	5,60,000
		48,326

∴ **Classification:**

Secured	₹5,60,000
Unsecured	₹48,326

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Workings:

Calculation of Outstanding Interest

Quarters ending	Interest (₹)		Closing balance with principal (₹)
31.12.2020	20,000	$(5,00,000 \times \frac{16}{100} \times \frac{3}{12})$	5,20,000
31.03.2021	20,800	$(5,20,000 \times \frac{16}{100} \times \frac{3}{12})$	5,40,800
30.06.2021	21,632	Do	5,62,432
30.09.2021	22,497		5,84,929
31.12.2021	23,397		6,08,326
	1,08,326*		

4. APC Ltd. provides the following Trial Balance as on 31st March 2023:

Particulars	Dr. Balance (₹)	Cr. Balance (₹)
Equity Share Capital 300000 shares of ₹10 each fully paid		30,00,000
12% Bank Loan		2,00,000
Furniture	2,25,000	
Machinery	7,50,000	
Building	12,50,000	
Non-current Investment	2,00,000	
Sales		48,00,000
Sales Return	4,00,000	
Interest Received on Investment		20,000
Interest on Bank Loan	20,000	
Purchase	33,20,000	
Purchase Returns		420,000
Opening Stock	2,00,000	
Discount	6,250	
Carriage on Goods Sold	1,39,000	
Rent and Taxes	60,000	
Trade Receivables	12,00,000	
Trade Payables		80,000
Advertisement	1,20,000	
Bad Debt	10,000	
Salaries	4,00,750	
Audit Fees	27,000	
Contribution of P.F.	60,000	
Cash at Bank and in hand	1,32,000	
Total	85,20,000	85,20,000

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Additional Information:

- (i) Closing Stock as on 31st March 2023 was ₹2,12,500
- (ii) Depreciation Rates: Furniture 10%; Machinery 20% and Building 10%
- (iii) Outstanding salaries as on 31st March 2023 was ₹62,250
- (iv) Trade receivables include a sum of ₹25,000 due from Mr. B. Reddy and trade payables include ₹15,000 due to him.
- (v) Create a provision for doubtful debt @ 5% on trade receivables.
- (vi) Provide for income tax ₹80,000.

Prepare a Statement of Profit and Loss for the year ended on 31st March 2023 and a Balance Sheet as on that date. [12]

Answer:

Statement of Profit and Loss for the year ended on 31.03.2023

Particulars	Note	₹
I. Revenue from operation (sales less returns)		44,00,000
II. Other Income (Income from investment)		20,000
III. Total revenue		44,20,000
IV. Expenses:		
Purchase		29,00,000
Changes in inventory i.e. (opening less Closing)		(12,500)
Employee Benefit expenses	1	5,23,000
Finance cost	2	24,000
Depreciation	5	2,97,500
Other expenses	3	4,21,500
		41,53,500
V. Profit before exceptional and extraordinary items and tax		2,66,500
VI. Exceptional items		Nil
VI Profit before extraordinary items and tax		2,66,500
VII. Extraordinary items		Nil
VIII. Profit before tax		2,66,500
IX. Tax (provision for tax)		80,000
X. Profit after tax		1,86,500

Balance Sheet as on 31.03.2023

I. Equity and Liabilities	Note	₹
1. Shareholders' Funds		
(a) Share Capital		30,00,000
(b) Reserve and Surplus (Balance of Profit)		1,86,500
2. Share Application money pending allotment		Nil
3. Non-current liabilities (12% Bank loan)		2,00,000
4. Current Liabilities		
Trade Payable (after set off of ₹15,000)		65,000

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Outstanding interest		4,000
Outstanding salary		62,250
Provision for Tax		80,000
Total		35,97,750
II. Assets		
1. Non-current Assets		
(a) Fixed Assets (Tangible)	5	19,27,500
(b) Non-current Investment		2,00,000
2. Current Assets		
Inventories		2,12,500
Trade Receivable	4	11,25,750
Cash and cash equivalent		1,32,000
Total		35,97,750

Notes to Accounts (Schedules):

