Paper 12- Company Accounts & Audit

INTERMEDIATE EXAMINATION

GROUP - II

(SYLLABUS 2016)

SUGGESTED ANSWERS TO QUESTIONS

DECEMBER – 2019

Paper-12: COMPANY ACCOUNTS AND AUDIT

Time Allowed: 3 Hours **Full Marks : 100**

The figures in the margin on the right side indicate full marks.
Whenever considered necessary, suitable assumptions may be made and
Clearly indicated in the answer.
The Question Paper has two sections, A and B. Both sections are to be answered as per
Instructions given against each.

Section A (Company Accounts)
Answer Question No. 1 and any three from Question Nos. 2, 3, 4 and 5.

1. (a) Choose the correct alternative: **1x6=6**

(i) At present, a company can issue preference shares which are
- **(A) irredeemable.**
- **(B) redeemable after the expiry of 20 years from the date of issue.**
- **(C) redeemable before the expiry of 20 years from the date of issue.**
- **(D) redeemable after the expiry of 25 years from the date of issue.**

(ii) In case of purchase of assets under instalment payment system, instalments due after 12 months from the reporting date are shown as
- **(A) Current liability**
- **(B) Current assets**
- **(C) Non-current liability**
- **(D) Non-current assets**

(iii) Bonus paid at the end along with the policy amount to the policy holders is called
- **(A) Production bonus**
- **(B) Reversionary bonus**
- **(C) Gratuitous bonus**
- **(D) Maturity bonus**

(iv) In relation to an Electricity Company the amount of security deposit = Load x Load factor of the category in which the customer falls x Current tariff x _________.
- **(A) Billing cycle + 45 days**
- **(B) Billing cycle + 30 days**
- **(C) Billing cycle + 15 days**
- **(D) Billing cycle + 20 days**

(v) In case of a Banking Company General Ledger does not contain
- **(A) Control Accounts of all personal ledger**
- **(B) Assets Accounts**
- **(C) Contra Accounts**

(D) Revenue Accounts

(vi) Losses of theft are covered by_______________ insurance policies.
(A) Burglary
(B) Fire
(C) Marine
(D) None of the above

(b) Match the following items in Column 'A' with items shown in Column 'B': 1x4=4

	Column A		Column B
(1)	Contribution on actuarial basis for Gratuity benefits	(A)	AS 17
(2)	Buyback of equity shares	(B)	AS 15
(3)	Capitalization of borrowing costs	(C)	Securities Premium A/c
(4)	Geographical segment	(D)	AS 16

(C) State whether the following statements are True or False: 1x4=4

(i) Rollover must be with the written consent of the debenture holders.
(ii) In case of Forfeiture of Shares, a shareholder is not able to pay the further calls and returns his shares to the company for cancellation voluntarily.
(iii) Cash comprises cash in hand and foreign currency balances.
(iv) Minimum aggregate value of Paid-up Capital and Reserve in case of a Banking Company incorporated outside India not having place(s) of business in the city of Mumbai or Kolkata or both should be ₹15 lakhs.

Answer :

1.(a) (i) (C)
(ii) (C)
(iii) (B)
(iv) (A)
(v) (D)
(vi) (A)

(b) 1. (B)
2. (C)
3. (D)
4. (A)

(c) (i) True
(ii) False
(iii) Ture
(iv) True

2. (a) Moti Ltd. invited applications for issuing 10,00,000 Equity Shares of ₹10 each at a premium of ₹2 per share. The amount was payable as follows:

On Application — ₹5 (including Premium)
One Allotment — ₹4
On First and Final call — ₹3

Applications for 15,00,000 shares were, received. Applications for 3,00,000 shares were rejected and pro rata allotment was made to remaining applicants. Excess application money was utilised towards sum due on allotment. Giri who has applied for 24,000 shares failed to pay the allotment and call money. His shares was forfeited.

Out of the forfeited shares, 10,000 shares were reissued for ₹8 per share fully paid up. Pass necessary Journal entries in the books of Moti Ltd. 8

(b) K Ltd. purchased goods from a US Company for US $ 50000 on 10.02.2019 and settled the due on 30.06.2019. K Ltd. closes the books of accounts on 31st March. Exchange rates were as follows:

Date	Rate
10.02.2019	47.40
31.03.2019	46.00
30.06.2019	47.80

Calculate the exchange loss/gain on the reporting date and on the settlement date and comment on their treatment as per AS 11. 4

Answer :

2.(a)

