

(GI-1, GI-2, GI-3, VI-1, SI-1, VDI-1)

DATE: 27.07.2021

MAXIMUM MARKS: 100

TIMING: 3¼ Hours

PAPER : AUDITING**DIVISION – A (MULTIPLE CHOICE QUESTIONS)****ANSWER (1-20) CARRY 1 MARK EACH**

1. Ans. c
2. Ans. b
3. Ans. c
4. Ans. d
5. Ans. d
6. Ans. b
7. Ans. a
8. Ans. a
9. Ans. a
10. Ans. d
11. Ans. d
12. Ans. c
13. Ans. a
14. Ans. c
15. Ans. a
16. Ans. b
17. Ans. c
18. Ans. c
19. Ans. c
20. Ans. d

ANSWER (21-25) CARRY 2 MARKS EACH

21. **Incorrect.** Any amount due to the bank under any credit facility is 'overdue' if it is not paid on the due date fixed by the bank.
22. **Incorrect:** The management is responsible for maintaining an adequate accounting system incorporating various internal controls to the extent appropriate to the size and nature of the business. Maintenance of Internal Control System is responsibility of management because the internal control is the process designed, implemented and maintained by those charged with governance/management to provide reasonable assurance the achievement of entity's objectives.
23. **Incorrect.** Materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures) may need to be revised as a result of a change in circumstances that occurred during the audit (for example, a decision to dispose of a major part of the entity's business), new information, or a change in the auditor's understanding of the entity and its operations as a result of performing further audit procedures.
24. Ans. d
25. Ans. b

**DIVISION B-DESCRIPTIVE QUESTIONS
QUESTION NO. 1 IS COMPULSORY**

ATTEMPT ANY FOUR QUESTIONS FROM THE REST

Answer 1:

Examine with reasons (in short) whether the following statements are correct or incorrect : (Attempt any 7 out of 8)

- (i) **Incorrect:** As per the Standard on Auditing (SA) 520 "Analytical Procedures" the term "analytical procedures" means evaluations of financial information through analysis of plausible relationships among both financial and non-financial data.
- (ii) **Incorrect:** As per the provisions of the Companies Act, 2013, a person is disqualified to be appointed as an auditor of a company if his relative is holding any security of or interest in the company of face value exceeding Rs. 1 lakh. Therefore, AB & Co. shall be disqualified for being appointed as an auditor of XYZ Ltd. as Mr. C, the relative of Mr. B who is a partner in AB & Co., is holding securities in XYZ Ltd. having face value of Rs. 2 lakh.
- (iii) **Incorrect:** As per SA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", fraudulent financial reporting May involve manipulation, falsification or alteration of account records or supporting documents from which financial statement are prepared, misrepresentation in, or intentional omission from, financial statement of events, transactions or other significant information or intentional misapplication of accounting principles relating to amounts, classification, manner of presentation or disclosure.
- (iv) **Correct:** According to SA-300, "Planning an Audit of Financial Statements", planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement.
- (v) **Incorrect:** "As per section 141 a person can not be appointed as Auditor of the company in case he is holding security of company, Holding company, Subsidiary Company, of any amount. in the above case A chartered Accountant having security of amount of 950 of S Ltd, hence he can not be appointed as Auditor of the company."
- (vi) **Incorrect:** The matter of difficulty, time, or cost involved is not in itself a valid basis for the auditor to omit an audit procedure for which there is no alternative. Appropriate planning assists in making sufficient time and resources available for the conduct of the audit. Notwithstanding this, the relevance of information, and thereby its value, tends to diminish over time, and there is a balance to be struck between the reliability of information and its cost.
- (vii) **False:** Any material weakness in the internal control noticed by the auditor should be communicated in writing to the management in a timely manner. However such communication should mention that the audit has not been conducted to determine the adequacy of internal controls.
- (viii) **True:** Generally management/employees don't commit fraud in high value items. Moreover, as a general practice, auditor checks high value items in detail. Thus it is less risky that high value fraud and error may not be detected. So, high materiality level leaves audit risk at lower degree.

