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 [20 marks]

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

(i) The cost records are to be maintained as specified in _____.
(a) CRA3
(b) CRA1
(c) CRA 4
(d) CRA 2

(ii) There are _____ to the Act clarifies or indicates that the schedules provide an illustrative list of acts and omissions constituting "professional or other misconduct
(a) two schedules
(b) three schedules
(c) four schedules
(d) five schedules

(iii) CAS 11 deals with _____.
(a) Administrative Overhead
(b) Factory Overhead
(c) Selling & Distribution Overhead
(d) Financial Cost

(iv) A manufacturing unit showed, during the Financial Year 2019-20, the following financial data (in ₹ lakh): Net Sales 2,400, Export Incentives 150, Other income 175, Adj. of Finished Stock (+) 125, Materials 725, Salaries 530, Overheads 145, and Tax 126.30. The Value Added as per Rules is (in ₹ lakh) _____.
(a) 1275
(b) 1420
(c) 1950
(d) 2675

(v) Remuneration of the Non-Executive Directors is treated as _____
(a) Employee Costs
(b) Administrative Overheads
(c) Salaries and Wages
(d) Management Expenses

(vi) Which of the following ratios appears as Profitability Ratio in Part D of Annexure to the Cost Audit Report?
(a) Net Profit to Net Sale
(b) Value added to Net Sales
(c) Profit before Tax to Value Added.
(d) Net Profit to Share Capital.

(vii) Propriety Audit in the context of Government Audit seeks to ensure that _____.
(a) public money are not spent for the benefit of a particular person
(b) public officer should exercise same vigilance as in respect of expenditure of his/her own money
(c) no authority should pass an order which will be directly or indirectly to its own advantage
(d) All of the above

(viii) Machinery used in defence, space and atomic energy sector and fulfilling turnover criteria is under
(a) regulated sector.
(b) unregulated sector.
(c) exempted by different statute.
(d) not applicable category.

(ix) The procedures followed by the cost auditor to reduce the audit risk to an acceptable level will not detect a misstatement that exists and that could be material is _____.
(a) Inherent risk.
(b) Detection risk.
(c) Control risk.
(d) None of the above.

(x) Consumer Service Audit is part of _____
(a) Business Activity Audit
(b) Social Audit
(c) Service Audit
(d) None of Above

Answer:

1. (i) (b) CRA 1
Reason: Pursuant to Rule 5(1) of the Companies (Cost Records and Audit) Rules, 2014, the form CRA 1 prescribes the form in which cost records shall be maintained.

(ii) (a) two schedules
Reason: As per section 22 of the Cost and Works Accountants Act, 1959 there are two schedules to the Act clarify or indicate that the schedules provide an illustrative list of acts and omissions constituting "professional or other misconduct".

(iii) (a) Administrative Overheads.
Reason: This standard deals with the principles and methods of classification, measurement and assignment of administrative overheads, for determination of the Cost of product or service, and the presentation and disclosure in cost statements.

(iv) (c) ₹ 1950 Lakh.
Reason: (Sales 2400 + Export Incentive 150 + Adj of Finished stock 125)-(Materials 725) = ₹ 1950 Lakh.

(v) (b) Administrative Overheads
Reason: As per the Generally Accepted Cost Accounting Principles (GACAP), Remuneration of the non-Executive Directors will not be considered as part of Employee Costs but will be treated as part of Administrative Overheads.

(vi) (c) Profit before Tax to Value Added
Reason: This is one of the four ratios identified as Profitability Rations in Part D of Annexure to the Cost Audit Report.

(vii) (d) All of the above
Reason: The objective of Propriety Audit is that public money is not spent for the benefit of a particular person. Public officer should exercise same vigilance as in respect of expenditure of his/her own money and no authority should pass an order which will be directly or indirectly to its own advantage.

(viii) (b) Unregulated sector
Reason: Machinery used in defence, space and atomic energy sector and fulfilling turnover criteria is under unregulated sector

(ix) (b) Detection risk.
Reason: "Detection risk" is the risk that the cost auditor will not detect a misstatement that exists in an assertion that could be material, either individually or when aggregated with other misstatements. Detection risk is a function of the effectiveness of an audit procedure and of its application by the auditor.

