Intermediate
Group II
Paper 12 : COMPANY ACCOUNTS & AUDIT
(SYLLABUS – 2016)

Section A – Accounts of Joint Stock Companies

Objectives

1. (a) Choose the correct answer from the given four alternatives:

(i) X Ltd. holds 51% of Y Ltd., Y Ltd. holds 51% of W Ltd., Z Ltd. holds 49% of W. Ltd. As per AS 18, Related Parties are :
(A) **X Ltd., Y Ltd. & W Ltd.**
(B) X Ltd. & Z Ltd.
(C) Y Ltd. & Z Ltd.
(D) X Ltd. & Y Ltd. only

(ii) The fair value of Plan assets of A LTD. at beginning and end of the year 2015-2016 were ₹ 4,00,000 and ₹ 5,70,000 respectively. The employer' s contribution to the plan during the year was ₹ 1,40,000. If benefit payments to retirees were ₹ 1,00,000 what would be the actual return on plan assets (as per AS15) ?
(A) ₹ 1,50,000 lakhs
(B) **₹ 1,30,000 lakhs**
(C) ₹ 1,20,000 lakhs
(D) Insufficient Information

(iii) General Ledger of a Banking Company does not contain ________________
(A) Control Accounts of all personal ledgers
(B) Assets' Accounts
(C) Contra Accounts
(D) **Balance Sheet**

(iv) The Electricity Act,2003 replaced which of the following three existing legislations?
(A) The Indian Electricity Act, 1910
(B) The Electricity (Supply) Act, 1948
(C) The Electricity Regulatory Commissions Act, 1998
(D) **All of the above**

(v) Losses of theft are covered by ____________ insurance policis
(A) **Burglary**
(B) Fire
(C) Marine
(D) None of the above

(vi) Cash receipts from disposal of fixed assets is a cash flow from _________ activity
(A) Operating

(B) **Investing**
(C) Financing
(D) None of the above

(vii) Which of the following is not a component of Cash Flow Statement
(A) Cash payments to suppliers for goods and services
(B) **Charging of Depreciation**
(C) Cash advances and loans made to third parties
(D) Cash repayments of amounts borrowed

(viii) "Cost of Materials Consumed" will come in
(A) Profit and Loss Account
(B) Balance Sheet
(C) Bothe (A) & (B)
(D) None of the above

(ix) 10% Debenture will come under _____________ of Balance Sheet (Shedule III)
(A) Long term Borrowing
(B) Current Liabilities
(C) Non Current Assets
(D) Other current Labilitirs

(x) Which of the following is/are statutory book/s of a company
(A) Register of Charges
(B) Register of Members
(C) Register of Debenture holders
(D) All of the above

(xi) For which of the following Share Premium Account may be applied?
(A) issue of fully paid bonus shares to the members of the company;
(B) writing off preliminary expenses of the company;
(C) writing off the expenses of the commission paid or discount allowed on any issue of shares or debentures of the company
(D) **All of the above**

(xii) Which of the following is not a source of Bonus issue of Shares
(A) Free Reserves
(B) Securities Premium Account
(C) Capital Redemption Reserve Account
(D) **Asset Revaluation Reserves**

(xiii) The term current asset doesn't cover
(A) **Car**
(B) Debtors
(C) Stock
(D) Prepaid expenses

(xiv) Premium on redemption of redeemable preference shares can be paid out of?
(A) Capital Redemption Reserve account
(B) **Existing shares premium account**
(C) Proceed of fresh issue of shares
(D) All of the above

(xv) When shares are allotted, they will be credited to which account?
(A) **Share Capital Account**
(B) Share Allotment Account
(C) Share Application Account
(D) Share First and Final Call Account

(b) Match the following:

	Column 'A'		Column 'B'
1.	**AS 16**	**A.**	**Export Credit Guarantee Corporation**
2.	**Underwriting**	**B.**	**Benefits provided in exchange for the termination of employment**
3.	**Banking Service**	**C.**	**Segment Revenue minus segment expenses**
4.	**Central Electricity Regulatory Commission**	**D.**	**Borrowing Cost**
5.	**Termination benefits**	**E.**	**Two types**
6.	**Segment Result**	**F.**	**Automated Teller Machines (ATM)**
7.	**Government grants**	**G.**	**Body Corporate**
8.	**ECGC**	**H.**	**Is void**
9.	**Issue of Shares at a Discount**	**I.**	**Are available for distribution**
10.	**Free Reserves**	**J.**	**Assistance by government in return for compliance with conditions**

Answer:

	Column 'A'		Column 'B'
1.	AS 16	**D.**	Borrowing Cost
2.	Underwriting	**E.**	Two types
3.	Banking Service	**F.**	Automated Teller Machines (ATM)
4.	Central Electricity Regulatory Commission	**G.**	Body Corporate
5.	Termination benefits	**B.**	Benefits provided in exchange for the termination of employment
6.	Segment Result	**C.**	Segment Revenue minus segment expenses
7.	Government Grants	**J.**	Assistance by government in return for compliance with conditions
8.	ECGC	**A.**	Export Credit Guarantee Corporation
9.	Issue of Shares at a Discount	**H.**	Is void
10.	Free Reserves	**I.**	Are available for distribution

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

(i) **A company can issue bonus shares even if its Articles does not authorise to do so.**
(ii) **In case of Forfeiture of Shares a shareholder is not able to pay the further calls and returns his shares to the company for cancellation voluntarily.**

(iii) Any surplus cash may be utilized by the company for buy-back and avoid the payment of dividend tax.
(iv) Transfer to capital redemption reserve account is allowed from Dividend Equalisation fund.
(v) When debentures are issued at discount, it is prudent to write off the loss during the life of debentures.
(vi) In order to spread the risk of under-subscription , the principal underwriters may enter into subsidiary agreements with sub-leasees.
(vii) Marked applications are those applications which bear the stamp of an underwriter.
(viii) Interest expenses are Finance Cost.
(ix) Qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.
(x) An issuance of stock following a company's Initial Public Offer is called a Follow on Public Offer.

Answer:

(i) False
(ii) False
(iii) True
(iv) True
(v) True
(vi) False
(vii) True
(viii) True
(ix) True
(x) True

Study Note 1 – Accounting of Shares and Debentures

2. (a) Following items appear in the Trial Balance of Miral Ltd. as on 31st March,2016:

Particulars	₹
4,500 Equity Shares of ₹100 each	**4,50,000**
Capital Redemption Reserve	**50,000**
Plant Revaluation Reserve	**20,000**
Securities Premium	**35,000**
General Reserve	**1,00,000**
Profit and Loss A/c (Cr. Balance)	**50,000**
Capital Reserve (including ₹35,000 being Profit on Sale of Machinery)	**75,000**

The company decided to issue to equity shareholders bonus shares at the rate of 1 share for every 3 shares held. Company decided that there should be the minimum reduction in free reserves. Pass necessary Journal Entries in the books of Miral Ltd.

Answer:

Particulars		L.F.	Dr. Amount	Cr. Amount
Capital Reserve A/c	Dr.		35,000	
Capital Redemption Reserve A/c	Dr.		50,000	
Securities premium A/c	Dr.		35,000	

General Reserve A/c Dr. To, Bonus to share holders A/c (Being Bonus issue of 1 share for every 3 shares held, by utilizing various reserves)		30,000	 1,50,000
Bonus to Shareholders A/c Dr. To, Equity Shares Capital A/c (Being, Capitalisation of Profit)		1,50,000	 1,50,000

(b) Write a note on issue of Sweat Equity Shares.

Answer:

Issue of Sweat Equity Shares [Section 54] notwithstanding anything contained in section 53, a company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled —

(a) the issue is authorised by a special resolution passed by the company;
(b) the resolution specifies the number of shares, the current market price, consideration, if any, and the class or classes of directors or employees to whom such equity shares are to be issued;
(c) not less than one year has, at the date of such issue, elapsed since the date on which the company had commenced business; and
(d) where the equity shares of the company are listed on a recognised stock exchange, the sweat equity shares are issued in accordance with the regulations made by the Securities and Exchange Board in this behalf and if they are not so listed, the sweat equity shares are issued in accordance with such rules as may be prescribed.

The rights, limitations, restrictions and provisions as are for the time being applicable to equity shares shall be applicable to the sweat equity shares issued under this section and the holders of such shares shall rank pari passu with other equity shareholders.

3. (a) Pipli Ltd. furnishes the following summarized Balance Sheet as at 31st March,2016

Particulars	₹'000
Authorised Issued and Subscribed 3,00,000, Equity Shares of ₹10 each	**3,000**
25,000, 9% Preference Shares of ₹100 each fully paid up issued two months back for buy back purposes)	**2,000**
Capital Reserve	**20**
Revenue Reserve	**4,000**
Securities Premium	**500**
Profit & Loss A/c	**1,800**
10% Convertible Debentures	**400**
Current Liabilities	**40**
Fixed Assets (at cost less depreciation)	**2,760**
Non-current Investments	**5,000**
Current Assets	**4,000**

(i) The Company passed a resolution to buy back 20% of its equity capital @ ₹15 per share. For this purpose, it sold its investments of ₹30 lakhs for ₹25 lakhs.

(ii) The company redeemed the preference shares at a premium of 10% on 1sth April,2016.

(iii) Included in its investments were 'investments in own debentures' costing ₹3 lakhs (face value ₹3.30 lakhs). These debentures were cancelled on 1st April,2016.

You are required to pass necessary Journal entries and prepare the Balance Sheet on 01.04.2016.

Answer:

Journal

Date	Particulars	L.F.	Dr. Amount ₹'000	Cr. Amount ₹'000
	Bank A/c Dr. Profit and Loss A/c Dr. To, Investments A/c (Beingthe investment sold for Buy-back)		2,500 500	 3,000
	9% Redeemable Preference Share Capital A/c Dr. Premium on redemption of Preference Share A/c Dr. To, Preference Shareholders A/c (Being the amount due to Preference Shareholders)		2,000 200	 2,200
	Preference Shareholders A/c Dr. To, Bank A/c (Being the payment made to Preference Shareholders)		2,200	 2,200
	Revenue Reserve A/c Dr. To Capital Redemption Reserve A/c (being the creation of Capital Redemption Reserve to the extent of the face value of Preference Shares redeemed & equity shares bought bask as per the law)		2,000	 2,000
	Equity Share Capital A/c Dr. Securities Premium A/c Dr. To, Equity Shares Buy-back A/c (Being cancellation of shares bought back)		600 300	 900
	Equity Shares Buy-Back A/c Dr. To, Bank A/c (Being the payment made for shares bought back)		900	 900
	10% Debentures A/c Dr. To, Investments (Own debentures) A/c To, Capital Reserve A/c (Being cancellation of own debentures and transfer of Profit on cancellation of Debentures)		330	 330
	Securities Premium A/c Dr. To,Premium on Redemption of Preference Shares A/c (Being premium on redemption of preference shares adjusted through securities premium)		200	 200

Balance Sheet of Pipli Ltd. as at 01.04.2016

Particulars	Note No.	Amount ₹
I. Equity and Liabilities		
(1) Shareholders' Finds		
(a) Share Capital	1	2,400
(b) Reserves and Surplus	2	5,350

(2) Non-Current Liabilities [10% Debentures](400-330)		70
(3) Current Liabilities		40
Total		**7,860**
II. Assets		
(1) Non-current Assets		
(a) Fixed Assets		2,760
(b) Non-current Investments [5,000 – 3,000 – 300]		1,700
(2) Current Assets [4,000 + 2,500 – 2,200 – 900]		3,400
Total		**7,860**

Particulars	**Amount ₹**
1. Share Capital	
Authorised Capital	
2,40,000 Equity Shares of ₹10 each	2,400
Issued & Subscribed Capital	
2,40,000 Equity Shares of ₹10 each (60,000 Equity Shares bought back)	2,400
2. Reserves and Surplus	
Revenue Reserve [4,000 – 2,000]	2,000
Capital Reserve [20+30]	50
Capital Redemption Reserves	2,000
Securities Premium [500-200-300]	0
Surplus (P&L A/c)[1,800 – 500]	1,300
	5,350

(b) PQR Ltd. has an authorised capital of ₹300 crores divided into equity shares of ₹10 each and its Balance Sheet as at March 31, 2016 was as follows:

Particulars	**Amount ₹**
Share Capital Issued and fully paid-up	**200**
General Reserve	**20**
8% Debentures	**40**
Sundry Creditors	**20**
Fixed Assets	**120**
Current Assets	**30**
Own Debentures (nominal value ₹10 lakhs)	**9**
Cash at Bank	**21**

The Company decided:

1. **To redeem the 8% debentures due for redemption on September 30, 2016 and also to cancel its Own Debentures. [Due Date of Interest: 30th Sept. & 31st Mar.]**
2. **To pay interest to debenture holders being due on the date of redemption.**

Required: Record necessary entries to give effect to the above transactions.

