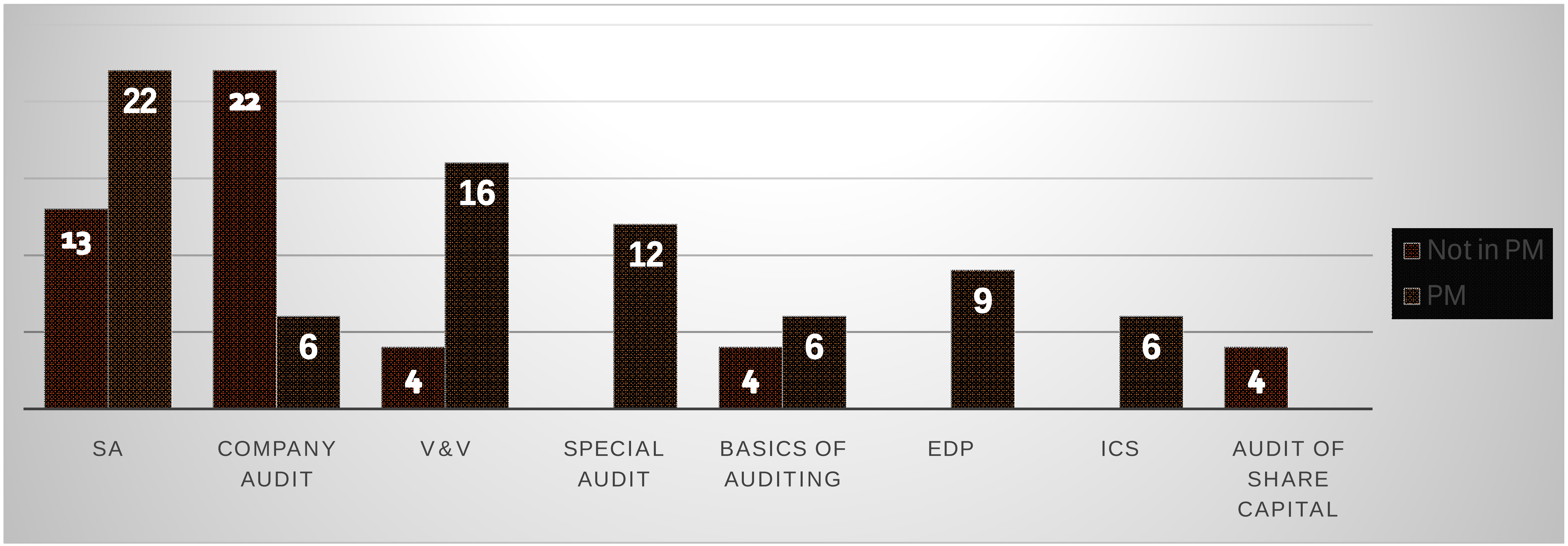
PAPER ANALYSIS / SUGGESTED ANSWERS / COMMON MISTAKES

CA IPC May 2016 Exams

By CA Ravi Taori

Highlights

- Around 50 marks paper was not from PM, they were new questions
- 35 Marks from SA, 28 Marks from Company Audit, 20 Marks from Vouching & Verification, 12 Marks from Special Audit



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1. Discuss the following :

(a) With reference to SA-550, "Identification of significant related party transaction outside the entity's normal course of business". 5

Identified Significant Related Party Transactions outside the Entity's Normal Course of Business

For identified significant related party transactions outside the entity's normal course of business, the auditor shall: (Sale to subsidiaries in Mauritius and Dubai then export to various countries for tax saving)
(a) Inspect the underlying contracts or agreements, if any, and evaluate whether:
(i) <u>The business rationale</u> (or lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets;
(ii) The terms of the transactions are <u>consistent with management's explanations</u>; and (But goods are not exported but sold to local manufacturer)
(iii) The transactions have been appropriately <u>accounted for and disclosed in accordance</u> with the applicable financial reporting framework; and (Sales were recorded when goods move out of factory gates, but it should be when they are delivered)
(b) Obtain audit evidence that the <u>transactions have been appropriately authorised and approved.</u> (Many BOD members were not aware about such arrangement and no BOD resolution to support it)

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(b) With reference to SA-530, meaning of audit sampling and requirements relating to sample design, sample size and selection of items for testing. 5

Audit Sampling: As per SA 530 on “Audit Sampling”, the meaning of the term “Audit Sampling” is the application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population.