(x) (b) Social Audit.
Reason: Consumer Service Audit is an audit of public responsibility of business enterprise in relation to its customers and is a part of social audit. The audit is based on the philosophy that the role of business should be conducive to raising the quality of life through its contribution in terms of better product-quality and services.

Section - B [80 marks]

2. (a) (i) What is the meaning of "Turnover" in relation to the Companies (Cost Records and Audit) Rules, 2014?
(ii) Whether separate Form CRA-2 is required to be filed by a company having two or more different types of products covered under cost audit? **3 + 3**

(b) (i) Which information are likely to be provided in Filing Form CRA-4? 6
(ii) The Companies (Cost Records and Audit) Rules, 2014 have not prescribed any specific formats for the cost statements. In what manner and format would the cost statements be kept under these Rules? 4

Answer:

2. (a) (i) Sub-section 91 of Section 2 of the Companies Act, 2013 defines "turnover" as "the aggregate value of the realization of amount made from the sale, supply or distribution of goods or on account of services rendered, or both, by the company during a financial year. For the purposes of these Rules, "Turnover" means gross turnover made by the company from the sale or supply of all products or services during the financial year. It includes any turnover from job work or loan license operations but exclude duties and taxes. Export benefit received should be treated as a part of sales.

(ii) CRA-2 Form (intimation for appointment of cost auditor to Central Government) has replaced the earlier Form 23C (application seeking approval for appointment of cost auditor). A single Form CRA-2 is required to be filed providing details of the sectors/industries covered under cost audit and details of cost auditor. For Companies appointing multiple cost auditors, only one single Form CRA-2 is required to be filed. Provision has been made in the Form to accommodate details of multiple cost auditors.

(b) (i) As per the Companies (Cost Records and Audit) Rules, 2014 every company covered under these rules shall, within a period of thirty days from the date of receipt of a copy of the cost audit report, furnish the Central Government with such report along with full information and explanation on every reservation or qualification contained therein, in Form CRA-4. The following information is provided in Filling Form CRA-4:

(1) Corporate identity number (CIN) or foreign company Registration number (FCRN) of the company
(2) General Information

(3) Details of Industries/Sectors/Product(s)/Service(s) (CETA heading level, wherever applicable as per Rules for Regulated and Non-regulated sector) for which the Cost Audit Report is being submitted
(4) Details of Industries/Sectors/Product(s)/Service(s) (CETA heading level, wherever applicable as per Rules for Regulated and Non-regulated sector) not covered in the Cost Audit Report
(5) Details of the cost auditor(s) appointed
(6) Details of observation of the Cost Audit report
(7) Attachment
- XBRL document in respect of the cost audit report and Company's information and explanation on every Qualification and reservation contained therein
- Optional attachment, if any.

(ii) Maintenance of records

(1) Every company under these rules including all units and branches thereof, shall, in respect of each of its financial year commencing on or after the 1st day of April, 2014, maintain cost records in form CRA-1.

Provided that in case of company covered in serial number 12 and serial numbers 24 to 32 of item (B) of rule 3, the requirement under this rule shall apply in respect of each of its financial year commencing on or after 1st day of April, 2015.

(2) The cost records referred to in sub-rule (1) shall be maintained on regular basis in such manner as to facilitate calculation of per unit cost of production or cost of operations, cost of sales and margin for each of its products and activities for every financial year on monthly or quarterly or half-yearly or annual basis.

(3) The cost records shall be maintained in such manner so as to enable the company to exercise, as far as possible, control over the various operations and costs to achieve optimum economies in utilization of resources and these records shall also provide necessary data which is required to be furnished under these rules.

3. (a) "While conducting an audit, the cost auditor shall comply with each of the Cost Auditing Standards relevant to the audit." – Discuss. 6

(b) The Cost Accountant of M/s. Suchana Fertilizers Ltd. has arrived at a profit of ₹ 85,25,200 based on Cost Accounting records for the year ended March 31, 2020. As Cost Auditor, you find the following differences between the Financial Accounts and Cost Accounts:

