Final
Group IV
Paper 19 : COST AND MANAGEMENT AUDIT
(SYLLABUS – 2016)

Objectives

1. Multiple Choice Questions:

(1) Choose the correct option among four alternative answers. (1 mark for correct choice, 1 mark for justification.)

(i) Rule 4 of the Companies (Cost Records and Audit) Rules, 2014 deals with:
(A) Application of Cost Records
(B) Application of Cost Audit
(C)Appointment of Cost Auditor
(D) Cost Audit Report.

(ii) Abnormal Loss due to flood or earthquake is charged to:
(A) Administrative Overhead Cost
(B)Material Cost
(C)Costing Profit and Loss Account
(D) Selling and Distribution Cost

(iii) XBRL is a language based on :
(A)XBL family of languages.
(B)XRL family of languages.
(C)XML family of languages .
(D) XGL family of languages.

(iv) Costing Taxonomy is best defined as a:
(A)Dictionary
(B)Made easy.
(C)Tax Ready Reckoner
(D)Referencer.

(v) Part B of the Annexure to Cost Audit Report deals:
(A)Service Sector
(B) Manufacturing Sector
(C)Both manufacturing and service sector
(D) None of the above.

(vi) The forex component of imported material is converted at the rate on :
(A) Date of Payment
(B) Date of Transaction

(C)Either of A or B
(D) None of A and B

(vii)KPI can be:
(A) Quantitative
(B) Qualitative
(C)Actionable
(D)All of the above.

(viii)CAS 14 deals with:
(A)Repair and Maintenance Cost.
(B)Pollution Control Cost
(C)Direct Expenses
(D)Packing material cost.

(ix)Operating Expense does not include:
(A)Rent
(B)Equipment
(C)Interest
(D)Payroll

(x) Outward transportation cost shall form part of :
(A) Cost of material
(B) Cost of Sale
(C) Packing material
(D)Administration Overhead

Ans:

(i) (B) Application of Cost Audit. Rule 4 of the Companies (Cost Records and Audit) Rules, 2014 prescribes the turnover based threshold limits for applicability of Cost Audit.

(ii) (C)Costing Profit and Loss Account. Rule 5(1) prescribes that any abnormal cost/loss should not be part of Material, Administrative or Selling and Distribution overheads or any other item of cost.

(iii) (C)XML family of languages . XBRL belongs to Extensible Markup Language family. It has been defined specifically to meet requirements of business and financial information.

(iv) (A)Dictionary. Costing Taxonomy is a dictionary of all cost elements required in cost audit report and compliance report.

(v) (B) Manufacturing Sector. This is as per Companies(Cost Records and Audit) Rules, 2014.

(vi) (B) Date of Transaction. This is as per CAS 6.

(vii) (D)All of the above. Key Performance Indicators are simply the variables, independent or inter-dependent, in respect of which goals can be set and performance can be measured to assess whether it is in furtherance of the enterprise objectives. These may be quantitative, qualitative, actionable, or trends.

(viii) (B)Pollution Control Cost**.** This standard deals with the principles and methods of classification, measurement and assignment of pollution control costs, for determination of Cost of product or service, and the presentation and disclosure in cost statements

(ix) (C)Interest. Operating expenses typically exclude interest expense, nonrecurring items (such as accounting adjustments, legal judgments, or one-time transactions), and other income statement items not directly related to a company's core business operations.

(x) (B) Cost of Sale. This is as per CAS 5

Subjective

2 (a) (i) A paper manufacturing company having turnover of ₹ 90 crore, in the year 2017-18 was incorporated in 2016-17 and commenced its production from March, 2017. From which financial year, the Cost Audit will be applicable?

(ii) Whether maintenance of Cost Accounting Records and Cost Audit thereof, subject to threshold limits prescribed, is applicable to products which are for 100% captive consumption?

(b) Mr. K was appointed as Cost Auditor of MNC Ltd. for the Financial Year 2017-18. State

(i) How long the Cost Auditor can continue to hold office for the financial year?

(ii) In what format the Cost Auditor shall submit his/her Report?

(iii) What was the formality to be observed by the Board of Directors if the cost Auditor did resign on 31.01.2018?

Ans: 2(a)(i)

Rule 3 of the Companies (Cost Records and Audit) Rules, 2014, states that every company, engaged in the production of goods or providing services specified in the Rules, shall maintain Cost Records if the overall turnover from all its product and services is Rs. thirty five crore or more during the immediately preceding financial year.

Applicability for Cost audit [Rule 4]
(1) Every company specified in item (A) of Rule 3 [Regulated Sector] shall get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is rupees fifty crore or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under rule 3 is rupees twenty five crore or more.
(2) Every company specified in item (B) of Rule 3 [Non –regulated Sector] shall get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is rupees one hundred crore or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under rule 3 is rupees thirty five crore or more.

In the present case, the Paper Industry falls under the Non-Regulated Sector and is required to maintain cost records from the Financial Year 2018-19 but is not required to get its cost records audited from the same year since it did not cross the threshold limit in the preceding financial year 2017-18.

2(a)(ii)

The Companies (Cost Records and Audit) Rules, 2014, has specified different products and services for which maintenance of cost accounting records and Cost Audit thereof, subject to threshold limits prescribed, are mandatory.

In case a product is manufactured and 100% captively consumed for production of some other product which is also covered under the Rules and is subject to Cost Audit, then the cost of such captively consumed product would form part of the final product which is also under cost Audit and as such a separate Cost Audit Report for the captively consumed product will not be necessary;

If the product, however is partly for captive consumption and is partly sold, or if the product is 100% captively consumed for production of some other product which is not covered under the Rules, then Cost Audit would be applicable for such captively consumed product.

2(b) (i) Rule 6(3) of the Companies (Cost Records and Audit) Rules, 2014, states that every Cost Auditor appointed by the Company shall continue in such capacity till the expiry of one hundred eighty days from the closure of the financial year or till he/she submits the Cost Audit Report for the financial year for which he /she has been appointed.

(ii) According to Rule 6(4) of the Companies(Cost Records and Audit) Rules, 2014 every cost auditor, who conducts an audit of the cost records of a company, shall submit the cost audit report along with his or its reservations or qualifications or observations or suggestions, if any, in form **CRA-3.**
(iii) As per Rule 6(3) of the Companies (Cost Records and Audit) Rules, 2014, any casual vacancy in the office of the Cost Auditor, by resignation or otherwise, shall be filled by the Board of Directors within 30 days of occurrence of such vacancy. The procedure followed for such appointment shall be the same as that of fresh appointment. The company shall inform the Central Government in Form CRA 2 within 30 days of such appointment of Cost Auditor.

3(a) SHARATHI LTD. a tyre and tube manufacturing company is having turnover of ₹75 crores from all its activities. The company has filed its prospectus with SEBI for a public issue of equity shares and it hopes to complete the public offering by September, 2018 end.
Whether cost audit will become applicable to the company? If yes, then from which financial year will cost audit become applicable?

(b)(i) Whether Value addition and distribution of earnings [Part D, Para 3] is to be computed based on Cost record data or audited financial data?
(ii) Whether Financial position and ratio analysis [Part D, Para 4] is to be computed based on Cost record data or audited financial data?

Ans:

3(a) According to Rule 4(2) of the Companies(Cost Records and Audit) Rules , 2014, every company specified in item (B) of rule 3 shall get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is **rupees one hundred crore** or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under rule 3 is **rupees thirty five crore or more.**
Conclusion:

(i) In this case the company does not fall under the criteria mention under Rule 4 (2) of the Companies (Cost Records and Audit) Rules, 2014 . Hence it is not required to undertake cost audit.
(ii)The company is in the process of listing on a stock exchange in India which will nowhere affect the applicability of the Companies (Cost Records and Audit) Rules, 2014. Hence, the company is not required to gets its cost records audited.

3(b)(i) Value Addition statement is to be computed based on audited financial accounts.
(ii) Financial Position and Ratio Analysis is to be computed based on audited financial accounts. This reporting Para has been aligned with the nomenclature of schedule iii of the Companies Act, 2013

4) Explain whether the following amounts to professional misconduct by a Cost Accountant:
(a) A , a practicing CMA, B is a practicing Advocate representing matters in courts of law. A and B agree to help each other in matters involving their professional expertise. Accordingly A recommends B in all tax litigations in courts of law. B consults A on all matters relating to costing and related matters, which come to him for arguing in various courts of law. They agree to 'share' the remuneration.

(b) Q, a CMA , certifies a financial forecast of his client which was forwarded to the client's bank based on which the bank sanctioned a loan to the client.

