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.) [10x2=20 marks]

(i) Exemptions from application of the Rules are provided to Companies whose revenue from exports, in foreign exchange, exceeds ________________ of total revenue and companies operating from Special Economic Zones.
(a) 45%
(b) 50%
(c) 75%
(d) 80%

(ii) Cost Auditing Standard 103 deals with ______________.
(a) planning an Audit of Cost Statements
(b) Cost Audit Documentation
(c) knowledge of process and business
(d) overall objectives of the Independent Cost Auditor

(iii) Field Balance Sheet Approach to audit can be applied in audit of ——————
(a) Non-Governmental Organisations (NGOs)
(b) Self Help Group
(c) Local Bodies
(d) Commercial Accounts

(iv) Cost Auditor's observation and suggestions are given in ____________
(a) CRA-3
(b) CRA -2
(c) CRA-1
(d) Annexure

(v) CAS 7 deals with ______________.
(a) Direct Material Cost
(b) Indirect Material Cost
(c) Packing Material Cost
(d) Employee Cost.

(vi) —————— is the evaluation of every resources declared in the industry.
(a) Performance Analysis
(b) Productivity Analysis
(c) Profitability Analysis
(d) Financial Analysis

(vii) _____________ of the Annexure to the Cost Audit Report prescribes the method of calculation of Value Addition.
(a) Part A
(b) Part B
(c) Part C
(d) Part D

(viii) The main emphasis of Management Audit is ___________
(a) problem solving
(b) problem identification
(c) problem definition
(d) problem avoidance

(ix) CAS 5 deals with_________
(a) equalized cost of transportation
(b) captive consumption
(c) capacity determination
(d) cost classification.

(x) _____________ is sometimes defined as an extension of Financial Audit.
(a) Internal Audit
(b) Management Audit
(c) Operational Audit
(d) Propriety Audit

Answer:

1. (i) (c) 75%.
Reason: The requirement of Cost Audit under these rules shall not apply to companies whose revenue from exports in foreign exchange exceed 75% of total revenue and companies operating in special economic zone.

(ii) (d) overall objectives of the Independent Cost Auditor
Reason: This Standard on Auditing 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.

(iii) (b) Self Help Group
Reason: The auditor prepares the Field Balance Sheet for the group, as on the date of the audit, based on the Self Help Group's (SHG's) internal records and then cross checks the correctness of balance sheet items. The primary objective is to ascertain the retained earnings of the SHG.

(iv) (a) CRA-3.
Reason: This is as per format prescribed by Companies(Cost Records and Audit) Rules, 2014.

(v) (d) Employee Cost
Reason: This standard deals with the principles and methods of classification, measurement and assignment of Employee cost, for determination of the Cost of product or service, and the presentation and disclosure in cost statements.

(vi) (b) Productivity Analysis.
Reason: Productivity involves variables of input resources and the output. Measuring, identifying and isolating the different input resources and analyzing their contribution to produce goods and services and their effect on costs and profitability is imperative of Productivity Analysis.

(vii) (d) Part D

Reason: Annexure to the Cost Audit Report - Part D prescribes the method of calculation of Value Addition. The term "Value Addition" has been defined under the Companies (Cost Records and Audit) Rules, 2014 as the difference between net output value (net sales adjusted for WIP and finished stock) and cost of bought out materials and services for the product under reference.

(viii) (b) Problem identification.
Reason: Management Audit pinpoints the areas requiring attention of management. It evaluates the existence of well defined objectives. It seeks to review appraise and evaluate the corporate plans and policies based on certain standards of objectivity.

(ix) (a) equalized cost of transportation.
Reason: 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.

(x) (c) Operational Audit
Reason: An operational Audit is sometimes defined as an extension of a Financial Audit. The objective of Operational Audit is to assist the organization in performing functions more effectively and economically with focus on the efficiency and effectiveness of operations.

Section - B [80 marks]

2. (a) What is Captive Consumption? What are the different cost components are considered to determine the Cost of Production for Captive Consumption?

(b) A steel company which produces Iron Casting Pipes and rod iron is covered under the Cost Audit according to the Companies (Cost Records and Audit) Rules 2014. From the expenditure data relating to 2017-18, determine the employees cost according to CAS -7.