Date	Particulars	L.F.	Dr.(₹)	Cr.(₹)
	Bank A/c Dr. To Equity Shares Application A/c (Being the application money received on 15,00,000 shares)		75,00,000	 75,00,000
	Equity Shares Application A/c Dr. To Equity Share Capital A/c (10,00,000 X ₹3) To Securities Premium Reserve A/c (10,00,000 X ₹2) To Bank A/c (3,00,000 X ₹5) To Equity Share Allotment A/c (2,00,000 X ₹5) (Being the application money adjusted)		75,00,000	 30,00,000 20,00,000 15,00,000 10,00,000
	Equity Shares Allotment A/c Dr. To Equity Share Capital A/c (Being the allotment money due)		40,00,000	 40,00,000
	Bank A/c Dr. To Equity Shares Allotment A/c Or Bank A/c Dr. Calls-in-Arrear A/c Dr. To Equity Shares Allotment A/c (Being the allotment money received except on 20,000 shares)**(WN 1)**		29,40,000 29,40,000 60,000	 29,40,000 30,00,000
	Equity Shares First and Final Call A/c Dr. To Equity Share Capital A/c (Being the First and Final Call money due)		30,00,000	 30,00,000
	Bank A/c Dr. To Equity Shares Allotment A/c Or Bank A/c Dr. Calls-in-Arrear A/c Dr. To Equity Shares First and Final Call A/c (Being the call money received except on 20,000 shares)		29,40,000 29,40,000 60,000	 29,40,000 30,00,000
	Equity Share Capital A/c Dr. To Forfeited Shares A/c To Equity Shares Allotment A/c To Equity Shares First and Final call A/c Or,		2,00,000	 80,000 60,000 60,000

	Equity Shares Capital A/c Dr. To Calls-in-Arrear A/c (₹60,000 + ₹60,000) To Forfeited Shares A/c (Being 20,000 shares forfeited due to nonpayment of allotment and call money)		2,00,000	 1,20,000 80,000
	Bank A/c (10,000 X ₹8) Dr. Forfeited Shares A/c (10,000 X ₹2) Dr. To Equity Shares Allotment A/c (Being 10,000 forfeited shares reissued for ₹8 per share fully paid -up)		80,000 20,000	 1,00,000
	Forfeited Shares A/c Dr. To Capital Reserve A/c (Being the gain on re-issue transferred to Capital Reserve account)**(WN 2)**		20,000	 20,000

Working Note-1

Calculation of Money Received on Allotment:

(i) Pro rata allotment = 12,00,000:10,00,000 = 12:10

(ii) No. of shares allotted to Giri = 24,000 X 10/12 = 20,000 shares

(iii) Money received on application from Giri (24,000 shares X ₹5) = ₹1,20,000

Less: Amount adjusted on application (20,000 shares X ₹5) = ₹1,00,000

Excess application money adjusted on allotment = **₹ 20,000**

(iv) Money due from Giri on allotment:

Money due from on allotment (20,000 X ₹4) = ₹80,000

Less: Excess application money adjusted [as per (iii)] = ₹20,000

Money not paid by Giri = **₹60,000**

(v) Money received on allotment:

Total amount due on allotment (10,00,000 X ₹4) = ₹40,00,000

Less: Excess application money adjusted = ₹10,00,000

= ₹30,00,000

Less: Money not paid by Giri [as per (iv)] = ₹ 60,000

= **₹29,40,000**

Working Note-2

Calculation of amount transferred to Capital Reserve:

Amount forfeited on 10,000 shares [₹80,000 X 10/20] = ₹40,000

Less: Discount on re-issue = ₹20,000

Gain on re-issue transferred to Capital Reserve **₹20,000**

(b) As per AS 11, transactions such as purchase, sales etc. are to be recorded in the books of accounts at the exchange rate prevailing on the date of transaction. Any exchange gain/ loss arising subsequently is to be transferred to Income Statement.

Value of the goods purchased	= $ 50,000
Exchange rate on the date of transaction	= ₹47.40/$
So, purchase to be recorded in the books = 50,000 x 47.40	= ₹ 23,70,000
Exchange rate on the date of reporting (31.03.19)	=₹46.00/$
Value of the payables on 31.03.19 = 50,000 x 46	= ₹ 23,00,000

Exchange gain on 31.03.2019 = ₹ (23,70,000 – 23,00,000) = ₹ 70,000, to be credited to P/L A/C.
Exchange rate on the date of settlement (30.06.19) = ₹ 47.80/$
Exchange loss on 30.06.19 = 50,000 x (47.80 — 46.00) = ₹ 90,000 to be debited to P/L A/c.

3. **(a) The following figures have been extracted from the books of M Limited for the year ended on 31.03.2019. You are required to prepare a Cash Flow Statement.**

(i) Net profit, before adjusting income tax but after taking into account the following items, was ₹10 lakhs.