According to the said SA, requirements relating to sample design, sample size and selection of items for testing are explained below

Sample Design - When designing an audit sample, the auditor shall consider the purpose of the audit procedure and the characteristics of the population from which the sample will be drawn.

Sample Size - The auditor shall determine a sample size sufficient to reduce sampling risk to an acceptably low level.

Selection of Items for Testing - The auditor shall select items for the sample in such a way that each sampling unit in the population has a chance of selection.

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(c) How does an audit programme help to plan and perform the audit ? 5

(a) **The Role of Audit Programme in Audit Plan and Performance:** The audit programme is helpful both in planning and performance stages of audit-

(b) (i)The audit programme **lists down areas** of audit before commencement.
(ii)The audit **timing is built therein**; thereby it becomes a schedule of audit plan.
(iii)The **staff who are entrusted** with the audit assignment is also specified. It is a plan of resource allocation of the firm.
(iv) It **specifies the procedures** to be checked during the audit.
(v) As the audit work is **split into various elements of procedures to be performed**, the audit programme acts as a **guiding chart or check list** during the performance of audit.
(vi) Since the staff in charge of each work is specified and they sign the programme, it extracts the **responsibility from the audit assistants.**
(vii) The working papers of the **audit staff can be reviewed against the audit programme** which helps a base of reference for evaluation of the performance before reporting on the financial statements.
(viii) It also helps in preparing a **diary of the performance and plan and also base for billing the clients** for the time and manpower involved in the audit.

(d) What are the specific risks related to internal control in an IT environment ? 5

Specific Risk to an Entity's internal Control: As per SA 315 "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment", IT system also poses specific risks to an entity's Internal Control. They are–

(i) Reliance on systems or programs that are **inaccurately processing data, processing inaccurate data** or both

(ii) **Unauthorised access to data** that may result in destruction of data or improper changes to data, including the recording of unauthorized or non existent transactions, or inaccurate recording of transactions. Particular risk may arise when multiple users access a common database.

(iii) The possibility of IT personnel **gaining access beyond those necessary** to perform their assigned duties thereby breaking down segregation of duties.

(iv) Unauthorised **changes to data** in Master files

(v) Unauthorised **changes to systems or programs.**

(vi) **Failure to make necessary changes** to systems or programs.

(vii) In appropriate **manual intervention**

(viii) Potential **loss of data or inability to access data** as required.

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State with reasons (in short) whether the following statements are correct or incorrect (Answer any eight) : 8×2 =16

(a) The scope of work of an internal auditor may extend even beyond the financial accounting.

True

Scope of Internal Auditor is covered in SA 610. It covers many other things than just checking book keeping. See next Slide

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I will help you in running your company achieving its objectives ethically!!!
1. Governance
Management
Internal Auditor
Illegal / Defective / Duplicate goods / theft / spoilage can happen.
2. Risk Management
Godown
6. Review of Operating & Financial Information
Stock Levels / Utilization / Output
3. Review of Operating Activities
Levels
Inward / Outward System
4. Monitoring Internal Control System
5. Review of Compliance with laws & regulations
VAT
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(b) An auditor has nothing to do with prudence or profitability of a company.

True
As per SA 200
→Our primary objective is to give opinion on whether financial statements give true & fair view / whether there are material misstatements.
→Secondary objective is to tell with reasonable assurance about material fraud & error.
→ We don't comment efficiency / effectiveness / profitability & Future Viability

(c) Evaluating responses to enquiries is an integral part of the inquiry process.

True
As per SA 500
Inquiry is one of the most important method of collecting audit evidence. Replies obtained are corroborated with other evidences and if there is difference are resolved.

(d) Internal control questionnaires are a good source of identifying weakness in internal control system.

True

It is one of the tool to review Internal Control System, where list of questions is sent to management, they fill it as per existing internal control system and send it to auditor for evaluation, which will let auditor know about deficiency.

(e) Cluster sampling is less effective than random sampling.

True

SA 530 Sampling is applicable.

In cluster sampling, as we randomly select few clusters, so our scope narrows down to part of population and selection is from limited area. But in random sampling whole population is open for selection hence variety of selection is better and effective as compared to cluster sampling.