Sl. No.	Particulars	₹ In lakh
(i)	Salary, wages and other allowances	750
(ii)	Bonus	100
(iii)	Contribution to Provident Fund	90
(iv)	Wages to contractors employees	100
(v)	Employees welfare	40
(vi)	Abnormal cost due to strike	80
(vii)	VRS payment for closure of Rod Iron section of the plant	62
(viii)	Arrear Salary (2016-17)	210
(ix)	Compensation paid against the past periods against Court order	67

[10 + 6]

Answer:

2. (a) Captive Consumption means the consumption of goods manufactured by one division and consumed by another division(s) of the same organization or related undertaking for manufacturing another product(s). Cost Accounting Standard 4 (CAS-4) deals with determination of cost of production for captive consumption.

To determine the cost of production for captive consumption, calculations of different cost components are given below:

(i) Material Consumed:
Material Consumed shall include materials directly identified for production of goods.

(ii) **Direct wages and salaries:** Direct wages and salaries shall include house rent allowance, overtime and incentive payments made to employees directly engaged in the manufacturing activities.

(iii) **Direct Expenses:**
Direct expenses are the expenses other than direct material cost and direct employees costs which can be identified with the product.

(iv) **Works Overheads:**
Works overheads are the indirect costs incurred in the production process.

(v) **Quality Control Cost:**
The quality control cost is the expenses incurred relating to quality control activities for adhering to quality standard. These expenses shall include salaries & wages relating to employees engaged in quality control activity and other related expenses.

(vi) **Research and Development Cost:**
The research and development cost incurred for development and improvement of the process or the existing product shall be included in the cost of production.

(vii) **Administrative Overheads:**
Administrative overheads need to be analysed in relation to production activities and other activities. Administrative overheads in relation to production activities shall be included in the cost of production.
Administrative overheads in relation to activities other than manufacturing activities e.g. marketing, projects management, corporate office expenses etc. shall be excluded from the cost of production.

(viii) **Packing Cost:**
If product is transferred/dispatched duly packed for captive consumption, cost of such packing shall be included. Packing cost includes both cost of primary and secondary packing required for transfer/ dispatch of the goods used for captive consumption.

(ix) **Absorption of overheads:**
Overheads shall be analysed into variable overheads and fixed overheads.
The variable production overheads shall be absorbed in production cost based on actual capacity utilisation.
The fixed production overheads and other similar item of fixed costs such as quality control cost, research and development costs, administrative overheads relating to manufacturing shall be absorbed in the production cost on the basis of the normal capacity or actual capacity utilization of the plant, whichever is higher.

(x) **Valuation of Stock of work-in-progress and finished goods:**
Stock of work-in-progress shall be valued at cost on the basis of stages of completion as per the cost accounting principles. Similarly, stock of finished goods shall be valued at cost. Opening and closing stock of work-in-progress shall be adjusted for calculation of cost of goods produced and similarly opening and closing stock of finished goods shall be adjusted for calculation of goods despatched.

(xi) **Treatment of Joint Products and By-Products:**
A production process may result in more than one product being produced simultaneously. In case joint products are produced, joint costs are allocated between the products on a rational and consistent basis. In case by-products are produced, the net realisable value of by-products is credited to the cost of production of the main product.

(xii) **Treatment of Scrap and Waste:**
The production process may generate scrap or waste. Realized or realizable value of scrap or waste shall be credited to the cost of production.

2. (b) The following items will not be included according to CAS-7:
VRS paid for closure of a unit
Abnormal cost charges to Profit and Loss A/C
Area salary not related to the current year
Compensation paid against past periods
Wages paid to contractor employees.

[As per explanation (1) of CAS-7 under para-4.7: Contract employees include employees directly engaged by the employer on contract basis but does not include employees of any contractor engaged in the organisation.]

Thus, employees cost:

Sl. No.	Particulars	₹ In lakh
(i)	Salary and wages	750
(ii)	Contribution to PF	90
(iii)	Employees welfare	40
(iv)	Bonus	100
	Total	**980**

3. (a) (i) A manufacturing firm has up its own power plant to cater its need in manufacturing process.

