Paper 19 – Cost and Management Audit

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Full Marks : 100 **Time allowed: 3 hours**

Answer Question No. 1 which is compulsory and carries 20 marks and any five from Question No. 2 to 8.

Section A (All questions are compulsory)

1. Choose the correct option among four alternative answer. (1 mark for correct choice, 1 mark for justification wherever applicable & necessary) [10*2=20 marks]

(i) Normal capacity is:
(A) Maximum production capacity of a plant.
(B) Difference between installed capacity and actual capacity utilization
(C) Volume of production achieved or achievable on an average over a period under normal circumstances
(D) Installed capacity minus inevitable interruptions.

(ii) CAS 20 deals with:
(A) Joint Costs
(B) Royalty and Technical Knowhow fee
(C) Research and Development Costs
(D) Interest and Financing charges.

(iii) Under Part D of the Annexure to the Cost Audit Report, information regarding Profit Reconciliation (for company as a whole) to be furnished for:
(A) Previous year only.
(B) Current year and previous 2 years.
(C) Current year and previous year.
(D) Previous three years.

(iv) Part C of the annexure to Cost Audit Report provides Abridged Cost Statement related to:
(A) Manufacturing Sector
(B) Service Sector
(C) None of the above
(D) Both of the above

(v) Cost Auditor's observation and suggestions are given in
(A) CRA-3
(B) CRA -2
(C) CRA-1
(D) Annexure

(vi) Position Analysis is one of the techniques used by Management Auditor for evaluation of:
(A) Profit of a Corporate.
(B) Net worth of a Corporate.
(C) Balance Sheet of a Corporate.
(D) Corporate image.

(vii) Under 'propriety audit' the auditors try to bring out cases of :
(A) Improper expenditure
(B) Avoidable or infructuous expenditure
(C) Both A & B
(D) None of the above.

(viii) Cost Auditing Standard 102 deals with:
- **(A) Planning an Audit of Cost Statements**
- **(B) Cost Audit Documentation**
- **(C) Overall Objectives of the Independent Cost Auditor and Conduct of an Audit in Accordance with Cost Auditing Standards**
- **(D) Knowledge of Business, Its processes and the Business Environment**

(ix) Internal Audit is applicable to every --------------company.
- **(A) unlisted**
- **(B) listed**
- **(C) Both A& B**
- **(D) None of above is correct.**

(x) Co-operative auditor to conduct an examination of:
- **(A) prepaid expenses**
- **(B) income received in advance**
- **(C) overdue debts**
- **(D) unpaid expenses.**

Section B [80 marks]

(Answer any 5 questions from this section)

2. (a) Answer the following questions with respect to Companies(Cost Records and Audit) Rules, 2014.
- **(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?**
- **(iii) A Company is engaged in both regulated and Non-regulated sectors and all its products are not covered under the rules. How to determine applicability of cost audit for the products covered under the regulated and Non-regulated sectors since different threshold limits have been prescribed under rule 4? [1+1+6]**

(b) Which of the following acts amount to professional misconduct on part of a practicing CMA?
- **(i) X, a CMA gives a certificate of Cost Of Production for attaching with a tender for a cost plus contract. He comes to know after signing the certificate that his client has won a case with a supplier on account of which the client is entitled to get a refund of substantial portion of the purchase price of the raw material. The certificate is not corrected.**
- **(ii) Y is a shareholder in PQ Ltd. holding 100 shares. The company's paid up capital is ₹5 crores (50 lac shares of ₹10 each). X accepts a certificate work from the company. [4+4]**

3. (a) How would you treat the following as per CAS-11 related to Administrative Overheads?
- **(i) Leased Assets**
- **(ii) Cost of Administrative Services procured from outside**
- **(iii) Cost of Software**
- **(iv) Fines. [8marks]**

(b) 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, 2015. 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. [8 marks]

4. (a) Mr. X, newly appointed CEO of ABC Ltd. engages you as a Management Auditor to give him a factual report , as to causes of demoralization of his staff. [8 marks]

(b) Write short note on - Probable format of environmental statement. [8 marks]

5. (a) ABC Pvt. Ltd took a consortium loan in 2016-17 amounting to ₹90 crores of which State Bank of India is the leading Bank for setting up a new plant in Haldia. During the year 2015-16 its outstanding loan was ₹60 crores of which repayment was made in the year 2016-17 to the extent of ₹15 crores. Should ABC Pvt. Ltd conduct internal audit as per Companies Act 2013? [6 marks]