Answer:

Date	**Particulars**		**L.F.**	**Dr. ₹**	**Cr. ₹**
30.09.2016	Interest on Debentures A/c	Dr.		1.60	

	To Debentureholders A/c [30×8%×6/12] To Interest on Own Debentures A/c [10×8%×6/12] (Being the interest due on debenture outstanding including own debentureholders as investments)			1.20 0.40
	Debentureholders' A/c Dr. To Bank A/c (Being the payment of interest to debentureholders)		1.20	 1.20
	General Reserve A/c Dr. To Debenture Redemption Reserve A/c (Being the transfer of General Reserve to DRR to have 50% of the debenture issue)		20	20
30.09.2016	8% Debentures A/c [40 – 10] Dr. To Debentureholders' A/c (Being the amount due on redemption)		30	 30
	Debentureholders' A/c Dr. To Bank A/c (being the payment made to debentureholders)		30	 30
	8% Debentures A/c Dr. To Own Debentures A/c To Gain on cancellation of Debentures A/c (Being the cancellation of own debentures)		10	 10
	Gain on Cancellation of Debentures A/c [10-9] Dr. To Capital Reserve A/c (being the Gain on cancellation of debentures transferred to capital reserve)		1	 1
31.03.2017	Interest on Own Debentures A/c Dr. To Profit and Loss A/c (Being the transfer of interest on own debentures to Profit and Loss A/c)		0.4	 0.4
31.03.2017	Profit and Loss A/c Dr. To Interest on Debentures A/c (Being the transfer of debenture interest to Profit and Loss A/c)		1.60	 1.60

4. (a) LR Ltd. had issued 1,00,000 Equity Shares of ₹50 each at par, the amount payable as ₹25 on Application, ₹10 on Allotment, ₹10 on First Call and ₹ 5 on Second Call. Applications were received for all the Shares. The Company had made the allotment to all applicants and calls made on the due dates. The Company received all amounts except the following -

- **First Call - On 2,400 Shares,**
- **Second Call - On 4,000 Shares (including the 2,400 Shares on which First Call was not received)**

The Company forfeited the above Shares after passing a resolution for the same. All the Forfeited Shares were reissued at ₹12 per Share. You are required to pass Journal Entries in the Company's books, for the above.

Answer:

Journal Entries in the books of LR Ltd.

S.No.	Particulars	Dr.(₹)	Cr.(₹)
1.	Bank A/c (1,00,000 x ₹ 25) Dr. To Equity Share Application A/c (Being application moneys received from applicants of 1,00,000 Shares at ₹25)	25,00,000	 25,00,000
2.	Equity Share Application A/c (1,00,000 x ₹ 25) Dr. Equity Share Allotment A/c (1,00,000 x ₹ 10) Dr. To Equity Share Capital A/c (Being allotment of 1,00,000 Shares and transfer of application moneys, recording allotment moneys due at ₹ 10 per share)	25,00,000 10,00,000	 35,00,000
3.	Bank A/c Dr. To Equity Share Allotment A/c (Being amounts received towards allotment from all allottees)	10,00,000	 10,00,000
4.	Equity Share First Call A/c (1,00,000 x ₹ 10) Dr. To Equity Share Capital A/c (Being Call Money on 1,00,000 Shares due at ₹10 per share)	10,00,000	 10,00,000
5.	Bank A/c Dr. To Equity Share First Call A/c (Being amount received on first call of ₹10 on 1,00,000 Shares except allottees for 2,400 Shares i.e. 97,600 Shares at ₹10)	9,76,000	 9,76,000
6.	Equity Share Second & Final Call A/c (1,00,000 x ₹ 5) Dr. To Equity Share Capital A/c (Being Final Call Money on 1,00,000 Shares due at ₹ 5 per share)	5,00,000	 5,00,000
7.	Bank A/c Dr. To Equity Share Second and Final Call A/c (Being amount received on Final Call of ₹ 5 on 1,00,000 Shares except allottees for 4,000 Shares i.e. 96,000 Shares at ₹ 5)	4,80,000	 4,80,000
8.	Equity Share Capital (4,000 x ₹ 50) Dr. To Equity Share First Call A/c (2,400 Shares x ₹ 10) To Equity Share Second and Final A/c (4,000 Shares x ₹ 5) To Shares Forfeited A/c [(2,400 x ₹ 35) + (1,600 x ₹ 45)] (Being forfeiture of 4,000 Shares on which 2,400 Shares both calls due and 1,600 Shares final call due, as per Resolution No dated)	2,00,000	 24,000 20,000 1,56,000
9.	Bank A/c (4,000 Shares x ₹12) Dr. Shares Forfeited A/c (4,000 Shares x (50-12) Dr. To Equity Share Capital (4,000 Shares x ₹50) (Being re-issue of 4,000 Forfeited Shares at ₹12 per Share)	48,000 1,52,000	 2,00,000
10.	Shares Forfeited A/c (1,56,000 – 1,52,000) Dr. To Capital Reserve A/c (Being Profit on Forfeiture of Equity Shares transferred to Capital Reserve)	4,000	 4,000

(b) Summer & Cool Ltd. planned to set up a unit for manufacture of bulk drugs. For the purpose of financing the unit, the Board of Directors have issued 10,00,000 Equity Shares of ₹10 each. 25% of the issue was reserved for Promoters and the balance was offered to the public. A Ltd., B Ltd. and C Ltd. have come forward to underwrite the public issue in the ratio of 3:2:1 and also

agreed for Firm Underwriting of 25,000, 17,500, 7,500 Shares respectively. The Underwriting Commission was fixed at 5%. The amount payable on application was ₹ 2.50 per share. The details of subscriptions are:

Particulars	Marked Forms of A	Marked Forms of B	Marked Forms of C
No. of Shares	3,25,000	1,50,000	1,00,000

Unmarked Forms were received for 60,000 Shares. From the above, you are required to show the allocation of liability among underwriters with workings. Also, pass Journal Entries in the books of the Company for

a. Underwriters' net liability and the receipt or payment of cash to or from Underwriters.

b. Determining the liability towards the payment of commission to the Underwriters.

Answer:

Computation of liability of underwriters (No. of shares):

Particulars	A	B	C	Total
Gross Liability (3:2:1)	3,75,000	2,50,000	1,25,000	7,50,000
Less: Firm underwriting	25,000	17,500	7,500	50,000
	3,50,000	2,32,500	1,17,500	7,00,000
Less: Marked application	3,25,000	1,50,000	1,00,000	5,75,000
	25,000	82,500	17,500	1,25,000
Less: Unmarked applications distributed to A, B and C in 3:2:1 ratio	30,000	20,000	10,000	60,000
	(5,000)	62,500	7,500	65,000
Less: Surplus of A distributed to B & C in 2:1 ratio	5,000	3,333	1,667	
Net Liability (excluding firm underwriting)	Nil	59,167	5,833	65,000
Add: Firm underwriting	25,000	17,500	7,500	50,000
Total Liability (No. of Shares)	25,000	76,667	13,333	1,15,000

(a) Computation of amounts receivable from / payable to underwriters:

Particulars	P	Q	R	Total
a. Total Liability (incl. Firm underwriting) (share)	25,000	76,667	13,333	1,15,000
b. Amount due at 2.50 per share (a x 2.50)	62,500	1,91,667	33,333	2,87,500
c. Amount paid for firm Underwriting at 2.50 per share	62,500	43,750	18,750	1,25,000
d. Balance due from Underwriters (b-c)	Nil	1,47,917	14,583	1,62,500
e. Underwriting commission payable by company	3,75,000 x 10 x 5% =1,87,500	2,50,000 x 10 x 5% =1,25,000	1,25,000 x 10 x 5% =62,500	3,75,000
f. Amount due to / (payable by) co. (d-e)	(1,87,500)	22,917	(47,917)	(2,12,500)

(b) In the Books of Summer & Cool Ltd.

Journal Entries

Particulars		Dr. (₹)	Cr.(₹)
Bank A/c	Dr.	1,25,000	
To Equity Share Capital A/c			
A Ltd – 25,000 x 2.5			62,500
B Ltd – 17,500 x 2.5			43,750
C Ltd – 7,500 x 2.5			18,750

(Being allotment of shares against amounts received towards subscription for Firm Underwriting at 25,000 ; 17,500 and 7,500 shares respectively from A, B, C at ₹2.50)		
B A/c (59,1667 x 2.50) Dr. C A/c (5,833 X 2.50) Dr. To Equity Share Capital A/c (Being allotment of share to underwriters. Application and allotment money credited to Equity Share Capital A/c)	1,47,917 14,583	 1,62,500
Underwriting Commission A/c Dr. To A A/c To B A/c To C A/c (Being the underwriting Commission payable to A,B and C at 5% of the normal value of the share underwritten)	3,75,000	 1,87,500 1,25,000 62,500
A A/c Dr. C A/c Dr. To Bank A/c (Being the amount paid to A and C in final settlement of underwriting commission due less amount receivable from them on share allotted)	1,87,500 47,917	 2,3,5,417
Bank A/c Dr. To B A/c (Being the amount received from B on shares allotted less underwriting Commission payable to him)	22,917	 22,917

Study Note 2 – Presentation of Financial Statements (As per Schedule III)

5. On 31st March, 2015 B&S Ltd. provides you the following ledger balances after preparing its Profit and Loss Account for the year ended 31st March,2015:

Particulars	Amount ₹
Credit Balances:	
Equity Share capital, fully paid shares of ₹10 each	**70,00,000**
General Reserves	**14,56,000**
Loan from State Finance Corp.	**10,50,000**
Secured by hypothecation of Plant & Machinery (repayable within one year ₹2,00,000	
Loans: Unsecured (Long term)	**8,47,000**
Sundry Creditors for goods & expenses (Payable within 6 months)	**14,00,000**
Profit & Loss Account	**7,00,000**
Proposed Dividend	**4,20,000**
Provision for Dividend Distribution Tax	**71,400**
	1,33,63,000
Debit Balance:	
Calls in arrear	**7,000**
Land	**14,00,000**
Buildings	**20,50,000**
Plant and Machinery	**36,75,000**
Furniture & Fixture	**3,50,000**
Stocks: Finished goods	**14,00,000**
Raw Materials	**3,50,000**

Sundry Debtors	14,00,000
Advances : Short-term	2,98,900
Cash in hand	2,10,000
Balances with banks	17,29,000
Patents & Trade Marks	4,00,000

The following additional information is also provided:

(i) 4,20,000 fully paid equity shares were allotted as consideration for Land & Buildings.

(ii) Cost of Buildings ₹28,00,000
Cost of Plant & Machinery ₹49,00,000
Cost of furniture & Fixture ₹4,37,500

(iii) Sundry Debtors for ₹3,80,000 are due for more that 6 months.

(iv) The amount of Balance with Bank includes ₹18,000 with a bank which is not a scheduled Bank and the deposits of ₹5 lakhs are for a period of 9 months.

(v) Unsecured loan includes ₹2,00,000 from from a Bank and ₹1,00,000 from related parties.

You are not required to give previous year figures. You are required to prepare the Balance Sheet of the Company as on 31st March,2015 as required under Schedule II of the Companies Act,2015.

Answer:

Balance Sheet of B&S Ltd. as on 31.03.2015

	Particulars	Note	₹
I	**Equity & Liabilities**		
(1)	Shareholders' Funds:		
	(a) Share Capital	1	69,93,000
	(b) Reserves & Surplus	2	21,56,000
(2)	Non-Current Liabilities		
	(a) Long Term Borrowing	3	16,97,000
(3)	Current Liabilities:		
	(a) Trade Payable		14,00,000
	(b) Other Current Liabilities	4	2,00,000
	(c) Short Term Provision	5	8,16,900
			1,32,62,900
II	**Assets**		
(1)	Non-current Assets		
	Fixed Assets		
	Tangible Assets	6	74,75,000
	Intangible Assets (Patents & Trade Marks)	7	4,00,000
(2)	Current Assets:		
	(a) Inventories	8	17,50,000
	(b) Trade Receivables	9	14,00,000
	(c) Cash & cash Equivalents	10	19,39,000
	(d) Short term Loans & Advances		2,98,900
			1,32,62,900

Notes:

1. Share Capital	**₹**
Issued, Subscribed & Paid up	70,00,000
Less: Calls in arrears	(7,000)
	69,93,000

2.	**Reserves & Surplus**		
	General Reserves		14,56,000
	Surplus (P&L A/c)		7,00,000
			21,56,000
3.	**Long term borrowings:**		
	Secured		
	Term Loan		
	Loan from State Finance Corp. (₹10,50,000 - ₹2,00,000)		8,50,000
	Unsecured		
	Bank Loan	2,00,000	
	Loan from related parties	1,00,000	
	Others	5,47,000	8,47,000
			16,97,000
4.	**Other Current Liabilities**		
	Loan from State Finance Corp. (repayable within one year)		2,00,000
5.	**Short term Provisions**		
	Provision for taxation		3,25,500
	Proposed dividend		4,20,000
	Provision for dividend distribution tax		71,400
			8,16,900

6. Tangible Fixed Assets:

Item	Closing Balance	Depreciation	Net
Tangible:			
Land	14,00,000	0	14,00,000
Building	28,00,000	7,50,000	20,50,000
Furniture	4,37,500	87,500	3,50,000
Plant & Machinery	49,00,000	12,25,000	36,75,000
	95,37,500	**20,62,500**	**74,75,000**

7.	**Intangible:**		
	Patents		4,00,000
8.	**Inventories**		
	Raw material		3,50,000
	Finished goods		14,00,000
			17,50,000
9.	**Trade Receivables**		
	(a) Outstanding debt for more than 6 months		3,80,000
	(b) Other debts (Bal. fig)		10,20,000
			14,00,000
10.	**Cash and Cash equivalents:**		
	Cash at bank with scheduled Banks including	17,11,000	
	Bank deposits for period of 9 months amounting with others	18,000	17,29,000
	Cash in hand		2,10,000
			19,39,000

6. **The following items appear in the Trial Balance of City Ltd. As at 31st, 2016:**

Particulars	₹
1. Revenue from Operations	48,00,000
2. Other Income	2,00,000
3. Expenses other than Interest	7,60,000
4. General Reserve (as on 1st April,2017)	2,60,000

5. **Profit and Loss Account (as on 01.04.2017) ₹6,56,000. The recommendation of the company's Board of Directors include equity dividend of 15% (Including Interim Dividend of ₹1,60,000)**
6. **Transfer to Debenture Redemption reserve @ 5%. (Assume Corporate Tax 30% and Dividend Distribution Tax @ 20%)**
7. **14% ,10,000 Preference Shares of ₹100 each fully paid up**
8. **12%, 20,000 Debentures of ₹100 each fully paid up**
9. **12,000 Equity Shares of ₹100 each**
10. **16,000 Equity Shares of ₹100 each, ₹25 paid up**

Required: Show the above items in Statement of Profit and Loss and Balance Sheet.