Ans:

(a) A CMA in practice shall be deemed to be guilty of professional misconduct if he either directly or indirectly shares commission or brokerage in the fees or profits of his professional business to any other than member of the Institute or accepts any part of the profits of the professional work of a lawyer, broker, etc. who is not a member of the Institute. Thus, as per Clauses 2 and 3 of Part I of the First Schedule to the Cost and Works Accountants Act, 1959 a member in practice can neither share fees or profits with a person who is not a member of the Institute nor he is permitted to receive and share the fees of other such as lawyers, engineers, etc.
A and B therefore cannot "share" any remuneration. They may, however, remunerate each other for "professional" services rendered on any reasonable basis separately which would be on time basis at rates depending on the extent of expertise. It is, however, important that care should be taken by the member not to extend his service beyond the normal sphere of professional practice and any reports or recommendations should clearly delimit the responsibilities assumed and services rendered.

(b) Under Clause (3) of Part I of Second Schedule to the Cost and Works Accountants Act, 1959, a CMA in practice is deemed to be guilty of professional misconduct if he permits his name or the name of his firm to be used in connection with an estimate of cost or earnings contingent upon future transactions in a manner which may lead to the belief that he vouches for the accuracy of the forecast. Accuracy does not refer to arithmetical accuracy. All forecasts are estimates based on certain assumptions duly evaluated on a consideration of various relevant factors and cannot be ascertained with accuracy. But, first of all, he should clearly indicate in his report the sources of information, the basis of forecasts and also the major assumptions made in arriving at the forecasts and, secondly, he should not vouch for the accuracy of the forecasts. In the instant case, CMA. Q is deemed to be guilty as it appears that he has certified the financial forecast without taking adequate safeguards.

5) Which of the following acts amount to professional misconduct on the part of a practicing Cost and Management Accountant?
(a) A firm of Cost Accountants undertake the Cost Audit of a Company. The audit work is conducted by one of the partners and two assistants. The report is however signed by another partner.

(b) Mr. X, a CMA was invited by the Chamber of Commerce to present a paper in a symposium on the issues facing Indian Jute Industry. During the course of his presentation he shared some of the vital information of his client's business under the impression that it will help the Nation to compete with other countries at international level.

Ans:

(a) Since the certificate is signed by a Cost Accountant in practice who is also a partner of the firm, the act of signing report doesnot amount to professional misconduct.

(b) Clause (1) of Part I of the Second Schedule to the Cost and Works Accountants Act, 1959 deals with the professional misconduct relating to the disclosure of information by a CMA in practice relating to the business of his clients to any person other than his client without the consent of his client or otherwise than as required by any law for the time being in force would amount to breach of confidence. The Code of Ethics further clarifies that such a duty continues even after completion of the assignment. The CMA may, however, disclose the information in case it is required as a part of performance of his professional duties. In the given case, Mr. X has disclosed vital information of his client's business without the consent of the client under the impression that it will help the nation to compete with other countries at International level. Thus it is a professional misconduct covered by clause(1) of Part I of Second Schedule to the Cost and Works Accountants Act, 1959.

6(a) Trial Balance as on 31.3.2017 *(relevant extracts only)*

Particulars	₹	Particulars	₹
Materials consumed	**2500000**	**Special Subsidy received from Government towards Employee salary**	**275000**
Salaries	**1500000**	**Recoverable amount from Employee out of perquisites extended**	**35000**
Employee training cost	**200000**		
Perquisites to Employees	**450000**		
Contribution to Gratuity Fund	**400000**		
Lease rent for accommodation provided to employees	**300000**		
Festival bonus	**50000**		
Unamortised amount of Employee cost related to a discontinued operation	**90000**		

Compute Employee Cost as per CAS 7

(b) How would you treat the following costs under Generally Accepted Cost Accounting Principles ?

- **i) Material acquired in exchange for other materials.**
- **ii) Employee share options.**
- **iii) Moisture losses in material in transit or storage.**
- **iv) Annual Maintenance Contracts(AMC).**

Ans:

6(a) Computation of Employee Cost

	Particulars	₹
	Salaries	1500000
Add	Net Cost of Perquisites to Employees = Cost of Perquisites (-) amount recoverable from employee = 4,50,000 (-) 35,000	415000
Add	Lease rent paid for accommodation provided to employee	300000
Add	Festival Bonus	50000
Add	Contribution to Gratuity Fund	400000
Less	Special subsidy received from Government towards employee salary	(275000)
	Employee Cost	**2390000**

Note:

i) i)Recoverable amount from employee is excluded from the cost of perquisites.

ii) ii)Employee training cost is not an employee cost. It is to be treated as an Overhead, hence, not included.

iii) iii)Special subsidy received is to be excluded, as it reduces the cost of the employer.

iv) iv)Unamortized amount of employee cost related to a discontinued operation is not an includible item of cost.

6(b) i) Where a material is acquired in exchange for other materials or services supplied, the cost of material acquired is taken as the cost of material supplied or services provided plus other applicable cost such as freight.

For e. g in Paper Industry, bagasse from the Sugar Mills is obtained mills by supplying coal to the sugar mills, in the cost statement , the cost of coal supplied is considered as the cost of bagasse procured.

ii) Cost of employee share options is treated as part of employee cost provided the same is not a notional cost and involves an actual cash outlay.

iii) Since most technical calculations are based on dry weight , it is advisable to account for materials which absorb moisture on a dry weight basis grossing up the rate. Dry weight can be air dry or bone dry. In case of wood used in paper industry, given that wood contains moisture, the rate for wood is accounted on the basis of Air Dry Weight which may be obtained after deducting standard or average moisture contents of such wood. Alternatively it can be accounted on bone dry weight after deducting the entire moisture on actual basis.

iv) It is usual to have Annual Maintenance Contracts(AMC) for specialised equipments particularly electronic equipments subject to sudden failures. These take the form of only servicing or servicing with parts(comprehensive). The AMCs specify the number of routine servicing calls that will be made in a year. Where a single machine is covered by AMC, costs get allocated to that machine. But where a fleet of machines are covered by single AMC, allocation of costs to cost centres can be made on basis of number of machines in each cost centre. Where the machines in various cost centres require different levels of service or vary in cost, a suitable allocation base has to be evolved based on such differences.

7(a) Purchase of Materials ₹ 3,00,000 (inclusive of Trade Discount ₹ 3,000); Fee on Board ₹ 12,000; Import Duty paid ₹ 15,000; Freight inward ₹ 20,000; Insurance paid for import by sea ₹ 10,000; Rebates allowed ₹ 4,000; Cash discount ₹ 3,000; CENVAT Credit refundable ₹ 7,000; Subsidy received from the Government for importation of these materials ₹ 20,000. Compute the landed cost of material (i.e. value of receipt of material).

(b)Answer the following with reference to CAS 24.
i)What do you understand by Net sales realization?
ii)What is reporting period?
iii)What is revenue from operations?
iv) What is the guideline for assignment of revenue?

Ans:

7(a) Computation of Material Cost Sheet

	Particulars	**Amount (₹)**
	Purchase price of Material	3,00,000
Add:	Fee on Board	12,000
Add:	Import Duties of purchasing the material	15,000
Add:	Freight Inward during the procurement of material	20,000
Add:	Insurance paid	10,000
	Total	**3,57,000**
Less:	Trade Discount	3,000
Less:	Rebates	4,000
Less:	CENVAT Credit refundable	7,000
Less:	Subsidy received from the Government for importation of materials	20,000
	Value of Receipt of Material	**3,23,000**

Note:
(i) Cash discount is not allowed, as it is a financial item.
(ii) Subsidy received, rebates and CENVAT Credit refundable are to be deducted for the purpose of computing the material cost.

(b)(i) Net Sales Realization: is the revenue from operations net of discounts and indirect taxes.
(ii) Reporting Period: is the period for which the cost statements are prepared.
(iii) Revenue from operations: is the income arising in the course of the ordinary activities of an entity from the sale of goods or rendering of services.
(iv) Revenue for each type of product or service shall be assigned directly to that product or service to the extent it is economically feasible. economic feasibility implies that it is practically feasible to assign the revenue to a particular product or service with reasonable cost and efforts. Reasonable cost and efforts are matters of judgment.

8 (a) How would you compute cost of utilities as per CAS 8 in following circumstances?
i) Utilities generated for the purpose of inter unit transfers.
ii) Utilities generated for the inter company transfers .

(b) How would you treat the following as per CAS 9 related to Packing Material Cost?
i) Primary and Secondary packing material cost.
ii) Finance cost directly attributable to packing material.

Ans:

8(a)(i) Cost of utilities generated for the purpose of inter unit transfers shall comprise of direct material cost, direct employee cost, direct expenses , factory overheads and the distribution cost incurred for such transfers.