Schedule - 1. Employee Benefit Expenditure	₹
Salaries	4,00,750
Outstanding Salaries	62,250
Contribution to P.F.	60,000
	5,23,000

Schedule - 2. Finance Cost	₹
Interest on loan	20,000
Outstanding Interest	4,000
	24,000

Schedule - 3. Other Expenditure	₹
Discount	6,250
Carriage	1,39,000
Rent	60,000
Advertisement	1,20,000
Bad Debt	10,000
Audit fees	27,000
Provision for Bad debt	59,250
	4,21,500

Schedule - 4. Trade Receivable	₹
Total Receivable	12,00,000
(-) Set off	15,000
	11,85,000
(-) Provision @ 5%	59,250
	11,25,750

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Schedule - 5. Fixed Assets	Furniture (₹)	Machine (₹)	Building (₹)
Balance	2,25,000	7,50,000	12,50,000
(-) Depreciation	22,500	1,50,000	1,25,000
	2,02,500	6,00,000	11,25,000
Total Fixed Assets			19,27,500
Depreciation			2,97,500

5. Write short note (any three):

[3×4=12]

- (a) Main Characteristics of a Company;
- (b) Accounting treatment of Borrowing Cost as per AS-16;
- (c) Central Electricity Regulatory Commission (CERC);
- (d) Importance of Cash flows.

Answer:

(a) Main Characteristics of a Company -

- (i) It is a distinct legal person existing independent of its members
- (ii) Liability of the members is limited to the extent of the face value of shares held by them.
- (iii) It has a perpetual succession i.e., the members of the company may keep on changing from time to time but this does not affect the company's continuity.
- (iv) The shares of a company are freely transferable except in case of a Private Limited Company.
- (v) A company being a legal person is capable of owing, enjoying and disposing of the property in its own name.
- (vi) A company, being a separate body can sue and be sued in its own name.
- (vii) Though a company is an artificial person yet it acts through human beings who are called directors of the company. There is a divorce between ownership and the management.
- (viii) It is a voluntary association of persons usually for profit.

(b) Accounting treatment of Borrowing Cost as per AS-16 -

- (i) Borrowing costs should either be capitalized or charged to P&L Account depending on the situation but deferment is not permitted.
- (ii) Borrowing costs are capitalized as part of cost of qualifying asset when it is probable that they will result in future economic benefits and cost can be measured reliably - other borrowing costs are charged to P&L Account in the accounting period in which they are incurred.
- (iii) Capitalization, on one hand reflects closely the total investment in the asset and on the other hand to charge the cost to future period against accrual of revenue.
- (iv) Notional interest cost are not allowed to be capitalized.

- (v) A qualifying asset is an asset that necessarily takes a substantial period of time (usually a period of 12 months unless otherwise justified on the basis of facts and circumstances) to get ready for its intended use or sale.
- (vi) Capitalization should be suspended during extended period in which active development is interrupted.
- (vii) Capitalization should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.
- (viii) Capitalization also ceases 'when part is completed, which is capable of being used independently of the whole.

(c) Central Electricity Regulatory Commission (CERC) -

Meaning: The Central Electricity Regulatory Commission shall be a body corporate, having perpetual succession and a common seal with power to acquire, hold and dispose of property, both movable and immovable, and to contract and shall, by the said name, sue or be sued.

Constitution: The Central Commission shall consist of the following Members namely:

- (a) A chairperson and 3 Members
- (b) The Chairperson of the Authority who shall be the Member, ex-officio.

Appointment: The Chairperson and Members of the Central Commission shall be appointed by the Central Government on the recommendation of the Selection Committee.

Functions: The functions of the Central Commission include regulating the tariff of generating companies, the interstate transmission of electricity, to issue licenses, to levy fees, to fix trading margin etc.

(d) Importance of Cash flows -

Cash flows are crucial to business decisions. Cash is invested in the business and the rationality of such investment is evaluated taking into account the future cash flows it is expected to generate. Economic value of an asset is derived on the basis of its ability to generate future cash flows. Economic value of an asset is given by the present value of future cash flows expected to be derived from the asset.