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(f) Errors of duplication affects the Trial Balance.

False

In error of duplication accounting entry gets repeated so we double debits as well credit , in such situation trial balance will tally.

(g) Substantive procedures do not test the balances of accounts.

False

It means to substantiate / confirm transactions & balances after test of controls. It covers analytical procedures & test of details (Vouching & Verification)

(h) The first auditors of a Government company was appointed by the Board of Directors.

False

As per Sec 139 in case of government company right to appoint first auditor should go to C&AG and if not appointed within 60 days of incorporation then BOD within 30 days, if they also fail then share holders within 60 days.

(i) The members of XYZ Ltd. preferred a complaint against the auditor stating that he has failed to send the auditor's report to them.

False

Auditor has to submit audit report to company / Audit Committee / BOD, it is companies responsibility to send it to shareholders.

(j) Mr. Pawan, a practising Chartered Accountant, is appointed as "Tax-Consultant" of ABC Ltd., in which his father. Mr. Singh is the Managing Director.

True

Disqualification of Sec 141 (3) are for auditor and not consultants. So there no disqualifications for them, but Sec 188 will be applicable if related party is appointed to any position being place of profit (earning).

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3. How you will vouch/verify the following ? 4x4 =16

(a) Preliminary expenses

PRELIMINARY EXPENSES	
Review Flow of Internal Control System	Appointment of Lawyer/CS/CA->Preparation of AOA/MOA -> Forms filing with ROC->Stamp Duty /Registration Fees payment -> Professional Bill-> After company formation BOD resolution to accept these expenses.
General Points	Date of Voucher/ Name of Client/ Authorisation/ Rubber Stamp/ Revenue Stamp (Payments above 5000)
Documents	Professional Bill/BOD Resolution/Prospectus/ Bank Statement
Registers	NA
Accounting	Preliminary Exp. A/c Dr XXX To Bank A/c XXX As per AS 26 these expenses should be written of immediately (P&L).
Revised Schedule III	Other Expenses/If not written of then Other Current Asset.
Special Points	Checked that no expenses other than those that constitute preliminary expenses are booked under this heading .e.g underwriting commission & brokerage fees. As per Income Tax Act 35D 1/5th is allowed as deduction each year

By CA Ravi Taori

(b) Customs & Excise Duties

CUSTOM DUTY	
Review Flow of Internal Control System	Order for import of goods-> Goods reach Indian port->Appoint C&F agent-> Bill of Entry->Bill of Lading-> Payment of custom duty ->Bill of C&F agent & its payment
General Points	Date of Voucher/ Name of Client/ Authorisation/ Rubber Stamp/ Revenue Stamp (Payments above 5000)
Documents	Bill of Entry/ Bill of Lading/ C&F Agent Bill/ Bank Statement
Registers	Import register/ Goods Inward Book
Accounting	Dr->P&L if it is inventory Dr-> Asset A/c if it is Capital Expenditure
Revised Schedule III	Custom Duty-> Other Expenses
CARO	Statutory Payment clause will be applicable.
Special Points	In case there is dispute regarding duty payable , check whether the provision for the same have been made or not Obtain a confirmation from the supplier regarding actual import of goods.

By CA Ravi Taori

(b) Customs & Excise Duties

EXCISE DUTY	
Review Flow of Internal Control System	Production of goods-> Levy of excise duty->Duty is payable Monthly/Quarterly by 5th of next month-> Excise Challan ER-7->Excise Registers -> Stock Register->PLA Register
General Points	Date of Voucher/ Name of Client/ Authorisation/ Rubber Stamp/ Revenue Stamp (Payments above 5000)
Documents	Excise Challan/Bank Statement
Registers	Stock Register/ PLA Register (ER-1/ER-2/ER-3)
Accounting	Disclosure Sales XXX Excise Duty(XXX) Net Sales XXX
Revised Schedule III	Other Expenses on closing stock which is manufactured but not sold.
CARO	Statutory Payment clause will be applicable.
Special Points	Excise can be paid with CENVAT on purchases. Compute ratio of excise duty to sales and compare for past 2 -3 years. In case of export , see whether Duty Drawback has been properly claimed or not As per Section 43B of Income Tax Act deduction of Bonus will not be given unless it is paid. **By CA Ravi Taori**