(ii) Cost of Utilities generated for the inter company transfers shall comprise direct material cost, direct employee cost, direct expenses, factory overheads, distribution cost and share of administrative overheads.

8(b) (i) Cost of primary packing materials shall form part of the cost of production.

Cost of secondary packing materials shall form part of distribution overheads

(ii) Finance costs directly incurred in connection with the acquisition of Packing Material shall not form part of Packing Material Cost.

9 Answer the following questions with respect to Cost Auditing standard 102.
(i) What is the objective of the standard?
(ii)What do you understand by audit documentation?
(iii) What is 'Firm'?
(iv)How long Cost Audit documentation be retained?

Ans:

9

(i) The objective of Cost Auditing standard 102 is to guide the members to prepare documentation that provides:
   (a) A sufficient and appropriate record of the basis for the Cost Auditor's Report; and
   (b) Evidence that the audit was planned and performed in accordance with Cost Auditing Standards and applicable legal & regulatory requirements.

(ii) Audit Documentation means the records, in physical or electronic form, including working papers prepared by and for, or obtained and retained by the Cost auditor, in connection with the performance of the audit.

(iii) Firm means a sole practitioner, partnership including LLP (Limited Liability Partnership or any other entity of professional cost accountants as may be permitted by law and constituted under The Cost and Works Accountants Act & Regulations.

(iv) The cost audit documentation should be retained for at least ten years from the date of the cost audit Report.

10) Answer the following questions with respect to Cost Auditing standard 104.
(i) What is the objective of the standard?
(ii) What is overall audit strategy?
(iii)What point to be evaluated regarding IT environment of an entity?
(iv)What is the effective date of the standard?

Ans:

(i) The objective of this standard is to enable the cost auditor to have knowledge of the client's business which is sufficient to identify and understand the events, transactions and practices that, in the cost auditor's judgment may have a significant effect on the examination of cost statements or on the preparation of the cost audit report.
(ii) Overall Audit Strategy sets the scope, timing and direction of the audit, and guides the development of the detailed audit plan.
(iii) The cost auditor should assess the following with regard to IT environment and controls.
  (i) Reliance on systems or programs that are inaccurately processing data, processing inaccurate data, or both.
  (ii) Unauthorized access to data that may result in destruction of data or improper changes to data, including the recording of unauthorized or non-existent transactions, or inaccurate recording of transactions. Particular risks may arise where multiple users access a common database
  (iii) The possibility of it personnel gaining access to privileges beyond those necessary to perform their assigned duties thereby breaking down segregation of duties.
  (iv) Unauthorized changes to data in master files.
  (v) Unauthorized changes to systems or programs.
  (vi) Failure to make necessary changes to systems or programs.
  (vii) Inappropriate manual interventions.
  (viii) Potential loss of data or inability to access data as required.

(iv) This standard is effective for audits on or after September 11, 2015.

11) The Cost Accountant of TRINCUS TEXTILES MILLS LTD. has arrived at a Profit of ₹ 20,10,500 based on Cost Accounting Records for the year ended March 31, 2017. Profit as per Financial Accounts is ₹22,14,100.

As a Cost Auditor, you find the following differences between the Financial Accounts and Cost Accounts:

		₹
(1)	**Profit on Sale of Fixed Assets**	**2,05,000**
(2)	**Loss on Sale of Investments**	**33,600**
(3)	**Voluntary Retirement Compensation included in Salary & Wages in F/A**	**50,25,000**
(4)	**Donation Paid**	**75,000**
(5)	**Insurance Claim relating to previous year received during the year**	**5,08,700**

(6)	**Profit from Retail trading activity**	**32,02,430**
(7)	**Interest Income from Inter-Corporate Deposits**	**6,15,000**
(8)	**Decrease in value of Closing WIP and Finished goods inventory**	
	as per Financial Accounts	**3,82,06,430**
	as per Cost Accounts	**3,90,12,500**

You are required to prepare a Reconciliation Statement between the two Accounts for the year ended March 31, 2017.

Ans:

RECONCILIATION OF PROFIT BETWEEN COST AND FINANCIAL ACCOUNTS FOR

THE YEAR ENDED MARCH 31. 2017

	₹	₹
Profit as per Financial Accounts:		22,14,100
Add: Loss on sale of investments	33,600	
Add: Voluntary Retirement compensation included in salary	50,25,000	
and wages in F/A - Not included in cost A/c	75,000	51,33,600
Add: Donation paid		73,47,700
Less: Profit on Sale of Fixed Assets-Not considered in cost A/c	2,05,000	
Less: Receipts of insurance claim related to previous year	5,08,700	
Less: Profit from Retail trading activity	32,02,430	
Less: Interest income from inter-corporate deposit-not considered in cost accounts	6,15,000	
Less: Difference in valuation of stock:		
Decrease in inventories as per cost accounts 3,90,12,500		
Decrease in inventories as per financial accounts 3,82,06,430	8,06,070	53,37,200
Profit as per Cost Accounts		20,10,500

12) In the Financial Accounts of CHEMICALS & FERTILIZERS LTD. for the year ended March 31,2017 the profit was ₹898,07,500. The profit as per Cost Accounting records for the same period was less. The following details are extracted from the accounting schedules and Cost Accounting records of the company.

	Financial Accounts ₹ 000	**Cost Accounts ₹000**
Opening : Semi Finished Goods	**31700**	**35210**
: Finished Goods	**83220**	**78590**
Closing : Semi Finished Goods	**35260**	**39420**
: Finished Goods	**89320**	**80450**
Urea & Transport subsidy	**348**	
Expenses on CSR	**56**	
Profit on sale of Fixed Assets	**150**	
Chemical used internally	**382**	**365**
Favourable Exch. Rate variation	**294**	

Post-retirement Medical grant	**584**	
Purchase Tax Refund	**453**	
Litigation Recovery-Prior year	**125**	

You are required to prepare a Reconciliation Statement and arrive at the Profit as per Cost Records for the year ended March 31, 2017.

Ans: CHEMICALS & FERTILIZERS LTD.

Reconciliation of Financial Profit and Costing Profit for the year ended March 31, 2017

Amount in ₹ thousand

Profit or loss as per Financial Accounts		89807.50
A. Less: Incomes not considered in Cost Accounts: i. Profit on sale of Fixed Assets ii. Urea & Transport Subsidy iii. Litigation Recovery-Prior year iv. Favorable Exch. Rate Variation v. Purchase tax Refund vi. Own consumption (chemicals) valuation difference (382-365)	 150 348 125 294 453 17	(1387.00)
B. Add: Expenses not considered in Cost Accounts i. Expenses on CSR ii. Post-retirement medical grant	 56 584	640.00
C. Less: Difference in Valuation of stock between Financial Accounts and Cost Accounts (9660-6070) (workings)		(3590.00)
Profit as per Cost Accounts		85470.50

Workings: Current Year(2016-17) (Amount in ₹ thousand)

	Financial Accounts	Cost Accounts
Opening Semi finished	31700	35210
Finished	83220	78590
Total	**114920**	**113800**
Closing semi finished	35260	39420
Finished	89320	80450
Total	**124580**	**119870**
Variation in inventory	9660	6070

Increase in Difference of stock valuation towards financial accounts = ₹3590

13)What points should you consider as an Management Auditor performing CSR Audit?

Ans: The concept of CSR rests on the ideology of give and take. Companies take resources in the form of raw materials, human resources etc. from the society. By performing the task of CSR activities, the companies are giving something back to the society. India`s new Companies Act 2013 has introduced several new provisions which change the face of Indian corporate business. One of such new provisions is Corporate Social Responsibility (CSR).

A CSR audit program can cover all or any of the following risks: -

- Effectiveness of the operating framework for CSR implementation
- Effectiveness of implementation of specific, large CSR projects
- Adequacy of internal control and review mechanisms
- Reliability of measures of performance
- Management of risks associated with external factors like regulatory compliance, management of potential adverse NGO attention, etc.

A CSR Audit should cover the following points:

- Human Rights: Fundamental Human Rights, Freedom of association and Collective bargaining, Nondiscrimination, Forced labor, Child labor
- Business behavior: Relations with clients, suppliers and sub-contractors, Prevention of corruption and anticompetitive practices
- Human Resources: Labor relations, Working conditions including steps taken for preventing accidents and health hazards, health and safety measures including compensation in case of any accidents, career development and training, Remuneration system that motivates the employees.
- Corporate Governance: Board of Directors, Audit and internal controls, Treatment of shareholders, Executive remuneration
- Environment: Incorporation of environmental considerations into the manufacturing and distribution of products, and into their use and disposal, effect on pollution, pollution control measures undertaken,
- Community Involvement: Impacts on local communities, contribution to social and economic development, General interest causes, creation of socials infrastructure like roads, schools, hospitals.

