

PAPER – 6F: MULTIDISCIPLINARY CASE STUDY

Case Study 5

Ludhiana, Punjab is famous industrial hub for manufacturing industrial goods, machine parts, auto parts, household appliances, hosiery, and apparels. PQR Ltd. is a manufacturing company based in Ludhiana manufacturing chain drives. Sanjiv Pahuja is the Managing Director of the company.

The chain drives manufactured by the company are used by various industries and are used in hydraulic lifts, overhead hoists, conveyer belts, etc. Ludhiana is also a major hub for manufacturing bicycles. The product of the company is procured by leading bicycle manufactures in the country. Bicycles and its parts using chain drives manufactured by PQR Ltd. are sold not only within the country but are exported all across the world. Having expertise in the business, the company is often engaged as consultants for installation of conveyor belts and other systems in manufacturing and automated movements of various materials. Thus, PQR Ltd. has both manufacturing and service revenue streams.

PQR Ltd. has deployed the following applications for its business activities:

Application Name	Purpose
QWERTY	Allows employees to fill and submit time sheets
ASDF	Financial accounting and reporting (has an interface with PQRT)
PQRT	Cost Accounting and reporting (has an interface with ASDF). This was provided free of cost along with ASDF application.
CRT	Internal knowledge repository
VMS	Internal share point portal used for utilities such as leave management, storing policies and procedures of PQR Ltd., creating email signatures, meeting room booking and cab booking system etc.
SWIPE	Logs employee swipe in / swipe out data

Sanjiv Pahuja is also coordinating implementation of Ind AS in the PQR Ltd. The company falls under phase 2 of IND AS implementation. Following are details of the financials (in Rs. Crores):

Revenue (including royalty income from patent registered in India)	1000
Direct expenses (including expense related to patent registered in India)	550
Depreciation as per books of accounts	100
Interest expense	50
Actuarial Gains	30
Advance tax	50
Expense relatable to patent chargeable to tax u/s 115BBF	50
Income relatable to patent chargeable to tax u/s 115BBF	75
Depreciation as per Income Tax	75

After promulgation of Goods and Service Tax, Sanjiv Pahuja is very apprehensive of its impact on the business. He is disturbed by the news reports and the general grapevine that have raised several challenges in the implementation of Goods and Service Tax. Highly concerned, the company appointed XYZ Co. Chartered Accountants to prepare Risk Control Table and ascertain the impact of GST on the processes followed.

XYZ Co. is leading firm of Chartered Accountants in Chandigarh rendering services to several big corporates in Punjab and Haryana. After a long discussion between the Managing Director of PQR Ltd. and XYZ Co. the firm of Chartered Accountants was asked to identify and suggest new controls which PQR Ltd. should design and implement due to GST implementation.

The Chartered Accountants deployed a team to study the existing processes within the company. Extensive interviews were also conducted of senior managerial personnel in the company.

It was noted that the PQR Ltd. uses 'WSM' ERP for accounting, financial reporting and inventory management. Below are the notes prepared during process understanding discussions held with respective team members of PQR Ltd.:

Purchase to pay process

1. Vendor creation process

Procurement team maintains list of vendors along with the agreed prices in WSM system. In case of better prices being available, the procurement team sends an initial requirement list to the prospective vendor. The initial requirements contain details such as government proofs and tax registrations. On receipt of the requirements from the vendor, the procurement team verifies the same to ensure validity of documents shared. Once the data requirements are fulfilled, the draft agreement is prepared by legal department and the proposal is shared for senior management approval.

Once approved, the vendor is added to the list of vendors in WSM application.

2. Purchase Requisition (PR) & Purchase Order (PO)

Individual employees and designated department heads can raise PR. The PR contains the item details and quantity. The PR is raised in IJK tool which has in – built workflow for PR processing. The PR is sent to supervisor of the requestor for business approval. Thereafter, it is transferred to procurement team for further processing. Procurement team verifies the requested items and approvals. Then it first checks whether any stock is available in house or at any other office location. If not, then it identifies appropriate vendor and raises PO in WSM application for the requested quantity and agreed amount.

3. Goods receipt & invoicing

- a. *In case of non-factory items:* On delivery of the requested item, requestor performs receipt by collecting the items and informing procurement team over email that requested items have been received. The invoice is separately sent to Finance for payment. A copy of the invoice is sent to Procurement for their records.
- b. *Goods receipt at factory / warehouse:* Designated personnel verifies the delivery challan against invoice and unloads the goods. The designated personnel informs the procurement team over email that requested items have been received. The invoice is separately sent to Finance for payment. A copy of the invoice is sent to Procurement for their records.