It's one month data is given below:
Number of units produced = 100 lakh units of which 5% is used by generating unit.

Material and utility used :
(i) Coal 300 MT @ ₹ 30,000 per MT
(ii) Oil 5 MT @ ₹ 1,60,000 MT
(iii) Cost of Water extraction and treatment : 6 lakh litres @ ₹ 3 per litre
(iv) Steam boiler cost ₹ 55 lakh with residual value5 lakhs after life of 10 years.
(v) Cost of Generating Plant is ₹ 90 lakhs with no residual value. Depreciation is charged on straight line method @ 10%
(vi) Generating Plant : 100 skilled workers@ ₹ 30,000 & 150 helpers @ ₹ 20,000 pm.
(vii) Boiler plant : 60 semi-skilled workers @ ₹ 25,000 & 100 helpers @ ₹ 20,000pm
(viii) Repair & Maintenance of generating plant & Boiler is ₹ 5.0 lakhs
(ix) Share of Administrative charges ₹ 20 lakh
(x) Realization from Sale of ash disposed is ₹ 1.5 lakh

Prepare a cost sheet for Electricity Generating Cost and calculate cost per unit.

3. (a) (ii) Tirupati Ltd., a manufacturing unit, produces two products A and B. The following information is extracted from the Books of the Company for the year ended March 31, 2018:

Particulars	Product A	Product B
Units Produced (Qty.)	**2,10,000**	**1,68,000**
Units sold (Qty.)	**1,68,000**	**1,36,500**
Machine hours utilized	**1,26,000**	**84,000**
Design charges (₹)	**1,57,500**	**1,89,000**
Software development charges (₹)	**2,62,500**	**3,78,000**

Royalty paid on sales ₹ 6,09,000 [@ ₹ 2 per unit sold for both the products].

(i) Royalty paid on units produced ₹ 3,78,000 [@ Re. 1 per unit produced for both the products].

(ii) Hire charges of equipment used in the manufacturing process of product PB only ₹ 53,000.

Note: No adjustments are to be made related to units held i.e. Closing Stock.
You are required to compute the Direct Expenses—keeping in view of Cost Accounting Standard (CAS)-10. [6 + 4]

(b) How can the cost audit report and compliance report is converted into the XBRL format? 6

Answer:

3. (a) (i)

Particulars	**Calculation**	**₹ In lakh**
Material Cost		
Coal	300 x 30,000	90.00
Oil	5 x 1,60,000	8.00
Water	6 x 3	18.00
Total Material Cost		**116.00**
Wages for Generator plant	(100 x 30,000) + (150 x 20,000)	60.00
Wages for Boiler plant	(60 x 25,000) + (100 x 20,000)	35.00
Depreciation - Generating Plant	90 x 0.10	9.00
Depreciation- Boiler plant	(55-5)/10	5.00
Repair &Maintenance		5.00
Administrative Expenses		20.00
Total Cost		**250.00**

As generating unit consumes 5%, effective unit produced for manufacturing = 95 lakh
Cost per unit = ₹ 250/95 = ₹ 2.63 (approx)

3. (a) (ii)

Tirupati Ltd.
Computation of Direct Expenses (As per CAS – 10)

Particulars	**Product A**	**Product B**
Royalty paid on sale	3,36,000	2,73,000
Add: Royalty paid on units produced	2,10,000	1,68,000
Add: Hire charges of equipment used in the manufacturing process of product-A only	53,000	-
Add: Design charges	1,57,500	1,89,000
Add: Software development charges related to production	2,62,500	3,78,000
Direct expenses (total)	**10,19,000**	**10,08,000**

3. (b) XBRL (Extensible Business Reporting Language) is an open source technology. Any of the following methods can be adopted to create the instance document required for filing of the respective reports.

- XBRL-enabled software packages developed by different software vendors which support the creation of cost reports in XBRL format can be used to create the necessary document.
- Various elements of Cost Audit Report and Compliance Report can be mapped into XBRL tags of the costing taxonomy using specialised XBRL software tools specifically designed for this purpose.

