
PAPER 3: ADVANCED AUDITING
MAY 2000

Answer questions **1** and **2** and **four** from the rest

Question 1

- (a) T Ltd., purchased goods on credit for Rs.5 crore for Export from ABC Ltd.,. Upon the Export order being cancelled T Ltd., decided to sell the same in the domestic market at a discounted price. Accordingly ABC Ltd., was requested to offer a price discount of 25%. ABC Ltd., wants to adjust the sales figure to the extent of discount requested by T Ltd., **(5 Marks)**
- (b) During the year under audit, Z Ltd., credited to the Profit and Loss Account, the entire profit of Rs.20 lakhs on the sale of land not required for its use. You are informed that the directors would like to propose dividend out of the above profit. **(5 Marks)**
- (c) Y Ltd., provided Rs.25 lakhs for inventory obsolescence in 1998-1999. in the subsequent year, it was determined that 50% of such stock was usable. The company wants to adjust the same through prior period adjustment account as the provision was made in the earlier year. **(5 Marks)**
- (d) VV Ltd., had announced a voluntary retirement plan for its employees on January 1,2000. The scheme envisaged an initial lump sum payment of maximum of Rs.2 lakhs and monthly payments over the balance period of service of employees coming under the plan. 200 employees opted for the scheme as on March 31, 2000. The total lump sum payment for these employees would be Rs.250 lakhs and the aggregate of future payments to them would amount to Rs.1,500 lakhs. However no payment had been made to the employees under the scheme up to 31st March, 2000. Nor the company made any provision in its accounts towards any liability under the scheme. **(5 Marks)**

Question 2

- (a) A Chartered Accountant holding certificate of practice and having four articled clerks registered under him accepts appointment as a full time lecturer in a college. Also he becomes a partner with his brother in a business. Examine. His conduct in the light of C.A.Act, 1949 and the regulations thereunder. **(4 Marks)**
- (b) XYZ Co., Ltd., has applied to a Bank for loan facilities. The Bank on studying the Financial Statements of the company notices that you are the auditor and requests you to call at the Bank for a discussion. In the course of discussions, the Bank asks for your opinion regarding the company and also asks for detailed information regarding few items in the Financial Statements. The information is available in your working paper file. What should be your response and why? **(4 Marks)**
- (c) A Chartered Accountant in practice, in spite of repeated requests from the Secretary of the Institute, fails to submit Form 18. Is he liable for misconduct? **(4 Marks)**
- (d) A Chartered Accountant availed a term loan of Rs.10 lakhs from a Nationalized Bank for furnishing his office. He issued two cheques for Rs.1 lakhs each towards repayment of the loan. The cheques were dishonored with the remark "Refer to Drawer". Is the Chartered Accountant liable for misconduct? **(4 Marks)**

Question 3

Indicate the precise nature of Auditor's liability in the following situations and support your views with authority, if any:

- (a)
- i. A Misstatement had occurred in the Prospectus issued by the Company. **(4 Marks)**
 - ii. Certain weaknesses in the internal control procedure in the payment of wages in a large construction company were noticed by the statutory auditor, who in turn bought the same to the knowledge of the

Managing Director of the company. In the subsequent year a Huge Defalcation came to the notice of the management. The origin of the same was traced to the earlier year. The management wants to sue the auditor for negligence and also plans to file a complaint with the Institute. **(4 Marks)**

- iii. Based upon the legal opinion of a leading advocate, X Ltd., made a provision of Rs.5 cores towards Income Tax liability. The assessing authority has worked out the liability at Rs. 15 crores. It is observed that the opinion of the advocate was inconsistent with legal position with regard to certain revenue items. **(4 Marks)**
- (b) Y Ltd., obtained an actuarial valuation for Gratuity liability at the year end. The actuary changed certain basic assumptions for working out the liability at this year end as compared to the ones adopted by him in the preceding year. State Auditor's responsibility in this matter. **(4 Marks)**

Question 4

Comment on the following:

- (a) "The Auditors need not review Accounting Policies unless there is a change in the basis of Accounting" **(8 Marks)**
- (b) "Where the Financial Accounting System has not been computerized, the auditor need not verify Computerized Management System" **(8 Marks)**

Question 5

Your firm has been appointed as Central Statutory Auditors of a Nationalized Bank. The Bank follows financial year as accounting year. State your views on the following issues which were brought to your notice by your Audit Manager.

- (a) In computing the aggregate of funded and non-funded exposure of a constituent for purpose of assigning risk weight in regard to capital adequacy, the Bank "Netted Off" the credit balance of Rs.10 lakhs in their Current Account against the total exposure of Rs.1 crore. **(4 Marks)**
- (b) The Bank has recognized on accrual basis income from Dividends on Securities and Units of Mutual Funds held by it as at the end of financial year. The dividends on Securities and units of Mutual Funds were declared after the end of financial year. **(4 Marks)**
- (c) The Bank is a consortium of member of Cash Credit Facilities of Rs.50 crores to X Ltd., Bank's own share is Rs.10 crores only. During the last two quarters against a debit of Rs.1.75 crores towards interest the credits in X Ltd.,s . Account are to the tune of Rs.1.25 crores only. Based on the certificate of lead Bank, the Bank has classified the account of X Ltd., as performing. **(4 Marks)**
- (d) In case of all such advances which have been classified as non-performing for the first time during the Current Financial Year, only the last date of the financial year has been reckoned as the date of account becoming non-performing. **(4 Marks)**

Question 6

- (a) Describe the role of Computer –assisted Audit Technique in E.D.P Environment. **(10 Marks)**
- (b) Briefly explain the uses of test packs while conducting examination of accounts in the absence of audit trail. **(6 Marks)**

Question 7

- (a) You have been appointed to carry out Management – cum – Operational Audit of a Public Ltd., Company. State whether the use of Quantitative ratios is more effective than the use of Financial ratios to gain real insight in to the Financial Statements. **(8 Marks)**

-
- (b) Internal Audit is said to be an “Independent appraisal activity within an organization for review of Accounting, Financial and other operations as a basis of service to the organization, it is a managerial control which functions by measuring and evaluating the effectiveness of other controls” – Explain briefly. **(8 Marks)**

Question 8

Write short notes on any **four** of the following:

(4×4=16 Marks)

- (a) Rolling Settlements
- (b) Carry forward system
- (c) Summary written report
- (d) Cut-off procedures
- (e) Incoming and outgoing Co-insurance.