(c) Floating assets

FLOATING ASSETS	
Meaning	Floating Asset means those Current Assets that are manufactured or purchased during the normal course of business. They continuously circulate from one form to other Cash->RM->WIP->FG->Debtor->Cash. They are held for a shorter period and may be converted into cash within a year.
Examples	Raw Materials, Work-In-Progress, Finished Goods, Consumables, Debtors, Sundry Receivables.
Valuation	Stocks / Inventories shall be valued at lower of - (i) Cost, or (ii) Market Price. Sundry Debtors and Bills Receivable shall be valued at Net Realisable Value.
Charge	Generally Debentures have charge on floating assets, in such charge creditors are paid after specific secured charge but before unsecured creditors. **By CA Ravi Taori**

(d) Recovery of bad debts written-off

RECOVERY OF BAD DEBT	
Review Flow of Internal Control System	Bad Debt written off (Chances of recovery low)-> Correspondence through letter/email-> Appointment of recovery agent-> Legal Case for recovery-> Final recovery-> Receipt Issued
General Points	Date of Voucher/ Name of Client/ Authorisation/ Rubber Stamp/ Revenue Stamp (Payments above 5000)
Documents	Correspondence Letters/Statement from recovery Agent/ Court Order (Decree)/Receipt/ Bank Statement
Registers	Register of Bad Debt Recoveries/ Bad Debt Recovery File
Accounting	Bank A/c Dr XXX To, Bad Debt Recovery XXX
Revised Schedule III	Shown in Other Income
Special Points	Confirmation from debtor. Authorisation for settlement. Liquidators letter in case of winding up of company. By CA Ravi Taori

4. (a) Mention the disclosure requirement of current investments as per Schedule III of the Companies Act, 2013. 6

Current Investments

(*i*) Current investments shall be classified as:

(*a*) Investments in **Equity Instruments**;

(*f*) Investments **in Partnership Firms**;

(*b*) Investment in **Preference Shares**;

(*d*) Investments in **Debentures or Bonds**;

(*e*) Investments in **Mutual Funds**;

(*c*) Investments in **Government or Trust Securities**;

(*g*) Other investments (specify nature).

Under each classification, details shall be given of names of the bodies corporate [indicating separately whether such bodies are**: (*i*) subsidiaries, (*ii*) associates, (*iii*) joint ventures, or (*iv*) controlled special purpose entities**] in whom investments have been made and the nature and extent of the investment so made in each such body corporate (**showing separately investments which are partly paid**). In regard to investments in the capital of partnership firms, the names of the firms (with the names of all their partners, total capital and the shares of each partner) shall be given.

(*ii*) The following shall also be disclosed:

(*a*) The **basis of valuation** of individual investments;

(*b*) Aggregate amount of **quoted investments and market value thereof**;

(*c*) Aggregate **amount of unquoted investments**;

(*d*) Aggregate **provision made for diminution in value of investments**.

By CA Ravi Taori

(b) What are the significant matters observed during the course of audit, a record of which should be kept in the Audit Note Book ? 6

Significant matters observed during the course of audit, a record of which should be kept in the Audit Note Book:

(d)Important **information about the company which is not apparent from the accounts.** (Promoters / Big Shareholders / Licensed Capacity / Number of Locations etc)

(a) Audit **queries not cleared immediately** *e.g.* missing receipts, vouchers, etc.

(c)**Unsatisfactory book-keeping arrangements, costing method, internal or financial administration or organisation.** (No segregation of duty / No fixed format / No timely accounting etc)

(b) The **mistakes or irregularities observed during the course of audit** *e.g.* cases of failure to comply with the requirements of the Companies Act, 2013 or the provisions contained in the Memorandum or Articles; a change in the basis of valuation of finished inventory and work-in-progress or in the computation of depreciation; failure to provide adequate depreciation, etc.

(e)Special points requiring consideration at the time of **verification of final accounts.** (Investment Classification & Valuation / Inventory Valuation / Prior Period Items etc)

(f) Important matters for **future reference.** (Provision for doubtful debts, Going Concern validity)

By CA Ravi Taori

(c) Write short note on the use of flowcharts in evaluation of internal control. 4

It is a graphic presentation of each part of the company's system of internal control. A flow chart is considered to be the most concise way of recording the auditor's review of the system. It minimises the amount of narrative explanation and thereby achieves a consideration or presentation not possible in any other form. It gives bird's eye view of the system and the flow of transactions and integration and in documentation, can be easily spotted and improvements can be suggested.