- **Depreciation on Assets ₹2,50,000.**
- **Discount on issue of Debentures written off ₹15,000.**
- **Interest on Debentures paid ₹1,75,000.**
- **Book value of investment ₹1,50,000 (Sold for ₹1,60,000).**
- **Interest received on investments ₹30,000.**

(ii) Income tax paid during the year ₹4,80,000.
(iii) 7,500 10% preference shares of ₹100 each were redeemed on 31.03.2019 at a premium of 5%. Further the company issued 25,000 equity shares of ₹10 each at a premium of 20% on 02.04.2018. Dividend on preference shares were paid at the time of redemption.
(iv) Dividends paid for the year 2017-18 ₹2,50,000 and interim dividend paid ₹1,50,000 for the year 2018-19.
(v) Land was purchased on 02.04.2018 for ₹1,20,000 for which the company issued 10,000 equity shares of ₹10 each at a premium of 20% to the land owner as consideration.
(vi) Current assets and liabilities were as follows:

Particulars	31.03.2018 (₹)	31.03.2019 (₹)
Stock	6,00,000	6,59,000
Sundry Debtors	1,04,000	1,06,550
Cash in hand	98,150	17,650
Bills Receivable	25,000	20,000
Bills Payable	22,500	20,000
Sundry Creditors	83,000	85,650
Out standing expenses	37,500	40,900

8

(b) The books of a Bank include a loan of ₹5,00,000 advanced on 30.09.2017, interest chargeable @ 16% p.a. compounded quarterly. The security for the loan being 7,000 shares of ₹100 each in a public limited company valued @ ₹90 each. There is no repayment till 31.12.2018. On 31.12.2018, the value of shares declined to ₹85 per shares. How would you classify the loan as secured or unsecured in the Balance Sheet? 4

Answer :

3. (a)

Cash Flow Statement
For the year ended 31.03.2019

Particulars	Amount (₹)	Amount (₹)	Amount (₹)
1. Cash Flow from Operating Activities:			
Net Profit		10,00,000	
Add: Adjustment for non-cash expenses			
Depreciation on assets	2,50,000		
Discount on issue of debentures	15,000		
Interest on debentures	1,75,000		
		4,40,000	
		14,40,000	
Less: Profit on sale of investment (1,60,000 -1,50,000)	10,000		
Interest received on investment	30,000	(40,000)	
Operating profit before adjustment for changes in W.C.		14,00,000	
Add: Decrease in Bills Receivable (25,000 - 20,000)	5,000		
Increase in Sundry Creditors (85,650 - 83,000)	2,650		
Increase in Outstanding Expenses (40,900 - 37,500)	3,400	11,050	
		14,11,050	
Less: Increase in Stock (6,59,000 - 6,00,000)	59,000		
Increase in Sundry Debtors (1,06,550 - 1,04,000)	2,550		
Increase in Bills Payable (22,500 - 20,000)	2,500	(64,050)	
		13,47,000	
Less: Income Tax paid		4,80,000	
Net Cash Flow from Operating Activities			**8,67,000**
2. Cash Flow from Investing Activities:			
Sale of investment		1,60,000	
Interest received on investment		30,000	
			1,90,000
3. Cash Flow from Financing Activities:			
Issue of shares at premium		3,00,000	
Redemption of preference shares at 5% premium		(7,87,500)	
Preference dividend paid		(75,000)	
Interest on debenture paid		(1,75,000)	
Equity dividend paid (2,50,000+1,50,000)		(4,00,000)	**(11,37,500)**
Total Cash Flow (1+2+3)			**(80,500)**
Add: Opening cash & cash equivalent			98,150
Closing cash & cash equivalent			**17,650**

Notes: Purchase of land against shares has not been shown in the C/F Statement as it does not amount to any inflow or outflow of cash.

(b)

Date	Particulars	Amount (₹)
31.12.2018	Balance of Loan (Principal)	5,00,000
	Add: Outstanding Interest	1,08,326
	Total Claim	**6,08,326**
	Less: Value of Security at that date (7,000 shares @ ₹85 per share)	5,95,000
	Balance	**13,326**

Classification : Secured Loan ₹ 5,95,000
Unsecured Loan ₹13,326

Workings:

Calculation of Outstanding Interest:

Quarters ending	Interest (₹)	Workings	Closing Balance with Principal (₹)
31.12.2017	20,000	(₹ 5,00,000 X 16% X 3/12)	5,20,000
31.03.2018	20,800	(₹ 5,20,000 X 16% X 3/12)	5,40,800
30.06.2018	21,632	(₹ 5,40,800 X 16% X 3/12)	5,62,432
30.09.2018	22,497	(₹ 5,62,432 X 16% X 3/12)	5,84,929
31.12.2018	23,397	(₹ 5,84,929 X 16% X 3/12)	6,08,326
	1,08,326		

