

Suggested Answer_Syl08_Dec13_Paper 6

INTERMEDIATE EXAMINATION

GROUP I

(SYLLABUS 2008)

SUGGESTED ANSWERS TO QUESTIONS

DECEMBER 2013

Paper- 6 : COMMERCIAL & INDUSTRIAL LAWS AND AUDITING

Time Allowed : 3 Hours

Full Marks : 100

The figures in the margin on the right side indicate full marks.

- Please : (i) Answer all bits of a question at one place
(ii) Open a new page for answer to a new question
(iii) Attempt the required number of question only.

Answer Question No. 1 and Question No. 5 which are compulsory and attempt any two from the rest in Section-I and any two from the rest in Section-II.

Section-I (50 Marks) (Commercial and Industrial Laws)

1. Comment on the following based on legal provisions (no mark for wrong reasons or justification) 2X7
 - (a) 'A' authorized 'B' to buy 1000 Bales of cotton for 'A' and to pay out of A's fund remaining in B's hand. B buys 500 bales and paid from A's fund. On 20.11.13 'A' revoked the Authority given to 'B'. Intimation of revocation was received on 24.11.13. A refused to accept 500 bales so purchased because it was revoked.
 - (b) A Bill dated 01.01.2012 was accepted on 02.01.2012 is made payable 90 days after date. Hence its due date is 6th April, 2012.
 - (c) In every factory wherein more than 150 workers are ordinarily employed, provision shall be made for cooling drinking water during hot weather. — Comment.
 - (d) Mr. Arun a supervisor in a factory submitted disputes for settlement under Industrial Disputes Act, 1947— comments.
 - (e) Two bodies Corporate cannot form Limited liability partnership—Comment.
 - (f) Mrs. Loreto drawing salary of ₹ 9,500 who joined the Company on 20.01.2013, availed maternity leave from 08.02.2013 to 04.04.2013. Is she eligible for Bonus for 2012-13?
 - (g) It is the seller who is to bear the cost of delivery, (Sales of Goods Act) State the correct position.

Answer:

1. (a) The Principal i.e. 'A' may revoke the Authority of the Agent i.e. 'B' any time before the Authority has been exercised. In this case "B" received the intimation after execution of Part order.
The Principal i.e. 'A' cannot revoke the Authority given to his agent as 'B' after the Authority has been partly exercised so far as regards such acts and obligation as arise from acts already done in the Agency.
- (b) Due date is -

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Accepted on 02.01.2012 = 3rd April, 2012

Hence January 30 Days

February 29 Being leap year

March $\frac{31}{90}$ Days

+ Grace Period 3 Days i.e. due date 3rd April.

(c) Where more than 250 workers are ordinarily employed.

(d) No. Where an industrial dispute connected with an individual workman arises in an establishment, a workman or any trade union of workmen of which such workman is a member, refer, in such manner as may be prescribed such dispute to the Grievance Settlement Authority provided for by the employer for settlement.

But, a person who is employed in a supervisory capacity and draw wages exceeding INR 10,000 is not treated workman under this act. So, Mr. Arun cannot submit dispute for settlement.

(e) Two bodies corporate can also form LLP and where all the partners are bodies corporate, at least two nominees of such bodies corporate shall act as designated partners.

(f) According to Section 2(13) of the payment of Bonus Act, every employee of an establishment covered under the Act is entitled to bonus from his employer in an accounting year provided he worked in that establishment for not less than thirty days in the year on a salary of less than ₹10,000/- per month. Under Section 14, the days when an employee has been on maternity leave with salary or wages during the accounting year will be included in calculating the total working days for the purpose of payment of bonus. In the instance case, the salary is falling within the limit. Also, her maternity leave period will be treated as working days. Therefore, she is eligible for bonus for the year 2012-13.

(g) Unless otherwise agreed, the expense of and incidental to putting the goods into a deliverable state shall be bourn by the seller.