Profit is an accounting concept. Profit is derived on accrual assumption. Profit and cash flows from operational activities are not the same. Dividend decision is taken on the basis of profit, although it is to be paid in cash. Similarly, debt servicing capacity of a company is determined on the basis of cash flows from operations before interest. Ploughing back of profit is a much talked about source of financing modernisation, expansion and diversification. Unless retained profit is

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supported by cash, ploughing back is not possible. Thus cash flows analysis is an important basis for making several management decisions.

Section – B (Auditing)

Answer Question No. 6 and any three from Question Nos. 7,8,9 and 10.

6. (a) Choose the correct answer from the given four alternatives: [6x1=6]
- (i) Dividend cannot be paid out of
- (a) current year's profit after providing depreciation.
 - (b) undistributed profits for any previous financial year or years after providing for depreciation.
 - (c) profit on revaluation of any fixed assets.
 - (d) money provided by the Central Government or a State Government.
- (ii) An auditor should submit a Disclaimer of Opinion when
- (a) he is satisfied with the truth and fairness of financial statements.
 - (b) he has certain reservations as to the presentation of truth and fairness in financial statements.
 - (c) some material information is not available.
 - (d) the effect of any disagreement with the management is not so material.
- (iii) SA 530 stands for
- (a) Audit Documentation
 - (b) Audit Sampling
 - (c) Responsibility of Joint Auditor
 - (d) Agreeing the terms of Audit Engagements
- (iv) The first Auditor of a Company shall be appointed by the Board of Directors within
- (a) 30 days from the date of registration.
 - (b) 90 days from the date of registration.
 - (c) 30 days from the date of first AGM.
 - (d) 1 year from the date of registration.
- (v) As per SQC 1, Audit working papers should be retained for a period of
- (a) 2 years
 - (b) 5 years
 - (c) 7 years
 - (d) 10 years
- (vi) Preventive Control is a type of ____
- (a) Internal Control
 - (b) Detective Control

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- (c) Verification
- (d) None of the above

Answer:

- (i) — (c)
- (ii) — (c)
- (iii) — (b)
- (iv) — (a)
- (v) — (c)
- (vi) — (a)

b) Match the following: [4×1=4]

	Column 'A'		Column 'B'
1.	Sec. 204 of the Companies Act	A.	Excise Duty
2.	GAR 7 Challan	B.	Section 123
3.	Declaration of Dividend	C.	₹ 5,00,000
4.	Maximum fees for contravention of Section 139	D.	Secretarial Audit

Answer:

	Column 'A'		Column 'B'
1.	Sec. 204 of the Companies Act	D.	Secretarial Audit
2.	GAR 7 Challan	A.	Excise Duty
3.	Declaration of Dividend	B.	Section 123
4.	Maximum fees for contravention of Section 139	C.	₹ 5,00,000

(c) Say True or False for the following question: [4×1=4]

- (i) Routine checking is a substitute of vouching.
- (ii) "Debenture" includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not.
- (iii) An auditor of a company can render Investment Banking Service.
- (iv) Internal audit is conducted by the staff of the entity or by an independent professional appointed for that purpose.

Answer:

- (i) False
- (ii) True
- (iii) False

(iv) True

Answer any three questions out of the following four questions [3×12=36]

7. (a) **Discuss the various methods of obtaining audit evidences. How will you assess the reliability of audit evidences obtained? [5+3=8]**

Answer:

An auditor applies the following methods for obtaining sufficient and appropriate audit evidence.

- (i) **Inspection:** Inspection involves examining records or documents, whether internal or external, in paper form or otherwise or a physical verification of a tangible asset. Inspection can provide reliable audit evidence depending on their nature and source and effectiveness of the internal control over their generation and processing.
- (ii) **Observation:** Observation consists of looking at a process or procedure being performed by others on a real time basis. For example, the auditor may observe the inventory counting by the entity's personnel and obtain evidence that it is done correctly.
- (iii) **External Confirmation:** External confirmation represents audit evidence obtained by the auditor as a direct written response from a third party, in paper form or by electronic or any other medium. For example, confirmation from the customer about the terms of agreement.
- (iv) **Recalculation:** Recalculation consists of checking the mathematical accuracy of documents or records. This may be performed manually or electronically.
- (v) **Re-performance:** Re-performance involves auditor's independent execution of procedures or controls that were originally performed as part of entity's internal control.
- (vi) **Analytical Procedures:** Analytical procedures involve evaluation of financial information by studying possible relationships among both financial and non-financial data and investigating identified fluctuations from previous years that are inconsistent.
- (vii) **Inquiry:** Inquiry consists of seeking information, both financial and non-financial, from knowledgeable persons within or outside the entity. Inquiries may range from formal written inquiries addressed to external parties to informal inquiries addressed to client's staff.