{One Mark for Correct or Incorrect
and 1 Mark for Explanation}

Answer 2:

(a) Documentation of Significant Matters and Related Significant Professional Judgments

Judging the significance of a matter requires an objective analysis of the facts and circumstances.

Examples of significant matters include:

- ◆ Matters that give rise to significant risks.

{2 M}

- ◆ Results of audit procedures indicating (a) that the financial statements could be materially misstated, or (b) a need to revise the auditor’s previous assessment of the risks of material misstatement and the auditor’s responses to those risks.
- ◆ Circumstances that cause the auditor significant difficulty in applying necessary audit procedures.
- ◆ Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter Paragraph in the auditor’s report.

An important factor in determining the form, content and extent of audit documentation of significant matters is the extent of professional judgment exercised in performing the work and evaluating the results.

Documentation of the professional judgments made, where significant, serves to explain the auditor’s conclusions and to reinforce the quality of the judgment. Such matters are of particular interest to those responsible for reviewing audit documentation, including those carrying out subsequent audits, when reviewing matters of continuing significance (for example, when performing a retrospective review of accounting estimates).

Some examples of circumstances in which it is appropriate to prepare audit documentation relating to the use of professional judgment include, where the matters and judgments are significant:

- ◆ The rationale for the auditor’s conclusion when a requirement provides that the auditor ‘shall consider’ certain information or factors, and that consideration is significant in the context of the particular engagement.
- ◆ The basis for the auditor’s conclusion on the reasonableness of areas of subjective judgments (for example, the reasonableness of significant accounting estimates).
- ◆ The basis for the auditor’s conclusions about the authenticity of a document when further investigation (such as making appropriate use of an expert or of confirmation procedures) is undertaken in response to conditions identified during the audit that caused the auditor to believe that the document may not be authentic.

{ 2 M }

Answer:

(b) The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client’s business.

Plans should be made to cover, among other things:

- (a) Acquiring knowledge of the client’s accounting systems, policies and internal control procedures;
- (b) Establishing the expected degree of reliance to be placed on internal control;
- (c) Determining and programming the nature, timing, and extent of the audit procedures to be performed; and
- (d) Coordinating the work to be performed.

{ 3 Point Each 1 Mark }

Answer:

(c) Substantive Analytical Procedure: Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. The application of planned analytical procedures is based on the expectation that relationships among data exist and continue in the absence of known conditions to the contrary. However, the suitability of a particular analytical procedure will depend upon the auditor’s assessment of how effective it will be in detecting a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated.

{ 2 M }

In some cases, even an unsophisticated predictive model may be effective as an analytical procedure. For example, where an entity has a known number of employees at fixed rates of pay throughout the period, it may be possible for the auditor to use this data to estimate the total payroll costs for the period with a high degree of accuracy, thereby providing audit evidence for a significant item in the financial statements and reducing the need to perform tests of details on the payroll. The use of widely recognised trade ratios (such as profit margins for different types of retail entities) can often be used effectively in substantive analytical procedures to provide evidence to support the reasonableness of recorded amounts. {2 M}

Answer:

(d) Reserves are amounts appropriated out of profits that are not intended to meet any liability, contingency, commitment or diminution in the value of assets known to exist as at the date of the Balance Sheet.

On the contrary, provisions are amounts charged against revenue to provide for:

- (i) Renewal or diminution in the value of assets; or
- (ii) A known liability, the amount whereof could only be estimated and cannot be determined with accuracy; or
- (iii) A claim which is disputed. {1 M}

Amounts contributed or transferred from profits to make good the diminution in value of assets due to the fact that some of them have been lost or destroyed as a result of some natural calamity or debts have proved to be irrecoverable are also described as provisions. Provisions are normally charged to the Statement of Profit and Loss before arriving at the amount of profit. Reserves are appropriations out of profits.

Difference between Reserves and Provisions

The difference between the two is that provisions are amounts set aside to meet specific/ identified liabilities or diminution in recoverable value of assets. These must be provided for regardless of the fact whether the Company has earned profit or not. Reserves on the other hand, represent amounts appropriated out of profits, held for equalising the dividends of the company from one period to another or for financing the expansion of the company or for generally strengthening the company financially. {1 M}

If we examine the Balance Sheet of a company, at a given time, and deduct the total liabilities to outside trade payables from the value of assets shown therein, the difference between the two figures will represent the net worth of the company based on the book values of assets as on that date. The same shall include the capital contributed by the shareholders as well as total undistributed profit held either to the credit of the Statement of Profit and Loss or to reserves; the reserves again will be segregated as revenue or capital reserves.