Answer:

City Ltd.

Statement of Profit and Loss for the year ended 31st March,2016

	Particulars	Note No.	₹
I.	Revenue from Operations		48.00
II.	Other Income		2.00
III.	Total Revenue [I+II]		50.00
IV.	Expenses:		
	Finance Costs		2.40
	Other Expenses		7.60
	Total Expenses		10.00
V.	Profit before Tax [III + IV]		40.00
VI.	Tax Expense [30% of ₹40 lakhs]		(12.00)
VII.	Profit for the period		28.00
	Basic Earnings per Equity Share:		
	= [Profit for the period – Pref. Divided]/ No. of Equity Shares		
	= (28 – 1.4) / 16,000 = ₹166.25		

An extract of Balance Sheet of City Ltd. As at 31st March,2016

Particulars	Note No.	₹
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	26.00
(b) Reserves and Surplus	2	32.60
(2) Non-Current Liabilities		
(a) Long-term Borrowings [10% Debentures]		20.00
(3) Current Liabilities		

(a) Other Current Liabilities [Interest accrued on Debentures]		2.40
(b) Short-Term Provisions	**3**	14.96
		95.96

Notes to Accounts:

1. Share Capital

Particulars	₹
Issued Capital	
28,000 Equity Shares of ₹100 each	28.00
10,000 14% Pref. Shares of ₹100 each	10.00
	38.00
Subscribed Capital and Fully paid up	
12,000 Equity Shares of ₹100 each	12.00
14%, 10,000 Pref. Shares of ₹100 each	10.00
Subscribed Capital but not fully paid	
16,000 Equity Shares of ₹100 each, ₹25 paid up	4.00
	26.00

2. Reserves and Surplus

Particulars		₹
Debenture Redemption Reserve		10.00
General Reserve [2.60 + 1.40]		4.00
Surplus i.e. Balance in Statement of Profit and Loss:		
Opening Balance	6.56	
Add: Profit for the period	28.00	
Less: Transfer to General Reserve @ 5%	(1.40)	
Less: Interim Dividend	(1.60)	
Less: Proposed Pref. Dividend	(1.40)	
Less: Proposed Equity Dividend [15% of (12 Lakhs + 4 Lakhs) – 1.60 Lakhs]	(0.80)	
Less: Divided Distribution Tax [20% of (1.60 + 1.40 + 0.8)]	(0.76)	
Less: Debenture Redemption Reserve [50% of ₹20 Lakhs]	(10)	18.60
		32.60

3. Short-term Provisions

Particulars	₹
Provision for Tax	12.00
Proposed Pref. Dividend	1.40
Proposed Equity Dividend	0.80
Corporate Dividend Tax	0.76
	14.96

Study Note 3 – Cash Flow Statement

7. MMY Ltd's Comparative Balance Sheet for June 2016 and June 2015 and the Company's Income Statement for the year June 30, 2016 are as follows:

XYZ Ltd.
Comparative Balance Sheet
June 2015 and June 2016

(₹ in Crores)

		2016		2015
Sources of funds:				
Shareholder's funds	140		140	
Share Capital	110	250	92	232
Loan funds		135		40
		385		272
Application of funds				
Fixed Assets				
Plant and Equipment	430		309	
Less : Accumulated depreciation	(218)	212	(194)	115
Investments		60		75
Current Assets				
Inventory	205		160	
Accounts receivable	180		270	
Pre-paid expenses	17		20	
Cash	26	428	10	460
Less : Current liabilities and provisions				
Accounts payable	230		310	
Accrued liabilities	70		60	
Deferred income-tax provision	15	315	113	8
		378	82	
			385	272

XYZ Ltd.
Income Statement
For the year ended June 30, 2012

(₹ in Crores)

Sales	**1,000**
Less : Cost of goods sold	**530**
Gross margin	**470**
Less : Operating expenses	**352**
Net operating income	**118**
Non-operating items:	
Loss on sale of equipment	**(4)**
Income before taxes	**114**
Less : Income-taxes	**48**
Net income	**66**

Additional information:

(vi) Dividends of ₹ 48 crores were paid in 2016.
(vii) The loss on sale of equipment of ₹ 4 crore reflects a transaction in which equipment with an original cost of ₹ 12 crore and accumulated depreciation of ₹ 5 crore were sold for ₹ 3 crore in cash.

Required:
Using the indirect method, determine the net cash provided by operating activities for 2010 and construct a statement of cash flows.

Answer:

Statement of net cash flows provided by operating activities
by using indirect method for the year ended June 30, 2016

(₹ in Crores)

Particulars	**Amount**
Operating Activities	
Net Income	66
Adjustment to convert net income to a cash basis	
Depreciation and amortization charges (218 – 194 + 5)	29
Decrease in accounts receivable (270 – 180)	90

Increase in inventory (205 – 160)	(45)
Decrease in pre-paid expenses (20 – 17)	3
Decrease in accounts payable (230 – 310)	(80)
Increase in accrued liabilities (70 – 60)	10
Increase in deferred income tax (15 – 8)	7
Loss on sale of equipment	4
Net cash flow from operating activities	**84**
Cash Flow from Investing Activities	
Additions to property, building & equipment (430 – 309 + 12)	(133)
Decrease in long term investments (75 – 60)	15
Proceeds from sale of equipment	3
Net cash used in investing activities	**(115)**
Cash Flows from Financing Activities	
Increase in bonds payable (135 – 40)	95
Cash dividends paid	(48)
Net cash used in financing activities	**47**
Net increase in cash & cash equivalents	16
Cash & cash equivalents at the beginning of year	**10**
Cash & cash equivalents at the end of year	**26**

8. Prepare Cash Flow for MG Ltd. for the year ended 31.03.2016 from the following information:

1. **Sales for the year amounted to ₹135 crores out of which 60% was cash sales.**
2. **Purchases for the year amounted to ₹55 crores out of which credit purchase was 80%.**
3. **Administrative and selling expenses amounted to ₹18 crores and salary paid amounted to ₹22 crores.**
4. **The Company redeemed debentures of ₹20 crores at a premium of 10%. Debenture holders were issued equity shares of ₹15 crores towards redemption and the balance was paid in cash. Debenture interest paid during the year was ₹1.5 crores.**
5. **Dividend paid during the year amounted to ₹10 crores. Dividend distribution tax @17% was also paid.**

6. **Investment costing ₹12 crores were sold at a profit of ₹2.4 crores.**
7. **₹8 crores was paid twords income tax during the year.**
8. **A new plant costing ₹21 crores was purchased in part exchange of an old plant. The book value of the old plant was ₹12 crores but the vendor took over the old plant at a value of ₹10 crores only. The blanace was paid in cash to the vendor.**
9. **The following balances are provided**

Particulars	₹ in crores	₹ in crores
	01.04.2015	**01.04.2016**
Debtors	**45**	**50**
Creditors	**21**	**23**
Bank	**6**	

Answer:

In the books of MG Ltd.

Cash Flow Statement for the year ended 31st March,2014

Particulars	₹ in crores	₹ in crores
Cash from Operating Activities		
Cash Sales (135 × 60%)	81	
Receipts from Customers	49	
(-) Cash purchases (55 × 20%)	(11)	
(-) Payment to customers	(42)	
Administration & Selling Expenses (18+22)	(40)	
	37	
(-) Tax paid	(8)	29
Cash from Investing Activities		
Sale of Investment (12+2.4)	14.4	
Plant & Machinery purchase (21 – 10)	(11)	3.4
Cash from Financing Activities		
(-) Redemption of Debentures (20×110% - 15)	(7)	
(-) Interest on Debentures	(1.5)	
(-) Dividend paid	(10)	
(-) Dividend Distribution Tax	(1.7)	(20.2)
Balance		**12.2**
+ Opening Bank		**6**
Closing Balance of Bank		**18.25**

Working Note:

1. **Calculation of Receipt from Customer**

Debtors Account

Particulars	₹ in crores	Particulars	₹ in crores
To Balance b/d	45	By Bank	49
To Sales	54	By Balance c/d	50
	99		**99**

2. Calculation of Payment to Creditors

Creditors Account

Particulars	₹ in crores	Particulars	₹ in crores
To C/B	42	By Balance	21
To Balance	23	By Purchase	44
	65		**65**

Study Note 4 – Accounts of Banking, Electiricity and Insurance Company

9. (a) Following are the details of interest on advance of Patta Commercial Bank as on 31st March, 2017:

(₹ in crore)

Particulars	Interest Earned	Interest Received
	₹	₹
Performing Assets:		
Terms Loan	**480**	**360**
Cash Credit and Overdraft	**2,500**	**2,010**
Bills Purchased and Discounted	**300**	**300**
Non-Performing Assets:		
Term Loan	**250**	**50**
Cash Credit and Overdraft	**800**	**60**
Bill Purchased and Discounted	**200**	**40**

Find out the income to be recognized for the year ended 31st March, 2017.

Answer:

As per RBI Circular, Interest on non-performing assets are considered on Cash Basis where as interest on performing assets are considered on Accrual Basis.

Statement Showing the Recognition of Income

Particulars	Amount (₹ in crore)	Amount (₹ in crore)
1. Interest on Term Loans		
i. Performing Assets	480	
ii. Non-performing Assets	50	530
2. Interest on Cash Credit and Overdraft		
i. Performing Assets	2,500	
ii. Non-Performing Assets	60	2,560
3. Interest on Bills Purchased and Discounted		
i. Performing Assets	300	
ii. Non-Performing Assets	40	340

Income to be Assets		3,430

(b) During the two years, the following bills were discounted @ 16% p.a. by a bank:

Date of Bill	Customer	Amount ft)	Term (Months)
27.12.2013	**W**	**1,00,000**	**3**
09.02.2014	**X**	**1,50,000**	**4**
11.05.2014	**Y**	**3,00,000**	**3**
09.02.2015	**Z**	**4,50,000**	**4**

Required: Give the necessary journal entries for the year ended on 31st March, 2014 and on 31st March, 2015.