As per SA 500, reliability of audit evidence depends on its source (whether internal or external) and nature (whether visual, documentary or oral). However, the following generalizations may be considered useful while assessing the reliability of audit evidence.

- (i) Evidence obtained from independent and external sources are more reliable.

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- (ii) Internal evidence becomes more reliable when the related internal control over its preparation and maintenance is effective.
- (viii) Evidence obtained directly by the auditor is more reliable than those obtained indirectly or by inference.
- (ix) Evidence in documentary form is usually more reliable than oral representation.
- (x) Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies or facsimiles or documents that have been filmed or digitized. In order to be certain about the reliability of audit evidence in relation to a particular matter, an auditor should try to obtain evidence from various sources. In case there appears any inconsistency, the auditor must obtain additional evidence by conducting other audit procedures.

(b) 'Checklist and Internal Control Questionnaire are not the same.'—Discuss. [4]

Answer:

Difference between Checklist and Internal Control Questionnaire

Sl. No	Basis	Check List	Internal Control Questionnaire
1	Point of Time	It is issued at the commencement of audit and reported back after completion of audit.	It can be issued at any point of time and reported back immediately.
2	Issued to	It is issued to the audit staff to be followed by them during audit and reported back at completion.	It is issued to various people at different levels in the organization.
3	Contents	It contains instructions to be followed by audit assistants.	It contains questions to be answered by the employees of the organization.
4	Objective	It works as a guideline for audit staff so that none remains unchecked.	This is used to collect the information to know about the internal control system and to evaluate the weaknesses therein.

8. (a) Discuss the provisions of Companies Act, 2013 as regards reporting of frauds by Company Auditor. [6]

Answer:

The provisions of Companies Act 2013 regarding reporting of frauds by a company auditor are as follows:

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- (1) For the purpose of sub-section (12) of section 143, in case the auditor has sufficient reason to believe that an offence involving fraud, is being or has been committed against the company by officers or employees of the company, he shall report the matter to the Central Government immediately but not later than sixty days of his knowledge and after following the procedure indicated herein below.
 - (i) auditor shall forward his report to the Board or the Audit Committee, as the case may be, immediately after he comes to knowledge of the fraud, seeking their reply or observations within forty-five days;
 - (ii) on receipt of such reply or observations the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government within fifteen days of receipt of such reply or observations;
 - (iii) in case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of forty-five days, he shall forward his report to the Central Government along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he failed to receive any reply or observations within the stipulated time.
- (2) The report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed post followed by an e-mail in confirmation of the same.
- (3) The report shall be on the letter-head of the auditor containing postal address, e-mail address and contact number and be signed by the auditor with his seal and shall indicate his Membership Number.
- (4) The report shall be in the form of a statement as specified in Form ADT-4.
- (5) The provision of this rule shall also, mutatis mutandis, to a cost auditor and a secretarial auditor during the performance of his duties under section 148 and section 204 respectively.

(b) Discuss the procedure for appointment for first Auditor of the Company and his tenure. [6]

Answer:

- First auditor of the company, other than a Government company, shall be appointed
- By the BOD within 30 days from the date of registration of the company;
 - If BOD fails to appoint, by the member of the company within 90 days at an extraordinary general meeting appoint the first auditor”;
 - In case of Government company, first auditor shall be appointed by CAG within 60 days from the date of registration;
 - If CAG fails to appoint, by the BOD of the company within next 30 days;
 - If again BOD fails to appoint the first auditor of the company, by the member of the company within 60 days at an extraordinary general meeting;

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- Tenure of the first auditor of the company in both the above cases till the conclusion of the first annual general meeting.