(i) Decrease in value of Closing WIP and Finished goods inventory	
as per Financial Accounts	**₹ 1,53,35,600**
as per Cost Accounts	**₹ 1,56,10,780**
(ii) Profit on Sale of Fixed Assets	**₹ 74,800**
(iii) Loss on Sale of Investments	**₹ 18,400**
(iv) Voluntary Retirement Compensation included in Salary & Wages in F/A	**₹ 17,50,000**
(v) Donation Paid	**₹ 36,000**
(vi) Major Repairs & Maintenance written off in F/A (Amount reckoned in Cost Accounts of ₹ 7,05,950 for this job)	**₹ 14,48,000**
(vii) Insurance Claim relating to previous year received during the year	**₹ 15,65,000**
(viii) Profit from Retail trading activity	**₹ 8,33,500**
(ix) Interest Income from Inter-Corporate Deposits	**₹ 8,40,000**

You are required to prepare a Reconciliation Statement and arrive at the Profit as per Financial Accounts.

Answer:

3. (a) While conducting an audit, the cost auditor shall comply with each of the Cost Auditing Standards relevant to the audit. A Cost Auditing Standard is relevant to the audit when the Cost Auditing Standard is in effect and the circumstances addressed by the Cost Auditing Standard exist.

Conduct of audit:

(i) The Cost Auditing Standards provide the standards for the cost auditor's work in fulfilling the overall objectives of the cost auditor. The Cost Auditing Standards deal with general responsibilities of the cost auditor, as well as cost auditor's further considerations relevant to the application of those responsibilities to specific topics.

(ii) In performing an audit, the cost auditor may be required to comply with legal or regulatory requirements in addition to Cost Auditing Standards. In such cases in addition to complying with each of the Cost Auditing Standard relevant to the cost audit, it may be necessary for the cost auditor to perform additional audit procedures in order to comply with the legislative and regulatory requirements. The Cost Auditing Standards do not override law or regulations that govern audit process.

The form of the cost auditor's opinion will depend upon the applicable cost reporting framework and any applicable laws or regulations such as Companies Act and Rules prescribed thereunder.

(iii) The need for the auditor to depart from a relevant requirement is expected to arise only where the requirement is for a specific procedure to be performed and, in the specific circumstances of the audit, that procedure would be ineffective in achieving the aim of the requirement.

In exceptional circumstances, the cost auditor may judge it necessary to depart from a relevant requirement in a Cost Auditing Standard. In such circumstances, the auditor shall perform alternative audit procedures to achieve the aim of that requirement

3. (b)

Particulars	Amount (₹)	Amount (₹)
Total Profit as per Cost Accounts		**85,25,200**
Add: Amount of incomes not considered in cost accounts		
Profit on Sale of Fixed Assets	74,800	
Insurance Claim relating to previous year received during the year	15,65,000	
Profit from Retail trading activity	8,33,500	
Interest Income from Inter-Corporate Deposits	8,40,000	33,13,300
Less: Amount of expenses not considered in cost accounts		
Loss on Sale of Investments	18,400	
VRS included in Salary & Wages	17,50,000	
Donation	36,000	
Repairs & Maintenance (₹ 14,48,000 – ₹ 7,05,950)	7,42,050	(25,46,450)
Difference in stock valuation as per cost and Financial records		2,75,180
Profit as per Financial Accounts		**95,67,230**

4. (a) Define Management Audit. Discuss about the uses of Management Audit.

2 + 6

(b) (i) What is meant by Corporate Service Audit?

(ii) Describe the areas of Corporate Services Audit, the scrutiny thereof and the evaluation criteria used in such audit.

2 + 6

Answer:

4. (a) Management audit is the unique process appraising the performance of directors, managers or in the other words, appraising the performance of the management. A working director is included as a manager for purposes of management audit. It is normally presumed to be a non-routine investigation into a performance of a manager or group of managers. But in a number of organizations management audit is now a regular feature to examine and improve managerial effectiveness.

Management audit is the systematic and dispassionate examination, analysis and appraisal of management's overall performance. It is a form of appraisal of the total performance of the management by means of an objective and comprehensive examination of the organisation structure, its components such as department, its plans and policies, methods of process or operation and controls, and its use of physical facilities and human resources. Thus management audit is concerned with evaluation and appraisal of the control system and information in the entire or in various segments of the organisation.

The uses of Management Audit are given below:

(i) Management audit is useful in synthesizing, accounting, economic and other data required by management in constructing basic policy framework.