4. The following is the trial balance of Beta Ltd. as on 31.03.2019:

Dr.			**Cr.**
Particulars	**(₹)**	**Particulars**	**(₹)**
Stock in trade on 01.04.18	**1,50,000**	**Purchase returns**	**20,000**
Purchases	**4,90,000**	**Sales**	**6,80,000**
Salaries	**60,000**	**Discount received**	**6,000**
Freight, Carriage etc.	**1,900**	**Balance of Profit and Loss (Cr.)**	**12,000**
Furniture	**34,000**	**Share capital (₹ 10)**	**2,00,000**
Contribution to P.F.	**10,000**	**Trade payables**	**49,000**
Rent and Rates	**8,000**	**General reserve**	**31,000**
Stationary	**3,800**		
Repairs	**4,000**		
Insurance	**6,000**		
Misc. expenses	**300**		
Staff welfare expenses	**5,000**		
Plant and machinery	**58,000**		
Cash at bank	**92,400**		
Patents	**9,600**		
Trade receivables	**65,000**		
	9,98,000		**9,98,000**

You are required to prepare Statement of Profit and Loss for the year ending 31st March, 2019 and Balance Sheet as at that date after taking into consideration the following information:

(i) Closing stock as at 31.03.2019 is ₹1,76,000.

(ii) Make a provision for income tax @ 40%.

(iii) Depreciate plant and machinery @ 15%, furniture @ 10% and patents @ 5%.

(iv) Outstanding rent ₹1,600 and outstanding salaries ₹1,800.

(v) The directors recommended a dividend @ 15% after transfer to General Reserve ₹4,000.

(vi) Dividend Distribution Tax payable at an effective rate of 20.36%.

(vii) Trade receivables of ₹5,000 are due for more than 6 months. Provide ₹1020 for doubtful debts.

(viii) The authorized capital of the company is ₹4,00,000 divided 40,000 equity shares of ₹10 each of which 20,000 shares have been issued and fully paid up. 2,000 shares were, however, issued for consideration other than Cash. **12**

Answer :

4.

Beta Ltd.
Balance Sheet as on 31st March, 2019

Particulars	Note No.	As on 31.03.2019 (₹)
EQUITY AND LIABILITIES		
Shareholder's Fund :		
(a) Share Capital	1	2,00,000
(b) Reserve & Surplus	2	1,18,600
Non-Current Liabilities		Nil
Current Liabilities :		
(a) Trade Payables		49,000
(b) Other current Liabilities	3	3,400
(c) Short-Term Provisions	4	50,400
Total		**4,21,400**
ASSETS		
Non-Current Assets :		
Fixed Assets :		
(a) Tangible Assets	5	79,900
(b) Intangible Assets		9,120
Current Assets :		
(a) Inventories		1,76,000
(b) Trade Receivables	6	63,980
(c) Cash & Cash equivalents	7	92,400
Total		**4,21,400**

Foot Note: Contingent Liability for Proposed Dividend and DDT = ₹36,108.

Statement of Profit and Loss
for the Year end 31st March, 2019

Particulars	Note No.	31.03.2019 (₹)
Revenue from Operations	8	6,80,000
Other Income	9	6,000
Total Revenue (A)		**6,86,000**
Expenses:		
Purchase of Stock-in Trade	10	4,70,000
Changes in Inventories of Stock-in-Trade	11	(26,000)
Employee Benefits Expense	12	76,800
Depreciation & Amortization expenses	13	12,580
Other Expenses	14	26,620
Total Expenses (B)		**5,60,000**
Profit Before Tax (A-B)		1,26,000
Less: Provision for taxation @ 40%		50,400
Profit after tax		75,600

Notes to Accounts:

Particulars	Amount (₹)	Amount (₹)
1. Share Capital		
Amortized: 40000 shares of ₹10 each		4,00,000
Issued, Subscribed and Paid up: 20000 shares of ₹10 each		2,00,000
Shares issued for consideration other than cash: 2000 shares of ₹10 each		20,000

2. General Reserves		
As on 1.04.2018	31,000	
Add: Transfer during the year	4,000	35,000
Profit and Loss: As on 1.04.2018	12,000	
Add: Profit during the year	75,600	
	87,600	
Less: Transfer to General Reserve	4,000	83,600
		1,18,600
3. Other Current Liabilities		
Outstanding Rent		1,800
Outstanding Salaries		1,600
		3,400
4. Short Term Provisions		
Provision for Taxation		50,400
5. Fixed Assets		
Tangible Assets		
Plant and Machinery	58,000	
Less: Depreciation	8,700	49,300
Furniture	34,000	
Less: Depreciation	3,400	30,600
		79,900
Patent	9,600	
Less: Amortization	480	9,120
6. Trade Receivables:		
Trade receivable due for more than 6 months		5,000
Trade receivable (Others)		60,000
		65,000
Less: Provision for doubtful debs		1,020
		63,980
7. Cash and Cash Equivalent: Cash at Bank		92,400
8. Revenue from Operations: Sales		6,80,000
9. Other Income: Discount received		6,000
10. Purchase of Stock-in trade: Gross Purchase Less: Returns (4,90,000 – 20,000)		4,70,000
11. Changes in inventories of Stock-in-trade: Opening – Closing (1,50,000 – 1,76,000)		(26,000)
12. Employee benefit expense:		
Salary Add: Outstanding (60,000 + 1,800)	61,800	
Contribution to PF	10,000	
Staff welfare exp.	5,000	76,800
13. Depreciation and Amortization Expenses:		
On Plant and Machinery @ 15%	8,700	