2. (a) Define Sales (Sales of Goods Act). 3
(b) Condition can be treated as warranty under a contract of sale. 2
(c) Mr. Pandit delivers Steel plate to Mr. Bahl for fabrication. Bahl refused to deliver the fabricated item and residual steel rejects fill the payment was made by Mr. Pandit. Whether Mr. Bahl has Authority to refuse. 2
(d) (i) The occupier himself shall be deemed to be the Manager of the factory for the purpose of Factories Act, 1948. State the validity of this Statement. 2
(ii) As per the Factories Act, Canteen is mandatory in all the factories. Offer your views based on Rules. 1
(e) While going to his work place riding on his bicycle Mr. Ram met an accident. Is the employer liable to pay Compensation under the Workmen's Compensation Act? 2
(f) The Employer has no authority to pay Part Bonus before the date on which such bonus becomes payable. Answer based on Payment of Bonus Act, 1965. 2
(g) Every person is competent to make a contract. Answer if this is wrong. 2
(h) Who are authorised to appear before the Commission (the Competition Act, 2002)? 2

Answer:

2. (a) Sec 4 defines sales as a contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price.

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A contract of sale is made by an offer to buy or sell goods for a price and the acceptance of such offer.

The contract may provide for the immediate delivery of the goods or immediate payment of the price or both or for the delivery or payment by installments, or that the delivery or payment or both shall be postponed.

Subject to provisions of any laws for the time being in forces, a contract of sale may be made in writing or by word of mouth, or partly in writing and partly by word of mouth or may be implied from the conduct of the parties.

(b) When condition to be treated as warranty.

- (i) Where a contract of sale is subject to any condition to be fulfilled by the seller, the buyer may waive the condition or elect to treat the breach of the condition as a breach of warranty and not as a ground for relating the contract as repudiated.
- (ii) Where a contract of sale is severable and the buyer has accepted the goods or part thereof, the breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty and not as a ground for rejecting the goods and treating the contract as repudiated, unless there is a term of contract, express or implied, to the effect.
- (iii) Nothing in this section shall affect the case of any condition or any warranty fulfillment of which is excused by law by reason of impossibility or otherwise.

(c) Bailee's particular Lien (section 170)

'Lien' means right of a person to retain possession of some goods belonging to another until claim of the person in possession is satisfied.

Where the bailee has, in accordance with the purpose of the bailment, rendered any service involving the exercise of labour or skill in respect of the goods bailed, he has, in the absence of a contract to the contrary, a right to retain such goods until he receives due remuneration for the services he has rendered in respect of them.

Therefore, in the given case, Mr. Bahl is entitled to retain the goods till he is paid for the services he has rendered.

- (d)** (i) The statement is correct. During any period for which no person has been designated as manager of a factory or during or during which the person designated does not manage the factory, any person found acting as Manager, or if no such is found, the occupier shall be deemed to be Manager.
- (ii) In every factory where in more than 250 workers are ordinarily employed, a Canteen or canteens shall be maintained by the occupier.

(e) (A) No unless it can be established that the bicycle was supplied by the employee for doing his duty (Tobacco Manufacturing India Ltd. V Maarian Stewarts AIR 1950 Cal 164)

Alternate answer - to allow mark in case answer is on the basis of following approach.

(B) The employer is liable to pay compensation only if personal injury is caused to a workman by an accident arising out of and in course of his employment. As a rule does not commence until he has reached the place of employment and does not continue when he has left the place of employment. Journey to and from the place of work is thus excluded from the notion of employment. However it is now a

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subject to the theory of national extension of the Employer's premises, so as to include in it an area which the workman passes and repasses in going to an in leaving the actual place of work, so that there may be some reasonable extension in both time and place of work and the workman.