(ii) Management audit assists in establishing, reviewing and improving the planning system.

(iii) Management audit makes substantial contribution to system of goal setting in the organization.

(iv) Management audit ensures that the management is getting the adequate information for correct decisions.

(v) Management audit ensures that the management properly uses the information that it is getting.

(vi) Management audit aids in the design and maintenance of adequate authority structure.

(vii) It helps in the improvement information system to expedite flow of information among responsibility centres.

(viii) It substantially contributes for improvement of entire communication system.

(ix) It helps management in pinpointing key functions or operations in the profit-making process.

(x) It helps management in establishing better criterion for measuring results.

(xi) It helps management to avoid wasteful, unnecessary and extravagant use of resources.

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

The scope of the Corporate Services Audit extends to the critical examination of the different aspects of services and the extent to which the corporate body has rendered satisfactory services. It also includes the evaluation of the degrees of responsiveness and awareness on the part of such enterprise. The performance of the management towards

customers, employees, shareholders, suppliers, the community and government is studied separately and properly evaluated by management auditor.

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

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

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

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

Community: Social cost and social benefit, public relation

Fellow- businessmen: Business ethics and fair trade dealings.

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

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

5. (a) Define Audit Committee. Discuss about the role of Audit Committee. 8

(b) (i) Write a short note on the role of Internal Auditor of a company to review Custodianship and Safeguarding of Assets. 4
(ii) What are the important matters to be considered for conducting Audit of Co-operative Societies? 4

Answer:

5. (a) Sub-section (5) of section 177 of the Companies Act, 2013 provides that the Audit Committee may call for the comments of the auditors about internal control systems, the scope of audit, including the observations of the auditors and review of financial statement before their submission to the Board and may also discuss any related issues with the internal and statutory auditors and the management of the company.

The Audit Committee shall have powers to investigate any activity within its terms of reference, to seek information from any employee, to obtain outside legal or other professional advice, to secure attendance of outsiders with relevant expertise, if it considers necessary.

The role of the Audit Committee to

(i) evaluation of internal financial controls and risk management systems;

(ii) reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems;

(iii) reviewing the adequacy of internal audit function, if any, including the structure of the internal audit department, staffing and seniority of the official heading the department, reporting structure coverage and frequency of internal audit;

(iv) discussion with internal auditors of any significant findings and follow up there on;

(v) reviewing the findings of any internal investigations by the internal auditors into

matters where there is suspected fraud or irregularity or a failure of internal control systems of a material nature and reporting the matter to the board;

(vi) discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern.

The Audit Committee shall mandatorily review the Internal audit reports relating to internal control weaknesses; and the appointment, removal and terms of remuneration of the Chief internal auditor shall be subject to review by the Audit Committee.

5. (b) (i) The Internal Auditor should review the control system to ensure that all assets are accounted for fully. He/she should review the means used for safeguarding assets against losses viz, fire, improper of negligent activities, theft, illegal activities etc. He/she should review the control system for intangible assets, e.g. the procedure relating to credit control. Where a company uses electronic control equipment, the physical and system control on processing facilities as well as data storage should be examined and tested. He/she should review adequacy of the insurance cover for the various risks involved. He/she should also verify the existence of assets.

Para 30 of the Companies (Cost Records and Audit) Rules, 2014 states that "Records of physical verification may be maintained in respect of all items held in the stock such as raw materials, process materials, packing materials, consumables stores, machinery spares, chemicals, fuels, finished goods and fixed assets etc. Reasons for shortages or surplus arising out of such verifications and the method followed for adjusting the same in the cost of the goods or services shall be indicated in the records."

(b) (ii) Section 17(2) of the Co-operative Societies Act, 1912 specifically requires the auditor to conduct an examination of the overdue debts, if any, and a valuation of the assets and liabilities of the society. The auditor of a co-operative society is also required to point out various irregularities, improprieties, and departures from the provisions of the Act, rules framed thereunder, and the bye-laws of the society.