14) Write short note on - Probable format of environmental statement .

Ans: The following are the main aspects which may be covered in the probable format of Environmental Statement :

i. Name and address of the owner/occupier of the industry, operation or process.

ii. Date of last environmental audit report submitted.

iii. Consumption of water and other raw materials during current and previous year.

iv. Pollution generated in air and water alongwith the output and the types of pollutants and the deviation from standards.

v. Generation of hazardous waste in current year and previous year from processes.

vi. Quantity of solid waste generated during current year and previous year and from recycling or reutilisation of waste, etc.

vii. Disposal practice for different type of waste.

viii. Practice in operation for conservation of natural resources.

ix. Additional investment proposal for environmental protection including abatement of pollution.

15) What do you understand by 'energy audit'? Briefly state the functions of energy auditor.

Ans: Energy Audit is the key to a systematic approach for decision-making in the area of energy management. It attempts to balance the total energy inputs with its use, and serves to identify all

the energy streams in a facility. It quantifies energy usage according to its discrete functions. Industrial energy audit is an effective tool in defining and pursuing comprehensive energy management programme.
As per the Energy Conservation Act, 2001, Energy Audit is defined as "the verification, monitoring and analysis of use of energy including submission of technical report containing recommendations for improving energy efficiency with cost benefit analysis and an action plan to reduce energy consumption".

In that context, energy management involves the basis approaches reducing avoidable losses, improving the effectiveness of energy use, and increasing energy use efficiency. The function of an energy auditor could be compared with that of a financial auditor. The energy auditor is normally expected to give recommendations on efficiency improvements leading to monetary benefits and also advise on energy management issues. Generally, energy auditor for the industry is an external party. The following are some of the key functions of the energy auditor:

(i) Quantification of energy costs and quantities

(ii) To correlate trends of production or activity to energy cost.

(iii) To devise energy database formats to depict to correct picture – By product, department or consumer.

While performing the aforesaid key functions, the energy auditor is required to carry out the following activities:

(i) To analyse the historical energy consumption and cost data.

(ii) To conduct preliminary energy audit with the objectives to identify:

(a) major energy consuming equipment and process;

(b) obvious inefficiencies and energy wastes; and

(c) priority areas for further detailed investigation.

(iii) To conduct detailed technical and economic analysis of energy efficiency measures involving large efficiency measures involving large capital investment or long payback periods.

16) What do you understand by "Corporate Services Audit"? Describe the areas of Corporate Services Audit, the scrutiny thereof and the evaluation criteria used in such audit.

Ans: The term "Corporate Services" is a generic term, which implies service oriented obligations of a corporate body to different interested 'Public' such as consumers, shareholders, community, fellow-businessmen, government etc. It includes the social responsiveness of a business enterprise.

Corporate Services Audit is the audit of social behavior of the company to assess the extent to which the company had met the expectations of the customers , employees, shareholders, suppliers and the community.

The scope of the Corporate Services Audit extends to the critical examination of the different aspects of services and the extent to which the corporate body has rendered satisfactory services. It also includes the evaluation of the degrees of responsiveness and awareness on the part of such enterprise. The performance of the management towards customers , employees, shareholders, suppliers , the community and government is studied separately and properly evaluated by management auditor.

The areas of Corporate Services Audit and the scrutiny and evaluation criteria can be categorized as follows:

Consumers: Quality of goods in right quantity, right price, right place and right time.

Employees : Pay, Safety, Welfare and Industrial Relations etc.

Shareholders: Safety of investment, satisfactory return and capital appreciation.

Community: Social cost and social benefit, public relation

Fellow- businessmen: Business ethics and fair trade dealings.

State: Compliance with various legislations, fair trade practices, payment of taxes etc.

The concept of Corporate Services Audit is that its appraisal system should consider the level of contribution a business entity makes to society and its environment towards raising the quality of life through better product quality and services rather than profit maximization. The Corporate Services Audit thus attempt to distinguish between the end and means of business and provides a new dimension to the concept of audit approach. In Corporate Services Audit , the auditor checks the company's response to different social needs.

17) Give an "Audit programme' as an Internal Auditor of Wage Audit.

Ans:

Audit programme as an internal Auditor of Wage Audit:

(I) Information about Auditee and audit work:

(i) Name of the Auditee .
(ii) Address/Location.
(iii) Period to be covered.
(iv) Estimated time(days) required.
(v) Audit Team members consists of Partner/Qualified/Semi-qualified etc.
(vi) Queries of the Auditor to be settled by the representative of the concern.
(vii) Report to be submitted to the representative of the company.

(II) Study of various records:

(i) Wage related policy manuals.
(ii) Grade Structure.
(iii) Incentive Rules.
(iv) Overtime Rule.
(v) Bonus Scheme.
(vi) Various Statutory deduction schemes as for example ESI, PF, EPF etc.

(III) Verification of:

(i) Payroll package is properly updated with employee's details and it is properly functioning.
(ii) Take out the list of employees for the purpose of verification that no entry is Bogus i.e Ghost Worker.
(iii) Ensure that all wage payments are made through banks.
(iv) Where payment is made in cash, whether it is done in presence of responsible officer.
(v) Cross verify wage with some employees , so that there will be assurance with system.
(vi) Checking of Daily Attendance Sheet, Absenteeism Statement, Manpower Planning and Deployment.
(vii) Checking of Employee Signature at the time of payment in case of cash payment and Attendance Register.
(viii) Checking of Appointment/Retirement records of Employees.

18) It is said that 'Cost Audit 'is 'Efficiency Audit'. Explain the statement. What is the evidence from the Cost Audit Report that Cost Audit is 'Efficiency Audit'?

Ans:

'Efficiency Audit' is systematic appraisal of management methods and is intended to assess the actual performance levels relative to applicable benchmarks or standards. The main purpose of Efficiency Audit is to ensure –

i)that every rupee invested in capital or in other fields give optimum returns, and

ii)the balancing investment between different functions and aspects designed to give optimum results. 'Cost Audit' may appropriately be called 'Efficiency Audit ' as outlined above.

The following points may be considered in favour of the argument:

i) The Cost Auditor has to provide details of Capacity Available and Utilised as part of Annexure to Cost Audit Report, Form CRA 3 (pursuant to Rule 6(4) of the Companies(Cost Records and Audit)Rules, 2014.) Para 1 of Part B(Manufacturing Sector) /Part C(Service Sector) deals with capacity utilization giving details of licensed capacity ,installed capacity, actual production etc. to counter the problem of underutilization of capacity. Thus cost audit can help in improving efficiency by reducing the idle capacity.

ii)Information revealed by the Annexure to Cost Audit Report under Para 2B , Part B/Part C which provide details of Utilities consumed can be highly useful in energy conservation and help firms to improve their efficiency in utilization of energy resources.

iii) Para 2A , Part B/Part C requires comparison of per unit actual consumption of major inputs with the Previous Year. Such comparison is a very important control ratio and helps in analyzing the production efficiency by bringing to focus the areas where wastage of raw materials occur.

iv)Efficiency of industrial units is affected by abnormal / non-recurring costs. An analytical study of information given under Para 2, PART D which deals with profit reconciliation can provide useful information to management to improve its working.

v)Para 4, Part D reveals information on Financial Position and Ratio Analysis. This information will guide management in setting up of a sound system for Utilisation of various resources and help in improving the resource utilization.

vi)Information given under Para 3 helps to analyse the efficiency of distribution of Earnings to various stake holders.

vii)Para 1 Part B/Part C provides information on 'Export Sale.' Similarly Para 2 A , Part B/Part C provides details of imported materials consumed This helps Govt. not only to promote exports but also to protect Indian Industry from unlawful dumping by foreign units.

viii) Similarly other paras like para 4 part D on financial position , para 5, Part D on Related Party Transaction, para 3, Part D on value addition , para 2, Part D on profit reconciliation , Para 6, Part D on reconciliation of Indirect Taxes, Cost Auditor's observations- will go a long way for cost reduction, increasing productivity , efficiency of the firm etc.

ix) On basis of the above points , it can be established that cost audit is well designed to bring to light the efficiency aspect of performance of a company and is thus appropriately called 'Efficiency audit'.

19 (i) What are the mandatory requirements for appointment of Internal Auditor in a listed company?
(ii) Who are the persons eligible for appointment as Internal Auditor?

Ans:

(i) (i)Rule 13 of the Companies (Accounts) Rules, 2014, makes it mandatory to appoint an Internal Auditor for every listed company.