- (f) The Employer may pay part bonus payable under the payment of Bonus Act before the date on which such Bonus becomes payable.
- (g) The parties to an agreement must be capable of entering into a contract. A person is considered competent if he is
(a) Eighteen year of age.
(b) Of sound mind
(c) Not disqualified from contracting by any law to which he is subject.
- (h) A complainant or defendant or the Director General may either appear in person or authorized one or more Chartered Accountants, or company Secretaries or Cost Accountants or Legal practitioners or any of his or its officers to present his or its case before the commission, (sec 35)
3. (a) Risk is transferred only on delivery—Comment. 2
- (b) Mr. Asim enters into a contract with Mr. Basu to sell 200 Tonnes Rice to Asim. It was revealed that Mr. Basu was agent of Mr. Roy. Who can be sued by Mr. Asim in case of failure to execute the contract? 2
- (c) X offers to sell to Y a painting which X knows is a copy of a well known Master piece. Y thinking that the painting is an original one and that X must be unaware of this accept X's offer. State the validity of the contract. 2
- (d) A on Board an English Ship on high seas, causes 'B' to enter into an agreement by an act amounting to criminal intimidation under the Indian Penal Code. 'B' subsequently refused to execute the said agreement. 'A' afterwards sues 'B' for breach of contract at Kolkata. Whether 'A' can succeed. 2
- (e) There is no time limit for payment of bonus under payment of Bonus Act 1965. Whether this is correct. 2
- (f) Sale of Goods Act is applicable to both movable and immovable goods. Offer your views. 2
- (g) Gratuity shall be payable to an employee only on completion of five years—Comment. 2
- (h) Mr. Amar of his own agrees to sell his house to Mr. Biman at ₹ 5 Lakh whereas the fair value is ₹ 15 Lakh. Hence the agreement is invalid as the consideration being inadequate. Offer your views. 2
- (i) Mr. Sunil deposited ₹ One Lakh with a company for 3 years. On maturity the company did not pay the Principal & interest inspite of demand. Mr. Sunil approached Consumer forum—Will he succeed? 2

Answer:

- (a) As per section 26 of the Sale of Goods Act, 1930, the goods remains at the seller's risk until the property therein is transferred to the buyer, but when the property in goods is transferred to the buyer the goods are at the risk of the buyer whether delivery of the goods has been made or not.

Thus risk prima facie passes with property unless otherwise is agreed by the parties. In other word the parties may in the contract have different stipulation as to time of passing of risk irrespective of what is provided in section 26 of the Act.

It is once again reiterated that the general rule is that in the absence of special terms, the risk follows ownership and not possession. Whoever is the owner of the goods has

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to bear the loss associated with the goods. Sec 26 further provides that the provision of this section does not affect the duties and liabilities of either the seller or buyer as the bailee of goods of the other party.

- (b) Rights of person dealing with Agent personally liable [Section 233]:** In cases where the agent is personally liable, a person dealing with him may hold either him or his principal or both of them liable.

In the given case, Mr. Asim enters into a contract with Mr. Basu to sell 200 Tonnes Rice to Asim. It was revealed later on that Mr. Basu was agent of Mr. Roy.

So, in case of failure to execute the contract, Mr. Asim can sue either Mr. Basu or Mr. Roy or both Mr. Basu and Mr. Roy.

- (c)** The contract is valid.

The rule of 'Caveat Emptor' i.e., 'let the buyer be aware' applies in case of Unilateral Mistake.

The term 'unilateral mistake' means where only one party to the agreement is under a mistake. As per section 22, "a contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to a matter of fact." A unilateral mistake is not allowed as a defense in avoiding a contract unless the mistakes brought about by another party's fraud or misrepresentation.

So, the contract remains valid and binding in spite of the mistake as Y will have to blame himself for ignorance of the fact.

- (d)** The given problem is a case of 'coercion' as according to section 15 of the Indian Contract Act, 1872 'coercion' includes any contract obtained by committing any act which is forbidden by the Indian Penal Code.

However, the Indian Penal Code need not be in force at place where the coercion is employed and at the time when coercion is employed.