The following matters are to be considered for conducting audit of Co-operative Societies

1. Examination of overdue debts
2. Overdue Interest
3. Certification of Bad Debts
4. Valuation of Assets and Liabilities
5. Adherence to Co-operative Principles
6. Observations of the Provisions of the Act and Rules
7. Verification of Members' Register and examination of their pass books
8. Special report to the Registrar
9. Audit classification of society

6. (a) Bhagirathi Sugar Mill Ltd. has a boiler that uses the unit's own by-product, cane waste (Bagasse), as fuel which has a market price of ₹ 950 per ton. The steam generated is first used for the generation of power and the exhaust steam is used in the process of sugar manufacture. The exhaust steam (after generation of power) transferred to the sugar manufacturing process is 84% of the cost of production of steam. The mill buys restricted amount of power from the grid. The following details are extracted from the Financial Accounts and Cost Accounting Records of the Sugar Mill:

Sugar produced	**29,20,000 quintals**
Steam generated and consumed	**17,82,000 ton**
Fuel (Bagasse) consumed for production of steam	**8,36,000 ton**
Conversion Cost of generation of steam	**₹ 11,15,68,000**
Steam used for generation of power	**7,48,400 ton**
Power purchased from the Electricity Board @ ₹ 7.50/kWh	**68,50,000 kWh**
Power generated from the Steam Turbine	**5,92,44,000 kWh**
Conversion Cost of generation of power (excluding cost of steam)	**₹ 5,08,75,000**

Find out (i) Gross Cost of Steam per ton of Steam, (ii) Average Cost of Power per kWh and (iii) Average Cost of Power per ton of Sugar.

8

(b) M/s. Manoj Ltd. makes a single product, which sells for ₹ 36 per unit and there is a great demand for the product.

The variable cost of the product is ₹ 22 as per details below:

	₹
Direct Material	**10**
Direct Labour (₹ 3/hour)	**6**
Variable Overhead	**6**
	22

The labour force is currently working at 100% capacity and no extra time can be made available. A customer has approached the company with a request for a manufacture of a special order at ₹ 10,000.
The cost of order would be ₹ 4,000 for Direct Materials and 600 labour hours will be required and variable overhead/hr. will be ₹ 3.
Should the company accept this order?

8

Answer:

6. (a)

(i) Gross Cost of Steam	**₹**
Cost of fuel consumed for production of Steam (8,36,000 × 950)	79,42,00,000
Conversion cost of generation of Steam	11,15,68,000
	90,57,68,000
Gross cost of Steam / ton (90,57,68,000 / 17,82,000)	**508.29**
(ii) Average Cost of Power per KWh	
Steam for Power (7,48,400 × 508.29)	38,04,04,236
Conversion Cost of generation of Power (including cost of Steam)	5,08,75,000
Grid Power Cost (68,50,000 × 7.50)	5,13,75,000
	48,26,54,236
Average cost of Power per KWh	7.30254
48,26,54,236/ (68,50,000 + 5,92,44,000)	**₹ 7.30 (approx.)**
(iii) Average cost of Power per ton of Sugar	₹ 165.2926
(48,26,54,236/ 29,20,000)	**165.29 (approx.)**

6. (b) Labour time is the key or the limiting factor.

If this order is accepted:

Labour will have to be diverted from the standard products to this special order.
Contribution/labour hour from the standard product will be
₹

Product price	36
Less: Variable cost	22
Contribution	14

Contribution/labour hr. = ₹ 14/2 hours = ₹ 7

If the order from customer is accepted, its opportunity cost will be 600 hours @ ₹ 7 = ₹4,200.

Comparison of opportunity cost with the contribution from the special order:

	₹
Direct Material	4,000
Direct Labour (600 hrs. X ₹ 3)	1,800
Variable Overhead (600 hrs. X ₹ 3)	1,800
Total variable cost	7,600
Sale price	10,000
Contribution	2,400

Conclusion: Though this order is giving a contribution of ₹ 2,400, the opportunity cost of accepting this order is ₹ 4,200.

Thus, if this order is accepted, there will be a loss of profit of ₹ 1,800 (i.e. ₹ 4,200 – 2,400)

So, this order should not be accepted.