Revenue reserves represent profits that are available for distribution to shareholders held for the time being or any one or more purpose

Examples- to supplement divisible profits in lean years, to finance an extension of business, to augment the working capital of the business or to generally strengthen the company's financial position.

Capital Reserve, on the other hand represents a reserve which does not include any amount regarded as free for distribution through the Statement of Profit and Loss {1 M}

Examples- share premium, capital redemption reserve.

It may be noted that if a company appropriates revenue profit for being credited to the asset replacement reserve with the objective that these are to be used for a capital purpose, such a reserve shall also be in the nature of a capital reserve.

A capital reserve, generally, can be utilised for writing down fictitious assets or losses or (subject to provisions in the Articles) for issuing bonus shares if it is realised. But the amount of share premium or capital redemption reserve account can be utilised only for the purpose specified in Sections 52 and 55 respectively of the Companies Act, 2013.

Answer 3:

(a) Liabilities in addition to borrowings (discussed above), include trade payables and other current liabilities, deferred payment credits and provisions. Verification of liabilities is as important as that of assets, considering if any liability is omitted (or understated) or overstated, the Balance Sheet would not show a true and fair view of the state of affairs of the entity. {1 M}

Further, a liability is classified as current if it satisfies any of the following criteria:

- It is expected to be settled in the entity’s normal operating cycle
 - It is held primarily for the purpose of being traded
 - It is due to be settled within twelve months after the reporting period
 - The entity does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments does not affect its classification.
- {2 M}

Answer:

(b) External confirmation procedures frequently are relevant when addressing assertions associated with account balances and their elements, but need not be restricted to these items. For example, the auditor may request external confirmation of the terms of agreements, contracts, or transactions between an entity and other parties. External confirmation procedures also may be performed to obtain audit evidence about the absence of certain conditions. For example, a request may specifically seek confirmation that no “side agreement” exists that may be relevant to an entity’s revenue cut-off assertion. Other situations where external confirmation procedures may provide relevant audit evidence in responding to assessed risks of material misstatement include:

- Bank balances and other information relevant to banking relationships.
 - Accounts receivable balances and terms.
 - Inventories held by third parties at bonded warehouses for processing or on consignment.
 - Property title deeds held by lawyers or financiers for safe custody or as security.
 - Investments held for safekeeping by third parties, or purchased from stockbrokers but not delivered at the balance sheet date.
 - Amounts due to lenders, including relevant terms of repayment and restrictive covenants.
 - Accounts payable balances and terms.
- {4 Point Each 1/2 Mark}

Answer:

(c) The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit. The inherent limitations of an audit arise from:

(i) The Nature of Financial Reporting: The preparation of financial statements involves judgment by management in applying the requirements of the entity’s applicable financial reporting framework to the facts and {1 M}

circumstances of the entity. In addition, many financial statement items involve subjective decisions or assessments or a degree of uncertainty, and there may be a range of acceptable interpretations or judgments that may be made.

- (ii) The Nature of Audit Procedures: There are practical and legal limitations on the auditor’s ability to obtain audit evidence. For example:
 - 1. There is the possibility that management or others may not provide, intentionally or unintentionally, the complete information that is relevant to the preparation and presentation of the financial statements or that has been requested by the auditor.
 - 2. Fraud may involve sophisticated and carefully organised schemes designed to conceal it. Therefore, audit procedures used to gather audit evidence may be ineffective for detecting an intentional misstatement that involves, for example, collusion to falsify documentation which may cause the auditor to believe that audit evidence is valid when it is not. The auditor is neither trained as nor expected to be an expert in the authentication of documents. **{ 1 M }**
 - 3. An audit is not an official investigation into alleged wrongdoing. Accordingly, the auditor is not given specific legal powers, such as the power of search, which may be necessary for such an investigation.
- (iii) Timeliness of Financial Reporting and the Balance between Benefit and Cost: The matter of difficulty, time, or cost involved is not in itself a valid basis for the auditor to omit an audit procedure for which there is no alternative. Appropriate planning assists in making sufficient time and resources available for the conduct of the audit. Notwithstanding this, the relevance of information, and thereby its value, tends to diminish over time, and there is a balance to be struck between the reliability of information and its cost. **{ 1 M }**
- (iv) Other Matters that Affect the Limitations of an Audit: In the case of certain subject matters, limitations on the auditor’s ability to detect material misstatements are particularly significant. Such assertions or subject matters include:
 - ◆ Fraud, particularly fraud involving senior management or collusion.
 - ◆ The existence and completeness of related party relationships and transactions.
 - ◆ The occurrence of non-compliance with laws and regulations.
 - ◆ Future events or conditions that may cause an entity to cease to continue as a going concern. **{ 1 M }**

