

**PAPER – 19: COST AND MANAGEMENT AUDIT**

## PTP\_Final\_Syllabus 2012\_Dec2015\_Set 3

The following table lists the learning objectives and the verbs that appear in the syllabus learning aims and examination questions:

|                | <b>Learning objectives</b>   | <b>Verbs used</b>         | <b>Definition</b>   |
|----------------|--|---------------------------|---|
| <b>LEVEL C</b> | KNOWLEDGE<br><br>What you are expected to know   | List                      | Make a list of  |
|                |  | State                     | Express, fully or clearly, the details/facts                |
|                |  | Define                    | Give the exact meaning of                                   |
|                | COMPREHENSION<br><br>What you are expected to understand   | Describe                  | Communicate the key features of                             |
|                |  | Distinguish               | Highlight the differences between                           |
|                |  | Explain                   | Make clear or intelligible/ state the meaning or purpose of |
|                |  | Identify                  | Recognize, establish or select after consideration          |
|                | APPLICATION<br><br>How you are expected to apply your knowledge  | Illustrate                | Use an example to describe or explain something             |
|                |  | Apply                     | Put to practical use  |
|                |  | Calculate                 | Ascertain or reckon mathematically                          |
|                |  | Demonstrate               | Prove with certainty or exhibit by practical means          |
|                |  | Prepare                   | Make or get ready for use                                   |
|                |  | Reconcile                 | Make or prove consistent/ compatible                        |
|                | ANALYSIS<br><br>How you are expected to analyse the detail of what you have learned  | Solve                     | Find an answer to   |
|                |  | Tabulate                  | Arrange in a table  |
|                |  | Analyse                   | Examine in detail the structure of                          |
|                |  | Categorise                | Place into a defined class or division                      |
|                |  | Compare and contrast      | Show the similarities and/or differences between            |
|                |  | Construct                 | Build up or compile   |
|                | SYNTHESIS<br><br>How you are expected to utilize the information gathered to reach an optimum conclusion by a process of reasoning | Prioritise                | Place in order of priority or sequence for action           |
|                |  | Produce                   | Create or bring into existence                              |
|                |  | Discuss                   | Examine in detail by argument                               |
|                | EVALUATION<br><br>How you are expected to use your learning to evaluate, make decisions or recommendations                         | Interpret                 | Translate into intelligible or familiar terms               |
| Decide         |  | To solve or conclude      |   |
| Advise         |  | Counsel, inform or notify |   |
|                |  | Evaluate                  | Appraise or assess the value of                             |
|                |  | Recommend                 | Propose a course of action                                  |

**Paper 19 - COST AND MANAGEMENT AUDIT**

**Time allowed-3hrs**

**Full Marks: 100**

**Working Notes should form part of the answer.**

**—Wherever necessary, suitable assumptions should be made and indicated in answer by the candidates.**

**1. Answer any four Question [15×4=60]**

**(a) (i)** A company is engaged in construction of residential housing, offices, industrial units, Roads, Bridges, Marine facilities etc. having sites in India and abroad. The company also has Joint venture projects in India and abroad. Whether Companies (Cost Records and Audit) Rules 2014 would be applicable to the company? **[5]**

**(ii)** A company has units in SEZ and in non-SEZ areas. The Companies (Cost Records and Audit) Rules 2014 has exempted companies operating in special economic zones from cost audit. What would be applicability of the Companies (Cost Records and Audit) Rules 2014 on such a company in respect of maintenance of cost accounting records and cost audit? **[5]**

**(iii)** In the abridged cost statement, what are Industry specific operating expenses? When should this be used? **[3]**

**(iv)** Whether each and every transaction with Related Parties is to be disclosed under Para D-5 of Annexure to the Cost Audit Report? **[2]**

**(b)(i)** What is the procedure to be followed for fixing the remuneration of a cost auditor? **[5]**

**(ii)** Is there any obligation on the part of cost auditor to report offence of fraud being or has been committed in the Company by its officers or employees? **[3]**

**(iii)** The particulars relating to the import of Sealing Ring made by AB & Co. during December, 2014 are given below:

(a) Sealing Ring - 1,000 pieces invoiced £ 2.00 C.I.F. Mumbai Port.