It is also necessary for the auditor to study the significant features of the business carried on by the concern; the nature of its activities and various channels of goods and materials as well as cash, both inward and outward; and also a comprehensive study of the entire process of manufacturing, trading and administration. This will help him to understand and evaluate the internal controls in the correct perspective.

5. (a) Mention any six special points which you as an auditor would look into while auditing the books of a partnership firm. 6

Special Points in Audit of a Partnership Firm: Matters which should be specially considered in the audit of accounts of a partnership firm are as under:

i. **Confirming that the letter of appointment**, signed by a partner, duly authorised, clearly states the nature and scope of audit contemplated by the partners, specially the limitation, if any, under which the auditor shall have to function.

ii. **Examine the partnership deed** signed by all partners and its registration with the registrar of firms. Also ascertain from the partnership deed about capital contribution, profit sharing ratios, interest on capital contribution, powers and responsibilities of the partners, etc.

iii. **Studying the minute book**, if any, maintained to record the policy decision taken by partners specially the minutes relating to authorisation of extraordinary and capital expenditure, raising of loans, purchase of assets, extraordinary contracts entered into and other such matters which are not of a routine nature.

Verifying that the business in which the partnership is engaged is authorised by the partnership agreement; or by any extension or modification thereof agreed to subsequently.

By CA Ravi Taori

i. **Examining whether books of account appear to be reasonable** and are considered adequate in relation to the nature of the business of the partnership.

ii. Verifying generally that the **interest of no partner has suffered prejudicially by an activity engaged in by the partnership which, it was not authorised to do under the partnership deed or by any violation of a provision in the partnership agreement.**

iii. Confirming that a provision for the firm's **tax payable** by the partnership has been made in the accounts before arriving at the amount of profit divisible among the partners. Also see various requirements of legislations applicable to the partnership firm like Section 44(AB) of the Income-tax Act, 1961 have been complied with.

Verifying that the **profits and losses have been divided** among the partners in their agreed profit-sharing ratio.

(b) Draft an audit programme for conducting audit of accounts of a local body. 6

Background of Local Bodies: A municipality can be defined as a unit of local self government in an urban area.

By the term 'local self-government' is ordinarily understood the administration of a locality – a village, a town, a city or any other area smaller than a state – by a body representing the local inhabitants, possessing fairly large autonomy, raising at least a part of its revenue through local taxation and spending its income on services which are regarded as local and, therefore, distinct from state and central services.

Municipal government in India covers **five distinct types of urban local authorities**, viz., the municipal corporations, the municipal councils, the notified area committees, the town area committees and the cantonment committees.

Audit Programme for Local Bodies:

(i) The **Local Fund Audit Wing of the State Govt**. is generally in charge of the audit of municipal accounts. Sometimes bigger municipal corporations e.g. Delhi, Mumbai etc have power to appoint their own auditors for regular external audit. So the auditor should ensure authenticity of his appointment.

(ii) The auditor while auditing the local bodies should report on the **fairness of the contents and presentation of financial statements, the strengths and weaknesses of system of financial control**, the adherence to legal and/or administrative requirements; upon whether value is being fully received on money spent. His objective should be to detect errors and fraud and misuse of resources.

(iii) The auditor should ensure that the expenditure incurred conforms to the **relevant provisions of the law** and is in accordance with the financial rules and regulations framed by the competent authority.

(iv) He should ensure that **all types of sanctions, either special or general, accorded by the competent authority.**

(v) He should ensure that there is a provision of funds and the expenditure is incurred from the provision and the same has been authorized by the competent authority.

(vi) The auditor should check that the **different schemes, programmes and projects, where large financial expenditure** has been incurred, are running economically and getting the expected results.