Answer:

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr.(₹)
27.12.2013	Bills Discounted & Purchased A/c Dr. To Customers' A/c To Discount A/c (Being bills of₹ 1,00,000 discounted & purchased)		1,00,000	 96,000 4,000
09.02.2014	Bills Discounted & Purchased A/c Dr. To Customers' A/c To Discount A/c (Being bills of ₹1,50,000 discounted & purchased)		1,50,000	 1,42,000 8,000
30.03.2014	Bank A/c Dr. To Bill Discounted & Purchased A/c (Being the payment for the Bill received at date of maturity)		1,00,000	 1,00,000
31.03.2014	Discount A/c Dr. To Rebate on Bills Discounted A/c To Profit & Loss A/c (Being unexpired discount of ₹4,800 carried over to Next Year & Balance T/f to P & L A/c)		12,000	 4,800 7,200
01.04.2014	Rebate on Bills Discounted A/c Dr. To Discount A/c (Being Rebate in the beginning t/f to Discount A/c)		4,800	 4,800
11.05.2014	Bills Discounted & Purchased A/c Dr. To Customers' A/c To Discount A/c (Being bills of ₹ 3,00,000 discounted & purchased)		3,00,000	 2,88,000 12,000
12.06.2014	Bank A/c Dr. To Bills Purchased & Discounted A/c (Being the payment for X 's Bill received)		1,50,000	 1,50,000

14.08.2014	Bank A/c Dr. To Bills Purchased & Discounted A/c (Being the payment for Y 's Bill received)		3,00,000	 3,00,000
09.02.2015	Bills Discounted & Purchased A/c Dr. To Customers's A/c To Discount A/c (Being Bills of ₹ 4,50,000 discounted & purchased)		4,50,000	 4,26,000 24,000
31.03.2015	Discount A/c Dr. To Rebate on Bills Discounted A/c To Profit & Loss A/c (Being unexpired discount of ₹ 14,400 carried over to Next year & balance T/f to P & L A/c)		40,800	 14,400 26,400

Working Notes:

(i) Calculation of Date of Maturity

Date of Bill	Term in Months	Date of Maturity
27.12.2013	3	30.3.2014
09.02.2014	4	12.6.2014
11.05.2014	3	14.8.2014
09.02.2015	4	12.6.2015

(ii) Calculation of Total Discount Received & Unexpired Discount

Amount of Bill	Total Annual Discount @ 16% p.a.	Total Discount received	No. of Days After 31st March	Unexpired Discount as on 31st March
1,00,000	16,000	4,000	0	—
1,50,000	24,000	8,000	73 Days	4,800
3,00,000	48,000	12,000	0	—
4,50,000	72,000	24,000	73 Days	14,400

10. (a) From the following information Calculate

(c) Average Capital Cost,

(d) Annual Depreciation as per Regulation 14 of the Central Electricity Regulatory Commission (Terms and Conditions of Tariff) Regulations, 2009,

1. **Date of Commercial Operation of COD = 1 st April 2010**
2. **Approved Opening Capital cost as on 1st April 2010 = ₹3,00,000**
3. **Weighted Average Rate of Depreciation: 5%**
4. **Details of allowed Additional Capital Expenditure as follows:**

Particulars	1st year	2nd year	3rd year	4th year
Additional Capital Expenditure (Allowed)	**20,000**	**6,000**	**6,000**	**4,000**

Answer:

Average Capital Cost

Particulars	1st year	2nd year	3rd year	4th year
A. Opening Capital Cost	3,00,000	3,10,000	3,13,000	3,15,000
B. Additional Capital Cost	20,000	6,000	4,000	4,000
C. Closing Capital Cost (A + B)	3,20,000	3,16,000	3,17,000	3,19,000
D. Average Capital Cost [(A + C)/2]	3,10,000	3,13,000	3,15,000	3,17,000

1. **Computation of Depreciation**

Particulars	1st year	2nd year	3rd year	4th year
A. Average Capital Cost	3,10,000	3,13,000	3,15,000	3.17,000
B. Weighted Average Rate of Dep.	5%	5%	5%	5%
C. Annualized Depreciation (A x B)	15,500	15,650	15,750	15,850

(b) From the following information of VIDYUT ELECTRICITY CO. LTD., an Electricity generation Project, Calculate:

(1) Depreciation and

(2) Advance against Depreciation upto the year 2014-15 as per Regulation 21 of the Central Electricity Regulatory Commission (Terms and Conditions of Tariff) Regulations 2004.

- **Date of Commercial Operation of COD: 1st April, 2012**
- **Approved Opening Capital Cost as on 1st April, 2012: ₹10,00,000**
- **Weighted average Rate of Depreciation: 5.20%**
- **Details of allowed Additional Capital, Repayment of loan and Weighted Average Rate of Interest on Loan are as follows:**

(Amount in ₹)

Year	2012-13	2013-14	2014-15
Additional Capital Expenditure (allowed)	**70,000**	**20,000**	**15,000**
Repayment of Loan	**60,000**	**70,000**	**70,000**
Weighted Average Rate of Interest on Loan	**7.50%**	**7.60%**	**7.80%**

Answer:

VIDYUT ELECTRICITY CO. LTD.

A. Computation of Depreciation

(Amount in ₹)

	Particulars	2012-13	2013-14	2014-15
A	Opening Capital Cost	10,00,000	10,70,000	10,90,000
B	Additional Capital Cost	70,000	20,000	15,000
C	Closing Capital Cost	10,70,000	10,90,000	11,05,000

D	Average Capital Cost [(A+C)/2]	10,35,000	10,80,000	10,97,500
E	Weighted average rate of depreciation	5.20%	5.20%	5.20%
F	Annualized depreciation (D)×(E)	53,820	56,160	57,070
G	Advance against depreciation (ADD)	6,180	13,840	12,930
H	Total depreciation (including ADD) for tariff (F+G)	60,000	70,000	70,000

B. Computation of Depreciation

(Amount in ₹)

	Particulars	2012-13	2013-14	2014-15
A	Repayment of Loan (10% of loan amount)	60,000	70,000	70,000
B	Depreciation (Excluding AAD)	53,820	56,160	57,070
C	Difference between A&B (A-B)	6,180	13,840	12,930
D	Cumulative repayment of Loan	60,000	1,30,000	2,00,000
E	Cumulative Depreciation (Excluding AAD) at the beginning	53,820	1,09,980	1,67,050
F	Difference between D&E (D-E)	6,180	20,020	32,950
G	Advance against depreciation (AAD) (Minimum of C&F)	6,180	13,840	12,930

11. (a) Prepare the Fire Insurance Revenue Account of JS Fire Insurance Ltd. As per IRDA regulations for the year ended 31st March,2016 from the following details:

Particulars	Amount (₹)
Claims paid	**6,00,000**
Legal Expenses regarding claims	**10,000**
Premiums received	**12,50,000**
Re-insurance premium paid	**50,000**
Commission	**3,00,000**
Expenses of Management	**2,00,000**
Provision against unexpired risk as on 1st April,2015	**5,75,000**
Claims unpaid on 1st April,2015	**50,000**
Claims unpaid on 31st March,2016	**80,000**

Provide for unexpired risk @ 50% less reinsurance.

Answer:

FORM B – RA
Name of the Insurer: JS Fire Insurance Ltd.
Revenue Account for the year ended 31st March,2016

	Particulars	Schedule	Amount (₹)
1	Premium earned	1	11,75,000
2	Other income		-
3	Interest, dividend and rent		-
	Total (A)		11,75,000
4	Claims incurred	2	5,40,000
5	Commission	3	3,00,000
6	Operating expenses related to insurance business	4	2,00,000
	Total (B)		10,40,000
	Operating Profit (A-B)		**1,35,000**

Schedule 1 : Premium Earned (Net)	(₹)
Premium received	12,50,000
Less: Re-insurance premium	(50,000)
Net Premium	12,00,000
Adjustment for change in reserve for unexpired risks	(25,000)
	11,75,000

Schedule 2 : Claims Incurred	(₹)
Claims paid including legal expenses (5,00,000 + 10,000)	5,10,000
Add: Claims outstanding at the end of the year	80,000
Less: Claims outstanding at the beginning of the year	(50,000)
Total Claims Incurred	5,40,000

Schedule 3 : Commission	(₹)
Commission paid	4,00,000

Schedule 4 : Operating Expenses	(₹)
Expenses of Management	2,00,000

Working Note:

Change in the Provision for Unexpired Risk	(₹)
Unexpired risk reserve on 31st March,2016 = 50% of net premium (i.e. 50% of ₹12,00,000)	6,00,000
Less: Unexpired risk reserve as on 1st April,2015	(5,75,000)
	25,000

(b) From the following information of XY Marine Insurance Ltd. For the year ended 31st March,2016 find out

Particulars	Direct Business ₹	Re-insurance ₹
Premium Received	**92,00,000**	**7,86,000**
Premium Receivable as on 01.04.2015	**4,59,000**	**37,000**
Premium Receivable as on 31.03.2016	**3,94,000**	**33,000**
Premium Paid		**6,36,000**
Premium Payable as on 01.04.2015		**28,000**
Premium Payable as on 31.03.2016		**20,000**
Claim Paid	**73,00,000**	**5,80,000**
Claims Payable as on 01.04.2015	**94,000**	**16,000**
Claims Payable as on 31.03.2016	**1,01,000**	**12,000**
Claims Received		**2,10,000**
Claims Receivables as on 01.04.2015		**42,000**
Claims Receivables as on 31.03.2016		**39,000**

Answer:

In the book of XY Marine Insurance Ltd.

Net Premium Earned

Particulars	₹	₹
Premium from direct business received	92,00,000	
Add: Receivable on 31.03.2016	3,94,000	
Less: Receivable on 01.04.2015	(4,59,000)	91,35,000
Add: Premium on re-insurance accepted	7,86,000	
Add: Receivable on 31.03.2016	33,000	
Less: Receivable on 01.04.2015	(37,000)	7,82,000
		99,17,000
Less: Premium on reinsurance	6,36,000	
Add: Payable on 31.03.2016	20,000	
Less: Payable on 01.04.2015	(28,000)	(6,28,000)
Net Premium Earned		**92,89,000**

Net Claims Incurred

Particulars	₹	₹
Claims paid on direct business		73,00,000
Add: Reinsurance	5,80,000	
Add: Outstanding as on 31.03.2016	12,000	
Less: Outstanding as on 01.04.2015	(16,000)	5,76,000
		78,76,000
Less: Claims received from reinsurance	2,10,000	
Add: Outstanding as on 31.03.2016	39,000	
Less: Outstanding as on 01.04.2015	(42,000)	2,07,000
		76,69,000
Add: Outstanding direct claims at the end of year	1,01,000	
Less: Outstanding direct claims at the beginning of the year	(94,000)	7,000
Net Claims Incurred		**76,76,000**

Study Note 5 – Accounting Standards

12. (a) Friend Ltd. received a specific grant of ₹ 600 lakhs for acquiring the plant of ₹ 3,000 lakhs during 2012-13 having useful life of 10 years. The grant received was credited to deferred income in the balance sheet. During 2015-16 and due to non-compliance of conditions laid down for the grant of ₹ 600 lakhs the company had to refund the grant to the Government. Balance in the deferred income on that date was ₹ 420 lakhs and written down value of plant was ₹ 2,100 lakhs.

(i) What should be the treatment of the refund of the grant and the effect on cost of the fixed asset and the amount of depreciation to be charged during the year 2015-16 in profit and loss account?

(ii) What should be the treatment of the refund if grant was deducted from the cost of the plant during 2012-13?

Answer:

As per AS-12 , to the extent the amount refundable exceeds any such deferred credit, the amount should be charged to profit and loss statement.

(i) In this case the grant refunded is ₹ 600 lakhs and balance in deferred income is ₹420 lakhs,₹ 180 lakhs shall be charged to the profit and loss account for the year 2015-16. There will be no effect on the cost of the fixed asset and depreciation charged will be same as charged in earlier year.

(ii) As per AS-12 the amount refundable in respect of grant which related to specific fixed assets should be recorded by increasing the book value of the assets by the amount refundable. Where the book value of the asset is increased, depreciation on the revised book value should be provided prospectively over the residual useful life of the asset. Therefore, in this case the book value of the plant shall be increased by ₹ 600 lakhs. The increased cost of ₹ 600 lakhs of the plant should be amortised over 7 years (residual life). Depreciation charged during the year 2015-16 shall be 2,400/10 + 600/7 = 325.71 lakhs. Presuming the depreciation on SLM.

(b) A Ltd. purchased fixed assets costing ₹ 3,400 lakhs on 01.01.17 and the same was fully financed by foreign currency loan (U.S. Dollars) payable in three annual equal installments. Exchange rates were 1 Dollar = ₹ 62.50 and ₹ 65.00 as on 01.01.17 and 31.12.17 respectively. First installment was paid on 31.12.17. The entire difference in foreign exchange has been capitalized.
You are required to state, how these transactions would be accounted for.

Answer:

As per para 13 of AS 11 (Revised 2003) 'The Effects of Changes in Foreign Exchange Rates', exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or expenses in the period in which they arise. Thus exchange differences arising on repayment of liabilities incurred for the purpose of acquiring fixed assets are recognized as income or expense.

Calculation of Exchange Difference:

$$\text{Foreign currency loan} = \frac{₹\ 3,400\ \text{lakhs}}{₹62.50} = 54.4\ \text{lakhs US Dollars}$$

Exchange difference = ₹54.4 lakhs US Dollars × (65.00 – 62.50)
= ₹ 136 lakhs
(including exchange loss on payment of first installment)

Therefore, entire loss due to exchange differences amounting ₹ 136 lakhs should be charged to Profit and Loss Account for the year.

(c) Urvashi Ltd. is an engineering industry. The company received an actuarial valuation for the first time for its pention scheme which revealed a surplus of ₹12 lakhs. It wants to spread the same over the next 2 years by reducing the annual contribution to ₹4 lakhs instead of ₹10 lakhs. The average remaining life of the employee is estimated to 6 years. You are required to advice the company.

Answer:

According to AS – 15 (revised 2005) 'Employee Benefits', actuarial gains and losses should be recorded immediately in the statement of profit and loss as income or expenses.

Therefore, surplus amount of ₹12 lakhs is required to be credited to the profit and loss statement of the current year.