- Different third party packages can be integrated into the existing accounting systems to generate XBRL Cost statements.
- There are various web based applications available that take input reports in various formats viz. Microsoft Excel etc. and transform them into XBRL format.

The methodology adopted by an individual company will depend on its requirements and the cost accounting software and systems being used and other factors.

4. (a)

Selected statistics of Vijay & Company Limited for two years, are given below:

	(Amount in lakh)	
Particulars	**31.03.2018**	**31.03.2017**
Gross Profit	**36%**	**33.33%**
Stock turnover	**20 times**	**25 times**
Average Stock	**₹ 38,400**	**₹ 36,000**
Average Debtors	**₹ 87,500**	**₹ 1,68,750**
Income Tax rate	**50%**	**50%**
Net Income after tax as % of Sales	**6%**	**7%**
Maximum Credit period allowed to customers	**60 Days**	**60 Days**

You are required to:

(i) Prepare a statement of profits in comparative form for all the two years.

(ii) Evaluate the position of the company regarding profitability and liquidity on the basis of information supplied to you.

(iii) What additional information will you require to evaluate fully the position of the company on the liquidity fund? 10

(b) You are the Management Auditor of a large manufacturing company suffering from working capital crisis. Which areas you will cover to overcome the crisis? 6

Answer:

4. (a) (i)

Statement of Profit of Vijay & Company Limited for the year ended 31.03.2018 & 31.03.2017

Particulars	**31.03.2018 (₹)**	**31.03.2017 (₹)**
Sales	12,00,000	13,50,000
Less: Cost of Goods Sold	7,68,000	9,00,000
Gross Profit	4,32,000	4,50,000
Less: Operating Expenses	2,88,000	2,61,000
Profit before taxes	1,44,000	1,89,000
Less: Taxes	72,000	94,500
Net Profit	72,000	94,500

The Profitability of the Company is consistently improving. Its liquidity position, judged terms of debtors and stock turnover ratios, can be said to be very satisfactory. The stock turnover ratio being as high as 20 times. The debtors turnover ratios are also very high.

For 31.03.2018 = ₹ 12,00,000 ÷ ₹ 87,500 = 13.7 times
For 31.03.2017 = ₹ 13,50,000 ÷ ₹ 1,68,750 = 8.0 times

(iii) The amount of current liabilities and current assets, other than debtors and stock, are required to evaluate fully the position of the company on the liquidity front.

Workings :

(1) Year 2018,

Cost of Goods Sold	= Stock Turnover X Average Stock
	= 20 X ₹ 38,400
	= ₹ 7,68,000
Sales	= ₹ 7,68,000 X 100/ 64 = ₹ 12,00,000
Net Income	= 6% on ₹ 12,00,000 = ₹ 72,000

Therefore, Profit before tax ₹ 1,44,000

(2) Year 2017,

Cost of Goods Sold	= Stock Turnover X Average Stock
	= 25 X ₹ 36,000
	= ₹ 9,00,000

Sales = ₹ 9,00,000 X 100/ 66.67 = ₹ 13,50,000
Net Income = 7 % on ₹ 13,50,000 = ₹ 94,500

Therefore, profit before tax ₹ 1,89,000.

4. (b) Adequate working capital is required for smooth operation of the company. To ensure smooth flow of working capital the following action plan may be chalked out by the Management auditor:

(i) Estimation of working capital: The manager should prepare projected working capital statement based on the functional budgets such as sales, production, expenses, capital expenditure and the master Budget consisting of project profit and loss and balance sheet.

(ii) Cash flow statement/Cash budget: Month-wise cash flow statement showing inflow and outflow of cash head wise should be prepared to analyse major inflows and out flows affecting the entity. Any wasteful outflow can be traced and eliminated. Bank reconciliation statement to be prepared periodically so that outstanding can be traces and acted upon.

(iii) Inventory/Stock management: Raw material and Inventories should be properly classified to determine the level of stock material required. The method of valuation to be determined. To determine the time factor for receipt and consumption of material. This is required to assess the production schedule and to avoid wasteful expenditure on account of excess storage capacity and cost of storage of inventory. In no circumstances the production schedule to hamper .For this, the Economic Order Quantity procedure to be adopted for spending minimum cost of capital for maintaining the inventory. The system of inventory management needs to avoid wastes and scrap generated during storage and handling. Just in time philosophy may be adopted to reduce processing time, stock etc which will release the working capital.