Further, as per section 19, when consent to an agreement is obtained by coercion, the contract is voidable at the option of the party whose consent was obtained by coercion.

So, 'A' cannot succeed even though his act is not an offence by law of England.

- (e)** Bonus shall be paid within 8 (Eight) months from close of the Accounting year. However, where there is a dispute pending before any authority u/s 22, in such case, within a month from the date of the award becomes enforceable or the settlement comes into operation in respect of such dispute.
- (f)** Sale of goods Act is applicable only to movable goods other than actionable claims and money.
- (g)** False, completion of continuous period of five years shall not be necessary where the termination of the Employment of any employees is due to death or disablement due to accident.

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(h) This agreement is not void or invalid because Amar agreed of his own i.e. with free consent to sell at INR 5 lakhs. Hence the agreement is valid contract notwithstanding the inadequacy of the consideration.

(i) The company failing to repay the principal along with interest on the due date shall be liable for deficiency of service under consumer protection act. There is an inherent element of service for consideration. Hence deposit holder is a consumer under the, Act entitled to remedy for any default in payment of interest or of deposit.

4. (a) Answer any four:

4X4

(i) Effect of coercion.

(ii) Essential of a Contract of sale.

(iii) Consequences of misrepresentation.

(iv) Disposal of wastes and effluents (Factories Act, 1948).

(v) Rights of Consumers (Consumers Protection Act, 1986).

(b) Bonus under payment of Bonus Act 1965 is payable to all the employees by the Employer. State the correct position. 2

Answer:

(a)

i) Effects of coercion:

a. Option of aggrieved party to avoid the contract – when consent to an agreement is obtained by coercion, the contract is voidable at the option of the party whose consent was obtained by coercion [Section 19].

b. Obligation of aggrieved party to restore benefit – the party rescinding avoidable contract shall restore the benefit received by him under the contract, to the person from whom the benefit was received [Section 64].

c. Obligation of other party to repay or return – a person to whom money has been paid or anything delivered under coercion, must repay or return it [Section 72].

ii)

1. There must be at least two parties. However there may be a contract of sale between one part owner and another.

2. There must be a transfer or agreement to transfer the ownership of goods from one person to another. Mere transfer of possession is not sale.

3. The subject matter of sale must be "goods and movable".

4. The consideration of sale is called price which should be stated in terms of money.

5. All essential elements of a valid contract must be present in a contract of sale.

6. A contract of sale may be absolute or conditional.

iii) Consequence of Misrepresentation

1. Right to Rescind the Contract

The party whose consent was caused by misrepresentation can rescind (cancel) the contract but he cannot do so in the following cases:

(i) Where the party whose consent was caused by misrepresentation had the means of discovering the truth with ordinary diligence;

(ii) Where the party gave the consent in ignorance of misrepresentation;

(iii) Where the party after becoming aware of the misrepresentation, takes a benefit under the contract;

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- (iv) Where an innocent third party, before the contract is rescinded, acquires for consideration some interest in the property passing under the contract;
- (v) Where the parties cannot be restored to their original position.

2. Right to Insist upon Performance

The party whose consent was caused by misrepresentation may if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representation made had been true.

iv) Disposal of waste & effluents

Effective arrangement shall be made in every factory for the treatment of waster and effluents due to the manufacturing process carried on therein, so as to render them innocuous, and for their disposal.