On Furniture @ 10%	3,400	
Amortization: on Patent @ 5%	480	12,580
14. Other Expenses:		
Rent and rates including outstanding: (8,000+1,600)		9,600
Freight and Carriage		1,900
Stationary		3,800
Repairs		4,000
Insurance		6,000
Miscellaneous Expenses		300
Provision for Doubtful Debts		1,020
		26,620

Working Notes:

1) Dividend for the year proposed :15% on 2,00,000		30,000
2) Dividend distribution tax: 20.36% x 30,000		6,108
		36,108

5. Write short notes (any three): 4x3=12

(a) Rules for identification of Reportable Segments
(b) Issue of shares at a premium
(c) Accounting of depreciation by an Electricity company
(d) Disclosure requirement under Schedule III with respect to Trade Receivables

Answer :

5. (a)

Rules for identification of Reportable Segments

A business segment or geographical segment should be identified as a reportable segment if:

(a) its revenue from sales to external customers and from transactions with other segments is 10 per cent or more of the total revenue, external and internal, of all segments; or
(b) its segment result, whether profit or loss, is 10 per cent or more of -
  (i) the combined result of all segments in profit, or
  (ii) the combined result of all segments in loss, whichever is greater in absolute amount; or
(c) its segment assets are 10 per cent or more of the total assets of all segments.

A business segment or a geographical segment which is not a reportable segment as per the conditions mentioned above, may be designated as a reportable segment despite its size at the discretion of the management of the enterprise. If that segment is not designated as a reportable segment, it should be included as an unallocated reconciling item.

If total external revenue attributable to reportable segments constitutes less than 75 per cent of the total enterprise revenue, additional segments should be identified as reportable segments, even if they do not meet the 10 per cent thresholds as mentioned above, until at least 75 per cent of total enterprise revenue is included in reportable segments.

(b) Issue of Shares at a Premium [Section 52]

A company may issue shares at a premium, i.e., at a value greater than its face value. The power to issue shares at a premium need not be given in the Articles of Association. Premium so received shall be credited to a separate account called Securities Premium Account.
Section 52 of the Companies Act, 2013 gives the purposes for which share premium account may be applied by the company.

These are:
1. For the issue of fully paid bonus shares to the members of the company;
2. For writing off preliminary expenses of the company;
3. For writing off the expenses of the commission paid or discount allowed on any issue of shares or debentures of the company; and
4. For providing premium payable on the redemption of any redeemable preference shares or debentures of the company.
5. For the purchase of its own shares or other securities u/s 68.

(c) Accounting for Depreciation by an Electricity Company:

i. As per 2009 Regulation, it has been stated in the Tariff Policy that the depreciation rates for the assets shall be specified by the Central Electricity Regulatory Commission (CERC) and these rates of depreciation shall be applicable for the purpose of tariff as well as accounting.
ii. The Office of the Comptroller and Auditor General of India (CAG) has expressed an opinion that power sector companies shall be governed by the rates of depreciation as notified by the CERC for providing depreciation in respect of generating assets in the account instead of the rates as per the Companies Act, 2013. Accordingly, a Company should revise its accounting policies relating to charging of depreciation w.e.f. 1st April 2009 considering the rates and methodology notified by the CERC for determination of tariff through Regulations, 2009.
iii. As per 2009 Regulations, depreciation represents a Cash Flow for Repayment of Loan not by allowing Advance against Depreciation but by prescribing higher rates of depreciation for initial years of loan redemption.
iv. The CERC prescribes following two methods of depreciation:
   a. The Straight-line Method by application of a fixed rate over the fair life of the asset.
   b. Optimized Depreciated Replacement Cost (ODRC) based method under which the depreciation could be a method for replacement of the asset.