The Board of Directors of every listed company shall appoint an Audit Committee [Rule 6 of the Companies (Meetings of Board and its Powers) Rules]. It is the responsibility of the Audit Committee of a listed company to review the adequacy of the internal audit functions and review the Internal Audit Reports (Clause 49 of the Listing Agreement).

(ii) In terms of Section 138 of the Companies Act, 2013, read with Rule 13 of the Companies (Accounts) Rules, 2014,

(a) every listed company;
(b) every unlisted public company having (i) paid up share wealth of fifty crore rupees or more during the preceding financial year; or (ii) turnover of two hundred crore rupees or more during the preceding financial year; or (iii) outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more at any point of time during the preceding financial year; or (iv) outstanding deposits of twenty five crore rupees or more at any point in time during the preceding financial year; and
(c) every private company having (i) turnover of two hundred crore rupees or more during the preceding financial year; or (ii) outstanding loans or borrowing from banks or public financial institutions exceeding one hundred crore rupees

shall appoint (i) an individual or (ii) a firm of Internal Auditors as the Internal Auditor of the company. Such person or firm shall either be a Chartered Accountant or a Cost Accountant, or such other professional as may be decided by the Board to conduct the internal audit of the functions and activities of the company.

20) SAFA organised a three-day International Conference of Accountants in Mumbai. You are asked to conduct internal audit the accounts of the conference. Draft the internal audit programme for audit of receipt of participation fees from delegates to the conference.

Ans:

Audit of Receipts of Participation Fees

The organization of three-day International Conference of Accountants in Bangalore by SAFA is a one-time event. Normally, in view of mega-size of the event, a special cell is made in the organization to handle the entire event. Since few people would be handling the event, the internal controls may not be that strong and, thus, more emphasis is required to be given on substantive procedure. Audit of receipt of participation fees should be under the following areas:

(I) Internal Control System

- (i) Examine the organization structure of special cell created for the International Conference, if any, and division of responsibilities amongst persons and control/custody over receipt books.
- (ii) Verify the internal control system for restricting the participation of unregistered delegates.

(II) Rate of Participation Fees

- (i) Verify with reference to resolution passed by the Organizing Committee/SAFA.
- (ii) Also verify the rate from the literature/registration form circulated for promotion of conference.

(III) Receipts of Participation Fees

- (i) Verify counter foil of the receipts issued for individual registration.
- (ii) Ensure that receipts are issued for all the registration received in cash.
- (iii) Trace the receipts in Bank Statement or Cash Book – as the case may be.
- (iv) Verify Bank Reconciliation Statement and list out dishonoured cheques.
- (v) Verify subsequent recovery in respect of dishonoured cheques.

(IV) Overall Checking

- (i) Verify the total receipts of participation fees shown in the financial statements with reference to total number of receipts issued to participants.
- (ii) Cross check the total number of delegates with reference to the following:
  - (a) Kits distributed to participants.
  - (b) Bill of caterer for providing meals during conference.
  - (c) Capacity of the Hall.
  - (d) Participation Certificate if any issued.

(V) Foreign Delegates: In case of foreign delegates – if registration fees are higher – ensure that they are registered at higher fees.

(VI) Special Issues :

- (i) Take out list of absentees and in case of nil absentees, probe the issue further.
- (ii) If certain participants are exempted from payment of fees – obtain the list along with proper authorization in this regard.

21) The following figures are extracted from the Books of VENNELA LTD., a Multi products Company mainly producing Cement and Ready-mix Concrete for the years ended March 31, 2017 and 2016.

Year ended 31st March	2017	2016
Particulars	**(Amount in ₹ Millions)**	
Gross Sales including Excise Duty :	**7,720**	**6,180**
Excise Duty	**600**	**480**
Other Income	**450**	**300**
Export Incentives	**80**	**60**
Increase in Value of Stock of Finished Goods	**30**	**15**
Raw materials consumed	**2,640**	**2,160**
Direct wages, salaries, bonus, gratuity etc.	**660**	**528**
Power & Fuel	**360**	**288**
Stores and spares	**240**	**210**
Other manufacturing overheads	**645**	**555**
Administrative Overheads :		
Audit fees	**54**	**45**
Salaries & commission to directors	**72**	**60**
Other overheads	**390**	**330**
Selling and distribution overheads :		
Salaries & Wages	**54**	**45**
Packing and forwarding	**30**	**24**
Other overheads	**375**	**300**
Total depreciation	**180**	**180**
Interest Charges :		
On working capital loans from Bank	**90**	**75**
On fixed loans from IDBI	**135**	**105**
On Debentures	**45**	**45**
Tax paid including provisions	**474**	**300**
Dividend paid	**630**	**345**
Dividend Distribution Tax	**110**	**60**

You are required to calculate the following parameters as stipulated PART-D, PARA-3 of the Annexure to Cost Audit Report under the Companies (Cost Records and Audit) Rules, 2014 for the year ended March 31, 2017 and March 31, 2016:

(i) Value addition
(ii) Earning available for Distribution
(iii) Distribution of Earning to the different claimants

Ans:

Annexure to Cost Audit Report:-
Part D-3: Value Addition And Distribution Of Earnings (For **Vennela Ltd.** as a whole)
(Amount In ₹ Millions)

Sl.	Particulars	**Current**	**Previous**
No.		**Year 2016-17**	**Year 2015-16**
	Value Addition:		
1.	Gross Sales including Excise Duty	7720	6180
2.	Less: Excise Duty etc.	600	480
3.	Net Sales	7120	5700
4.	Add: Export incentives	80	60

5.	Add:/ (Less) Adjustment In Finished Stocks	30	15
		7,230	**5,775**
	Less: Cost of bought out input: (a) Cost of Raw materials consumed (b) Consumption of stores and spares (c) Power & Fuel (d) Other overheads	 2,640 240 360 1,584 -	 2,160 210 288 1,329 -
	Total cost bought out inputs	4,824	3,987
7.	**VALUE ADDED:**	**2,406**	**1,788**
8.	Add: Other income	450	300
9.	Add: Extra ordinary income	---	-----
10.	**Earnings available for distribution**	**2,856**	**2,088**
(1)	**Distribution of earnings to:** Employees as salaries and wages, bonus, gratuity etc. Directors- Salaries and commission	 714 72	 573 60
(2)	Shareholders as dividend	630	345
(3)	Company as retained funds (including depreciation)	676	600
(4)	Government as taxes Dividend Distribution Taxes Income taxes paid (including provisions)	 110 474	 60 300
		584	360
(5)	(1) Providers of Capital/Fund as interest on Debentures: Interest on debentures: Interest on Fixed loans from IDBI	 45 135	 45 105
		180	150
	Total distribution of earnings	**2,856**	**2,088**

Working Notes :

Particulars	Amount in ₹ Millions	Amount in ₹ Millions
	16-17	15-16
Other Overheads:		
Other manufacturing OH	645	555
Audit fees	54	45
Other admn OH	390	330
Packing & forwarding	30	24
Other selling & distribution OH	375	300
Int. on Wk. cap.	90	75
Total	1584	1329

Particulars	Amount in ₹ Millions	Amount in ₹ Millions
Salaries		

Direct wages & salaries	660	528
Salaries & Wages for selling & distribution	54	45
	714	573

Particulars	Amount in ₹Millions	Amount in ₹ Millions
Earnings available for distribution	2856	2088
Less, earning distributed to various stakeholders	2180	1488
Retained earnings including depreciation.	676	600

22) ABUNA ELECTRONICS LTD. is engaged in the manufacture of LED TV sets having its factories at Patna and Gujarat. The company manufactures picture tube at Patna which is consumed to produce LED TV sets at Gujarat factory. The following information pertaining to captively consumed picture tubes are extracted from the records of the company for the Half year ended March 31, 2017.