13.(a)

Particulars	**₹**
Expenditure incurred till 31.03.2016	**5,00,000**
Interest cost capitalized for the financial year 2015-16 @ 13%	**26,000**
Amount borrowed till 31.03.16 is	**2,00,000**
Assets transferred to construction during 2016-17	**1,00,000**
Cash payment during 2016-17	**75,000**
Progress payment received	**3,50,000**
New borrowing during 2016-17 @ 13%	**2,00,000**

Calculate the amount of borrowing cost to be capitalised.

Answer:

Total borrowing cost = 4,00,000 ×13/100 = ₹52,000

Particulars	**₹**
Expenditure incurred including previously capitalized borrowing cost (5,00,000 + 26,000)	5,26,000
Cash payment during 2016-17	75,000
Asset transferred during 2016-17	1,00,000
	7,01,000
Less: Progress payment received	3,50,000
	3,51,000

Money borrowed including previously capitalized interest cost 4,00,000 + 26,000

= 4,26,000

Capitalisation rate = 351/426 X 100 = 82.3%

Borrowing cost to be capitalized = 82.3% X 52,000 = 42,845

(b) From the following information of a company having two primary segments, prepare a statement classifying the same under appropriate heads.

		(₹ in lakh)
Segment Revenue	**A**	**27,150**
Segment Revenue	**B**	**3,280**
Inter Segment Revenue	**A**	**50**
Segment Profit	**A**	**4,640**
Segment Profit	**B Loss**	**197**
Dividend Income		**285**

Interest Expense		**43**
Tax Provision		**1,675**
Capital Expenditure	**A**	**1,300**
Capital Expenditure	**B**	**16**
Non Cash Expenses (excluding depreciation)		
Segment	**A**	**114**
Segment	**B**	**16**
Liabilities	**A**	**3,430**
Liabilities	**B**	**770**
Other Liabilities		**2,200**
Assets	**A**	**19,450**
Assets	**B**	**2,700**
Other Assets		**6,550**
Depreciation	**A**	**110**
Depreciation	**B**	**15**

Answer:

(₹ in lakh)

Particulars	**Segment A**	**Segment B**	**Others**	**Eliminations**	**Total**
I Revenue:					
a) External Revenue	27,150	3,280			30,430
b) Inter segment Revenue	50			-50	
Total	27,200	3,280		-50	30,430
II Result:	4,640	-197			4,443
a) Income from Investment					285
b) Interest Expenses					-43
c) Tax provision					-1,675
d) Net profit					3,010
III Assets:					
a) Segment assets (directly	19,450	2,700			22,150

		attributable & allocated)					
	b)	Unallocated assets					6,550
IV	Liabilities						
	a)	Segment Liabilities (directly attributable & allocated)	3,440	770			4,200
	b)	Unallocated liabilities					2,200
V	Others:						
	a)	Depreciation	110	15			125
	b)	Non cash expenses	114	16			130
	c)	Capital Expenditure	1,300	16			1,316

14. A Ltd. leased a machinery to B Ltd. on the following terms:

	(₹ in Lakhs)
Fair value of the machinery	**20.00**
Lease term	**5 years**
Lease Rental per annum	**5.00**
Guaranteed Residual value	**1.00**
Expected Residual value	**2.00**
Internal Rate of Return	**15%**

Depreciation is provided on straight line method @ 10% per annum. Ascertain unearned financial income and necessary entries may be passed in the books of the Lessee in the First year.

Answer:

Computation of Unearned Finance Income

As per AS 19 on Leases, **unearned finance income** is the **difference between (a)** the gross investment in the lease and **(b)** the present value of minimum lease payments under a finance lease from the standpoint of the lessor; and any unguaranteed residual value accruing to the lessor, at the interest rate implicit in the lease.

where :

(i) **Gross investment** in the lease is the aggregate of (i) minimum lease payments from the stand point of the lessor and (ii) any unguaranteed residual value accruing to the lessor.

Gross Investment = Minimum lease payments + Unguaranteed residual value

= (Total lease rent + Guaranteed residual value) + Unguaranteed residual value

= [(₹ 5,00,000 × 5 years) + ₹ 1,00,000] + ₹ 1,00,000 = ₹ 27,00,000

(ii) Table showing present value of (i) Minimum lease payments (MLP) and (ii) Unguaranteed residual value (URV).

Year	MLP inclusive of URV	Internal rate of return (Discount factor 15%)	Present Value
	₹		₹
1	5,00,000	0.8696	4,34,800
2	5,00,000	0.7561	3,78,050
3	5,00,000	0.6575	3,28,750
4	5,00,000	0.5718	2,85,900
5	5,00,000	0.4972	2,48,600
	1,00,000	0.4972	49,720
	(Guaranteed residual value)		________
			17,25,820
	1,00,000	0.4972	49,720
	(Unguaranteed residual value)		________
			17,75,540

Unearned Finance Income = (i) – (ii)
= ₹ 27,00,000 – ₹ 17,75,540 = ₹ 9,24,460

Journal Entries in the books of B Ltd.

Particulars		₹	₹
At the inception of lease			
	Machinery Account Dr.	17,25,820	
	To A Ltd.'s Account		17,25,820
	(Being lease of machinery recorded at present value of MLP)		
At the end of the first year of lease			
	Finance Charges Account (Refer Working Note) Dr.	2,58,873	
	To A Ltd.'s Account		2,58,873
	(Being the finance charges for first year due)		
	A Ltd.'s Account Dr.	5 ,00,000	
	To Bank Account		5,00,000
	(Being the lease rent paid to the lessor which includes outstanding liability of ₹ 2,41,127 and finance charge of ₹ 2,58,873)		
	Depreciation Account Dr.	1,72,582	
	To Machinery Account		1,72,582
	(Being the depreciation provided @ 10% p.a. on straight line method)		
	Profit and Loss Account Dr.	4,31,455	
	To Depreciation Account		1,72,582
	To Finance Charges Account		2,58,873
	(Being the depreciation and finance charges transferred to profit and loss account)		

Working Note:

Table showing apportionment of lease payments by B Ltd. between the finance charges and the reduction of outstanding liability.

Year	Outstanding liability (opening balance)	Lease rent	Finance charge	Reduction in outstanding liability	Outstanding liability (closing balance)
	₹	₹	₹	₹	₹
1	17,25,820	5,00,000	2,58,873	2,41,127	14,84,693
2	14,84,693	5,00,000	2,22,704	2,77,296	12,07,397
3	12,07,397	5,00,000	1,81,110	3,18,890	8,88,507
4	8,88,507	5,00,000	1,33,276	3,66,724	5,21,783
5	5,21,783	5,00,000	78,267	5,21,783	1,00,050*
			8,74,230	17,25,820	

The difference between this figure and guaranteed residual value (₹ 1,00,000) is due to approximation in computing the interest rate implicit in the lease.

Short Notes

15. Please write short note on —

(a) List the disclosure requirements of AS - 15

Answer:

Disclosure under AS-15:

a) In view of the varying practices, adequate disclosure of method of accounting for an understanding of the significance of such costs to an employer.

b) Disclosure separately made for statutory compliance or otherwise the retirement benefit costs are treated as an element of employee remuneration without specific disclosure.

c) Financial statements should disclose whether actuarial valuation is made at the end of the accounting period or earlier (in which case the date of actuarial valuation and the method used for accrual period if not based on actuary report).

(b) Purposes for which share premium account may be applied

Answer:

Purposes for which share premium account may be applied

Section 52 of the Companies Act, 2013 gives the purposes for which share premium account may be applied by the company.

These are:

(i) For the issue of fully paid bonus shares to the members of the company;

(ii) For writing off preliminary expenses of the company;

(iii) For writing off the expenses of the commission paid or discount allowed on any issue of shares or debentures of the company; and
(iv) For providing premium payable on the redemption of any redeemable preference shares or debentures of the company.
(v) For the purchase of its own shares or other securities u/s 68.

(a) Difference between Initial Public Offer and Follow on Public Offer

Answer:

Following are the difference between Initial Public Offer and Follow on Public Offer:

- IPO is made when company seeks to raise capital via public investment while FPO is subsequent public contribution.
- First issue of shares by the company is made through IPO when company first becoming a publicly traded company on a national exchange while Follow on Public Offering is the public issue of shares for an already listed company.

(b) Forfeiture of Shares vs. Surrender of Shares

Answer:

Forfeiture of Shares vs. Surrender of Shares

Forfeiture of Shares

When a shareholder fails to pay calls, the company, if empowered by its articles, may forfeit the shares. If a shareholder has not paid any call on the day fixed for payment thereof and fails to pay it even after his attention is drawn to it by the secretary by registered notice, the Board of Directors pass a resolution to the effect that such shares be forfeited. Shares once forfeited become the property of the company and may be sold on such terms as directors think fit. Upon forfeiture, the original shareholder ceases to be a member and his name must be removed from the register of members.

Surrender of Shares

After the allotment of shares, sometimes a shareholder is not able to pay the further calls and returns his shares to the company for cancellation. Such voluntary return of shares to the company by the shareholder himself is called surrender of shares. Surrender of shares has no separate accounting treatment but it will be like that of forfeiture of shares. The same entries (as are passed in case of forfeiture of shares) will be passed in case of surrender of shares.

(c) Advantages of buy-back

Answer:

Buy-back have the following advantages:

(i) A company with capital, which cannot be profitably employed, may get rid of it by resorting to buy-back, and re-structure its capital.
(ii) Free reserves which are utilized for buy-back instead of dividend enhance the value of the company's shares and improve earnings per share.

(iii) Surplus cash may be utilized by the company for buy-back and avoid the payment of dividend tax.
(iv) Buy-back may be used as a weapon to frustrate any hostile take-over of the company by undesirable persons.

(d) Differences between Shares and Debentures

Answer:

Differences between Shares and Debentures

	SHARES	DEBENTURES
Definition	An instrument to acknowledge the ownership of the company.	An instrument to acknowledge the creditors of the company.
Status	A shareholder is the owner and a member of the company.	A debenture holder is not a member but a creditor.
Return	A shareholder may receive dividend only when a company makes a profit.	A debenture holder has a right to interest even if the company does not make profit.
Rate of return	Dividend rate can vary depending on the profit position.	Debenture carries a fixed rate of interest.
Accounting treatment	Dividend is given out of appropriable profit and not chargeable to Profit and Loss account.	Debenture interest is chargeable to Profit and Loss account.
Redemption	In the case of shares, the concept of redemption does not apply. However as per the recent change in the Companies Act, a company can buy back shares in accordance with the provisions in the Act.	Debentures are normally redeemable although a company can issue perpetual debentures.
Voting rights	A shareholder has voting rights.	A debenture holder cannot have voting rights.
Status at the time of winding up	At the time of winding up share holders have the least priority regarding the return of amount due to them.	At the time of winding up debenture holders have a priority over the share holders regarding the return of amount due to them.

(e) Marked and Unmarked Applications

Answer:

Marked and Unmarked Applications:
'Marked' applications are those applications which bear the stamp of an underwriter. If the issue is not fully subscribed, 'marked' applications shall be applied in reduction of underwriter's liability.
The 'unmarked' applications are those applications which bear no stamp of an underwriter. These applications are received by the company directly from the public. The distinction between marked and unmarked applications becomes immaterial when the whole issue is subscribed by only one underwriter. When there are more than one underwriter, the

unmarked applications are divided amongst Underwriters in the ratio of their gross liability. When the issue is fully subscribed, the distinction between marked and unmarked applications becomes immaterial.

(f) Why Cash Flow Statement is Prepared?

Answer:

Cash Flow Statement is considered to be a summarized statement showing sources of Cash Inflows and application of cash outflows of an enterprise during a particular period of time. It is prepared on the basis of the published data as disclosed by the Financial Statement of two different financial periods. It is an essential tool for managerial decision-making. Cash Flow reports the management Net Cash Flow (i.e. cash inflow less cash outflow or vice versa) from each activity of the enterprise as well as of the overall business of the enterprise. The management of the enterprise gets a picture of movement of cash resources from the Cash Flow Statement and can assess the stronger and weaker area of movement of cash for different activities of the business for drawing up the future planning.

(g) Central Electricity Regulatory Commission (CERC)

Answer:

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: (i) A chairperson and 3 Members (ii) 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 inter-state transmission of electricity, to issue licenses, to levy fees, to fix trading margin etc.

(h) Distinction between Life and Non-life Insurance

Answer:

Distinction between Life and Non-life Insurance

There are certain basic differences between life policies and other types of policies. These are listed below:

(1) Human life cannot be valued exactly. Therefore each insured is permitted to insure his life for a specified sum, depending on his capacity to pay premiums. This is also one form of investment and the policy amount depends on his investment decision. In the event of the policy maturing the insurer must pay the policy amount as actual loss cannot be determined. This is not the case with other policies. Other policies are contracts of indemnity. Therefore not withstanding the amount for which the policy is taken, the insurer would pay (reimburse) only the actual loss suffered or the liability incurred.