(iv) Credit Management: The Company should lay down proper policy for evaluating customers, determine the credit period and offering discount for an early payment. An age wise analysis of debtors should also be prepared so as to avoid credit to defaulters and bad debt. Careful analysis of customers according to pattern of sales so as to exercise control over debit balances. The Company should through its purchase department endeavour to avail maximum credit period from creditors. These actions should increase the working capital.

(v) Funds flow Analysis: The company should prepare a funds flow analysis, distinguishing between long term short term sources and application of funds. Long term funds should be utilised for long term purposes and short term funds should be utilised for short term purposes. Working capital should not be utilised for capital assets.

(vi) Investment management: The idle funds of the company should be utilised for in short term securities to earn from idle short term funds.

(vii) WIP analysis: Minimum WIP should be monitored and for the purpose it is necessary to ensure no bottlenecks develop at any stage during production process.

5. (a) What is Audit Programme? What are the advantages and disadvantages of Audit Programme?

(b) Discuss about the salient features of Internal Audit and Operational Audit. [10 + 6]

Answer:

5. (a) An audit programme is a detailed plan of the auditing work to be performed, specifying the procedures to be followed in verification of each item and the financial statements and the estimated time required. To be more comprehensive, an audit programme is written plan containing exact details with regard to the conduct of a particular audit. It is a description or memorandum of the work to be done during an audit. Audit programme serves as a guide in arranging and distributing the audit work as well as checking against the possibility of the omissions.

Advantages of audit programme

The main advantages of an audit programme are as follows:

(i) It serves as a ready check list of audit procedures to be performed.

(ii) The audit work can be properly allocated to the audit assistants or the article clerks.

(iii) The auditor may easily know the extent of work done at any point of time. Thus, the progress of work done can be under the supervision and control of the auditor.

(iv) Audit programme would not only be useful for the audit assistants in carrying the audit work but for the principal too as he would be in a position to account for the individual responsibilities.

(v) A uniformity of the work can be attained as the same programme would be followed from time to time.

(vi) It is a useful basis for planning the programme for the following year.

(vii) It may be used as evidence by the auditor in the event when any charge is brought against him. He can prove that there has no negligence on his part and he exercised reasonable care and skill while performing the task.

Disadvantages of audit programme

The main disadvantages of an audit programme are as follows:

(i) The auditor's task becomes mechanical and the auditors may lose interest and initiative.

(ii) Drawing up of an audit programme may be unnecessary for a small concern.

(iii) Though audit programme helps in fixing responsibilities but inefficient staff may defend themselves by stating that the matter was not contained in the audit programme.

(iv) Rigid programmes cannot be laid down for each type of business.

Though an audit programme may suffer from the above disadvantages but these can be removed by taking some initiatives such as consulting the audit assistants, modifying the programme on the basis of experience gained during audit, etc.

5. (b) The salient features of Internal Audit and Operational Audit are given below:

Sl. No.	Internal Audit	Operational Audit
1.	Compliance objective	Risk identification, process improvement objective
2.	Financial accounts focus	Business focus
3.	Audit focus	Efficiency & improvement focus
4.	Transaction-based	Process-based
5.	Policies and procedures focus	Risk management focus
6.	Cost Centre wise budget monitoring	Accountability for performance improvement results
7.	Methodology : Focus on policies, transactions and compliance	Methodology : Focus on goals, strategies and risk management processes

6. (a) How should a Cost and Management Auditor evaluate MIS of an organization?

(b) What are the fields covered by CSR Audit? [10 + 6]

Answer:

6. (a) MIS is an essential managerial tool. It provides for identification of relevant information needs of managers at various levels, collection of data, processing the same to become usable to managers and timely dissemination of processed information to the users to help them to make effective decisions for planning, directing and controlling the respective operations.

A Cost and Management Auditor should take into consideration the following aspects while evaluating MIS of an organization:

i) Content, quality and source of information;
ii) Flow of information
iii) Correlation of information in decision areas.