(Amount in ₹Thousand)

Direct material inclusive of excise duty ₹ 94 thousand	**1,044**
Direct wages and salaries	**357**
Direct expenses	**80**
Indirect materials	**70**
Factory overheads	**320**
Administrative overheads (20% relating to production activities)	**640**
Quality control cost	**100**
Research and development cost	**125**
Selling and distribution expenses	**225**
Sale of scrap realised	**130**
Profit margin	**15%**

You are required to determine:

(i) The cost of production for purpose of captive consumption in terms of Rule-8 of the Central Excise Valuation (Determination of price of Excisable Goods) Rules and as per CAS-4, and

(ii) Also Assessable Value for the purpose of paying excise duty on Captive Consumption

Ans: **ABUNA ELECTRONIC LTD.**

Computation of Cost of Production(As per CAS 4)

Amount in ₹ thousand

Direct materials (exclusive of excise duty (1044-94)	950
Direct wages and salaries	357
Direct expenses	80
Factory overheads (320+70)	390
Quality control cost	100
Research and development cost	125
Administrative overheads (to the extent relates to Production activities)	128
Less: sale of scrap realised	(130)
Cost of production	**2000**
Add: 10% as per rule 8 of CEV (DPEG) Rules (10% of 2000)	200
Assessable Value as per rule 8 of the CEV (DPEG) Rules	**2200**

23) ASHIRBAD CEMENT LTD. has a captive power generation plant for its cement factory. The following information is available with regard to the power generation for the year ended March 31, 2017:

Coal consumption	**2400 tonnes @ ₹600 per tonne**
Oil	**3000 liters @ ₹50-50 per litre**
Water	**24000 gallons at ₹60 per gallon**
Stores and other consumables	**₹ 55,000**

Salaries of power generating plant:

2 supervisors each at ₹10,600 p.m., 5 skilled workers each at ₹6,100 p.m., 3 helpers each at ₹ 4,200 p.m.
Salaries to boiler house attendant, 8 workers, each at ₹4,200 p.m.
Cost of power generating plant— ₹15,00,000 having life of plant 15 years with ₹ 60,000 residual value.
Cost of Boiler plant— ₹6,00,000 having life of plant 10 years with no residual value.
Miscellaneous income received by sale of ash— ₹ 50,000.
Repair and maintenance— Power generating plant ₹ 1,50,000, Boiler house ₹ 1,26,000.
Share of Administrative Overhead— ₹ 1,35,000.
Power generated during the year: 3024250 KWH.
***Note:* No power generated is used by the power generated plant itself.**
You are required to prepare the Cost Sheet to calculate cost per kWh of electricity generated as per the Companies (Cost Records and Audit) Rules 2014 for the year ended March 31, 2017.

Ans: **ASHIRBAD CEMENT LTD**

STATEMENT SHOWING COST OF POWER GENERATED BY POWER GENERATED PLANT FOR YEAR ENDED MARCH 31, 2017

Power generated			3024250 kwh
Particulars		Total Amount (₹)	Cost Per Kwh (₹)
Coal consumption (2400 × 600) Less: Sale of Ash	1440000 50000	1390000	0.46
Oil 3000 litres at ₹ 50.50 per ltr. Water 24000 gallans at ₹60/- per gallan Stores and other consumables		151500 1440000 55000	0.05 0.48 0.02
Salaries of generating plant Supervisor (2 ×10600 ×12) Skilled Worker (5 × 6100 ×12) Helpers (3 x 4200 ×12)	 254400 366000 151200	771600	0.26
Salaries To Boiler House Attendant (8× 4200 ×12)		403200	0.13
Repairs and maintenance Generating plant Boiler house	 150000 126000	276000	0.09
Depreciation Generating Plant (1500000 - 60000)/15 Yrs. Boiler House (600000/10 Yrs.)	 96000 60000	156000	0.05
Share of administrative overhead		135000	0.04
Total cost of power generated		4778300	1.58

So, Cost per KWH of Electricity generated = ₹1.58

24) PHIMPEX LTD. in the business of Real Estate and Consumer Goods shows the following financial position for the year ending March31, 2017:

(Amount in ₹ crore)

	Year ended 31st March	
	2017	**2016**
Liabilities		
Share Capital	**33**	**33**
Securities Premium Account	**931**	**928**
General Reserve	**57**	**44**
Capital Redemption Reserve	**42**	**40**
Profit & Loss Account	**595**	**390**
Long Term Borrowings	**1013**	**670**
Deferred Tax Liability	**25**	**39**
Short Term Borrowing	**782**	**676**
Trade Payable	**715**	**747**
Miscl. Provisions	**77**	**73**
Total:	**4270**	**3640**
Assets:		
Fixed Assets (Tangible)	**647**	**614**
Capital WIP	**667**	**383**

Non-Current Investments	**2378**	**2048**
Long Term Loans	**53**	**66**
Inventories	**167**	**232**
Trade Receivables	**104**	**94**
Cash and Bank Balance	**107**	**69**
Other Current Assets	**25**	**30**
Advance for Equipment	**122**	**104**
Total:	**4270**	**3640**

Profit before tax for the year 2016-17 was ₹326 crores (Previous year ₹397 Crores)

You are required to compute the following figures/ratios as stipulated in PART-D, PART-4 to Annexure of cost Audit Report under the Companies (Cost Records and Audit) Rules, 2014 for the year ended 31st March, 2017:

i. **Capital Employed**
ii. **Net Worth**
iii. **Debt Equity Ratio**
iv. **PBT to Capital Employed**
v. **PBT to NET Worth**
vi. **Current Assets to Current Liabilities**

Ans: **PHIMPEX LTD.**

(Amount in ₹ crore)

Year ended March 31			**2016**	**2017**	**2017**
(i) Capital Employed:					
Fixed assets (Tangible)			614	647	
Non-current investments			2048	2378	
			2662	3025	
Particulars	Previous Year2016	Current Year2017			
Current Assets: (A)					
Inventories	232	167			
Trade Receivables	94	104			
Cash and Bank Balance	69	107			
Other Current Assets	30	25			
(A)	425	403			
Current Liabilities:					
Short term borrowings	676	782			
Trade payables	747	715			
Misc. Provision (B)	73	77	(1071)	(1171)	
			1591	1854	
	1496	1574			
Working Capital (A-B)					
CAPITAL EMPLOYED					
Average capital employed for the year ended March 31,2017			(1591+1854)÷2		1722.5

(ii) Net Worth: (For the year ended Mar31,2017 Share capital Securities premium a/c General reserve Capital redemption reserve Profit and loss account		 33 931 57 42 595	 1658
(iii) Debt (For the year ended March 31,2017) Long Term Borrowings Deferred Tax Liabilities Debt Equity Ratio: (1038/1658) = 62.60% = 62.6:100 or 0.63:1	 (1038÷1658) =62.60%	 1013 25 Or	 1038 62.6:100 0.63:1
Profit before tax (PBT) for the year ended March 31, 2016			326
(iv) PBT to Capital Employed:	(326÷1722.5)×100		18.93%
(v) PBT to Net Worth	(326÷1658)×100		19.66%
(vi) Current Assets to Current Liabilities: for 2017 (CA/CL) = (403/1574)		 Or	0.256 0.26:1

25) PRANTIKA LTD., a manufacturing company provides the following extracts from its records for the year ended March 31, 2017.

The Company's specifications—Capacity for the machines per hour	**1800 units**
No of shifts (each shift of 8 hours) per day	**3 shifts**
Paid holidays in a year (365 days):	
(i) Sunday	**52 days**
(ii) Other holidays	**13 days**
Annual maintenance is done within these 13 holidays.	**---**
Preventive Weekly Maintenance for the Machines is carried on during Sundays. Normal idle capacity due to Lunch time, shift changes etc. per shift.	**1 hour**
Production based on sales expectancy in past 5 years (units in Lakh):	**90.80**
	104.90
	78.46
	93.56
	91.30
Actual Production for the year ended March 31, 2015 (units in Lakh):	**97.80**

You are required to calculate:

(1) Installed Capacity

(2) Actual Capacity

(3) Normal Capacity

(4) Idle Capacity

(5) Abnormal Idle Capacity—Keeping in view of the relevant Cost Accounting Standard (CAS-2).

Ans:

1	Installed Capacity	365×8×3×1800=157.68 lakh units
2	Actual Capacity Utilization	[(97.80)÷157.68] × 100 = 62.02%
3	Normal Capacity	(104.90 + 93.56 + 91.30)/3 = 96.59 lakh unit
4	Idle Capacity	(157.68 – 97.80) = 59.88 lakh units (59.88)÷157.68 = 0.3798 = 0.3798 i.e. 37.98%
5	Abnormal idle	(113.40 – 97.80) = 15.60 lakh units i.e., or (15.60/113.40) =

	capacity	13.76%

26) In a manufacturing shop, product P requires 2 man hours and Product Q requires 6 manhours. In a month of 26 working days of 8 hours a day 2000 unit of P and 1000 unit of Q were produced. The Company employs 60 workers in the shop and the budgeted man-hours are 1,08,000 for the year. You are required to workout capacity ratio, activity ratio and efficiency ratio.

Ans:

Budgeted hours for the year = 108000 Hrs for the year
= 9000 for the month
Maximum possible hours = 26x8x60 workers = 12480 Hrs
Actual hours worked = Maximum possible hours worked = 12480 Hrs.