9. (a) What is the procedure to be followed for fixing the remuneration of a Cost Auditor? [4]

Answer:

Authority for fixing the Remuneration of a Cost Auditor:

Rule 14 of the Companies [Audit and Auditors] Rules 2014 has laid down the procedure of appointment and fixing the remuneration of a cost auditor. It states as follows:

Remuneration of the Cost Auditor: For the purpose of sub-section (3) of section 148 –

- (a) In the case of companies which are required to constitute an audit committee –
 - (i) The Board shall appoint an individual, who is a cost accountant in practice, or a firm of cost accountants in practice, as cost auditor on the recommendations of the Audit committee, which shall also recommend remuneration for such cost auditor;
 - (ii) The remuneration recommended by the Audit Committee under (i) shall be considered and approved by the Board of Directors and ratified subsequently by the shareholders;

(b) Discuss the basic elements of an audit report. [8]

Answer:

The Basic Elements of the Auditors' Report are –

- (i) Title: The Auditor's Report should have an appropriate title i.e. "Auditor's Report". It should be distinguished from other Reports, e.g. reports of officers of the entity, Board of Directors.
- (ii) Addressee: The Auditor's Report should be appropriately addressed as required by the circumstances of the engagement and applicable laws and regulations. Ordinarily, the Auditor's Report is addressed to the authority appointing the Auditor.
- (iii) Opening or Introductory Paragraph:
 - (a) The Auditor's Report should identify the Financial Statements of the entity that have been audited, including the date of and period covered by the Financial Statements.
 - (b) The Report should include a Statement that the Financial Statements are the responsibility of the entity's management and a Statement that the responsibility of the Auditor is to express an opinion on the Financial Statements based on the audit.
- (iv) Scope Paragraph:

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- (a) The Auditor's Report should describe the scope of the audit by stating that the audit was conducted in accordance with standards on auditing generally accepted in India.
- (b) The Report should include a statement that the audit was planned and performed to obtain reasonable assurance whether the Financial Statements are free of material misstatement.
- (c) The Auditor's Report should describe the Audit as including examining, on a test basis, evidence to support the amounts and disclosures in Financial Statements, assessing the accounting principles used in the preparation of the Financial Statements, assessing significant estimates made by management, in the preparation of Financial Statements, & evaluating the overall position of Financial Statements.
- (d) The Report should include a statement by the Auditor that the audit provides a reasonable basis for his opinion.
- (v) Opinion Paragraph: The Opinion paragraph of the Report should indicate the Financial Reporting framework used to prepare the Financial Statements. It should state the Auditor's opinion as to whether the Financial Statements give a true and fair view in accordance with the financial reporting framework and, where appropriate, whether the Financial Statements comply with the statutory requirements.
- (vi) Date of the Report: The date of an Auditor's Report is the date on which the Auditor signs the Report expressing an opinion on the Financial Statements. The Auditor should not date the Report earlier than the date on which the Financial Statements are signed or approved by Management.
- (vii) Place of Signature: The Report should name the specific location, which is ordinarily the city where the Audit Report is signed.
- (viii) Auditor's Signature: The Report should be signed by the Auditor in his personal name. Where a Firm is appointed as the Auditor, the Report should be signed in the personal name of the Auditor and in the name of the Audit Firm. The Partner/ Proprietor signing the Report should mention his ICAI Membership Number.