Answer:

- (d) Audit evidence is necessary to support the auditor’s opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits. In addition to other sources inside and outside the entity, the entity’s accounting records are an important source of audit evidence. Also, information that may be used as audit evidence may have been prepared using the work of a management’s expert. Audit evidence comprises both information that supports and corroborates management’s assertions, and any information that contradicts such assertions. In addition, in some cases the absence of information (for example, management’s refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence. **{ 2 M }**

Most of the auditor’s work in forming the auditor’s opinion consists of obtaining and evaluating audit evidence. Audit procedures to obtain audit evidence can include inspection, observation, confirmation, recalculation, re-performance and analytical procedures, often in some combination, in addition to inquiry. Although inquiry may provide important audit evidence, and may even produce evidence of a misstatement, inquiry alone ordinarily does not provide sufficient audit evidence of the absence of a material misstatement at the assertion level, nor of the operating effectiveness of controls. {1 M}

As explained in SA 200, “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing”, reasonable assurance is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (i.e., the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level. The sufficiency and appropriateness of audit evidence are interrelated. {1 M}

Answer 4:

- (a)** While planning the audit of an NGO, the auditor may concentrate on the following:
- (i) Knowledge of the NGO's work, its mission and vision, areas of operations and environment in which it operate.
 - (ii) Updating knowledge of relevant statutes especially with regard to recent amendments, circulars, judicial decisions related to the statutes.
 - (iii) Reviewing the legal form of the Organisation and its Memorandum of Association, Articles of Association, Rules and Regulations.
 - (iv) Reviewing the NGO's Organisation chart, then Financial and Administrative Manuals, Project and Programme Guidelines, Funding Agencies Requirements and formats, budgetary policies if any.
 - (v) Examination of minutes of the Board/Managing Committee/Governing Body/Management and Committees thereof to ascertain the impact of any decisions on the financial records.
 - (vi) Study the accounting system, procedures, internal controls and internal checks existing for the NGO and verify their applicability.
 - (vii) Setting of materiality levels for audit purposes.
 - (viii) The nature and timing of reports or other communications.
 - (ix) The involvement of experts and their reports.
 - (x) Review the previous year's Audit Report.
- {Each 1/2 Mark Any 8 Point}

Answer:

(b) The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error. This is because fraud may involve sophisticated and carefully organized schemes designed to conceal it, such as forgery, deliberate failure to record transactions, or intentional misrepresentations being made to the auditor. Such attempts at concealment may be even more difficult to detect when accompanied by collusion. {2 M}

Collusion may cause the auditor to believe that audit evidence is persuasive when it is, in fact, false. The auditor’s ability to detect a fraud depends on factors such as the skillfulness of the perpetrator, the frequency and extent of manipulation, the degree of collusion involved, the relative size of individual amounts manipulated, and the seniority of those individuals involved. While the auditor may be able to identify potential opportunities for fraud to be perpetrated, it is difficult for the auditor to determine whether misstatements in judgment areas such as accounting estimates are caused by fraud or error. {2 M}

Answer:

