

12. MISCELLANEOUS TOPICS

Q.No.1. what are the general considerations about the duties of an auditor that can be summarized on the basis of legal decisions taken by court so far? (B) (N13 - 5 M)

The statutory duties of the auditor cannot be limited in any way either by the Articles or by the directors or members but a company may extend them by passing a resolution at the general meeting or making a provision in the articles.

On taking into account the legal decisions in the cases which so far have been taken to courts, his duties and responsibilities can be summarized as follows:

- a) To verify that the statements of account are drawn up on the basis of the books of the business. The auditor is not responsible for failure to disclose the affairs of the company kept out of the books and concealed from him which could not be known in the ordinary course of exercise of reasonable care and diligence.
- b) The duty of the auditor is not limited to mere verification of the arithmetical accuracy of the statements of account. He must find out that these are substantially correct, having regard to provisions in the Articles and the statute governing the business of the organization under which it is being carried on.
- c) To confirm that the management has not exceeded the financial administrative powers vested in it by the Articles or by any specific resolution of the shareholders recorded at a general meeting.
- d) Auditor is not required to start an audit with a suspicion or to detect a fraud unless some information has reached him which excited his suspicion. This is because his duty is verification and not primarily detection of fraud.
- e) To perform his duties by exercising reasonable skill and care - For the verification of matters which are not capable of direct verification, he can rely on what he believes to be honest statements of the management. He must, however, review the verification of assets by the company and not rely merely on the statement made by the persons appointed by the company.

Q.No.2. Z Ltd. gave a guarantee to the Court for payment of excise dues of Rs. 10 lakhs for one of its subsidiaries. According to the company, since the guarantee was given on behalf of its subsidiary, no disclosure was required. Comment. (C) (PM)

FACTS OF THE CASE:

Z Ltd., in its books of account is required to record a contingent liability of Rs. 10 lakhs for the guarantee given by it for payment of excise dues of its subsidiary, to the Court. In the event, the subsidiary failed to meet its obligation, Z Ltd. would be required to pay Rs. 10 lakhs to the authorities concerned.

AS 4 also states that the existence and amount of guarantees undertaken by an enterprise are generally disclosed in financial statements by way of a note, even though the possibility that the loss will occur, is remote.

Thus, the amount of any guarantee given by a company on behalf of its subsidiary is required to be stated and where practicable, the general nature of such contingent liability, if material, be specified.

CONCLUSION: Accordingly, the views expressed by the company cannot be accepted.

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Q.No.3. Mr. X, a shareholder of the company pointed out that the Premium received on issue of shares prior to the date of Balance Sheet has been transferred to Statement of Profit and Loss for arriving at the figure of commission payable to the managing director. (C) (PM)

TREATMENT OF PREMIUM RECEIVED ON ISSUE OF SHARES:

- Premium received on issue of shares is capital receipt and should not be credited to Statement of Profit and Loss.
- As per the provisions of Sec. 198 of the Companies Act, 2013 on calculation of profits, premium on issue of shares should not be considered in computation of net profit. The same need to be complied with for the purpose of managerial remuneration.
- The auditor should have qualified the audit report and qualified the amount by which the profit stands inflated.

Q.NO.4. GIVE YOUR ASSERTIONS FOR THE FOLLOWING ITEMS APPEARING IN BALANCE SHEET OF A LIMITED COMPANY. (B) (PM)

		Rs.
1. Cash in hand		10,000
2. Investments		1,00,000
3. Secured Loans		10,00,000
4. Machinery	13,00,000	
Less: Current year depreciation	(1,30,000)	
		11,70,000

ANSWER:

1. Cash in Hand Rs.10,000:

This is the item of current assets, exhibited on the asset side of Balance Sheet. It implies:

- That the firm concerned has Rs. 10,000 in hand in valid notes and coins on the Balance Sheet date.
- That the cash was free and available for expenditure to the firm.
- That the books of accounts show a cash balance of identical amount at the end of the day on which the Balance Sheet is drawn up.

2. Investments Rs.1,00,000:

This is also the item to be exhibited on the asset side of Balance Sheet as per Schedule III to the Companies Act, 2013, as prescribed by Company Law. This description is not giving us a complete picture of investment. We, as an auditor, must know:

- Nature of Investment, type of Investment; whether it is short term or long term investment or trade investment or non-trade investment.
- Rate of interest receivable.
- Face value or market value of investments as on Balance Sheet date.