(d) Disclosure requirement under Schedule III with respect to Trade Receivables

Schedule III Disclosure Requirement	Points
1. Aggregate amount of Trade Receivables outstanding for a period exceeding 6 months from the date they are due for payment should be separately stated.	• Sch III requires separate disclosure of ―Trade Receivables O/s for a period exceeding 6 months from the date they become due for payment‖, only for the current portion of Trade Receivables.
2. Security-wise Details: Trade Receivables shall be separately sub-classified as – (a) Secured, considered Good (b) Unsecured, considered Good (c) Doubtful.	• Where no due date is specifically agreed upon, normal credit period allows by the Company should be taken into consideration for computing the due date, which may vary depending upon the Nature of Goods

3. Bad/Doubtful: Allowance for Bad and Doubtful Loans and Advances shall be disclosed under the relevant heads separately.	or Services sold and the Type of Customers, etc. • Amounts due under contractual obligations, e.g. dues in respect of Insurance Claims, Sale of Fixed Assets, Contractually Reimbursable Expenses, interest Accrued on Trade Receivables, etc, cannot be included within Trade Receivables, such Receivables should be classified as "Other Current Assets" and each such item should be disclosed nature-wise.
4. Directors, etc: Debts due by Directors or Other Officers of the Company or any of them either severally or jointly with any other person or debts due by Firms or Private Companies respectively in which any Director is a Partner or a Director or a Member should be separately stated	• Lean Period Activities: Receivables arising out of sale of materials/ rendering of services during a Company's lean period should be included under "Trade Receivables", if such activity is in the normal course of business. If they are not part of "normal course of business", they are to be classified under "Other Assets".

Section B (Audit)
Answer Question No. 6 and any three from Question Nos. 7, 8, 9 and 10.

6.(a) Identify the correct alternative in each of the following cases: 1x6=6

(i) Section 146 of the Companies Act, 2013 deals with
- **(A) Auditor not to render certain services**
- **(B) Auditor to sign Audit Reports**
- **(C) Auditor to attend general meeting**
- **(D) Punishment for contravention**

(ii) Which of the following is not included in the Current Audit File?
- **(A) Memorandum and Articles of Association**
- **(B) Current year's audit programme**
- **(C) Internal Control Questionnaire**
- **(D) Copies of budget**

(iii) Which of the following is not an external audit evidence?
- **(A) Quotations**
- **(B) Confirmation from debtors**
- **(C) Goods Received Note**
- **(D) Confirmation from bankers**

(iv) The ___________ shall act as the secretary of the Audit Committee.
- **(A) Auditor**
- **(B) Managing Director**
- **(C) Comptroller and Auditor General**
- **(D) Company Secretary**

(v) Cost Auditor is appointed by
- **(A) Audit Committee**
- **(B) Board of Directors**

(C) Board of Directors on recommendation from Audit Committee
(D) None of the above

(vi) Remuneration of Auditors is covered under the following section of Companies Act, 2013:
(A) Section 142
(B) Section 148
(C) Section 139
(D) Section 143

(b) Match the following items in Column 'A' with items shown in Column 'B': 1x4=4

Column A		Column B	
(1)	Section 144 of the Companies Act	(A)	Fundamental Accounting Assumption
(2)	Reporting of fraud by Auditor to Central Government	(B)	External and Internal Audit
(3)	Functional Classification of Audit	(C)	Form ADT-4
(4)	Going Concern	(D)	Auditors not to render certain services

(c) State whether the following statements are True or False: 1x4=4

(i) An audit work reflects the work done by the Management.
(ii) "Branch Office" in relation to a Company means any establishment described as such by the Company.
(iii) Cooling period of the individual auditor is 2 consecutive terms of 5 years.
(iv) There is no difference between Statutory and External audit.

Answer :

6. (a) (i) (C)
(ii) (A)
(iii) (C)
(iv) (D)
(v) (C)
(vi) (A)

(b) 1. (D)
2. (C)
3. (B)
4. (A)

(c) (i) False
(ii) True
(iii) False
(iv) False

7. (a) Discuss the basic principles of governing an audit as per SA 200. 6

(b) "The existence of a good internal check system reduces to a great extent the work of the auditor but does not reduce his liability."— Discuss. 6

Answer:

7. (a) SA 200 issued by ICAI (CA) gives the following basic principles that govern the auditor's responsibilities whenever an audit is carried out:

(i) Integrity, objectivity and independence:- The auditor should be straight-forward, honest, sincere and free form any influence on his audit work. He should maintain impartiality and be free of any interest.

(ii) Confidentiality: - He should not disclose the client's information to anybody without the client's permission or under any regulatory requirement.

(iii) Skills and competence:- The audit should be performed and audit report be prepared by adequately trained, experienced and competent person.

(iv) Work performed by others:- The auditor should carefully supervise the work performed by others (such as his subordinates, other auditors, experts etc.) as remains responsible for the work delegated by him to his assistants, other auditors or experts.

(v) Documentation: - Proper working papers should be maintained by the auditor to evidence the audit work. Working paper which is maintained is to demonstrate that the audit is in adherence to the basic principles.

(vi) Planning: - The auditor should obtain the knowledge about client's business to determine the nature, timing and the extent of the audit procedures.