The state government may make rules prescribing in the arrangements to be made u/s 12(1) or requiring that the arrangements made in accordance with sub-sec (1) shall be approved by each authority as may be prescribed.

v) Rights of Consumers: Section 6 of the Act recognizes the following six rights of consumers:

- 1) Right to safety, i.e., the right to be protected against the marketing of goods and services which are hazardous to life and property.
- 2) Right to be informed, i.e., the right to be informed about the quality, quantity, potency, purity, standard and price of goods and services, as the case may be, so as to protect consumer against unfair trade practices.
- 3) Right to choose. It means right to be assured, wherever possible, access to a variety of goods and services at competitive prices. In case of monopolies, say, railways, telephones etc., it means right to be assured of satisfactory quality and service at a fair price.
- 4) Right to be heard, i.e., the consumers interests will receive due consideration at appropriate forums. It also includes right to be represented in various forums formed to consider the consumers' welfare.
- 5) Right to seek redressal. It means the right to seek redressal against unfair practices or restrictive trade practices or unscrupulous exploitation of consumers. It also includes right to fair settlement of the genuine grievances of the consumers.
- 6) Right to consumer education. It means the right to acquire the knowledge and skill to be an informed consumer.

(b) Every employee shall be entitled to be paid by his employer in an accounting year, bonus, in accordance with the provisions of this act, provided he has worked in the establishment for not less than 30 working days in that year.

However notwithstanding anything content in the Act, and employee shall be disqualified from receiving bonus under this Act if he is dismissed from service for

- a) Fraud or
- b) Riotous or violent behavior while on the premises of the establishment or
- c) Thefts miss appropriation or sabotage of any property of the establishment.

Section -II (50 Marks) (Auditing)

5. Comment on the following statements based on legal provisions: 2X7
(No mark for wrong reasons or justification)
- (a) Test checks may be applied to all transactions.
 - (b) There is no need to design better "Internal Control" in an EDP or Computerized system.
 - (c) Management audit concerns with the appraisal of Management policies methods etc.

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- to determine better means of control only.
- (d) CAS-10 provides the standard cost Audit practice in respect of Material cost.
 - (e) M/s. X Associates were appointed in AGM held on 30.09.13 as auditor for 2013-14 but the auditor who was present in the Annual General Meeting declined to accept the appointment. Board of Directors thereafter passed a Resolution on 10.10.13 to appoint M/s. A. Associates as Auditor in place of M/s. X Associates.
 - (f) Besides Public Limited Company, Companies Auditors' Report Order 2003 (CARO) is applicable to all Private Companies.
 - (g) Under GAAP/GAAS, what are the Reporting Standards in respect of "DISCLOSURES"?

Answer:

5. (a) False - Transaction like opening and closing entries, depreciation entries and non-recurring exceptional transactions should not be subject to test check. Cash Book and Pass Book should be thoroughly checked.
- (b) Computerization automatically implies a constant review of the system to increase the efficiency in producing a reliable data.
As a result, the internal controls are normally better designed under "Computerized System". Automatic checks are instituted and the responsibilities of various persons are clearly stated. Periodical maintenance, up gradation & revision modifications are carried out.
- (c) to determine not only better means of control but also to determine (1) greater improved methods (2) more efficient operations (3) greater use of human and physical facilities (4) waste and deficiencies.
- (d) CAS-10 provides standard Cost Audit practice in respect of "Direct Expense".
- (e) If the Auditor declines the appointment in the AGM and hence no auditor was appointed in the AGM. It should be regarded that no auditor has been appointed by the Company at its AGM held on 30.09.2013. In such cases the company must inform to the Central Govt. within a period of 7 days. On receipt of information, the Central Govt. may appoint a person to fill in the vacancy in the office of auditor [Section 224(3) & 224(4)]. So, the appointment by BOD is not valid.
- (f) CARO is applicable to Private Company whose turnover exceeds INR 5 crores or where the paid up Capital & Reserves is more than INR 50 lakhs.
- (g) Reporting standards in respect of Disclosure :
If the auditor does not make any adverse comment in his report, the financial statements are taken as reasonably adequate.
6. (a) **Although Audit Report on the Accounts for Financial year ending 31.03.13 was addressed to share-holders, but Auditor did not send such Report to the share-holders, who therefore, preferred a complaint against the Auditor. Advise the share-holders as to their Right. 2**
- (b) **What are the points Auditor shall state in his report when he discovers that loan has been given by a limited company during the year. 2**
- (c) **When Gross Profit for 2011 42,000
and for 2012 45,000
Current Assets for 2012 16,000
Current Liabilities for 2012 20,000
Sales for 2011 60,000
Sales for 2012 75,000**