- (c) Reversal of Income : If any advance, including bills purchased and discounted, becomes NPA as at the close of any year, the entire interest accrued and credited to income account in the past periods, should be reversed or provided for if the same is not realised. This will apply to Government guaranteed accounts also. {1 M}
- In respect of NPAs, fees, commission and similar income that have accrued should cease to accrue in the current period and should be reversed or provided for with respect to past periods, if uncollected.
- Further, in case of banks which have wrongly recognised income in the past should reverse the interest if it was recognised as income during the current year or make a provision for an equivalent amount if it was recognized as income in the previous year(s). {1 M}
- Furthermore, the auditor should enquire if there are any large debits in the Interest Income account that have not been explained. It should be enquired is there are any communications from borrowers pointing out differences in Interest charge, and whether action as justified has been taken in this regard. {1 M}

Answer:

- (d) Permission of Central Government for Removal of Auditor Under Section 140(1) of the Companies Act, 2013: Removal of auditor before expiry of his term i.e. before he has submitted his report is a serious matter and may adversely affect his independence. Further, in case of conflict of interest the shareholders may remove the auditors in their own interest. {1 M}
- Therefore, law has provided this safeguard so that central government may know the reasons for such an action and if not satisfied, may not accord approval.
- On the other hand if auditor has completed his term i.e. has submitted his report and thereafter he is not re-appointed then the matter is not serious enough for central government to call for its intervention. {1 M}
- In view of the above, the permission of the Central Government is required when auditors are removed before expiry of their term and the same is not needed when they are not re-appointed after expiry of their term. {1 M}

Answer 5:

- (a) In today's digital age when companies rely on more and more on IT systems and networks to operate business, the amount of data and information that exists in these systems is enormous. A famous businessman recently said, "Data is the new Oil". {1 M}
- The combination of processes, tools and techniques that are used to tap vast amounts of electronic data to obtain meaningful information is called data analytics. While it is true that companies can benefit immensely from the use of data analytics in terms of increased profitability, better customer service, gaining competitive advantage, more efficient operations, etc., even auditors can make use of similar tools and techniques in the audit process and obtain good results. The tools and techniques that auditors use in applying the principles of data analytics are known as Computer Assisted Auditing Techniques or CAATs in short. {2 M}
- Data analytics can be used in testing of electronic records and data residing in IT systems using spreadsheets and specialised audit tools viz., IDEA and ACL to perform the following,
- check completeness of data and population that is used in either test of controls or substantive audit tests {1 M}

- selection of audit samples – random sampling, systematic sampling
- re-computation of balances – reconstruction of trial balance from transaction data
- reperformance of mathematical calculations – depreciation, bank interest calculation.

Answer:

- (b)** Information which assist the Auditor in accepting and continuing of relationship with Client: As per SA 220, "Quality Control for an Audit of Financial Statements" the auditor should obtain information considered necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement and when considering acceptance of a new engagement with an existing client. The following information would assist the auditor in accepting and continuing of relationship with the client: {1 M}
- (i) The integrity of the principal owners, key management and those charged with governance of the entity; {1 M}
 - (ii) Whether the engagement team is competent to perform the audit engagement and has the necessary capabilities, including time and resources; {1 M}
 - (iii) Whether the firm and the engagement team can comply with relevant ethical requirements; and {1 M}
 - (iv) Significant matters that have arisen during the current or previous audit engagement, and their implications for continuing the relationship. {1 M}

Answer:

- (c)** (a) Modification of Opinion: The auditor shall modify the opinion in the auditor's report when-
- (i) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or {1 M}
 - (ii) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.
- (b) Disclaimer of Opinion: The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive. {1 M}
- The auditor shall disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.
- (c) Adverse Opinion: The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements. {1 M}
- (d) Qualified Opinion: The auditor shall express a qualified opinion when-
- (i) The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or {1 M}

- (ii) The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.

Answer:

- (d) As per the guidelines, Agricultural Advances are of two types,
- (1) Agricultural Advances for "long duration" crops and
 - (2) Agricultural Advances for "short duration" crops
- The "long duration" crops would be crops with crop season longer than one year and crops, which are not "long duration" crops would be treated as "short duration" crops. The crop season for each crop, which means the period up to harvesting of the crops raised, would be as determined by the State Level Bankers' Committee in each State.
- The following NPA norms would apply to agricultural advances (including Crop Term Loans):
- A loan granted for short duration crops will be treated as NPA, if the installment of principal or interest thereon remains overdue for two crop seasons and,
 - A loan granted for long duration crops will be treated as NPA, if the installment of principal or interest thereon remains overdue for one crop season.