(vii) Audit evidence: - The auditor should obtain sufficient appropriate audit evidence through performing the compliance and substantive procedures.

(viii) Accounting system and internal controls: - An understanding of the accounting system and the related internal controls help in determining the nature, timing and extent of other audit procedures.

(ix) Audit conclusions and reporting: - On the basis of conclusions drawn from the audit evidence obtained the auditor should give unqualified report or qualified report or adverse report or the disclaimer report.

7. **(b)** In an organisation, an auditor is appointed to authenticate the books of accounts and final financial statements based on all available evidences. He is also to express an unbiased opinion on the exhibition of true and fair view of the financial performance and financial state of affairs through the Income Statement and the Balance Sheet respectively. Thus keeping in mind such an objective the auditor needs to decide the extent of examination that he should conduct to arrive at any conclusion. The auditor, in this context, can resort to either detailed checking or test checking. Detailed checking refers to the examination of books of accounts in detail. Test checking, on the other hand, is the technique of checking some transactions selected as sample from the group of transactions and drawing conclusion on that basis, taking sample transactions selected to be the representative of the remaining transactions. Detailed checking is time consuming as well as laborious whereas test checking relieves the auditor from such pain. Thus, in actual practice, often the auditor is found reporting to test checking, provided the internal check system is satisfactory. Reliance on an effective internal check system and thereby streamlining the audit process enables the auditor to devote more time in examining the critical areas of accounting including valuation of closing stock, valuation of assets and liabilities, determining the reasonableness of provisions etc.

However, such reliance simultaneously increases the risk of the auditor. This is because even a sound internal check system cannot guarantee the non-existence of any error or fraud in the accounts. Thus, when the auditor applies test checking instead of a detailed checking, there is every possibility that any such error or fraud remains undetected.

8. (a) Discuss the provisions relating to 'Punishment for Contravention' under section 147 of the companies Act 2013. 6

(b) List down the certain services which are not to be rendered by the Auditor of a Company. 6

Answer :

8. (a) Punishment for Contravention (Section 147):

(1) If any of the provisions of sections 139 to 146 (both inclusive) is contravened, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees, or with both.

(2) If an auditor of a company contravenes any of the provisions of section 139, section 143, section 144 or section 145, the auditor shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees or four times the remuneration of the auditor, whichever is less.

Provided that if an auditor has contravened such provisions knowingly or willfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees or eight times the remuneration of the auditor, whichever is less.

(3) Where an auditor has been convicted under sub-section (2), he shall be liable to—
 (i) refund the remuneration received by him to the company; and
 (ii) pay for damages to the company, statutory bodies or authorities or to any other persons for loss arising out of incorrect or misleading statements of particulars made in his audit report.

(4) The Central Government shall, by notification, specify any statutory body or authority or an officer for ensuring prompt payment of damages to the company or the persons under clause (ii) of subsection (3) and such body, authority or officer shall after payment of damages to such company or persons file a report with the Central Government in respect of making such damages in such manner as may be specified in the said notification.

(5) Where, in case of audit of a company being conducted by an audit firm, it is proved that the partner or partners of the audit firm has or have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to or by, the company or its directors or officers, the liability, whether civil or criminal as provided in this Act or in any other law for the time being in force, for such act shall be of the partner or partners concerned of the audit firm and of the firm jointly and severally.

Provided that in case of criminal liability of an audit firm, in respect of liability other than fine, the concerned partner or partners, who acted in a fraudulent manner or abetted or, as the case may be, colluded in any fraud shall only be liable.

(b) AUDITOR NOT TO RENDER CERTAIN SERVICES [SECTION 144]

An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case maybe, but which shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company) namely:—

(a) accounting and book keeping services;
(b) internal audit;
(c) design and implementation of any financial information system;
(d) actuarial services;
(e) investment advisory services;
(f) investment banking services;
(g) rendering of outsourced financial services;
(h) management services; and

(i) any other kind of services as may be prescribed.

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

Explanation :— For the purposes of this sub-section, the term "directly or indirectly" shall include rendering of services by the auditor:-

i. in case of auditor being an individual, either himself or through his relative or any other person connected or associated with such individual or through any other entity, whatsoever, in which such individual has significant influence or control, or whose name or trade mark or brand is used by such individual;
ii. in case of auditor being a firm, either itself or through any of its partners or through its parent, subsidiary or associate entity or through any other entity, whatsoever, in which the firm or any partner of the firm has significant influence or control, or whose name or trade mark or brand is used by the firm or any of its partners.