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- Then (i) Calculate the Gross Profit ratio for 2011 & 2012.
(ii) State the effect of rise or fall in G. P. ratio. 2
- (d) How an auditor shall report in his Audit Report to comply with CARO in respect of 4
(i) "Transaction in which Directors are interested"
(ii) "Internal control on purchase of assets and sale of goods".
- (e) What are the essentials of good working papers? State at least 4 points. 2
- (f) As in the case of other audits, the information technology audit too take some basic steps—what are such basic steps? 4
- (g) Management Audit can be conducted by the Chartered Accountant only—Comment. 2

Answer:

6. (a) It is not the duty of the Auditor to send the copy of Audit Report to each & every share holders. Although Audit Report is addressed to Shareholders but the same is submitted to the management of the Company who forward such Audit Report along with Directors Report giving Directors reply if any against Auditors comment to the Shareholders.
The Auditor cannot be held liable for the failure to send the Report to the Shareholders.
- (b) An auditor shall disclose in the Auditor's Report the following in respect of loan given by a limited company:
- Whether the loans are properly secured. Also, give the details of parties and amount involved in the transaction.
 - Whether the rate of interest and other terms and conditions of loan, secured or unsecured are prima facie prejudicial to the interest of the company.
 - Whether the payment of the principal amount and interest are also regular.
 - If over payment is more than one Lakh, whether reasonable steps have been taken by the company for recovery/payment of the principal and interest.

Also, to ensure that loans have been shown as Fixed Deposit.

(c) Gross Profit Ratio = $\frac{GP}{Sales} \times 100$

GP Ratio for 2011 $\frac{42,000}{60,000} \times 100 = 70\%$

GP Ratio for 2012 $\frac{45,000}{75,000} \times 100 = 60\%$

Effect: of low G.P. Ratio

May indicate unfavorable purchasing policies, inability of management to develop Sales Volume, over investment of plant facilities, increase in revenue expense etc.

- (d) i) Auditor shall state in his Audit Report
- Whether transactions that need to be entered into register in pursuant of Sec 301 of the companies Act have been so entered.
 - Whether each of these transactions has been made at prices which are reasonable having regard to the prevailing market price at the relevant time.

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These should be commented only in the Case of transactions exceeding the value of INR 5 crores.

ii) Is there an adequate internal Control procedure commensurate with the size of the Company and the nature of its business for the purchase of inventory and fixed assets and the sale of goods? Whether there is a continuing failure to correct major weaknesses in internal control?

(e)

- (i) Completeness i.e., they should contain all the essential information so that they may be of maximum utility. Facts which are not important should be omitted.
- (ii) Organisation and Agreements. The working paper should be so arranged that one may not find any difficulty in locating a particular matter. If they are not properly arranged it will entail loss of time in finding a particular fact while preparing the Report.
- (iii) Clearness. The facts in the working papers should be set out clearly.
- (iv) The facts stated should be readily apparent to the reader later on, e.g. schedules, where necessary, should be fully explanatory so that it will not be necessary to puzzle over various sections,
- (v) Papers should be clearly fastened together, arranged in a logical order, properly and adequately referenced and the subject matter clearly marked on the top.
- (vi) Sufficient space should be left after each note so that any decision taken by the auditor may be taken down in that space.
- (vii) It is therefore felt that if audit working papers are handed over to the clients, an auditor may not be able to depend himself, if any dispute arises in future.

(f) Basic Steps are

- i) Planning
- ii) Studying & evaluating Control
- iii) Testing and evaluating Control
- iv) Reports
- v) Follow up

(g) False: Besides Chartered Accountant, Management Audit can be conducted by

- i) Company talent which may include
 - a) Administrative Staff
 - b) An Audit Committee
 - c) An Officer on Special Duty
- ii) Outside Management Consultants viz.
 - a) Chartered Accountants or
 - b) Cost Accountants or
 - c) Management Consultants having no vested interest in the Company Management etc.
- iii) Company Talent as well as Management Consultants.