(b) As an internal auditor of DEF Ltd. the Managing Director has asked you to enquire into the causes of abnormal wastage of raw materials during the month of September, 2017.
The wastage percentages are as follows:

June, 2017	1.3%
July, 2017	1.1%
August, 2017	1.4%
September, 2017	3.8%

How will you proceed to carry out the Assignment? [10 marks]

6. The following are the financial statements of KODIAC LTD. For the year ended March 31, 2017.

Balance Sheet as on March 31, 2017

(Amount in ₹ Lakh)

Equity & Liabilities		Assets	
Shareholders' Fund:		Non-Current Assets:	
Equity share capital	560	Fixed Assets (Net)	2,100
Preference Share Capital	280	Goodwill	280
Reserves & Surplus:	560	Current Assets:	
Non-Current Liabilities:		Cash at bank	140
Long term debt	1,680	Trade Receivables	700
Current Liabilities:		Inventories	980
Trade Payables	840		
Outstanding Expenses	80		
Provision for tax	200		
	4,200		4,200

Profit and Loss Account for the year ended March 31, 2017

(Amount in ₹ Lakh)

Sales:		
Cash		560
Credit		2,240
		2,800
Less: Expenses:		
Cost of goods sold	1,680	
Administrative, Selling and General Expenses	280	
Depreciation	196	
Interest on Long-term debt	84	2,240
Profit before Taxes		560
Taxes		280
		280
Less: Preference dividend		34
Net Profit for Equity shareholders		246
Add: Reserves at April 1, 2016		364
		610
Less: Dividend paid to Equity Shareholders		50
Reserves at March 31, 2017		560

The Ratios of Kodiac Ltd. For the years ended March 31 and their Industry Average ratios and are given below:

	2014-15	2015-16	2016-17	Industry Average 2016-17
Current Ratio	2.54	2.10		2.30
Acid-test Ratio	1.10	0.96		1.20
Debtors Turnover	6.00	4.80		7.00
Stock Turnover	3.80	3.05		3.85
Long-term Debt to total Capital	37%	42%		34%
Gross Profit margin	38%	41%		40%
Net Profit Margin	18%	16%		15%
Return on Equity	24%	29%		19%
Return on Total Assets	7%	6.8%		8%
Tangible Assets turnover	0.80	0.70		1.00
Interest Coverage	10	9		10

Required:

(1) Complete the financial Ratios Calculation for the year 2016-17.

(2) Analyse the financial performance of the company and Offer year suggestions to the management for improvements in performance. (6+5+5)

7. (a) The following are condensed comparative financial statement of KBC LTD., a single product manufacturing company for three years ended 31st March, 2017, 2016 and 2015.

(Amount in ₹ Lakh)

Equity & Liabilities	2017	2016	2015
Shareholders' Fund:			
Equity Share Capital	3,000	2,000	2,000
Reserves and Surplus	4,360	3,250	2,440
Non-Current Liabilities:			
Term Loans	3,080	1,650	1,500
Debentures	1,600	1,600	1,600
Other Long-term Loans	1,200	1,500	1,400

Current Liabilities:			
Current Liabilities	**2,660**	**1,252**	**1,720**
Short term Provisions	**800**	**600**	**500**
Total	**16,700**	**11,852**	**11,160**
Assets			
Non-Current Assets:			
Fixed Assets:			
Tangible Assets	**4,066**	**3,808**	**3,600**
Intangible Assets	**---**	**---**	**---**
Capital Work in Progress	**1,704**	**---**	**---**
Non-Current Investments:			
Investment in subsidiaries	**800**	**400**	**400**
Current Assets:			
Inventories	**4,030**	**2,490**	**2,320**
Trade Receivables	**4,810**	**3300**	**3,040**
Cash and Cash equivalents	**610**	**404**	**760**
Short term Loans and Advances	**680**	**1,450**	**1,040**
Total	**16,700**	**11,852**	**11,160**