(b) Customs duty was paid @ 100% on invoice Value (which has converted to Indian currency by adopting an exchange rate of ₹ 17.20 per £)

(c) Clearing charges - ₹1,800 for the entire consignment, and'

(d) Freight charges - ₹1,400 for transporting the consignment from Mumbai Port to factory premises.

It was found on inspection that 100 pieces of the above material were broken and, therefore, rejected.

There is no scrap value for the rejected part. No refund for the broken material would be admissible as per the terms of contract. The management decided to treat 60 pieces as normal loss and the rest 40 pieces as abnormal loss. The entire quantity of 900 pieces was issued to production.

Calculate

I. Total cost of material, and

II. Unit cost of material issued to production.

Also state briefly how the value of 100 pieces rejected in inspection will be treated in costs. **[4]**

**(iv)** State the reasons of over-absorption and under-absorption of overheads and list the methods of their absorption. **[3]**

**(c)(i)** The Companies (Cost Records and Audit) Rules, 2014 requires submission of a single cost audit report at company level. What is the procedure of certifying and submission of cost audit report of a company where more than one cost auditor is appointed? **[5]**

**(ii)** What is installed capacity and how is this different from total available capacity? How the installed capacity is to be calculated in a multi-product company using the same machine/facilities? Should installed capacity be the capacity at the beginning of the year or at the end of the year under audit? **[5]**

**(iii)** Is CRA-3 applicable for companies whose financial year commenced prior to April 1, 2014? Which Rules are applicable to companies whose financial year commenced on January 1, 2014? **[3]**

**(iv)** The Companies (Cost Records and Audit) Rules, 2014 covers "Generation, transmission, distribution and supply of electricity" with no corresponding CETA Heading. Whether the Quantitative Information and Abridged Cost Statement in respect of Electricity are required to be reported under the Service Sector in the absence of a CETA Heading? **[2]**

**(d)(i)** What are the principles of measuring 'overheads' as per CAS 3? **[5]**

**(ii)** How would you assign administrative overheads as per CAS 11? **[3]**

**(iii)** How are 'inward' and 'outward' transportation cost treated as per CAS 5? **[3]**

**(iv)** How would you determine the cost of material consumed in production for captive consumption as per CAS 4? **[4]**

**(e)(i)** What are the factors need to be considered by the auditor of the company while formulating the audit strategy? **[7]**

**(ii)** State the factors on which content and form of audit documentation will depend? **[3]**

**(iii)** As a cost auditor of the company, what are the areas required to be check with regards to IT environment and controls? **[5]**

## **(2) Answer any two questions [10×2=20]**

**(a)** As an operational auditor of the company, how would you evaluate the performance of a company? **[10]**

**(b)** As an auditor of a company, how would you verify the Inventory of the company? **[10]**

**(c) (i)** Needs of Plantation Industry for a strong Internal Control System and consequent importance of integrated and well-organised Internal Audit System in Plantation Industry. Explain. **[5]**

**(ii)** Explain the different types of Operational Auditors. **[5]**

## **(3) Answer any two questions [10×2=20]**

**(a) (i)** The management of Up and Down Ltd. is worried about their increasing labour turnover in the factory and before analyzing the causes and taking remedial steps, they want to have an idea of the profit foregone as a result of labour turnover in the last year.

Last year sales amounted to ₹83,03,300 and the P/V Ratio was 20%. The total number of actual hours worked by the direct labour force was 4.45 lakhs. As a result of the delays by the

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personnel department in filling vacancies due to labour turnover, 1,00,000 potentially productive hours were lost. The actual direct labour hours included 30,000 hours attributable to training new recruits, out of which half of the hours were unproductive.