(2) Life insurance contracts are long-term contracts. Once a policy is taken premiums have to be paid for number of years till maturity and the policy amount is paid on maturity. Of course, a life policy can be surrendered after certain number of years and the insured is paid a proportion of the premiums paid known as surrender value. In the case of other policies they are for a short period of one year although the policy can be renewed year after year.

(3) Life insurance is known also by another term 'assurance' since the insured gets an assured sum. Other policies are known as insurance.

(4) The determination of profit is by different methods for life and general insurance business. In the case of life business periodically actuaries estimate the liability under existing policies. On that basis a valuation Balance Sheet is prepared to determine the profit. In the case of general insurance business a portion of the premium is carried forward as a provision for unexpired liability and the balance net of claims and expenses is taken as profit (or loss).

Section B – Auditing

Objectives

1. (a) Multiple Choice Questions:

1. **Authorization for Government Audit.**
   - **A. BOD**
   - **B. Audit committee**
   - **C. CAG**
   - **D. None of the above**
2. **Final Audit is known as ______.**
   - **A. Tax Audit**
   - **B. Internal Audit**
   - **C. Annual Audit**
   - **D. All of the above**
3. **Maximum term of Individual Auditor**
   - **A. 1 term of 5 years**
   - **B. 2 term of 5 years**
   - **C. 3 term of 5 years**
   - **D. None of the above**
4. **SA 300 stands for __________.**
   - **A. Responsibility of Joint Auditor**
   - **B. Overall planning of audit**
   - **C. Audit Planning**
   - **D. None of the above**
5. **Audit is conducted to draw overall opinion on _________.**
   - **A. Financial Statement**
   - **B. Cost Statement**
   - **C. Income Statement**
   - **D. None of the above.**
6. **An auditor is required to retain the books of accounts for how long.**

A. 1 yrs
B. 5 yrs
C. 7 yrs
D. None of the above.

7. An audit committee should have _____ directors.
A. 2
B. 3
C. 5
D. 10

8. Form ____ is used for maintenance of cost records by the company.
A. CRA-1
B. CRA-3
C. CRA-5
D. None of the above

9. SA-700 stands for ________.
A. Audit Planning
B. Joint Auditor
C. Forming an opinion and reporting on Financial Statement.
D. None of the above

10. A nomination and remuneration committee should have ______ directors.
A. 5
B. 10
C. 2
D. 3

Answer:

Sl/No.	Answer
1.	C
2.	C
3.	A
4.	C
5.	A
6.	C
7.	B
8.	A
9.	C
10.	D

1.(b). Fill in the blanks:

1. A _________ is detailed plan of the auditing work to be performed.
2. __________ are the property of the auditor.
3. A ______ audit is a non statutory audit.
4. Continuous audit is necessary where _____________ are inadequate.
5. The person conducting an audit is known as _______.

Answer:

Sl/No.	Answer
1.	Audit programme
2.	Working papers
3.	Partial
4.	Internal controls
5.	Auditor

1.c. Match the followings:

	Column I		Column-II
1.	**Independent appraisal activity**	**A**	**Secretarial Audit Report**
2.	**Verification**	**B**	**Final product of audit**
3.	**Audit report**	**C**	**Section 123**
4.	**Form MR3**	**D**	**Internal Audit**
5.	**Declaration of dividend**	**E**	**Proving the truth**

Answer:

Sl/No.	Answer
1.	D
2.	E
3.	B
4.	A
5.	C

1.d. State whether the following statement are true or false.

1. **Section 70 deals with the Audit of Debenture.**
2. **An audit committee should have 4 directors.**
3. **SA 299 stands for "Responsibility of Joint Auditor" as issued by ICAI.**
4. **First auditor of the company is appointed by the BOD within 45 days.**
5. **Internal check is a continuous critical review of financial and operating activities by staff members of the auditor.**

Answer:

Sl/No.	Answer
1.	False. Section 71
2.	False. 3 Directors.
3.	True
4.	False. 30 days
5.	False. Internal Audit

Auditing Concepts, Audit working papers and Audit Evidence

2.a. List down the advantages of the Statutory Audit.

2.b. Distinguish between Internal Audit, Internal Control, and Internal Check.

Answer:

2.a Advantages of Statutory Audit

The auditor expresses his independent opinion after following relevant audit procedures and checking the external and internal evidences necessary for the conduct of audit. He comments on the truthfulness and fairness of statement of affairs of the organization as on certain date and also about the fact that no misstatement or misrepresentation has been made in the Financial Statements under report.

Such an independent opinion by the auditor increases the reliability, authenticity and credibility of the Financial Statements which may further be used by different users for various purposes such as:
(i) The members/shareholders/stakeholders, for their economic decisions and for exercising their voting rights.
(ii) For timely tax assessments.
(iii) For determining the purchase or sale consideration in case of ongoing concern.
(iv) Settlement of partners' accounts in case of admission, retirement or death of partner on account of goodwill or otherwise.
(v) Before the court, in case of settlement of disputes with employees, creditors or debtors.
(vi) For determining the actual value of business or shares in case of merger, acquisition, etc.
(vii) For getting financial assistance from financial institutions, banks or investors.
(viii) In case of non-profit organizations, for getting government grants and availing tax exemptions.
(ix) Evaluation of the internal control systems and strengthening it by removing the inherent weaknesses, and checking the efficacy of the internal checks.
(x) For checking the integrity of the management which manages the funds and affairs on behalf of the real owners or shareholders.
(xi) For other users of financial statements like creditors, investors and government agencies, it ensures that any assertions in the Financial Statements are neither overstated/understated nor misrepresented.
(xii) For the proper distribution of profits by way of payment of wages and other benefits.
(xiii) For ensuring of proper distribution of profits as dividends.
(xiv) For ensuring that all legal requirements are fulfilled and statutory compliances are adhered.
(xv) For settlement of insurance claims or other recoveries from government bodies or otherwise.

Internal Check/Internal Control and Internal Audit

2.b. Distinguish between Internal Audit, Internal Control and Internal check

SL No.	Basis	Internal Audit	Internal Control	Internal Check
1.	Way of Checking	In an internal audit system, each component of work is checked.	In internal controls systems, work of one person is automatically checked by	It operates in routine to doubly check every part of a transaction at the time of

			another.	occurrence and recording of the same.
2.	Objective	Its objective is to evaluate the internal control system and to detect frauds and errors.	Its objective is to ensure adherence to management policies, safeguarding of assets, prevention and detection of frauds and errors, accuracy and completeness of accounting records.	Its objective is to ensure that no one employee has exclusive control over any transaction or group of transactions and their recording in the books.
3.	Point of Time	In an internal audit system, work is checked after it is done.	In an internal control system, checking is done simultaneously with the conduct of work. Every transaction is checked as soon as it is entered.	Methods of recording transactions are devised where work of an employee is checked continuously by correlating it with the work of others.
4.	Thrust of system	The thrust of internal system is to detect errors and frauds	The thrust of internal check system is to prevent errors.	The thrust of internal control lies in fixing of responsibility and division of work to avoid duplication.
5.	Cost Involvement	In an internal audit system, work is checked specially; therefore cost is involved in addition to accounting	The system proves to be costly in case of small businesses because more number of employees are engaged	It is a part of internal control and a method of division of work, therefore does not add to the cost.
6.	Report	The internal auditor submits his report to the management.	Internal Controls provide for built in MIS reports.	The summary of day to day transactions work as report for the senior.

3.a. Discuss the methods to obtain Audit Evidence.

3.b. State the objective of Internal Control.

Answer:

3.a.

While auditing, the auditor come across various assertions of the management. The auditor has to evaluate these assertions so that he would be able to express his opinion on the financial statements. This evaluation can be made in the light of some facts and reasons. These facts and reasons are called Audit Evidence'. The auditor should evaluate whether he has obtained sufficient appropriate audit evidence so that reasonable conclusions can be drawn there from. It is to be noted that sufficiency an appropriateness are interrelated and apply to evidence obtained from both substantive and compliance procedures.

Methods to Obtain Audit Evidence

Auditor obtains evidence in performing compliance and substantive procedures by any one or more of the following methods –

(a) Inspection -It consists of examining records, documents, or tangible assets. Inspection of records and documents provides evidence of varying degrees of reliability depending on their nature, source and the effectiveness of internal controls over their processing.

(b) Observation -It consists of witnessing a process or procedure being performed by others.

(c) Inquiry and Confirmation -Inquiry consists of seeking appropriate information from a knowledgeable person inside or outside the entity, Confirmation consists of the response to an inquiry to corroborate information contained in the accounting records.

(d) Computation -It consists of checking the arithmetical accuracy of source documents and accounting records or performing independent calculations.

(e) Analytical Review -It consists of studying significant ratios and trends and investigating unusual fluctuations and items.

3.b.

Objectives of Internal Control

Each organization must have a system of internal control in place for achieving the preset goals. Other than accomplishing the desired goals and objectives of the organization, this system plays a very important role in any organization. The main objectives of internal control are enumerated below:

i) **Compliance:** To have compliance with law and the accounting practices generally accepted and followed in the country. The accounting process also needs to be in compliance with these.

ii) **Reliance:** To increase the reliance on the internal systems, people and accounting practices followed by the organization, so that the chances of frauds are reduced.

iii) **Safeguarding:** To safeguard the organization's accounts, employees and assets by formation of fool-proof policies, rules and regulations.

iv) **Security:** To provide security to customers, employees and property of the organization. Physical security systems like security guards, locks and anti-theft devices are used for providing protection.
v) **Increased efficiency:** To assist in human resource and performance management, and to keep proper control over business activities to achieve maximum levels of efficiency.
vi) **Evaluation:** To evaluate the accounting system for proper authorization of transactions.
vii) **Review and correction:** To review the working of the business, locate weak points in operations and to take corrective measures for proper working.
viii) **Authorization:** To provide proper authority for purchase, sale, valuation, verification and possession of assets.
ix) **Delegation:** To provide for division of duties among the employees where all staff members work cohesively.
x) **Accurate planning:** To ensure that the auditors and the accountants of the organization make all the financial reports correctly and to ensure that financial planning is done accurately.
xi) **Conformity with accounting principles:** To conform to the basic accounting concepts, and principles that was governing an organization.
xii) **Resource utilization:** To ensure that all the resources: Man, Material, Money and Machines of the organization are optimally used.
xiii) **Safeguarding of resources:** To protect the resources of the organization against mismanagement or fraud and to ensure that the company's activities are in accordance with laws and regulations.
xiv) **Setting future Corporate Goals**: An efficient system of internal control helps the organization in goal setting. However, the organization should have certain policies, rules and regulations in place to achieve the preset goals.

4.a. Distinguish between Permanent and Current Audit File.
4.b. Discuss the basic element of Internal Control.

Answer:

4.a.
Permanent and Current Audit File: In case of recurring audits, some working papers files may be classified into permanent audit files and current audit files: while the former is updated with the Information of continuing importance, the latter contains information relating to audit of a single period. The contents of these files are given below:

Sl/No.	Permanent Audit File	Current Audit File
1	Legal and organizational structure of the entity, e.g. Memorandum of Association and Article of Association in case of a company	Correspondence relating to acceptance of annual reappointment.
2	Extracts or copies of legal documents, agreements and minutes relevant to the audit.	Extracts of important matters in the minutes of Board Meetings and General Meetings relevant to the audit.
3	A record if study and evaluation of internal controls.	Copies of management letters.

4	Analysis of significant ratios & trends.	Analysis of transactions and balances.
5	Copies of the audited financial statements of previous year(s).	Copies of communication with other auditors, experts and third parties.
6	Notes regarding significant accounting policies.	Auditprogramme
7	Significant audit observations of the earlier years.	Conclusions reached on significant aspects of audit.

4.b.

Basic element of Internal Control: An effective system of internal control should have the following basic elements:

1. Financial and other Organizational Plans: This may take the form of manual suitably classified by flow charts. It should specify the various duties and responsibilities of both management and staff, stating the powers of authorisation that reside with various members. This is important as in the event of staff absence or otherwise the correct flow of work and the internal control system could be vitiated by any wrong implementation of procedures by staff either unintentionally or willfully.

2. Competent Personnel: In any internal control system, personnel are the most important element. When the employees are competent and efficient in their assigned work, the internal control system can be worked and operated efficiently and effectively even if some of the other elements of the internal control system are absent.

3. Division of Work: This refers to the procedure of division of work properly among the employees of the organization. Each and every work of the organization. Each and every work of the organization should be divided in different stages and should be allocated to the employees in accordance with quality and skill. .

4. Separation of operational responsibility from record keeping: If each department of an organization is being assigned to prepare its own records and reports, there may be a tendency to manipulate results for showing better performance. So in order to ensure reliable records and information, recordkeeping function is separated from the operational responsibility of the concerned department.

5. Separation of the custody of assets from accounting: To protect against misuse of assets and their misappropriation, it is required that the custody of assets and their accounting should be done by separate persons. When a particular person performs both the functions, there is a chance of utilizing the organisation's assets for his personal interest and adjusting the records to relieve himself from the responsibility of the assets.