These points are discussed in detail in the below:

i) Content, quality and source of information include the following:
   1) Whether the information collected is relevant to the decision problem so as to improve the quality of decisions?
   2) Whether the reporting of MIS is uniform and regular both for financial and nonfinancial information?
   3) Whether the information adequately caters to the needs of the decision makers?
   4) Whether unwanted data is included in the information?
   5) Whether the manager uses the data effective or merely as a post mortem exercise?

ii) Flow of information: A cost auditor has to proceed on the following lines:

   I) <u>System organization</u>:
      a) Whether the system is centralized or decentralized?
      b) How the information flows from various units to the control section?
      c) Estimating the volume of data involved, transmission time and cost.
      d) Benefit-cost analysis of centralized vs. decentralized information.

   II) <u>Data collection and management</u>: Appraisal includes the following points:
      a) Data collection methods,
      b) Filtration and classification of data.
      c) Matching of data with decision problems.
      d) Extent of study carried out by management with regard to existing frequency.
      e) Constraints if any in the system design.

III) Correlation of information in decision areas: The cost auditor is required to appraise this aspect from the following angles:
   a) Whether input- output analysis is attempted?
   b) Whether MIS helps in reducing uncertainty?
   c) Cost effectiveness of MIS.
   d) Effectiveness of information supplied to users.
   e) Provision of feedback by MIS for corrective action.
   f) Ability of MIS to optimize the value of information.

6. (b) A Corporate Social Responsibility Audit is an assessment of company's performance on corporate social responsibility objectives. It evaluates measurable goals intended to help the business meet the expectations stakeholder groups have regarding social and environmental responsibilities. Balancing social responsibility with business performance is imperative in today's business arena.

A Corporate Social Responsibility (CSR) Audit should cover the following points:

i) Human Rights: Fundamental Human Rights, Freedom of association and Collective bargaining, Non-discrimination, Forced labour, Child labour

ii) Business behaviour: Relations with clients, suppliers and sub-contractors, Prevention of corruption and anticompetitive practices

iii) Human Resources: Labour relations, Working conditions including steps taken for preventing accidents and health hazards, health and safety measures including compensation in case of any accidents, career development and training, Remuneration system that motivates the employees.

iv) Corporate Governance: Board of Directors, Audit and internal controls, Treatment of shareholders, Executive remuneration

v) Environment: Incorporation of environmental considerations into the manufacturing and distribution of products, and into their use and disposal, effect on pollution, pollution control measures undertaken,

vi) Community Involvement: Impacts on local communities, contribution to social and economic development.

vii) General interest causes, creation of socials infrastructure like roads, schools, hospitals.

7. (a) TNT Ltd. has received an enquiry for supply of 2,00,000 numbers of Special Type of Machine Parts. Capacity exists for manufacture of the machine parts, but a fixed investment of ₹ 80,000/- and working capital to the extent of 25% of Sales Value will be required to undertake the job.

The costs estimated as follows:
Raw Materials - 20,000 Kgs @ ₹ 2.50 per kg
Labour Hours- 9,000 of which 1,200 would be overtime hours payable at double the labour rate.
Labour Rate- ₹ 2 per hour.
Factory Overhead – ₹ 2 per direct labour hours.
Selling and Distribution Expenses – ₹ 23,000

Material recovered at the end of the operation will be ₹ 6,000 (estimated).
The Company expects a Net Return of 25% on Capital Employed.

You are Management Accountant of the Company. The Managing Director requests you to prepare a Cost and Price Statement indicating the price which should be quoted to the Customer.

(b) The financial profit and loss account for the year 2017-18 of a company shows a net profit of ₹ 29,60,000. During the course of Cost Audit, it was noticed that:

(i) The company was engaged in trading activity by purchasing goods at ₹ 6,00,000 and selling it for ₹ 7,50,000 after incurring repacking cost of ₹ 25,000,

(ii) Some discarded assets sold off with no scrap value for ₹ 90,000,

(iii) Some renovation of machinery was carried out at a cost of ₹ 6,00,000, having a productive life of five years, but entire amount was charged to financial accounts

(iv) Interest was received amounting to ₹ 1,40,000 from outside investments

(v) Voluntary Retirement payment of ₹ 3,50,000 was not included in the Cost Accounts,

(vi) Insurance claim of previous year was received to the extent of ₹ 2,50,000 but was not considered in the Cost Accounts.