7. (a) What are the difference between IFRS, US GAAP and Indian GAAP in respect of "Interest paid". 2

(b) How you will adjust the expenses relating to previous year but disclosed in current year.2

(c) Contingent liabilities for bill discounted has not been disclosed inspite of Auditor's advice. How an Auditor shall dealt with such situation . 2

(d) H. Ltd., is the Holding Company of both ADC Ltd. and XYZ Ltd. Mr. Saxena a Chartered Accountant having a certificate of practice is a part time employee of XYZ Ltd. Can Mr.

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Saxena be appointed as Auditor of ADC Ltd. in its AGM.	2
(e) Explain Compliance Audit	4
(f) Explain Computer Auditing	4
(g) Management Audit concerns with the review, appraisal of an organisation, management policies etc. Why review and appraisal are necessary?	2

Answer:

(a) On the basis of cash flows:

Indian GAAP - Interest paid are classified as financing cash flows except in the case of financial enterprises where interest paid is classified as operating cash flows

IFRS – Interest paid may be classified as either operating or financing cash flows. Accounting policy choice once made should be followed consistently

US GAAP - Interest paid are classified as operating cash flows

On the basis of disclosure requirements:

Indian GAAP – Interest paid, received and dividend received are classified as operating cash flows

IFRS – Interest paid, received and dividend received are classified as operating cash flows

US GAAP - Interest paid, received and dividend received are classified as operating cash flows

(b) Income or Expense relating to previous year but arise in current year shall be as per Provisions of AS-5. Such items are passed through prior period adjustment account. Previous years items are normally included in the determination of net Profit and loss for Current Period or to show such items in the Statements of Profit and Loss after determination of Current Net Profit & Loss.

In either case, the objective is to indicate the effect of such item on the current profit or loss.

(c) In this case Auditor has no alternative but to "qualify his report" by indicating the fact in his audit Report to the share holders.

(d) In this case, Mr. Saxena being a part-time employee of XYZ Ltd. is not eligible to be appointed as auditor of XYZ Ltd. [Section 226(3)(b)].

A person who is disqualified as above is also disqualified for appointment to be an auditor of

1. it's holding Company
2. it's subsidiary company
3. a subsidiary of it's holding company. – Sec 226.(4)

Therefore, Mr. Saxena cannot be appointed as an auditor of ADC Ltd. since it is a subsidiary of it's holding company i.e., H Ltd.

(e) It is common to us that the business undertakings require some certified statement on various matters and the auditors certify such statements after carrying out audit which might be necessary under the- particular cases. All such audits are called Compliance Audit. Suppose when a company applied to a bank for some loan, a certified statement showing the turnover of the company for the past two or three years along with the current year might be necessary, and for this purpose the certified statements

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are to be attached with the application, otherwise the application will be rejected. So these certified statements showing the turnover of the company fall under the category of compliance audit. Internal audit for compliance could be more broad base to include compliance which documents procedures / policies, compliance with statutory requirements in the relevant areas etc.