4. Payment

Finance checks the PO raised in WSM and matches the same with invoice received. On satisfactory verification of quantity and price, the invoice is approved and payment is released. There may also exist non – PO based expenses for which invoice is the only document. These are processed on invoice receipt and payment released by Finance. Procurement is not involved in these expenses.

5. Reconciliations& Reporting

On monthly basis, the Finance team files returns and makes payment of VAT, CST, Excise and Service Tax.

Order to cash process

1. Customer creation

Directors and above designated personnel send requests to Receivables team. Receivables team obtains the required government proofs and tax registrations from the prospective customer. These documents are vetted by the Receivables team and they provide their approval. On receiving Receivables approval, the customer agreement is prepared by legal department in consultation with the Director who raised the customer request. The agreement is then sent for BOD review and upon approval, shared with the customer for their signatures and approval. Once approved and signed, the customer is added to the list of customers in WSM application.

2. Customer Invoicing

- a. *Services: For those customers where billing is based on time and motion basis, the invoices are raised as per the frequency mentioned in the customer agreement. The amount is based on the hours charged which is recorded in the timesheet and appears as work in progress (WIP) amount. Timesheets are recorded in the WSM ERP. There is an approval workflow built into WSM ERP for reviewing and approving timesheets. Where billing is based on milestones or fixed price, the invoice is raised as per the frequency in the agreement. The amount is based on the percentage of completion (POC). The invoices are generally due in 30 days after receipt.*
- b. *Manufacturing: Sales Order (SO) is created in WSM against the PO received from customer. Designated personnel at the factory / warehouse review the order and ascertain whether stock exists for immediate shipment or production is required. If not in stock, indent is created for the production. Once produced / stock ready, quality checks are performed and invoice is generated at factory / warehouse from WSM ERP. Goods are then shipped along with the invoice. Invoice once generated in the WSM system cannot be changed.*

3. Accounts Receivable

The Receivables team uses the WSM application to extract the Debtors Ageing Report. This report is used to track outstanding dues and send email reminders. The receivables are divided into buckets of 30 days, 60 days, 90 days, 180 days and 360 and above days.

4. Reconciliations & Reporting

On monthly basis, the Finance team files returns makes payment of VAT, CST, Excise and Service Tax after considering the taxes paid on inputs.

QUESTIONS

A. Multiple Choice Questions (2 Marks each).

1. In the Risk Control Table of PQR Ltd., controls should be firstly classified into:
 - i. Preventive
 - ii. Detective
 - iii. Manual
 - iv. Automated
 - v. Entity Level
 - vi. Corrective

(a) i, iii & v

- (b) iii, iv & v
 - (c) i, ii & iii
 - (d) i, ii & vi
2. Which of the following statements are true?
- i. Control risk is the sum audit risk and detection risk.
 - ii. As per SA 402, there can be a Type 1 or Type 2 report.
 - iii. Maker checker control (segregation of duties) is a compensating control.
3. Which of the following statements are false?
- i. Detective controls provide greater audit comfort than preventive controls
 - ii. Automated controls can be preventive or detective in nature
 - iii. Statutory auditor can help management prepare Risk Control Table
 - iv. Control Deficiencies are required to be reported on the face of the audit report
- (a) i, ii & iii
 - (b) i, ii & iv
 - (c) i, iii & iv
 - (d) ii, iii & iv
4. Goods and Service Tax is:
- (a) Source based tax on consumption of goods and services
 - (b) Destination based tax only on sale of goods and services
 - (c) Destination based tax on consumption of goods and services
 - (d) Source based tax on supply of goods and services
5. PQR Ltd. undertook following transactions in October 2017:
- 1. Purchase of Raw material – Rs. 1,00,000 (excluding GST) from trader based in Punjab
 - 2. Local Sales of goods – Rs. 60,000 (excluding GST)
 - 3. Sale of goods to Andaman & Nicobar – Rs. 60,000 (excluding GST)
- Assume rates to be 9% (CGST, SGST, UTGST & IGST). The net tax payable in cash by PQR Ltd. is:
- (a) CGST – Rs.1,800 & UTGST – Rs.1,800
 - (b) CGST – Rs. 3,600
 - (c) IGST – 3,600
 - (d) UTGST – Rs. 5,400
6. Following are the GST amounts paid on purchase transactions of PQR Ltd. for the month of October 2017.
- i: Ball bearings from job worker – Rs. 5,000