10. Write short notes (Any three)

(3x4=12)

- (a) Audit of a Hospital.**
- (b) Elements of 'cost of inventory' as per AS 2.**
- (c) Auditor's duty regarding unclaimed dividend**
- (d) Auditor's duty regarding Issue of Debentures.**

Answer:

(a) Audit of a Hospital

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 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.
- (vi) Interest and/or dividend income should be vouched with reference to the Investment Register and Interest and Dividend warrants.
- (vii) 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.
- (viii) Where receipts of subscription show significant deviations from budgeted figures, it should be thoroughly inquired into and the matter be brought to the notice of the trustees or the Managing Committee.
- (ix) Government grants or grants from local bodies should be verifies with the reference to the correspondence with the concerned authorities.
- (x) Clear distinction should be made between the items of capital and revenue nature.
- (xi) The capital expenditure should be incurred under proper authorization by a valid resolution of the trustees or the Managing Committee.
- (xii) Verify the system of internal check as regards purchases and issue of stores, medicines etc.
- (xiii) Examine that the appointment of the staff, payment of salaries etc. are duly authorized.
- (xiv) Physically verify the investments, fixed assets and inventories.
- (xv) Check that adequate depreciation has been provided on all the depreciable assets.

(b) Elements of 'cost of inventory' as per AS 2

Cost of inventory includes the following

1. Cost of purchase
 2. Cost of conversion
 3. Other costs incurred in bringing the inventories to their present location and condition.
-
1. Cost of purchase includes—
Purchase price, Duties and Taxes, Freight inward, other expenditures directly attributable to the acquisition less duties and taxes recoverable by

enterprises from taxing authorities. Trade discount, Rebate, Duty drawback, Other similar items.

2. Cos of conversion —

It consists of the cost directly related to the units + Systematic Allocation of fixed and variable production overheads that are incurred in converting material into finished goods.

Fixed Production overhead means Indirect cost of production that remains relatively constant regardless of volume of production. Allocation of fixed production overhead is done on normal capacity.

Variable Production overhead means indirect cost of production that varies directly or nearly directly with the volume of production. Allocation of variable production overhead is done on actual production.

In case of Joint-products, when the cost of conversion of each product is not identifiable separately, total cost of conversion is allocated between the products on the rational and consistent basis, if by-products, scrap or waste materials are not of material value, they are measured at net realisable value, then the net realisable value is deducted from cost of conversion. Net cost of conversion is distributed among the main products.

3. Other costs: Cost incurred in bringing the inventories to their present location and condition.

(c) Auditor's duty regarding unclaimed dividend

In connection with the unclaimed dividend, the auditor must consider the following points:

- (i) He shall collect the list of the names of the shareholders to whom dividend could not be paid.
- (ii) He shall verify the calculation of unclaimed dividend.
- (iii) He shall verify that the unpaid dividend has been transferred to a separate account namely Unpaid Dividend Account within seven days from the expiry of 30 days allowed for declaration and payment of dividend.
- (iv) In case there is any default on the part of the company to deposit the unpaid dividend within the stipulated time as mentioned above, the company needs to pay interest @12% p.a. The auditor must verify whether there is any fault on the part of the company and if so whether they have deposited the interest and the penalty.
- (v) The auditor shall also verify whether the company has published the details of unpaid dividend in its own website and also in other website(s) approved by the government for this purpose.
- (vi) In case the company has made any payment during the year from the Unpaid Dividend Account to any shareholder on his application for the same, the auditor must verify that the payment has been made to the right person and the amount so paid is determined properly. (vii) In case any amount of dividend is remaining unpaid for more than seven years, the auditor shall verify whether the same along with the interest accrued thereon has been transferred by the company to IEPF. He shall verify the

same based on the statement submitted by the company to the IEPF and the receipt issued by the IEPF in this context.

- (viii) The auditor shall also verify whether all the shares in respect of which unpaid dividend has been transferred to IEPF, have also been transferred to such fund.

(d) Auditor's duty regarding Issue of Debentures

- (i) The auditor should verify that the prospectus had been duly filed with the registrar before the date of allotment of debentures.
- (ii) He should check the amount collected in the cash book with the counterfoils of receipts issued to the applicants and also cross check the amount into the application and allotment book.
- (iii) He should examine the debenture trust deed and note the conditions contained therein as to issue and repayment.
- (iv) If the debentures are covered by a mortgage of a charge, it should be verified that the charge has been correctly recorded in the register of mortgage and charges" and it has also been registered with the registrar of the companies.
- (v) Compliance with SEBI guidelines should also be ensured.
- (vi) Where debentures have been issued as fully paid up to vendors as a part of the purchase consideration, the contract in this regard should be checked.