(9) What precautions should be taken by an auditor while applying test check techniques ? 4

The **precautions that should be taken may be the following:**

1. First check internal control system
2. 100% checking in some areas
3. Stratification
4. Unbiased Selection
5. Prepare test check plan and train team members
6. Carefully decide sample size
7. Study some transactions from beginning till end
8. Evaluate errors

6. (a) What are the matters to be included in Director's Responsibility statement ? 6

Board of Directors Report (DIRECTOR RESPONSIBILITY STATEMENT)

→Effectiveness of Internal financial controls (In case of Listed Company)

→Maintenance of adequate accounting records for Safeguarding the assets & Preventing and detecting fraud and other irregularities;

→Compliance with accounting standards & explanation for material departures

→Consistency of Accounting Policy , Reasonableness of Estimates , Whether financial statement gives true and fair view;

→Application of going concern basis

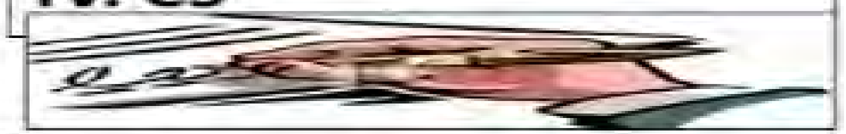
By CA Ravi Taori

(b) Discuss the provisions of Section 134 of the Companies Act, 2013 regarding the authentication of financial statements. 6

Standalone + Consolidated Financial Statements → AUTHENTICATION

STEP 1
APPROVAL of financial statements by Board of Directors

STEP 2
I. Signature on behalf of board by CHAIRPERSON if authorised by BOD or 2 DIRECTORS & One Should be MD
II. CEO (If Director)
III. CFO
IV. CS



STEP 3
Auditors report shall be attached to every financial statement.

→ In case of ONE PERSON COMPANY only ONE DIRECTOR should sign.
→ Legally it is not required that auditor should sign financial statements but it is done as per largely followed CUSTOMS

(c) State the factors to be considered to verify the validity of any transaction. 4

It is also the function of audit to establish that payments have been made validly to persons who are shown to be recipients. For example, it must be verified that salaries to partners were paid according to a provision contained in the partnership deed and the directors fees were paid according to the provisions in that regard in the Articles of Association or the resolution passed by members of the company at a general meeting. For checking the validity of a transaction, it is usually necessary to refer to documentary evidence. It may exist in any of the following forms-

- ✓The legal provisions, if any, having bearing on the accounts of the entity under audit.
- ✓ The rules or regulations governing the internal working of the organisation, e.g., the Articles of Association, Partnership Deed, Trust Deed, etc
- ✓ Minutes of the proceedings of a meeting of members of the company, that of the directors or that of the Managing committee.
- ✓ Copy of an agreement, e.g., Managing Director's agreement, Lease Deed, vendor's agreement, agency agreement, contract with an employee, etc

An auditor should have a clear and precise knowledge of legal provisions under which the concern was registered or is functioning, as well as those which constitutes the basis of various transactions entered into, more particularly the provisions as regards maintenance and audit of its accounts. He should also study the rules, if any, framed for regulating the internal management of the entity; these may be embodied in some of the documents mentioned above. If he has any doubt on any legal point, by way of guidance, he should call for legal opinion. However, unless he is convinced of the reasonableness of the legal opinion, he should not act on it. In the case of *Republic of Bolivia Exploration Syndicate Ltd.* [1914], it was held that auditors are *prima facie* responsible for *ultra vires* payments made on the faith of their balance sheet but whether, and to what extent, they are considered responsible for not having discovered them in their audit would depend upon the circumstances of each case. An auditor is responsible for detecting payments that are *ultra vires* the company (*Leed Estate Building & Investment Society v. Shepherd*).

7. Write short notes on any **four** of the following : 4×4 =16

(a) Provisions for applicability of internal audit as per Companies Act, 2013.

Applicability of Internal Audit

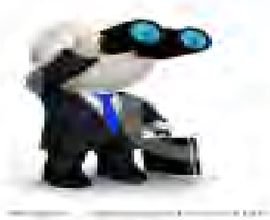
TYPE OF COMPANY	O/S LOANS / BORROWINGS (BANKS & FIs)	TO	DEPOSITS	PAID UP SHARE CAPITAL
Listed Company	All Listed Companies			
Private Company	100 Cr or more	200 Cr or more		
Public Company (Unlisted)	100 Cr or more	200 Cr or more	25 Cr or more	50 Cr or more

All conditions should be with respect to figures of preceding year.