Profit and Loss Account for the year ended March 31.	**2017**	**2016**
	(Amount in ₹ Lakh)	
Income:		
Revenue (including excise duty) from Operations	**29,040**	**24,510**
Expenditure:		
Material consumed	**11,340**	**9,008**
Excise duty on despatches	**6,690**	**6,852**
Employee Costs	**1,650**	**1,380**
Other Manufacturing expenses	**1,100**	**960**
Selling and distribution expenses	**3,102**	**2,802**
Administration expenses	**500**	**460**
Interest on:		
Term Loans	**692**	**402**
Debentures	**240**	**240**
Other long term loans	**160**	**200**
Depreciation	**604**	**400**
Difference in Stock	**1,652**	**536**
	27,730	**23,240**
Profit before Taxation (PBT)	**1,310**	**1,270**
Provisions for Taxation	**200**	**460**
Profit After Taxation (PAT) (Transferred to Balance Sheet)	**1,110**	**810**

You are required to compute the following values of (i), (ii), (iii) and ratios as stipulated in PART-D, PARA-4 to the Annexure of Cost Audit Report under the Companies (Cost Records and Audit) Rules, 2014 for the year ended March 31, 2016 and 2017 respectively.

(i) Capital Employed
(ii) Net Worth
(iii) Net Revenue from Operations
(iv) PBT to Capital Employed
(v) PBT to Net Worth
(vi) PBT to Net Revenue from Operations
(vii) Debt-Equity Ratio **[2+2+2+1+1+1+1]**

(b) H is an employee of M/s. P Co. and gets following emoluments and benefits:

(i)	Salary	₹ 2,500 per month
(ii)	Dearness allowance On first ₹ 1,000 of salary On next ₹ 1,000 of salary On balance of every ₹ 1,000	 ₹ 4,000 ₹ 1,000 ₹ 500 or @ 50% of part thereof
(iii)	Employers Contribution to Provident Fund	8% of Salary and D.A.
(iv)	Employer's Contribution to ESI	4% of Salary and D.A.
(v)	Bonus	20% of Salary and D.A.
(vi)	Other allowance	₹ 2,725 per annum

Harish works for 2400 hours per annum, out of which 400 hours are non-productive but treated as normal idle time. A worker works for 18 effective hours in job No. 11, where the cost of direct labour is @ effective hourly cost of Harish and direct material equal to direct labour cost, overhead applied is 100%, of Prime Cost.
The sale value of the job is quoted to earn a profit of 15%.

You are requested to find out:
(A) Effectively Hourly cost of Harish, and
(B) The effective sale value of job No. 11. [marks 6]

8. Answer any 4 questions [marks 4*4]

(a) What disclosures are required to be made in Cost Statement as per CAS-19 as regard to Joint COSTS?

(b) Explain in one sentence the following with respect to Government Expenditure Audit:
- Audit against Rules and Orders
- Audit of Sanctions
- Audit against provision of Funds.

(c) A Management Audit team should be multidimensional. Discuss.

(d) The operating performance of the three division of ABC Ltd. for year ending 31st March 2017 is as follows:

Particulars	Division A (₹)	Division B (₹)	Division C (₹)
Sales	38,00,000	1,70,00,000	2,00,00,000
Operating Profit	2,00,000	5,00,000	10,00,000
Investment	20,00,000	62,50,000	80,00,000

(i) Using operating profit margin percentage as criterion, which is most profitable division?
(ii) Using rate of return on investment as the criterion, which is most profitable division?
(iii) Which of the two measures do you think gives better indication of overall performance?

(e) The president of the L N T Company has just returned from a management seminar in which the benefits of economic value added have been trumpeted. He wants to know what the calculation would be for LNT, and asks his financial analyst to find out.

The financial analyst knows that the company's cost of capital is 12.5%, having recently calculated it from the company's mix of debt, preferred stock, and common stock. He then reconfigures information from the income statement and balance sheet

into the following matrix, where some expense line items are instead treated as investments.

Account Description	Performance	Net Investment
Revenue	$6,050,000	
Cost of goods sold	4,000,000	
General & administrative	660,000	
Sales department	505,000	
Training department		$75,000
Research & development		230,000
Marketing department	240,000	
Net income	$645,000	
Fixed assets		3,100,000
Cost of patent protection		82,000
Cost of trademark protection		145,000
Total net investment		$3,632,000

The return on investment for LNT is 17.8%, using the information from the preceding matrix. The calculation is $645,000 of net income divided by $3,632,000 of net investment. Finally, he includes the return on investment, cost of capital, and net investment to calculate Economic Value Added.
Find the EVA.