Answer 6:

- (a) Obtain an understanding of entity's process of charging depreciation and amortization. Obtain the fixed asset register maintained by the entity. There is always a risk that an entity could capitalize expense of revenue nature to increase its profit or charge capital expenditure directly in income and expense statement to reduce its profit. To address this risk, the auditor may choose to check the nature of asset from fixed asset register and further, there is always a risk that fake asset has been capitalized in the books and to mitigate this risk, auditors should physically verify the fixed assets, atleast the ones that are material in value. Obtain a list of all additions/ deletions along with their proper approval from the authorised person for the same.

Select the sample of assets from the Fixed Assets Register, on materiality considerations and verify the rates of depreciation, depreciation calculation.

- Obtain the list of all the components identified by the management.
- Ensure Intangible assets like patents, goodwill, copy rights have been properly amortized over the period.
- Ensure depreciation is charged on the assets from the date when it is ready to use.
- Ensure depreciation on revalued amount has been properly accounted from revaluation reserve.
- Depreciation computation as per Income tax Act, 1961- Ensure that additions are tallying with the additions as per Companies Act and the opening WDV to the Tax audit schedule for the assessment year preceding the previous year under audit.
- Perform analytical procedures to obtain audit evidence as to overall reasonableness of depreciation and amortisation expense- check the arithmetical accuracy of records and perform independent calculations example- compute or re-compute the depreciation expense for the year (Refer the format below that could be used for compiling reasonability of the expenditure for the year).

Answer:

- (b) The assertions are as follows:
- (i) the firm owns the plant and machinery;
 - (ii) the historical cost of plant and machinery is Rs. 2 lacs; } {1 M}
 - (iii) the plant and machinery physically exists;
 - (iv) the asset is being utilised in the business of the company productively; } {1 M}
 - (v) total charge of depreciation on this asset is Rs. 83,000 to date on which Rs. 13,000 relates to the year in respect of which the accounts are drawn up; and } {1 M}
 - (vi) the amount of depreciation has been calculated on recognised basis and the calculation is correct. } {1 M}

Answer:

- (c) 1. **Examination of overdue debts** - Overdue debts for a period from 6 months to 5 years and more than 5 years will have to be classified and shall have to be reported by an auditor. Overdue debts have far reaching consequences on the working of a credit society. It affects its working capital position. A further analysis of these overdue debts from the viewpoint of chances of recovery will have to be made, and they will have to be classified as good or bad. The auditor will have to ascertain whether proper provisions for doubtful debts are made and whether the same is satisfactory.
2. **Overdue Interest** - Overdue interest should be excluded from interest outstanding and accrued due while calculating profit. Overdue interest is interest accrued or accruing in accounts, the amount of which the principal is overdue. In practice an overdue interest reserve is created and the credit of overdue interest credited to interest account is reduced.
3. **Certification of Bad Debts** - A peculiar feature regarding the writing off of the bad debts as per Maharashtra State Co-operative Rules, 1961, is very interesting to note. As per the said rules, bad debts can be written off only when they are certified as bad by the auditor. Bad debts and irrecoverable losses before being written off against Bad Debts Funds, Reserve Fund etc. should be certified as bad debts or irrecoverable losses by the auditor where the law so requires. Where no such requirement exists, the managing committee of the society must authorise the write-off.
4. **Valuation of Assets and Liabilities** - Regarding valuation of assets there are no specific provisions or instructions under the Act and Rules and as such due regard shall be had to the general principles of accounting and auditing conventions and standards adopted. The auditor will have to ascertain existence, ownership and valuation of assets. Fixed assets should be valued at cost less adequate provision for depreciation. The incidental expenses incurred in the acquisition and the installation expenses of assets should be properly capitalised. If the difference in the original cost of acquisition and the present market price is of far reaching significance, a note regarding the present market value may be appended; so as to have a proper disclosure in the light of present inflatory conditions. The current assets be valued at cost or market price, whichever is lower. Regarding the liabilities, the auditor should see that all the known liabilities are brought into the account, and the contingent liabilities are stated by way of a note.
5. **Adherence to Co-operative Principles** - The auditor will have to ascertain in general, how far the objects, for which the co-operative organisation is set up, have been achieved in the course of its working. The assessment is not necessarily in terms of profits, but in terms of extending of benefits to members who have formed the society. Considered from the viewpoint of social benefits it may be looked into that how far the sales could be affected

