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**PAPER 3- ADVANCED AND MANAGEMENT AUDITING  
MAY 1998**

Answer Questions **1 and 2 and any four** from the rest

**Question 1**

- (a) Mr.K, a Chartered Accountant not in practice was employed by Do-well Ltd., on salaried basis as Chief Internal Auditor to be in-charge of internal control and internal audit department of the company. Mr. K largely relied on the work of the unqualified employees of the company. The Statutory Auditor subsequently found that the internal control was weak, that there were omission to record Cash Sales and collections from Debtors and the statements attested by the Chief Internal Auditor were all either untrue or false.  
The company seeks your advice whether any action could be taken against Mr.K under provisions of Chartered Accountant Act. **(5 Marks)**
- (b) A Chartered Accountant in practice entered into Partnership with his uncle in Textile business which, however, did not take off. Will he be held guilty of professional misconduct? **(5 Marks)**
- (c) A search U/s. 132 of the Income Tax Act.
- i. In the premises of a leading merchant led to the discovery of two sets of accounts books – One set to record all the income correctly and another set to record only limited income. A Chartered Accountant has issued the Tax Audit Report on the basis of second set of account books. Is he liable to the Income – Tax Department in the above circumstance? **(3 Marks)**
  - ii. Would your answer be different, if the first set of account books carried evidence of checking by the Chartered Accountant? **(2Marks)**
- (d) Excel Ltd., is a Manufacturing Company in durable consumer goods with an annual turnover of Rs.1,000 lakhs. The Company receives orders from its commission agents all over the country, but goods are dispatched directly to the customers. The documents including Transport bills are sent through the bank for collection.  
At the end of the 6<sup>th</sup> year, it is found that documents covering the dispatch of goods worth Rs.100 lakhs were still lying with the banks not cleared by the customer even though the normal collection period of 20 days from the date of dispatch has expired. Should Revenue be recognized in the above case? **(5 Marks)**

**Question 2**

As an Auditor, state your views on the following situations:

- (a) The debenture trust deed executed by Trust Me Ltd., stipulated the creation of a sinking fund for redemption of debenture. In terms of the Trust Deed, a specific amount was to be transferred to the sinking fund from out of the profits of each year. In spite of substantial profits in the year 1997, no amount is found transferred to the Sinking Fund Account. **(4 Marks)**
- (b) A suit for damages of Rs.1 lakh for breach of contract of sale (breach occurred in 1995) was decreed in favour of May Ltd., in March, 1997. The company has included the amount in its turnover for the financial year 1997. **(4 Marks)**
- (c) Note No.7 of Published Accounts of December Ltd., is as follows:  
“The process of work-in-progress materials estimated to remain in several pots of smelting plant is not taken into account, both at the beginning and at the end of the year for the following three reasons;
- i. The cost of work-in-progress material put into the pots immediately before commissioning of the smelting plant stood capitalized.
  - ii. The quantity of work-in-progress materials is expected to be the same at any point of time.
  - iii. It is extremely difficult to measure exactly the amount of fill in the pots”. **(4 Marks)**

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- (d) In the course of audit of a manufacturing company, it comes to light that it has outstanding forward contracts for purchase of raw materials at a price, which is higher than the current market price. However, there is no mention of this in the financial statements of the year. **(4 Marks)**

**Question 3**

Can the Statutory Auditor rely upon the work of an internal auditor? Discuss . **(16 Marks)**

**Question 4**

(a) As Statutory Central Auditors of a Nationalized Bank, mention the aspects that are to be commented upon in the Long form Audit Report in relation to :

- i. Bad and Doubtful Debts, and
- ii. Vigilance

**(8 Marks)**

(b) State the procedure for verification of Agent's Balances in the course of Audit of General Insurance Company. **(8 Marks)**

**Question 5**

Discuss with reference to the Accounting Standards the nature of classification and disclosure requirements in the statement of Profit and Loss of an entity in the following cases:

- (a) Losses sustained as a result of enemy action.
- (b) Disposal of long term investments of a Trading entity.
- (c) Setting up of group gratuity scheme where there was none.
- (d) Payment of arrears of Bonus for the earlier year as a result of settlement with the workers in the current year. **(4×4=16 Marks)**

**Question 6**

State the salient feature of the directions to the Auditors of Government Companies issued by the Comptroller and Auditor General of India U/s. 619(3) of the Companies Act, 1956 in relation to:

- (a) System of Account ; and **(10 Marks)**
- (b) System of Financial Control **(6 Marks)**

**Question 7**

The responsibilities of Joint Auditors are Joint and Several" – Discuss. **(16 Marks)**

**Question 8**

Write short notes on any four of the following:

- (a) Tagging and Tracing
- (b) Cash and cash equivalents
- (c) Permanent investments in the case of Banks
- (d) Objectives of operational auditing
- (e) Provision for unpaid Excise Duty

**(4×4=16 Marks)**