6. Authorization: In a internal control system, all the activities must be authorized by a proper authority. The individual or group which can grant either specific or general authority for transaction s should hold a position commensurate with the nature and significance of the transactions and the policy for such authority should be established by the top management.

7. Managerial supervision and review: The internal control system should be implemented and maintained in conformity with the environmental and elemental changes of the concern. By adapting any specific control system permanently, the extent to which the procedures of flexible controls have been followed in real practice should be observed and re-examined.

5.a. Write a short note on Statutory Report.
5.b. Is Internal Audit an important tool for the management.
Answer:

5.a.

Statutory Report:

Statutory Audit of a public company implies the audit of the transactions of the company which are the subject-matter of the report under section 143. The auditor, however, has to certify as correct only as much of the Statutory Report as relates to the shares allotted by the company, cash received in respect of such shares and other receipts and payments of the company. The auditor, therefore, must:

(a) Examine the internal check with regard to the control over amounts collected. And
(b) Study the Memorandum, Articles of Association and the Prospectus for ascertaining the amount of authorized capital, its composition, terms of issue, particulars of any underwriting contract entered in to, the rate of underwriting commission, shares agreed to be issued for consideration other than cash and particulars of important agreements entered into by the company.

In addition he should carry out an audit of the issue of shares. The under mentioned steps are also necessary:
i. Vouch the payment of the underwriting commission.
ii. Vouch the brokerage paid on issue of share by examining the application and confirming that they bear the stamps of the brokers or agents to whom brokerage has been paid. Refer to minutes of the Directors authorizing the payment of such brokerage. Also see that the provisions of section 40 have not been contravened.
iii. V ouch the payment of preliminary Expenses and see that the amount paid does not exceed the amount fixed by the Articles or the prospectus.
iv. Vouch all other receipts and payments of the company up to date within seven days of the report; pay special attention to receipts and payments on capital account, e.g., sale proceeds of assets acquired from the vendor of the business, payments made to him, purchase of fixed assets, etc.
Check in detail amounts deposited in the bank and withdrawals thereof with the entries in the bank Pass Book. Obtain a certificate from the Bank as to the bank balance as at the date up to which the statutory report has been prepared.

Verify that the amounts receivable and payable which have been adjusted in the books of account but have been excluded from the balance of receipts and payments.

The statutory audit culminates in the preparation of the statutory report. Its main content, with which the audit is concerned, is the abstract of Receipts and Payments made up to a date within 7 days of the report, exhibiting under distinctive heads, receipts of the company from shares, debentures and other sources, payment made and balance left in hand. The Statutory

Report is required to be certified by the auditors of the company, in so far as the report relates to shares allotted by the company, cash received in respect of which the checking of accounts, as per details given above, has been carried out.

5.b.

Internal audit is an important management tool for the following reasons:
a. Internal audit ensures compliance of Companies (Auditors Report) Order, 2016.

b. It ensures compliance of accounting standards and policies.

c. It ensures reliability of MIS through internal audit's independent appraisal and review.

d. It looks into the standard of efficiency of business operation.

e. It can evaluate various problems independently and suggest improvement.

f. This system makes the internal control system effective.

g. It ensures the adequacy, reliability, accuracy and understandability of financial and operational data.

h. It performs as an integral part of 'Management by system'.

i. It can add valuable assistance to management in acquiring new business, promoting new products and expansion or diversification of business etc.

Audit under companies Act

6.a. State the provision related to disqualification of Auditor.
6.b. Discuss the certain services which need not to be rendered by the Auditor.

Answer:

6.a.

The following persons shall not be eligible for appointment as an auditor of a company, namely:—
(a) a body corporate other than a limited liability partnership registered under the Limited Liability Partnership Act, 2008;
(b) an officer or employee of the company;
(c) a person who is a partner, or who is in the employment, of an officer or employee of the company;
(d) a person who, or his relative or partner—
(i) is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company. Provided that the relative may hold security or interest in the company of face value not exceeding one thousand rupees or such sum as may be prescribed;
(ii) is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of such amount as may be prescribed; or

(iii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for such amount as may be prescribed;

(e) a person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed;
(f) a person whose relative is a director or is in the employment of the company as a director or key managerial personnel;
(g) a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies;
(h) a person who has been convicted by a court of an offence involving fraud and a period of ten years has not elapsed from the date of such conviction;
(i) any person whose subsidiary or associate company or any other form of entity, is engaged as on the date of appointment in consulting and specialised services as provided in section 144.

6.b.

AUDITOR NOT TO RENDER CERTAIN SERVICES [SECTION 144]

An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case maybe, but which shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company, namely:—
(a) accounting and book keeping services;
(b) internal audit;
(c) design and implementation of any financial information system;
(d) actuarial services;
(e) investment advisory services;
(f) investment banking services;
(g) rendering of outsourced financial services;
(h) management services; and
(i) any other kind of services as may be prescribed.

Provided that an auditor or audit firm who or which has been performing any non-audit services on or before the commencement of this Act shall comply with the provisions of this section before the closure of the first financial year after the date of such commencement.

Explanation.—For the purposes of this sub-section, the term "directly or indirectly" shall include rendering of services by the auditor,—
(i) in case of auditor being an individual, either himself or through his relative or any other person connected or associated with such individual or through any other entity, whatsoever, in which such individual has significant influence or control, or whose name or trade mark or brand is used by such individual;

(ii) in case of auditor being a firm, either itself or through any of its partners or through its parent, subsidiary or associate entity or through any other entity, whatsoever, in which the firm or any partner of the firm has significant influence or control, or whose name or trade mark or brand is used by the firm or any of its partners.

7.a. Discuss the manner of rotation of auditor by the company before expiry of their term.
7.b. List down the duties of the Auditor.

Answer:

7.a.

The Audit Committee shall recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent.

(1) Where a company is required to constitute an Audit Committee, the Board shall consider the recommendation of such committee, and in other cases, the Board shall itself consider the matter of rotation of auditors and make its recommendation for appointment of the next auditor by the members in annual general meeting.

(2) For the purpose of the rotation of auditors
(i) in case of an auditor (whether an individual or audit firm), the period for which the individual or the firm has held office as auditor prior to the commencement of the Act shall be taken into account for calculating the period of five consecutive years or ten consecutive years, as the case may be;
(ii) the incoming auditor or audit firm shall not be eligible if such auditor or audit firm is associated with the outgoing auditor or audit firm under the same network of audit firms.

Explanation. I - For the purposes of these rules the term "same network" includes the firms operating or functioning, hitherto or in future, under the same brand name, trade name or common control.
Explanation. II - For the purpose of rotation of auditors,-
(a) a break in the term for a continuous period of five years shall be considered as fulfilling the requirement of rotation;

(b) if a partner, who is in charge of an audit firm and also certifies the financial statements of the company, retires from the said firm and joins another firm of chartered accountants, such other firm shall also be ineligible to be appointed for a period of five years.

7.b.

Every auditor of a company shall have a right of access at all times to the books of account and vouchers of the company, whether kept at the registered office of the company or at any other place and shall be entitled to require from the officers of the company such information and explanation as he may consider necessary for the performance of his duties as auditor and amongst other matters inquire into the following matters, namely:—

(a) whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members;

(b) whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company;

(c) where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other securities have been sold at a price less than that at which they were purchased by the company;

(d) whether loans and advances made by the company have been shown as deposits;

(e) whether personal expenses have been charged to revenue account;

(f) where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading. Provided that the auditor of a company which is a holding company shall also have the right of access to the records of all its subsidiaries in so far as it relates to the consolidation of its financial statements with that of its subsidiaries.

8.a. Pankaj Ltd was incorporated on 1St August 2016. Pankaj. Who is related to the chairman of the company, is appointed as the Auditor of the Company by the Board of Director (BOD) at its first meeting on 4th September. Is the appointment is valid as per the provision of the Act prevailing for appointment of Auditor?

8.b. If Annual General Meeting is not held in time, the Auditor automatically vacates his office. Critically comment.

Answer:

8.a.

Under section 141(3)(f) a person whose Relative is a Director or is in the employment of the Company as a Director or Key Managerial Personnel, is not eligible for appointment as Auditor. Hence, Pankaj who is related to the Chairman is primarily not qualified for appointment.

The Board of Director can appoint First Auditor within 30 days from the date of incorporation of the company. In this case, the First Auditor should have been appointed within 30 days i.e within 31st August.

Hence the appointment of Pankaj by the BOD on 4th September is invalid. In this case the company in General Meeting is empowered to make the appointment. Members shall appoint the Auditor within 90 days in an AGM.

8.b.

When AGM is not held:
The Auditor appointment is not for a particular financial year, but from the conclusion of one AGM till the actual conclusion of next 6th AGM, and as ratified by Members at every AGM.
For ratification of Auditors appointment, AGM should be held. Where the AGM is not held, ratification of Auditors appointment cannot be done. Thus the existing auditor shall continue to be the Auditor of the company. The companies act provides that if at any AGM the auditor is not appointed or reappointed the existing auditor shall continue to be the auditor of the Company.[Section 139(10)]

The company duties in this regard:

1. The company should convene a general meeting of the members to appoint a new Auditor or reappoint the retiring auditor
2. When the existing auditor is reappointed the company shall pass a resolution for his re appointed.
3. However where the company proposes to appoint a new auditor, the applicable provisions relating to appointment of auditor should be complied with.

9.a. Mr Pankaj was appointed as Auditor of PKJ Ltd by the board to fill the casual vacancy that arose due to death of the Auditor originally appointed in AGM. Subsequently, Mr Pankaj also regin on health grounds during the tenure of appointment. The board filled this vacancy by appointing you through duly passed Board resolution. Critically comment.

9.b. While conducting the audit of a PKJ Limited company for the year ended 31st March, the Auditor wanted to refer to the minutes book. The Board of Director refused to show the minutes book to the auditor. Explain the position of the auditor as per the provision of the Act.

Answer:

9.a.

Appointment of Auditors in case of Casual Vacancy
A causal vacancy can be filled by BOD within 30 days. If such casual vacancy is caused due to resignation of the existing auditor, the company should approve the same in a General Meeting convened within 90 days on board of director recommendation.

In the given case Mr Pankaj was appointed to fill casual vacancy which was caused due to death of the previous auditor. Subsequently he resigns due to his health problem as auditor of the company and board appoints another auditor through board resolution.

Considering the above provisions, appointment by Board Resolution to fill the Casual Vacancy caused by the resignation is valid. But the appointment should be approved by the Company in a general meeting, convened within 3 months of BOD recommendation. For companies in which an Audit committee u/s 177 is required, the recommendations of that committee shall also be considered for casual vacancy.

9.b.

Section 143(1) lays downs that the company auditor has a right of access at all times to all the books of accounts and vouchers. This includes all statutory records such as minute's book, fixed assets register etc of the company required to be verified for conducting the audit. As part of audit work, it is necessary to refer to the Minutes Book and note the decisions of the director and shareholders. This is required to verify the actions of the company and to vouch specific transactions. If the directors have refused to produce the minute book the auditor may consider extending the audit procedure and to qualify his report in any appropriate manner.
The Auditor shall also report whether he has obtained all information and explanations which to the best of his knowledge and belief, were necessary for the purpose of his audit. This has to be answered in the negative or with a qualification, if minute book is not properly produced to the Auditor. The effect of this aspect in the Financial Statements should also be mentioned.

Cost Audit & Audit Report & Certificate

10.a. Is Rotation applicable to cost auditor. Critically comment.
10.b. Discuss the importance of Audit Report.

Answer:

a. Is Rotation applicable to cost auditor
The provisions for maintenance of cost accounting records and cost audit are governed by Section 148 of the Companies Act, 2013. The provisions of Section 148 clearly states that no person appointed under Section 139 as an auditor of the company shall be appointed for conducting audit of cost records of the company. Section 148 also provides that qualifications, disqualifications, rights, duties and obligations applicable to auditors (financial) shall apply to a cost auditor appointed under this section. The eligibility, qualifications and disqualifications are provided in Section 141 of the Act and powers and duties are provided in Section 143. Section 143(14) specifically states that the provisions of Section 143 shall mutatis mutandis apply to a cost auditor appointed under Section 148. There are no other provisions governing the appointment of a cost auditor. Section 139(3) of the Act, applicable to appointment of auditors (financial), and Rule 6 of Companies (Audit and Auditors) Rules, 2014 deals with the provision of rotation of auditors and these provisions are applicable only to appointment of auditors (financial). The Act does not provide for rotation in case of appointment of cost auditors and the same is not

applicable to a cost auditor. It may, however, be noted that though there is no statutory provision for rotation of cost auditors, individual companies may do so as a part of their policy, as is the practice with Public Sector Undertakings.

b. Importance of Audit Report.
i. An Audit report is the end product of the auditing and is very important & concluding part of the audit process.
ii. Audit report gives the auditor's opinion on the accounts & record of the company, as examined by him.
iii. Audit Report reflects the work done by the auditor.
iv. Audit report is the instrument which, measures the auditors responsibility in regard to the true & fairness of the financial statement of the company.
v. Audit Report indicates the real position of the financial status of the company & which is used by different people as a reliable document.