- ii. Metal purchases from dealer following composition scheme – Rs. 10,000
- iii. Fixed Assets – Rs. 50,000 (The GST amount has been capitalized in the Gross Block of PQR)
- iv. Consumables from unregistered dealer – Rs. 1,000

The GST credit of PQR Ltd. for the month of October 2017 is:

- (a) 5,000
- (b) 15,000
- (c) 66,000
- (d) 16,000

7. PQR Ltd. has agreed to provide consultancy services to ABC Ltd. Following are the clauses related to billing.

- i. ABC Ltd. incurs the conveyance charges for PQR Ltd. staff who visit ABC Ltd. for providing the services. These expenses are liability of PQR Ltd. however these are not included in the sale value.
- ii. PQR Ltd. will charge interest @ 2%p.a. for any delayed payments
- iii. PQR Ltd. receives special subsidy from a non-Government body on consultancy given to specific industries. ABC Ltd. falls under these industries and hence PQR Ltd is entitled to receive subsidy on services provided to ABC Ltd.

Which of the above items will be included in calculating value of taxable supply?

- (a) i & ii
- (b) i & iii
- (c) ii & iii
- (d) i, ii and (iii)

8. Read the following statements:

- i. In case PQR Ltd. supplies exempted goods or services or both, it is required to issue a bill of supply instead of a tax invoice
- ii. In case PQR Ltd fails to pay creditors' dues within 6 months, the input tax credit claimed on these purchases will become ineligible.
- iii. In case PQR Ltd. receives an advance towards goods to be supplied, tax will not be payable on receipt of such advance. Turnover of PQR Ltd. in the preceding financial year is 1 crore.

Which of the above statement are true?

- (a) i & ii
- (b) i & iii
- (c) ii & iii
- (d) i, ii and (iii)

9. PQR Ltd. has entered into agreement with XYZ Ltd. which manufactures bicycles. The highlights of the agreement are as follows:

- PQR Ltd. to provide 1000 chain drives on monthly basis.

- PQR Ltd. to incur the freight, packing and insurance charges during each supply of chain drives.
- PQR Ltd. to provide servicing of the drives every fortnight.
- Payment for the servicing activity carried out during a month to be released at the end of the month.
- PQR Ltd. to assist XYZ Ltd. with maintenance of conveyor belts on quarterly basis and installation of new assembly lines as and when required.
- Payment for maintenance of conveyor belts to be released on quarterly basis after the maintenance activity is carried out.
- Terms of payment for installation of new assembly lines to be finalised as and when the requirement thereof arises.

The agreement is entered into for a period of one year.

Which of the above statement(s) is/are true?

- The agreement involves a composite supply of goods (chain drives) and services (freight, packing and insurance) wherein the supply of chain drives is the principal supply.
 - The agreement involves a mixed supply of goods (chain drives) and services (freight, packing and insurance).
 - The agreement involves continuous supply of services wherein servicing is carried out of the chain drives.
 - The agreement involves mixed supply wherein the individual supplies are supply of chain drives, supply of servicing activity, supply of maintenance service and supply of installation service.
- (i), (iii)
 - (ii) and (iii)
 - (iv)
 - (i), (ii) and (iii)

- For the applications relevant for audit, which of the areas are required to be tested by the statutory auditors?
 - Change management
 - Change Management & Logical Access
 - Change Management, Logical Access & Backup Procedures
 - Change Management, Logical Access, Backup Procedures & Cyber Security

B. Descriptive/Numerical Questions

- Identify the existing risk at each stage, at different levels and control procedures in the given format of Risk Control Table for :
 - purchase to pay process
 - order to cash process.

Area	Risk	Control	Preventive / Detective	Manual / Automated / Entity Level

8 Marks

(b) Identify changes required in process and controls due to implementation of GST.

7 Marks

12. Which applications that are deployed by PQR Ltd for business activities are relevant for the audit? Give reasons.

5 Marks

13. Calculate Total Comprehensive Income and evaluate whether MAT is applicable. Transition amount need not be calculated. Ignore MAT on transition amount.

10 Marks