Existing Company covered under above criteria shall comply within 6 months from commencement (26th March 2014)

By CA Ravi Taori

<u>**Who can become Internal Auditor?**</u>



CHARTERED ACCOUNTANT
(May or may not be in practice)

COST ACCOUNTANT

SUCH OTHER PROFESSIONAL

He may or may not be employee of company

<u>**APPOINTMENT & SCOPE OF INTERNAL AUDITOR ?**</u>

Appointment of Internal Auditor

INTERNAL AUDITOR

Audit Committee /Board shall, in consultation with the Internal Auditor, formulate the scope, functioning, periodicity and methodology.

By CA Ravi Taori

(5) Prohibition to buy-back its own securities in certain circumstances.

(i) Prohibition for buy back in certain circumstances:

As per provisions of Section 70 of the Companies Act 2013:

A. No company shall directly or indirectly purchase its own shares or other specified securities—

(a) Through **any subsidiary company including its own subsidiary companies**; or

(b) Through **any investment company or group of investment companies**; or

(c) If a default, by the company, in repayment of deposit or interest payable thereon, **redemption of debentures or preference shares or payment of dividend to any shareholder or repayment of any term loan or interest payable thereon to any financial institutions or bank, is subsisting.**

Provided that the buy – back is not prohibited if the default is remedied and a **period of three years** has elapsed since the cessation of the default.

No company shall directly or indirectly purchase its own shares or other specified securities in case such company has not complied with provisions of Sections 92,123, 127 and 129. **Section 92 relates to the filing of Annual Return, Section 123 and 127 to declaration and payment of dividend and Section 129 to the financial statement of the company.**

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(c) Advantages of CAAT.

Advantages of CAAT:

(i) ***Audit effectiveness***: **The effectiveness and efficiency of auditing procedures will be improved through the use of CAAT in obtaining and evaluating audit evidence, for example –**

(iii) ***Effective test checking and examination in depth:*** **CAAT permits effective examination in depth of selected transactions since the auditor constructs the lost audit trail.**

(a) Some transactions may be tested more effectively for a similar level of cost by using the computer.

(b) In applying analytical review procedures, transactions or balance details of unusual items may be reviewed and reports got printed more efficiently by using the computer.

(ii) ***Savings in time:*** **The auditor can save time by reviewing the EDP controls using CAAT than through other audit procedures.**

(d) Changes in accounting policies.

Change in Accounting Policies: Same accounting policies are adopted for similar events or transactions in each period so as to enable the user to compare the financial statements of an enterprise over a period of time. However, Accounting Standard 5, "Net Profit or Loss for the period, Prior Period Items and Changes in Accounting Policies" provides that accounting policies can be changed under the following circumstances-

(1) if the adoption of a different accounting policy is required by statute; or
(2) for compliance with an accounting standard; or
(3) if it is considered that the change would result in a more appropriate presentation of the financial statements of the enterprise

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A more appropriate presentation of events or transactions in the financial statements occurs when the new accounting policy results in more relevant or reliable information about the financial position, performance or cash flows of the enterprise. AS 5 also requires any change in accounting policy consequent upon the adoption of an Accounting Standard should be accounted for in accordance with the specific transitional provisions, if any, contained in that Accounting Standard. However, disclosures required by AS 5 should be made unless the transitional provisio s of any other Accounting Standard require alternative disclosures in this regard. For instance, how an enterprise should deal with intangible items appearing in its balance sheet when it applies AS 26, Intangible Assets, for the first time.

By CA Ravi Taori

(e) Recognition of interest on deposits.

Recognition of Interest on Deposits:

(i) Accounting Standard 9 on Revenue Recognition requires that the revenue arising from interest should be recognised on a time proportion basis taking into account the amount outstanding and the rate applicable. Such revenues should only be recognised when no significant uncertainty as to measurability or collectability exists.

(ii) Further, according to Section 128 of the Companies Act, 2013, books are to be maintained on accrual basis. Again, accrual method of accounting is a fundamental assumption of accounting policies.

(iii) Though the interest becomes due for payment only at maturity date, it accrues each quarter. Interest accrued but not due should be shown under current assets in the balance sheet as per Schedule III Part I requirement of the Companies Act, 2013.

(iv) As such, the profits and current assets are understated and true and fair view of the accounts are thus vitiated.

(v) On considerations of materiality of the item, the auditor may appropriately decide to qualify the audit report.