11.a. Pankaj Limited, requiring to maintain Cost Accounts and Records contends that the auditor need not to report on the non maintenance of Cost Records as because the provision related to the Cost Audit is not made applicable to them. As an auditor how would you react to the above situation.

11.b. Discuss the significance of Opening Paragraph.

Answer:

a.
As per section 148(1) requires that every company shall maintain books of accounts containing particulars relating to utillisation of material or labour or other items of cost, if such class of company is notified by the Central Government. Where maintenance of cost records has been prescribed which includes these Cost accounts and records as prescribed by the Central Government. The Auditor of the company need to go for in-depth audit of cost records rather he need to determine whether the records maintained are prima facie complete in all respect.
So we may conclude that in the present case the auditor should report for non maintenance of the cost records.

b. Significance of Opening Paragraph:
(a) The Opening or Introductory Paragraph identifies the Financial Statements of the entity that have been audited, including the date of and period covered by the Financial Statements.
(b) The 'Opening Paragraph' seeks to bring to the notice of the Users of Financial Statements, that preparation of the accounts is the responsibility of the Management of the enterprise, whereas the responsibility of the Auditor is to express an opinion on the said accounts based on the audit carried out by him.
(c) Through the Opening Paragraph, the Auditor communicates the basic message that the preparation of Financial Statements requires Management to make significant accounting

estimates and judgements, as well as to determine the appropriate accounting principles and methods used in preparation of the said Financial Statements.

Auditing of different types of undertaking

12.a. List down the steps taken by the Auditor for conducting the audit of Hospital.
12.b. Discuss the significance of Scope Paragraph.

Answer:

a. Audit of 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 therefrom is not utilized for any other purposes.
(viii) Where receipts of subscription show a 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.

Significance of Scope Paragraph:
(a) The 'Scope Paragraph' seeks to inform the Users about the practices and procedures followed in the conduct of audit by the Auditor.
(b) In the Scope Paragraph, the Auditor states that the audit was planned and performed in accordance with Auditing Standards generally accepted in India, and also that the audit provides a reasonable basis for his opinion.
(c) The significance of the Scope Paragraph lies in the fact that the Auditor intends to convey to the readers of his report, about the scope of audit by highlighting the nature and progress of audit. The test check approach of audit adopted by the Auditor in performing his audit work as also the significant aspect of evaluation of accounting principles and accounting estimates is also clarified.
(d) The basic objective of auditing that the Auditor provides only "reasonable assurance" is emphasized in the Scope Paragraph. Thus, this paragraph signifies the inherent limitations of audit.

Vouching & Verification

13.a. As an Auditor state how will you verify 'Loans and Advances' appearing in the financial statement of the company.
13.b. Discuss the basic element if Audit report.

Answer:

a.
Loans and advances may be different types like
(1) Loans against the security of Land & Building.
(2) Loans against the security of goods.
(3) Loans against the security of stocks & shares.
(4) Loans against the security of Insurance Policies.
(5) Loans against the personal security of the borrower.

Therefore, in each case the duty of auditor in general is as under:
(i) Examine whether a proper loan ledger has been maintained upto date or not.

(ii) Examination of the Security ledger against each loan.

(iii) Examine the loan agreement and find out the rate of interest, due dates of installments, penalty, interest etc.

(iv) Ascertain whether any loan is doubtful of recovery. In case it is doubtful, a provision for the expected loss is to be made.

(v) Verify that loans have got proper sanction from the authority.

(vi) Obtain a letter of confirmation from the parties to whom loans are advanced. In case of loans to directors, prior approval of the Central Government is obtained.

b. Basic element of Audit report: The basic element of Audit report is enumerated below;

1. Title
2. Addressee
3. Opening or Introductory Paragraph:
4. Scope Paragraph
5. Opinion Paragraph
6. Date of the Report
7. Place of Signature
8. Auditor's Signature

Short Notes

14. Write Short Notes on the followings
a. Disclaimer of Opinion
b. Joint Audit
c. Audit of Municipalities and Panchayats (Local Bodies)

Answer:

a. Disclaimer of Opinion
A Disclaimer of Opinion Report is given when the Auditor is unable to form an overall opinion about the matters contained in the Financial Statements.

A Disclaimer of Opinion should be expressed when the possible effect of a limitation on scope is so material and pervasive that the Auditor has not been able to obtain sufficient appropriate audit evidence and is, accordingly, unable to express an opinion on the Financial Statements.

It may happen in situations such as -- (a) when books of account of the Company seized by Income-Tax Authorities, (b) when it is not possible for the Auditor to obtain certain information or (c) when scope of audit work is restricted.

The Auditor will state in his Report that he is unable to term an opinion on the Financial Statements. Such Report is called as "Disclaimer of Opinion Report".

b. Joint Audit

In big corporate more than one persons or firm of Chartered Accountants are appointed as a Joint Auditor for conducting the audit of the company. This practice of appointing joint auditor accrues great advantages to the company. In a big organisation the task of carrying audit cannot be accomplished with single individual so for overcoming such situation joint auditor whereas appointed.

Advantages of Joint Audit: The various advantages that accrue out of Joint Audit are enumerated below;

i. Lower workload
ii. Timely completion of work
iii. Sharing of expertise
iv. Improved quality of services
v. Healthy competition
vi. Quality of performance
Disadvantages of Joint Audit: The disadvantages of Joint Audit are enumerated below;
i. Superiority complex of some auditor
ii. Costly for small entity
iii. Lack of coordination in work
iv. Uncertainty about liability of work
v. Psychological problem
vi. Difficulty in fixation of work among other

c. Audit of Municipalities and Panchayats (Local Bodies)
The major objective of audit of Municipalities and Panchayats are enumerated below;
(i) To ensure on the fairness and correctness of contents in the Financial Statement
(ii) To report on adequacy of Internal control
(iii) To ensure value of money is fully received on amount spent.
(iv) To detect the frauds and errors.

The following points are to be considered necessary for carrying on audit of Municipalities and panchayats (Local Bodies);

(i) To ensure that the expediters incurred conform to the relevant provision of the law and is in accordance with the financial Rules and regulation formed by the compliant authority.
(ii) To encase that sanction is accorded by the competent authority either special or general.
(iii) To encase that there is provision of funds for expenditure and is authorized by competent Authority.
(iv) To ensure that where huge financial expenditure is made is run economically and is expected to contribute growth.

15. Write Short Notes on the followings
a. Cut off Procedure
b. Need of Internal Audit
c. Audit Committee- Section 177

Answer:

a. Cut off Procedure

i) Definition: Periods usually coincide with calendar months, which lead to the need for specific demarcation between transactions forming the part of one period from those included in the following period. Thus, cut-off procedures are adopted to allocate revenues and costs to the proper accounting period.

ii) Areas of concern: Close attention should be paid to the accounts payable and accounts receivable functions. These two functions are the most susceptible to recording of transactions in the wrong accounting period.

iii) Cut-off points: Serially numbered documents like invoice for sales or purchase bills are allocated to the respective accounting periods by establishing cut-off points based on the serial numbers.

iv) Importance: Cut-off procedures require detailed testing by the auditor so as to ensure proper accounting of assets and liabilities, which may arise without the corresponding physical delivery of goods taking place.

v) Example: The purchase procedure involves a number of steps, like issuing purchase requisitions, inviting quotations, selecting sellers and defining the terms of purchase, entering agreement, receipt of goods, storage of goods, payment, etc. All the documents and vouchers that substantiate the proof of authentication of these transactions are serially numbered. It is the auditor's duty to examine the cut-off points and ensure that the transaction has been recorded in the period in which the title in goods is transferred, irrespective of the period of physical delivery of goods and to ensure compliance of the Indian Accounting Standards and the relevant Statute.

b. Need of Internal Audit:

The need for internal audit has becoming in demand due to the enunciated reasons:

i. Increased size and complexity of businesses.

ii. Enhanced compliance requirements.

iii. Focus on risk management and internal controls to manage them.

iv. Unconventional business models.

v. Intensive use of information technology.

vi. Stringent norms mandated by regulators to protect investors.

vii. An increasingly competitive environment.

c. Audit Committee- Section 177

Constitution of an Audit committee is mandatory for the;

(i) Every listed Company; and

(ii) Such directors or classes of the companies, as may be prescribed.

As per the Rule 6 of the Companies (Meetings of the Board and its Power) Rules, 2014 following class of the companies have been prescribed for this purpose;

(i) All public companies with a paid up share capital ₹ 10 Crore or more;

(ii) All Public Companies having turnover of ₹ 100 Crore or more;

(iii) All Public Companies having in aggregate, outstanding Loans, or borrowings and debentures or deposits exceeding ₹ 50 Crore or more.

An Audit committee shall have minimum 3 Directors majority of them should be Independent Director. Majority of the member of the Audit Committee able to read & understand the financial statement.

Function of Audit Committee: The various Functions of the Audit Committee is enumerated below;

(i) For the appointment and fixation of the remuneration of Auditor.

(ii) Examination of the Financial Statement.

(iii) Scrutiny of Inter Corporate Loans and Investment,

(iv) Valuation of the Assets of the Company,

(v) Evaluation of the internal financial control and risk management system of the entity.

(vi) Evaluation of the use of the funds rose through public offers.

(vii) Evaluation of any related party transaction.

Powers of the Audit Committee: The powers of the Audit Committee are enumerated below;

(i) Audit Committee has the power to call for comments of the Auditor about Internal Control Systems and the scope of the Audit including its observation.

(ii) Before submission of the report to the Board the Audit Committee have the power to review the Financial Statement.

(iii) Power to discuss any issues with the Statutory & Internal Auditor and the Management of the Company in relation to matter contained in the Financial Statement.

16. Write Short Notes on the followings
a. Audit Note Book
b. Qualified Opinion/ Report
c. Audit certificate

Answer:

a. Audit Note Book

An audit book is usually a bound book in which a large variety of maters observed during the course of audit are recorded. The audit note book is a permanent record of the auditor. For each individual audit, the auditor usually maintains a separate audit note book. The audit note book should be maintained clearly, completely and systematically. An audit note book is a great evidential tool available as a defense with the auditors in the event of any charge is brought against them. In case of City Equitable Fire Insurance Company, the auditors were relieved because they have maintained record of the audit work performed at each stage.

Contents of Audit Note Book

i. Name of the business enterprise.
ii. Organisation structure.
iii. Important provisions of Memorandum of Association (MOA) and Articles of Association (AOA).
iv. Communication with the previous auditor, if any.
v. Management representations and instructions.
vi. List of books of accounts maintained by the enterprise.
vii. Accounting methods, internal control systems followed by the enterprise, applicable laws etc.
viii. Key management personnel.
ix. Errors and fraud discovered.
x. Matters requiring explanations or clarifications.
xi. Special points that need attention in the audit report.

b. Qualified Opinion/ Report

A Qualified Audit Report is one where an Auditor gives an opinion on the truth and fairness of Financial Statements, subject to certain reservations.

ii. The Auditor's Reservation is generally stated as: "Subject to the above, we report that the Balance Sheet shows a true and fair view."

iii. The overall impact of all reservations or qualification taken together is not material enough to vitiate the overall true and fair view of Financial Statements, but it is important that such a matter(s) should be brought to the attention of the shareholders.

iv. The Report should also give detailed reasons along with quantitative impact on the qualifications on Financial Statements.

A Qualified Opinion should be expressed when the Auditor concludes that –

(a) An Unqualified Opinion cannot he expressed, or

(b) The effect of any disagreement with Management is not so material and pervasive as to require an Adverse Opinion, or

(c) The Limitation on scope is not so material and pervasive as to require a Disclaimer of Opinion.

c. Audit certificate

Sometimes apart from an audit report for general use, an auditor is often called upon to give a certificate for special purpose. The certificate should include the following: —

i. Auditor should see that there is a suitable declaration by the management about the subject matter.

ii. Auditor should give the certificate on his letter head or on stationary carrying his name and address to avoid misunderstanding.

iii. Auditor should clearly state his limitations and indicate the extent to which he has relied upon a technical expert if any.

iv. Auditor should indicate the specific record covered by the certificate.

v. Auditor should mention the manner in which the audit was conducted.

vi. Auditor should indicate in the certificate if he has made certain fundamental assumptions. Auditor should make a reference to the information and explanations obtained. Auditor should give clear title to it, indicating whether it is a report or a certificate.

vii. Auditor should mention whether he has used any general purpose statement like Profit & Loss Account for his investigation and also, state whether that general purpose statement has been audited by other auditors.

viii. Auditor should be careful while interpreting any law related matter, he should clearly mention that he is expressing merely his own opinion.

ix. Auditor should see that the certificate should be self contained documents. Auditor should clearly mention the responsibility assumed by him.

x. Auditor should, if he has referred the audited statements, clearly mention that the figures are used from the audited statements and relied upon.

xi. Auditor should address the certificate to the client or the Public Authority or the person requiring it as the case may be. In appropriate circumstances it may be issued by using the words as “to whom so ever it may concern“.