(vii) Opening stock or raw materials and finished goods was overvalued by ₹ 2,40,000 and closing stock of finished goods was overvalued by ₹ 1,10,000 in the financial accounts, and

(viii) Donation of ₹ 80,000 towards CSR commitment was not considered in the Cost Accounts.

Work out the profit as per the Cost Accounts and briefly explain the adjustment, if any, carried out. [8 + 8]

Answer:

7. (a)

Statement of Estimated Cost and Price Quotation

Product: Special Type Machine Parts.	**Quantity = 2,00,000 units**	
	₹	₹
Materials (20000 Kgs. @ ₹ 2.50)	50,000	
Less: Estimated Scrap value	6,000	44,000
Labour-		
(9000 hrs. – 1200 OT hrs.) x ₹ 2 per hour	15,600	
1200 OT hrs. X ₹ 4 per hour	4,800	20,400
Prime Costs		**64,400**
Add: Factory overhead (9000 hrs. @ ₹ 2)		18,000
Factory Cost		**82,400**
Add: Selling and Distribution Expenses		23,000
Total Cost		**1,05,400**
Add: Profit		28,360
Sales		**1,33,760**

Selling Price / unit = ₹ 1,33,760/2,00,000 units = Re. 0.67

Working Notes:

Calculation of Sales
Let Sales be S
S = Total Cost + 25 % of Capital Employed.
S = 1,05,400 + 25/100 x (80,000+S/4)
S = 1,05,400 + 20,000 + S /16
S – s /16 = 1,25,400
15S = 1,25,400 x 16
15S = 20,06,400
S = 1,33,760
Sales = ₹ 1,33,760
Profit = Sales – Cost = 1,33,760 – 1,05,400 = ₹ 28,360

Working Capital = 1/4th of Sales = 1,33,760 x 1/4 = ₹ 33,440.

7. (b)

Profit Reconciliation as per Cost and Financial Records for the year 2017-18

Sl. No.	Particulars	₹ In '000	₹ In '000
1	**Profit as per Financial Accounts for Audited Products**		**29,60,000**
2	Less : Incomes not considered in the Cost Accounts		
	a) Trading Profit (7,50,000-6,00,000-25,000)	1,25,000	
	b) Profit on Sale of Old Assets	90,000	
	c) Interest received from Outside Investments	1,40,000	
	d) Insurance claim for previous year received	2,50,000	
	Total		(-) 6,05,000
3	Add : Expenses not considered in the Cost Accounts		
	a) Donation towards CSR Commitment	80,000	
	b) VRS Expenses	3,50,000	
	c) Renovation (4/5th Outlay of 600000)	4,80,000	
	Total		9,10,000
4	Add : Valuation of stocks (240000 - 110000) (Over valuation of opening stock and closing stock in financial accounts)		1,30,000
5	Other adjustments ---		-
	Profit as per the Cost Accounts		**33,95,000**

8. Answer any four. 4x4=16

(a) What are the duties of the companies in relation to provisions of section 148 of the Companies Act 2013 and Rules framed thereunder?
(b) Write a short note on Marketing Audit and its areas.
(c) Discuss about the mandatory review area of the Audit Committee.
(d) How do you define 'Packing Material' as per the Generally Accepted Cost Accounting Principle? What is the treatment of such cost?
(e) What is the role of C&AG in the Audit of Government Company?

Answer:

8. (a) Every company required to get cost audit conducted under section 148 (2) of the Companies Act, 2013 shall:-

(i) Appoint a cost auditor within one hundred and eighty days of the commencement of every financial year,
(ii) Inform the cost auditor concerned of his or its appointment,
(iii) File a notice of such appointment with the Central Government within a period of thirty days of the Board meeting in which such appointment is made or within a period of one hundred and eighty days of the commencement of the financial year, whichever is earlier, through electronic mode, in form CRA-2, along with the fee as specified in Companies (Registration Offices and Fees) Rules, 2014,
(iv) Within a period of thirty days from the date of receipt of a copy of the Cost Audit Report, furnish the Central Govt. with such report along with full information and explanation on every reservation or qualification contained therein, in form CRA-4 along with fees specified in Companies (Registration Offices and Fees) Rules, 2014.