Standard hours produced

Product P = 2000 x 2 =	4,000 Hrs.
Product Q = 1000 x 6 =	6,000 Hrs.
	10,000 Hrs.

(i) Capacity ratio
Standard capacity usage ratio = Budgeted/maximum possible hours x 100
= 9000/12480 x 100 = 72.12%
Actual capacity usage ratio = Actual hour worked/maximum possible hours
= 12480/12480 x 100 = 100.00%

(ii) Activity Ratio = Actual production in terms of Standards Hrs/Budgeted Hrs.
= 10000/9000x100 = 111.11%

(iii) Efficiency Ratio = Actual production in Standard Hour / Actual hours worked
= 10000/12480 x 100 = 80.13%

27) The following is a summary of the Profit and Loss Account of M/s. Straw Berry Company Limited for the year ended 31.03.2017

		₹ in lakh
Sales		**13,540**
Cost of Sales:		
Raw Materials, Stores and Spares	**5,600**	
Excise Duty	**830**	
Salaries and Wages	**1,400**	
Power and Fuel	**470**	
Repairs and Maintenance: Major		
Breakdown Repairs Other	**35**	
regular maintenance	**94**	
Carriage Outwards	**320**	
Insurance General	**34**	

Insurance-Transit **Advertisement and Sales Promotion** **Rent, Rates and Taxes Printing,** **Stationery etc. Travelling and** **Conveyance** **Other Administrative expenses** **Depreciation** **Interest**	**22** **720** **97** **437** **776** **426** **391** **1,494**	
Profit		**13,146**
		394

There was a major breakdown of machinery resulting in loss of production for 42 days, in June and July, 2016 and a labour strike for 97 days from 14.2.2017 to 21.5.2017. The Company produced a single product (Steel-Billet) and the production during the year was 942000 kgs.
You are required to compute the amount of abnormal cost on account of the breakdown and strike and the impact on cost per unit of output. Where do these figures find a place in the Cost Audit Report?

Ans:

Period Costs incurred when there is no production are deemed as abnormal and the costs apportioned for such periods are excluded from cost of production of the product.

Particulars	**₹ in lakh**
Salaries & Wages General Insurance Rent, rates & taxes Other administrative expenses Depreciation Interest	1,400 34 97 426 391 1,494
Total Fixed Cost	3,842

Total period of production stoppage:

Due to machinery breakdown Due to strike 14.02.2014 to 31.03.2014	42 days 46 days
	88 days

Fixed Costs apportioned to the period of production stoppage

= ₹ 3842 lakhs x 88 / 365 Major breakdown repair	₹ 926.29 lakhs ₹ 35.00 lakhs
Total abnormal cost	₹ 961.29 lakhs

This work out to approximately 9.85%of the total cost of production and should be excluded from the respective elements of cost in the cost sheets and should be stated in Reconciliation Statement of Para 2,PART D of the Annexure to the Cost Audit Report.
The abnormal cost included in Cost of Production is ₹9,61,29,000/9,42,000 = ₹102.05 per Kg.

Working Notes:
Cost of Production

	₹ in lakhs
Raw Materials, Stores and Spares Salaries & Wages Power & Fuel Repairs and Maintenance Insurance General Rent, Rates & Taxes Printing, Stationery Travelling & Conveyance Other Admn. Exp. Depreciation	5,600 1,400 470 129 34 97 437 776 426 391
Cost of Production	9,760

Abnormal cost=961.29*100/9760=9.85%

Note:

(i) Excise Duty is not forming part of Cost of Material.
(ii)Carriage outward and insurance in transit are considered not forming part of cost of production.

(iii) Advertisement and Sales Promotion and Interest are not forming part of Cost of Production.

28) The following information pertains to REACON CEMENT LTD., a manufacturing cement company for the year that ended as follows:

The year ended March 31.	2016-17	2015-2016
Rated Capacity per Hr (in MT)	80	80
Break down (Hrs)	2,177	1,01
Planned Maintenance (Hrs)	247	422
Power restrictions (Hrs)	1,237	1,48
Shortfall (there are no orders) (Hrs)	792	677
Want of wagons (Hrs)	495	635
Total stoppage (Hrs)	4,948	4,23
Total running (Hrs)	3,888	4,58
Total available Hours	8,836	8,81
Production during the year (in MT)	2,48,844	3,29,92
Hourly Rate of Production (in MT)	64	72
Capacity Utilization (%)	62.21	82.48
Annual Installed Capacity (in MT)	4,00,000	4,00,000

Based on information stated above, you as a Cost Auditor are required to offer your comments on
(i) The performance of the company
(ii) Your suggestion for improvement.

Ans:

(i) Performance of the Company:

(a) Rated capacity = 80 MT/Hr : Rated capacity achieved in 2012-13=(72/80)x100 =90% Rated capacity achieved in 2013-14= (64 /80)x100 = 80%
The capacity achievement as % of rated capacity has declined from 90% to 80% in 2013-14.

Further the Capacity Utilization has gone down to 62.21% in 2013-13 from 82.48% of previous year; a reduction of 20.27%

(b)From the data available the following observations are noted:-

1. Breakdown hours have gone up from 1,015 hours to 2,177 hrs, an increase by 114.48%
2. Planned Maintenance hrs has reduced from 422 hrs to 247 hrs i.e. by 41.47%
3. Shortfall hrs due to lack of orders has increased from 677 hrs to 792 hrs i.e. by 16.99%
4. The total stoppage hrs. has increased from 4,230 hrs to 4,948 hrs i.e. by 16.97%
5. The total running hrs has come down from 4,582 hrs to 3,888 hrs i.e. by 15.15%
6. The production has come down from 3,29,928 Mt to 2,48,844 Mt i.e. by 24.58%

From the above findings, it can be pointed out that the under utilization of capacity to the extent of little over 20% can be attributed mainly to:-

- Increased total stoppage hours of 4,948 of 2013-14 as against that of 4,230 hrs in 2012-13 and
- The net increase of 718 hrs (4,948-4,230) is again due to increase of break down by 1,162 hrs (2,177-1,015) in the year 2013-14

(ii) Suggestion:

Therefore, the Company should look into the aspect of proper maintenance, securing sufficient orders to avoid lost time. Better utilization of capacity can be alsobe achieved by improving availability of wagons. The company may also carry out a cost-benefit analysis to have captive source of power.

29) ALLIED LTD. has the following Balance Sheet as on March 31, 2017 and March 31,2016

(Amount in ₹ Lakh)

Year ended March 31	2017	2016
SOURCES OF FUNDS:		
Shareholders' Fund	**2,972**	**1,886**
Loan Funds	**4,644**	**4,060**
	7,616	**5,946**
APPLICATIONS OF FUNDS:		
Fixed Assets	**4,279**	**3,600**
Cash and Bank	**707**	**684**
Debtors	**1,914**	**1,522**
Stock	**3,560**	**3,008**
Other Current Assets	**2,000**	**1,805**
Less: Current Liabilities	**(4,844)**	**(4,673)**
	7,616	**5,946**

The Income statement of ALLIED LTD. for the year that ended is as follows:

(Amount in ₹ Lakh)

Year ended March 31	2017	2016
Sales	**26,718**	**16,778**
Less: Cost of Goods Sold	**25,152**	**15,173**
Gross Profit	**1,566**	**1,605**
Less: Selling, General & Administrative expenses	**1,242**	**782**
Earnings before Interest & Tax (EBIT)	**324**	**823**
Less: Interest Expenses	**256**	**246**
Profit before Tax (PBT)	**68**	**577**
Less: Tax	**28**	**230**
Profit After Tax	**41**	**347**

Required:

(i) Calculate for the year 2016-17:
(a) Inventory Turnover Ratio
(b) Return on Net Worth
(c) ROI
(d) ROE
(e) Profitability Ratios

(ii) Give brief comments on the financial position of company

Ans:

(i)Various Ratios for the year 2016 – 2017

(a) Inventory Turnover Ratio= Cost of Goods sold/Average inventory=25152/3284=7.66

(b)Return on Net Worth=Profit after Tax/Net Worth=40/2972*100=1.35%
(c) ROI=Net profit before interest but after tax/Average Capital employed=296/6781*100=4.37%
Net profit before interest but after tax=256+40=296
Average capital employed=(7616+5946)/2=6781

(d)ROE= PAT available to Equity Share holders/Average shareholders' Funds=40/2429=1.65%

Average shareholders' Funds=(2972+1886)/2=2429

(e) Profitability Ratios:
Gross Profit Ratio = (1,566/26,718) × 100 = 5.86%
Operating Profit Ratio = (68+256) =(324 /2,6718) × 100 =1.21%
Net Profit Ratio=(40 /2,6718) × 100 = 0.15%.