7. (a) Prashant Auto Parts Ltd. has received an enquiry for supply of 3,00,000 numbers of special type of auto components. The Company can execute the assignment provided a capital investment of ₹ 5,00,000 and working capital to the extent of 3 months' cost of sales are made available. The costs estimated are as follows:

Raw Materials - @ ₹ 4.50 per unit

Direct Labour Hours - 10,000

Labour Rate – ₹ 5.50 per hour

Factory Overheads – ₹ 5 per direct labour hour

Selling and Distribution expenses – ₹ 50,000

Borrowed funds will be available @12% on additional capital outlay. The company expects a net Return of 25% on Sales. The Managing Director wants a Cost and Price statement, indicating the price which should be quoted to the customer. 8

(b) There was a strike from 17.08.2019 to 28.10.2019 in a company of which you are Cost Auditor for the year ending 31.03.2020. Although the Company began working from 29.10.2019 production could effectively begin only from 30.11.2019. The expenses incurred during the year ending 31.03.2020 were:

	₹ In lakh
Salaries & Wages (Direct)	**4,000**
Salaries & Wages (Indirect)	**3,000**
Power (Variable 90%)	**1,600**
Depreciation	**2,000**
Other Fixed Expenses	**2,800**
Repairs and Maintenance	**1,600**
(Variable ₹ 1,200 lakhs)	
Total	**15,000**

Detailed examination of the records that of the above the following relate to the period 17.08.2019 to 29.11.2019.

	₹ In lakh
Salaries & Wages (Indirect)	**900**
Depreciation (Non-productive)	**700**
Other Fixed Expenses	**1,000**
Repairs and Maintenance (Indirect)	**200**
Total	**2,800**

Calculate the amount which in your opinion, should be treated as abnormal for execution from the product Costs.

8

Answer:

7. (a)

Special type Auto Components: 3,00,000 Nos.	**₹ in'000**	**₹ in '000**
Materials (3,00,000 @ ₹ 4.50)	13,50,000	
Labour 10000 Hrs @ ₹ 5.50	55,000	
Prime Costs		14,05,000
Factory Over Heads (10000 × 5)	50,000	
Factory Cost		14,55,000
Selling and Distribution Cost	50,000	
Cost of Sales		15,05,000
Interest @12% on [5,00,000 +(15,05,000 x 3/12)]	1,05,150	
Total Cost		**16,10,150**
Profit		5,36,717
Sales		**21,46,867**

Working Notes : Calculation of Sales

Sales = Total Cost × (1.00-0.25%)= 16,10,150/0.75 = ₹ 21,46,867

Profit = Sales - Cost = 21,46,867 - 16,10,150 = ₹ 5,36,717

Quote Per Unit = 21,46,867/300000 = ₹ 7.16

7. (b) The strike period in the given question is from 17.08.2019 to 28.10.2019.

Therefore the total strike period in the given question is (15+30+28) = 73 days

We can say that the total non strike period for the F.Y. 2019-20 is (366-73) = 293 days

But the production effectively started by the company from 30.11.2019. It means that the production was shut down for a period of (15+30+31+29) = 105 days.

Statement showing bifurcation of Expenses between Strike and Non-strike days

₹ In lakh

Particulars	**Amount**	**Amount**
Total expenses incurred during F.Y. 2019-20		15,000.00
Less: Variable Expenses		
Power (1,600-160)	1,440	
Repairs and Maintenance	1,200	(-) 2,640.00
Total Fixed Cost incurred in the F.Y. 2019-20		12,360.00
Since the strike is for 73 days the total expenses incurred during strike period is (73/366 x 12,360)		2465.25

The total Cost incurred during the period 17.08.2019 to 29.11.2019 when operations where shut down (Given)		2,800.00
Therefore, the expenses which are incurred from 29.10.2019 to 29.11.2019 are (2,800-2,465.25 as calculated above)		**334.75**

Therefore, the total fixed expenses incurred in the said period which should be recognised as abnormal are ₹ 2465.25 lakhs and not the entire amount of ₹ 2,800 lakhs.

8. Answer any four. **4x4=16**

(a) What do you mean by Internal Check? Is it different from Internal Audit? Explain.

(b) What are the steps of Management Audit?

(c) Describe the needs for capacity determining.

(d) ABC Co. has planned for an investment of ₹ 800.00 lakh with 50% Loan from Banks at 10% interest.

Direct Cost for the year = ₹ 480.0 lakhs and 50% of which is Material cost. Other expenses are at ₹ 80.0 lakh.

The goods will be sold at 150% of direct cost. Tax rate is assumed at 50%.