An analysis of costs incurred consequent on labour turnover revealed the following:

|                                |         |
|--------------------------------|---------|
| Settlement cost due to leaving | ₹43,820 |
| Recruitment Costs              | ₹26,740 |
| Selection Costs                | ₹12,750 |
| Training Costs                 | ₹30,490 |

Assuming that the potential lost as a consequence of labour turnover could have been sold at prevailing prices. Find out the profit foregone last year on account of labour turnover. **[6]**

**(ii)** From the following figures decide whether it is worthwhile to investigate the variance:

|  | ₹      |
|--|--------|
| 1. Cost of investigation of variance                     | 6,400  |
| 2. Cost of correction of out-of-control process          | 20,000 |
| 3. Cost of allowing the process to remain out of control | 95,000 |
| 4. Probability of being in control                       | 0.90   |

**[4]**

**(b)** Tarun Textiles Ltd. has been having low profits. A special task force appointed for reviewing performance and prospects has the following to report:

The company has 1,200 looms working 2 shifts per day. There are 25 sections of 48 looms each. Each section has 24 weavers and a jobber. Thus there are 1,250 direct labourers, other than indirect labourers and service hands. The working time is between 7 a.m. and 12 mid-night, comprising 2 shifts of 8 hours each, with half hour interval between shifts. The production is 18 lakh metres per month and the realization is ₹3 per metre. The average wage of the direct labourer is ₹800 per month and the fixed costs amount to ₹1,75,000 per month. The product cost is ₹2.25 per metre in addition to direct wages.

The following suggestions are to be considered:

- (i) Labour productivity can be improved by changing the layout of the machines.
- (ii) Given the space available, with the proposed change in layout, only 1,008 looms can be re-installed, with 48 looms in each section.
- (iii) Technically, a section of 48 looms can be run with 12 weavers, a helper and a jobber. It will be necessary to increase the age of direct labour, for such sections, by ₹110 per head per month. There will be some drop in production per loom. The company is not for retrenchment of labour.
- (iv) The company can run a third shift between 12 mid-night and 7 a.m., with a half hour interval. However, for the six and half hours' work, eight hours' wage will have to be paid.

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(v) Only 18 lakh metres can be sold at the present price of ₹3 per metre. There is an export offer for ₹4.5 lakh metres at ₹2.70 per metre.

(vi) As an initial step, the company can switch to 3 shift working, with 12 sections having 25 direct labourers each and 9 sections having 14 direct labourers each. Progressive conversion to 14 hands per section, for all sections, can be planned, as direct labourers retire or voluntarily leave the job. The production with three shift working will be 22.5 lakh metres. Additions to fixed costs will amount to ₹50,000 per month.

Examine the implications of the proposals for the company's profits and give your advice.

**[10]**

**(c)(i)** X Ltd presented the following particulars on 31.3.2015.

You are asked to compute the Inventory Turnover Ratio of each material:

|                         | Material X | Material Y |
|-------------------------|------------|------------|
|                         | ₹          | ₹          |
| Stock (as on 1.4.2014)  | 12,000     | 16,000     |
| Purchases               | 60,000     | 1,00,000   |
| Stock (as on 31.3.2015) | 18,000     | 24,000     |

**[5]**

**(ii)** Manufacture's specification capacity for a machine per hour = 1500 units

No. of shifts (each shift of 8 hours each) = 3 shifts

Paid holidays in a year (365 days):

Sundays                      52 days

Other holidays                8

Annual maintenance is done during the 8 other holidays.

Preventive weekly maintenance is carried on during Sundays.

Normal idle capacity due to lunch time, shift change etc =1 hour.

Production during last five years = 76.20, 88, 65.82, 78.5, 76.6 lakhs units

Actual production during the year = 76.40 lakhs units.

Calculate Installed capacity, Available capacity, Actual capacity, Idle capacity and Abnormal idle capacity as per CAS 2 from the data given.

**[5]**