(ii) Comment:

There is a substantial decline in Profitability in the current Year from ₹ 823 Lakhs of previous year to ₹ 324 Lakhs. This is mainly due to huge increase in the operating expenses. There has been substantial increase in the Interest charges also. During the year 2016-17 both fixed financial expenses and operating expenses have increased. During current year both operating and financial leverages have been adversely affected. It can be seen that the company is suffering from a liquidity crisis during the year.

30) Short Questions:

(a) How would you assign administrative overheads as per CAS 11?

(b) Explain how installed capacity is calculated as per CAS 2 by a manufacturing concern?

(c) A Company engaged in manufacturing of chemicals is consistently recording higher sales turnover, but the net profits is showing a declining trend since the last 5 years. As a Management Auditor appointed to find out the reasons for the same, mention the points you would investigate. (any 4 points)

(d) Management Audit and Operational Audit are complementary and supplementary to one another". Discuss in brief.

(e) What is the Role of Management with regard to Internal Control?

(f) What points should be considered in audit programme of Local Bodies?

(g) Trial Balance extract of M/s Rashid Ltd. as on 31.03.2017 is given below:

Particulars	Amount (₹)	Particulars	Amount (₹)
Materials Consumed	32,00,000	Special subsidy received from Govt. towards employees Salary	2,80,000
Salaries	18,00,000		
Employees training cost Perquisites to employees Contribution to Gratuity Fund Festival Bonus	1,80,000 4,50,000 4,10,000	Recoverable amount from employees out of perquisites extended	30,000
Lease rental for accommodation	65,000		
Unamortised amount of employee cost related to a discontinued operation	3,00,000 80,000		

Compute employees cost.

(h) The following figures are extracted from the statement prepared by the Cost Accountant and the Trial Balance of ABC Ltd., which is a single product company calculate Value Added:

₹ in lacs

	31.03.2017
Gross sales inclusive of Excise Duty	2,040
Excise Duty	295
Raw Materials consumed	1,140
Direct Wages	35
Power and Fuel	30
Stores and	6
Spares	16
Depreciation charged to production cost centres	
Factory overheads:	5
Salaries and wages	2
Depreciation	1
Rates and Taxes	6
Other overheads	
Administrative overheads:	10
	2
Salaries and Wages	162
Rates and Taxes	
Other overheads	
Selling and distribution	7
overheads: Salaries and Wages	6
Packing and Forwarding	1
Depreciation	124
Other overheads	85
Interest	12
Bonus and Gratuity	840
Gross Current Assets	324

(i) Purchase of material $ 50,000 [Forward contract rate $ = 54.40 but $ = 54.60 on the date of importation]; Import Duty paid ₹ 5,65,000; Freight inward ₹ 1,62,000; Insurance paid for import by road ₹ 48,000; Cash discount ₹ 33,000; CENVAT Credit refundable ₹ 37,000; Payment made to the foreign vendor after a month, on that date the rate of exchange was $ = 55.20. Compute the landed cost of material.

(j) A factory operates a standard cost system, where 2,000 kgs of raw materials @ ₹12 per kg were used for a product, resulting in price variance of ₹6,000(F) and usage variance of ₹3,000(A). Then what will be the standard material cost of actual production?

Ans:

(a) Assignment of administrative overheads to the cost objects shall be based on either of the following two principles:
(i) Cause and effect – Cause is the process or operation or activity and effect in the incurrence of cost.
(ii) Benefits received – Overheads are to be apportioned to various cost objects in proportion to the Benefits received by them.

The cost of shared services should be assigned to user activities on the basis of actual usage. Where the resources by way of infrastructure are shared the cost should be assigned on a readiness to serve basis. General management cost should be assigned on rational basis.
(b) Installed capacity Installed capacity is usually determined based on:
i) Technical specifications of facility.
ii) Technical evaluation.
iii) Capacities of individual or interrelated production or operation Centres.
iv) Operational constraints or capacity of critical machines or equipment.
v) Number of shifts or machine hours or man hours.
In case technical specifications of facility are not available, the estimates by technical experts on capacity under ideal conditions shall be considered for determination of installed capacity. In case the installed capacity is assessed as per direction of the government or regulator it shall be in accordance with the said directives.

(c) As per the facts that there has been consistently high turnover but declining net profits is an anomalous situation. It may be attributed to one or more following reasons requiring further investigation:

i) Unfavorable Sales mix
ii) Negative Impact of Financial Leverage - Higher Debt and Interest would result in lower profit.
iii) Other items included in Sales - Where the amount of Excise Duty goes up considerably the total sales may show an increase which is not represented by a real increase in quantity/value.
iv) High Administrative and Selling Expenses - A reduction in profit could also be due to increase in administrative overheads and sales overheads at a rate higher than he rate of increase in sales.

(d) Management Audit is wider in scope compared to Operational Audit.

Management Audit is concerned with quality of managing whereas Operational Audit centres on the quality of operation. Operational Audit is an audit for the management and Management Audit is an audit of the management also.

The basic difference between the two audits is not in method, but in the level of appraisal. In management audit, the auditor is to make his tests to the level of top management, its formulation of objectives, plans and policies and its decision making. It is not that he just verifies the operations of control and procedures and fulfillment of plans in conformity with the prescribed policies.

The auditor is to reach the root i.e., the functions of top management which lay down objectives and policies, provide means and procedures of implementation and control and which actually engage in direction and control on a continuous basis. In addition to what would normally be covered in an operational audit, management audit would also encompass the relevance and effectiveness of the aims, duties and decisions of management at various levels, plans, policies and decisions of the top management. Every aspect of the functions of Board of Directors should be in conformity with the objects set out in the constituting document. Similarly, the managing director, if any, should act not only in accordance with the mandate he has received but he should ensure that the decisions he takes are in conformity with the objects of the company and the policies formulated by the Board. The effectiveness of management under the control of managing director and the various members of the Board including those in charge of finance, production, sales etc., should be subject to review of the management auditor.

Therefore, it can be said that the two audits are complementary and supplementary to one another.

(e) The responsibility of Management with regard to internal Control can be summarized as under-

1. **Creation of system:** Management is responsible for maintaining an adequate accounting system incorporating various internal Controls to the extent appropriate to the size and nature of the Business. The Management is vested with the responsibility of carrying on the business, safeguarding its assets and recording the transactions in the books of account and other records.
2. **Review of system:** The system installed, should be reviewed by the Management to ascertain, whether-
   - (a) The prescribed Management policies are being properly interpreted by the employees and are faithfully implemented,
   - (b) The prescribed procedures need a revision due to changed circumstances or whether they have become obsolete or cumbersome, and
   - (c) Effective corrective measures are taken promptly when the system appears to breakdown
3. **Internal Audit:** it is desirable that the Management also installs an internal audit System as an independent function to check, amongst other things, the actual operation of the Internal Control System and report any deviations or non-compliances.

(f) The audit programme for local bodies include the following:
• All sanctions are accorded by competent authority
• Expenditure incurred are according to provisions and as per regulations framed by competent authority • Different schemes, programmes, and projects are running economically and the purpose such programme is achieved.

(g) Computation of Employee Cost

Particulars		Amount (₹)
Salaries		18,00,000
Add: Perquisite to employees	4,50,000	
Less: Recoverable from Employees	30,000	
		4,20,000
Add: Lease rent Provided to Employees		3,00,000
Add: Festival Bonus		65,000
Add: Contribution to Gratuity Fund		4,10,000
		29,95,000
Less: Subsidy received from Government towards Employees Cost		2,80,000
		27,15,000

(h)

Net sales	1,745
Less : (i) Cost of Bought Out Materials & Service (Raw Materials and Stores & Spares)	1,146
(ii) Power & Fuel, other bought out services	30
(iii) Over heads (excluding Salaries & Wages, Rates & Taxes and depreciation)	298
(Y) =(i)+(ii)+(iii)	1,474
Value Addition : (X) - (Y) =	271

(i) Computation of Landed Cost of Material

Particulars	₹
Purchase price of material [50,000 × 54.60]	2730000
Add: Import Duties of purchasing the material	565000
Add: Freight Inward during the procurement of material	162000
Add: Insurance of the material (In case of import of material by road/Sea)	48000
Total	**3505000**
Less: CENVAT Credit refundable	37000
Value of Receipt of Material	**3468000**

(j) Total material cost variance = Material price variance +Material usage variance

= 6,000(F) + 3,000(A)

= 3,000(F)

Actual material cost = 2,000x12

= ₹ 24,000

Hence, the standard material cost of actual production = 24,000 + 3,000(F) = ₹ 27,000