{Any 6
 Points
 Each
 1/2
 Mark}

at lower prices. For the achievement of these activities, cost accounting methods, store control methods, techniques of standard costing, budgetary control etc. should be adopted. However, these modern techniques are mostly not in application and as such in practice a wide gap is found in the goals to be achieved and the actual achievements. While auditing the expenses, the auditor should see that they are economically incurred and there is no wastage of funds. Middlemen commissions are, as far as possible, avoided and the purchases are made by the committee members directly from the wholesalers. The principles of propriety audit should be followed for the purpose.

6. **Observations of the Provisions of the Act and Rules** - An auditor of a co-operative society is required to point out the infringement with the provisions of Co-operative Societies Act and Rules and bye-laws. The financial implications of such infringements should be properly assessed by the auditor and they should be reported. Some of the State Acts contain restrictions on payment of dividends, which should be noted by the auditor.
7. **Verification of Members' Register and examination of their pass books** - Examination of entries in members pass books regarding the loan given and its repayments, and confirmation of loan balances in person is very much important in a co-operative organisation to assure that the entries in the books of accounts are free from manipulation. Specifically in the rural and agricultural credit societies, members are not literate and as such this is a good safeguard on their part. Of course this checking will be resorted to on a test basis, which is a matter of judgement of the auditor.
8. **Special report to the Registrar** - During the course of audit, if the auditor notices that there are some serious irregularities in the working of the society he may report these special matters to the Registrar, drawing his specific attention to the points. The Registrar on receipt of such a special report may take necessary action against the society. In the following cases, for instance, a special report may become necessary:
 - (i) Personal profiteering by members of managing committee in transactions of the society, which are ultimately detrimental to the interest of the society.
 - (ii) Detection of fraud relating to expenses, purchases, property and stores of the society.
 - (iii) Specific examples of mis-management. Decisions of management against co-operative principles.
 - (iv) In the case of urban co-operative banks, disproportionate advances to vested interest groups, such as relatives of management, and deliberate negligence about the recovery thereof. Cases of reckless advancing, where the management is negligent about taking adequate security and proper safeguards for judging the credit worthiness of the party.
9. **Audit classification of society** - After a judgement of an overall performance of the society, the auditor has to award a class to the society. This judgement is to be based on the criteria specified by the Registrar. It may be noted here that if the management of the society is not satisfied about the award of audit class, it can make an appeal to the Registrar, and the Registrar may direct to review the audit classification. The auditor should be very careful, while making a decision about the class of society.
10. **Discussion of draft audit report with managing committee** - On conclusion of the audit, the auditor should ask the Secretary of the society to convene the managing committee meeting to discuss the audit draft report.

The audit report should never be finalised without discussion with the managing committee. Minor irregularities may be got settled and rectified. Matters of policy should be discussed in detail.

Answer:

(d) Few Techniques of how receipts are suppressed are:

- (1) Teeming and Lading: Amount received from a customer being misappropriated; also to prevent its detection the money received from another customer subsequently being credited to the account of the customer who has paid earlier. Similarly, moneys received from the customer who has paid thereafter being credited to the account of the second customer and such a practice is continued so that no one account is outstanding for payment for any length of time, which may lead the management to either send out a statement of account to him or communicate with him.
- (2) Adjusting unauthorised or fictitious rebates, allowances, discounts, etc. to customer' accounts and misappropriating amount paid by them.
- (3) Writing off as debts in respect of such balances against which cash has already been received but has been misappropriated.
- (4) Not accounting for cash sales fully.
- (5) Not accounting for miscellaneous receipts, e.g., sale of scrap, quarters allotted to the employees, etc.
- (6) Writing down asset values in entirety, selling them subsequently and misappropriating the proceeds.

**(Any 4
Points
Each 1
Mark)**

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