9. (a) With reference to the Companies (Cost records and Audit) Rules 2014, as amended, discuss provisions relating to maintenance of cost accounting records and cost audit. 6

(b) Discuss briefly some of the situations calling for qualifications in Audit Report. 6

Answer:

9. (a) With reference to the Companies (Cost Records and Audit) Rules 2014, as amended:
The provisions regarding Maintenance of Cost Accounting Records and Cost Audit are as follows –

The Rules state that cost records are to be maintained in Form CRA-1, which provides principles to be followed for different cost elements. The principles are in sync with the cost accounting standards issued by the Institute of Cost Accountants of India. Since the Rules are principle based, no format has been prescribed for maintenance of cost accounting records like pre-2011 industry specific rules. It is opened for industry to maintain cost accounting records according to its size and nature of business so long as it determines a true and fair view of the cost of production, cost of sales and margin of the products/services. The cost audit report is required to be in conformity with the "cost auditing standards" as referred to in Section 148 of the Companies Act, 2013. It may be noted that the Council of the Institute of Cost Accountants of India has made it mandatory for cost accountants in practice to follow and conform to the Cost Accounting Standards issued by it and it is incumbent on the cost auditors to report any deviations from cost accounting standards.

(b) Some situations calling for qualifications in Audit Reports are :

i. Where the Auditors are unable to obtain all the information and explanations which they consider necessary for the purposes of their audit, e.g. –

(a) Absence of satisfactory documentary evidence of the existence of ownership of the material assets, such as, title deeds in respect of land,

(b) Absence of vouchers in respect of material payments made by the Company,
(c) Destruction of books and records by fire or accident,
(d) Non-availability of books and records owing to unavoidable circumstances, such as books and records of "a foreign branch with which no communication is possible.

ii. Where proper books of accounts have not been kept in accordance with the law.
iii. Where the Balance Sheet and P&L Account are not in agreement with the hooks of account and returns.
iv. When the information required by law is not furnished.

v. When the accounts do not disclose a true and fair view like –

(a) Where the accounting practices followed by the Company are not considered appropriate to the circumstances and nature of the business e.g. treatment of HP Sales as outright sales,
(b) Where there has been a change in accounting principles or procedures in relation to material items, such valuation of stock, depreciation, treatment of by-product cost, etc. without adequate explanation and disclosure of effect of the change,
(c) Where difference of opinion with management has arisen regarding valuation or realisability of assets, such as Stock-in-Trade, Debtors, Loans & Advances or the extent of liabilities, contingent or otherwise,
(d) Where income or expenditure is not properly reflected so as to show a fair figure of profit for the year,
(e) Where information is not required by law to be disclosed but the disclosure of which is considered essential by the Auditors in order to show a true and fair view,
(f) Where there is a contravention of the provisions of the Companies Act having a bearing upon the accounts and transactions of the Company e.g. donations to political parties or for political purposes in contravention of Section 182, or contributions to charitable or other funds in excess of the limitation specified in Section 181;
(g) Where the Company has contravened the provisions of its Memorandum and Articles of Association.

10. Write short notes (any three): **4x3=12**
(a) Branch Audit
(b) Information Systems Audit
(c) Audit of Municipalities and Panchayats (Local Bodies)
(d) Audit of interest on debentures

Answer :

10 (a) Branch Audit

"Branch office", in relation to a company, means any establishment described as such by the company - section 2(14) of the 2013 Act. Where a company has a branch office, the accounts of that office shall be audited either by the auditor appointed for the company (herein referred to as the company's auditor) under this Act or by any other person qualified for appointment as an auditor of the company under this Act and appointed as such under section139, or where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country and the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be such as may be prescribed.

Provided that the branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

(b) Information Systems Audit:

According to Ron Weber, "Information systems auditing is an organizational function that evaluates asset safeguarding, data integrity, system effectiveness, and system efficiency in computer based information systems". It has arisen for seven major reasons:

i. The consequences of losing the data resource;
ii. The possibility of misallocating resources because of decision based on incorrect data or decision rules;
iii. The possibility of computer abuse if computer systems are not controlled;
iv. The high value of computer hardware, software, and personnel;
v. The high costs of computer error;
vi. The need to maintain the privacy of individual persons; and
vii. The need to control the evolutionary use of computers.

(c) Audit of Municipalities and Panchayats (Local Bodies)

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

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

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

(d) Audit of interest on debentures:

A predetermined fixed rate of interest is payable on debentures irrespective of the fact that company has earned the profit or not. Debenture holders are creditors of the company, they are not the owners. They have no voting powers and cannot influence the management but their claim of interest rank ahead of the claims of the shareholders. Auditor's Duty:

i. The payment of interest should be vouched by the auditor with the acknowledgement of the debenture-holders, endorsed warrants and in case of bearer debentures with the coupons surrendered.
ii. The auditor should reconcile the total amount paid with the total amount due and payable with the amount of interest outstanding for payment.
iii. He should ensure that the interest paid on debenture like that on other fixed loans, must be disclosed as a separate item in the Profit & Loss Account.