8. (b) Marketing audit is an independent examination of the entire marketing effort of a company, or some specific marketing activities covering objectives, programme

implementation, and organisation for purposes of determining what is being done, appraising which is being done, and recommending what should be done in future.
The essential feature of marketing audit is that marketing audit is carried out periodically at regular intervals and not only when the company is facing marketing problems and difficulties. Such audit covers both marketing place and control and evaluate the basic framework for marketing action as also the performance within the framework. It covers the appraisal of the entire system and process of marketing taking into account all the elements of the marketing operations.

Marketing Audit may be horizontal or vertical. Horizontal Audit covers a major part of the Marketing Audit and evaluates the total appraisal of the marketing efforts of a company. Vertical Audit concentrates on single item of function of marketing operation of a company identified by horizontal audit or otherwise and which becomes the subject of thorough examination and evaluation.

The Marketing Audit covers the following areas:
(i) Objectives: Marketing objectives should be clearly established. Major of the companies do not have clearly defined objective except achieving high sales volume or making high profit on the sales. The search in audit of a clear objective will make the management aware of the gap between the operational policies.
(ii) Programme: The auditor should carry out an appraisal for the programme which the company laid down for achieving the objective.
(iii) Implementation: The auditor should take up the examination of the company's implementation of the marketing programme.
(iv) Organization: A suitable organization assist in a success of a marketing plan. The audit should appraisal the marketing organization by reviewing the formal lines of authority and responsibility, delegation of authority, status of marketing head and his staff, adequacy of the personnel, proper manning of key tasks and assignment etc.

8. (c) The Audit Committee shall mandatorily review the following information as per Clause 49 of the Listing Agreement:
(i) Management discussion and analysis of financial condition and results of operations
(ii) Statement of significant related party transactions (as defined by the audit committee), submitted by management
(iii) Management letters/ letters of internal control weaknesses issued by the statutory auditors
(iv) Internal audit reports relating to internal control weaknesses; and
(v) The appointment, removal and terms of remuneration of the Chief Internal Auditor shall be subject to review by the Audit Committee.

8. (d) The Cost Accounting Standard on Packing Material Cost (CAS 9) defines Packing Materials as materials used to hold, identify, describe, store, protect, display, transport, promote and make the product marketable.

Packing Materials for the purpose of the standard are classified into primary and secondary packing materials. Primary Packing Material is that packing material which is essential to hold and preserve the product for its use by the customer. Secondary Packing Material is that packing material that enables to store, transport, inform the customer, promote and otherwise make the product marketable. For example, in pharmaceutical industry, cartons used for holding strips of tablets and card board boxes used for holding cartons.

Packing material costs shall be directly traced to a cost object to the extent it is economically feasible. Where the packing material costs are not directly traceable to the cost object, these may be assigned on the basis of quantity consumed or similar measures like technical estimates. The packing material cost of reusable packing shall be assigned to the cost object taking into account the number of times or the period over which it is expected to be reused. Cost of primary packing materials shall form part of the cost of production. Cost of secondary packing materials shall form part of distribution overheads.

8. (e) Role of C&AG in the Audit of a Government company:

The auditor of a Government company is appointed by the C&AG.

The C&AG have powers under section 143 of the Companies Act, 2013 as follows:

(i) to direct the manner in which the company's accounts shall be audited by the auditor and to give such auditor instructions in regard to any matter relating to the performance of his functions as such;

(ii) to conduct a supplementary or test audit of the company's accounts by such person or persons as he may authorise in this behalf; and for the purposes of such audit, to require information or additional information to be furnished to person or persons so authorised, on such matters, by such person or persons, and in such form, as the Comptroller and Auditor-General may, by general or special order direct.

In addition, the C&AG has a right to comment upon or supplement the audit report in such manner as he thinks fit.