- (f) Computer Auditing: In information processed on computer the one way of auditing is to get the printouts of all records, accounts and information and then check it as usual, but this is very time consuming and cannot evaluate the system internal controls and certain errors found etc., remains undetected. The other more acceptable way is to evaluate the controls in the computer information system and then decides the nature timing and extent of the substantive procedure to be followed and makes use of computer conducting compliance tests as well as substantive test, but and the auditor must have sufficient knowledge of computer system even in certain cases specialized skills in operation of computer system.
- (g) Necessary to determine
- Better means of Control
 - Greater improved method
 - More efficient operations
 - Greater use of human and physical facilities and
 - Waste and deficiencies
8. (a) How the verification of 'Know-how' will be conducted by you? 2
- (b) Explain the circumstances of materiality according to ICFAI 2
- (c) The company auditor incurred liability for defending against a civil proceedings although the Auditor worked honestly while performing his audit work. Whether such liability is to be borne by the Auditor? 2
- (d) State the correct position if following statements are wrong:
- Only Chartered Accountants are eligible for appointment as internal Auditor. 2
 - To comply with Corporate Governance, a listed company shall submit quarterly compliance report to the Registrar of Companies within 30 days? 1
- (e) A company licensed to operate as per provision of Sec. 25 of Companies Act, 1956. How an auditor shall report in his audit report to comply with CARO in respect of Fixed Deposit. 2
- (f) What is Voucher Audit? 2
- (g) As an Auditor what are the points/areas, you will consider while auditing in the case of data processing through computer service centre. 4
- (h) Why the company itself feels the need of management audit? 2

Answer:

8. (a) To verify "know-how"
- Check the minute book to see that acquiring "Know-how" is properly sanctioned.
 - Auditor should see that Know-how is properly accounted in the books -
 - If it is related to Plant & Machinery, it should be capitalized.
 - If it is regarding manufacturing process, it must be debited to P&L A/c.
 - If lump sum amount is paid for both the amount be allocated between capital & revenue appropriately.
 - Regular payment like royalty etc. be charged to P&L A/c.
- (b) According to the ICFAI, the circumstances of materiality are as under:
- Mistake discovered like valuation of stock, calculation of depreciation, calculation of interest, estimation of liability etc.
 - Non-disclosure of abnormal and unusual items or non-recurring income or expenditure etc.
 - Non-disclosure of items violating the Statutory Provision etc.

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(c) Right of Company auditor regarding Indemnity

The Co. auditor has a right to be indemnified out of the assets of the company against any liability incurred by him in defending against any civil & criminal proceeding by the company if it is provided that the auditor worked honestly while performing his audit work, as per section 633.

So, the auditor is not liable to bear the same as he worked with honesty while performing his audit work.

- (d) (i) The qualification of the Internal Auditor is not guided by any Statutory Provisions. This is determined by the management.
(ii) Quarterly compliance Report is submitted to Stock Exchange within 15 days from the close of quarter.
- (e) CARO is not applicable to a Section 25 companies. Hence no specific report under CARO is necessary.
- (f) Any audit with reference to some documentary evidence may be termed as Voucher Audit. The financial Audit is mainly carried out with reference to Voucher.

Statutory auditor certifies the statement of Accounts including the Balance Sheet after Carrying out audit which is mainly with reference to documentary evidence. However it should be remembered that after promulgation of the manufacturing and other companies (Auditor's Report) order 1988, a Statutory Auditor has also to carry out some audit which is not directly based on documentary evidences.

- (g) In this type of cases, the Auditor should:
- i) Verify that the Vendor is reliable and suitable having the skills experience and reputations.
 - ii) Evaluate the suitability of the contacted term with regard to fixed cost, variable cost, the scope and timing of activities, the service centre's responsibilities in terms of maintaining data integrity and providing suitable backup and recovery.
 - iii) Check the compliance with the terms of contract.
 - iv) Seek to ensure that his ability to collect and evaluate evidence in relation to the attainment of the objectives of outsourcing is not inhibited.
- (h) The following are the circumstances wherein the company itself feels that management audit is useful -
- i) Company itself feels the need of management audit to assess its managers' performances and link an incentive system to the results of such assessment.
 - ii) To overcome the human limitations of Top Management.
 - iii) To improve the management's production.
 - iv) Circumstances of corporate planning deficiencies, organization's structured defects, ineffective management control system etc. warrants the necessity of management audit.
 - v) In the circumstances of acquisition of another business entity, the acquiring organization needs to evaluate financial aspects, technical aspects and management aspects and analysis of these aspects takes the form of management audit.