Determine (i) Net profit margin (ii) Return on Assets (iii) Assets turnover (iv) Inventory Turnover.

(e) A company bought a new technology for its auto component unit for two products P and Q. The condition was to pay a lump of ₹ 20,00,000 (equally distributable for both products having a service life of 5 years) and Royalty of ₹ 5 per unit produced. The vendor's technicians were to be paid travelling expenses for maintenance. The company incurs cost for software services and interest for borrowing of ₹1,60,000.

The following information is extracted from the Books of the Company for the year ended March 31, 2020:

Particulars	Product P	Product Q
Unit produced (Qty.)	50000	40000
Royalty paid on production (₹)	5/unit	5/unit
Travelling charges (₹))	20,000	20,000
Design charges (₹)	18,000	15,000
Software services charges (₹))	50,000	40,000
Hire charges for special equipment (₹))	12,000	—
Interest on Bank borrowing (₹))	80,000	80,000

You are required to compute the Direct Expenses — keeping in view of CAS - 10.

Answer:

8. (a) Internal Check is a system of instituting checking of the day-to-day transactions as part of the routine system, whereby the work of one person is checked independently or is complimentary to the work of another person i.e. resulting in the prevention and early detection of errors or fraud. Therefore, the systems are so designed that no single individual is responsible for all the stages involved in a transaction, i.e. duties are allocated in such a way that no single individual has an exclusive control over any one transaction or a group of transactions.

Internal Auditing on the other hand is an independent appraisal function established within an organisation to examine and evaluate its activities as a service to the Organisation. The objective of Internal Auditing is to assist members of the organisation in the effective discharge of their responsibilities. Internal auditing furnishes them with analyses, appraisals, recommendations, counsel and information concerning the activities reviewed.

Internal Check and Internal Audit are two important ingredients of Internal Control. Internal Checks are procedures in-built in the overall system itself and take place concurrently with the execution of the transactions, whereas Internal Audit is a distinct function which is carried out after the transactions have taken place.

8. (b) The steps of management audit are :-

1. Select an area of operation of management

2. Establish what should be the objective, standard or target of the operation.

3. Determine whether the actual results meet the standards, norms or targets. If not, why not?

(i) Is the target too difficult?

(ii) Is failure to achieve the target costing the organisation?

4. Establish what is done to ensure the achievement of the norms, target and standards. What steps are taken for –

(i) planning

(ii) operations, execution and implementation e.g. sue of up-to-date technology.

(iii) Measurement of performance and controls?

5. Carryout a detailed investigation, collective evidence as well as document for audit findings

6. Report the findings of the audit and make recommendations.

8. (c) The need for determining "production capacity" in respect of industrial organisation in India arises from the following reasons :-

- To meet the requirement under Section 129 of the Companies Act, 2013, that prescribes the form and contents of the balance sheet as well as profit and loss account (Schedule III of the Companies Act).
- For purpose of Cost Audit Report under section 148 of the Companies Act, 2013 where a cost audit has been ordered by Government.
- For internal management purpose, to be used
- In planning, scheduling and controlling production, and
- In planning expansion of capacity and correction of imbalances.
- For assessment of capacities for national level planning.
- For fixing the price of product(s) after ascertaining the capacity costs and per unit incidence thereof etc.

8. (d)

Particulars	₹ in lakh
Sales : 480 x 1.5	720
Direct Cost	480
Gross Profit	240
Operating Exp + interest	120
Profit before Tax	120
Net profit after Tax	60
(i) Net Profit Margin (60/720)	8.33%
(ii) Return on Assets (60/800)	7.5 %
(iii) Assets turnover (720/800)	0.9
(iv) Inventory Turnover (240/720) ×100	33.33%

8. (e)

Computation of Direct Expenses (as per CAS-10)

(Amount in ₹)

Particulars	Product P	Product Q
Amortized cost for Technical knowhow	2,00,000	2,00,000
Royalty paid on Units Produced	2,50,000	2,00,000
Hire charges of equipment used in A	12,000	—
Travelling Expenses	20,000	20,000
Design charges	18,000	15,000
Software services	50,000	40,000
Direct Expenses	**5,50,000**	**4,75,000**

N.B. Interest on bank borrowing shall not form part of Direct Expenses.