3. Secured Loan Rs.10, 00,000:

It Implies that the company has secured loan from some parties, worth Rs.10,00,000. The description does not give us a complete picture. We, as an auditor, must know:

- The name of the lender,
- The nature of security provided; and
- The rate at which interest is payable.

4. Machinery Rs.11, 70,000:

The Company owns the Plant and Machinery whose WDV as on date of Balance Sheet is Rs.11,70,000. Gross block is Rs.13,00,000.

- a) The Machinery physically exists.
- b) The asset is being utilized in the business of the company productively.
- c) Charge of depreciation on this asset is Rs.1,30,000 relates to the year in respect of which the accounts are drawn up.
- d) The amount of depreciation has been calculated on recognized basis and the calculation is correct.

Q.No.5. M, Statutory Auditor of ABC Ltd. wants to verify cash on hand as on 31st March, 2016. The Management informs Mr. M. that it is not possible to cooperate, as cashier has been hospitalized. Advise Mr. M. on how to deal with the situation. (PM)

VERIFICATION OF CASH ON HAND:

The scope of audit may be limited for varied reasons,

- i) The entity may impose restriction on scope of audit,
- ii) The limitation may be imposed by circumstances. When the audit is carried out under and as per statute, the auditor should not accept the assignment when his duties are curtailed by agreement, unless required by any Law.

When audit is carried out in accordance with the entity's terms voluntarily, the auditor may indicate his scope in his audit report.

Sometimes, the circumstances may impose restrictions on audit scope. For example, if the auditor is appointed after the year end, he may not be able to participate in inventory checking or sometimes, the records required may not be available so that the auditor may not be able to check details in the manner he liked. Such limitations in scope may warrant an auditor to express disclaimer of opinion or qualified opinion in his audit report depending upon the circumstances.

The non co-operation of ABC Limited will amount to limitation on scope of auditors.

Q.No.6. Outstanding Liabilities. (C)

- a) **Purchases:** In some instances, invoices relating to purchases of goods that have been taken into stock are received too late to be included in the Purchase Day Book of the closing month. As a result, those will be included in the accounts of the succeeding period.

In such a case, a schedule of such invoices should be prepared and their total debited to Purchases Account and carried down as an outstanding liability.

If the precise amount of liability on account of such purchases cannot be ascertained; an estimate made by a responsible official might be accepted.

- b) **Wages, Salaries, etc.:** The amounts debited to these accounts should represent the amount actually chargeable for the year.

Thus, if the amount payable at the close of the year has been paid in the succeeding period, a provision there for should be made. While doing so, it should also be verified that the corresponding provision made at the end of the previous year has been brought in as a credit, for arriving at the amount chargeable for the year.

- c) **Rent and Taxes:** The amount charged towards the rent should be the annual rent as provided for in the lease.

If any rent for the year was outstanding at the close of year or has been paid in advance, the amount outstanding or paid in advance should be adjusted as a liability or asset respectively. Municipal taxes usually are payable in advance. As a result a proportion of last payment is usually carried forward as unexpired to the next period.

- d) **Freight:** Carriage and freight account may not be rendered till some time after the period to which they relate. In such a case a provision for the amount outstanding may be made on an estimate and while doing so the amount provided in the earlier year may be taken into account.

Q.No.7. Balance Sheet Audit. (C)

A Balance Sheet audit consists of the verification of all includible Balance Sheet items, together with the examination of expense and income accounts, which are so closely related to these items that it cannot be properly verified without such analysis and test.

In outline form, a Balance Sheet audit will include the following:

- a) An examination of partnership agreement, the memorandum and articles of association, minutes of the board of directors, and the system of accounting in force.
- b) The establishment of ownership of all assets included in the Balance Sheet.
- c) Proofs that all assets owned are included.
- d) The inclusion of the asset in the Balance Sheet in accordance with the accepted principles of accounting.
- e) Proof that all liabilities are included and at proved amounts.
- f) The examination of adjusting and closing entries or any other entries necessary to the preparation of the Balance Sheet.
- g) Evidence that the distinction has been made in recording transactions between capital and revenue; and that capital and revenue have been created on the basis of accepted accounting principles.
- h) Proof that the share capital issues have been made in compliance with the requirements of law and they are correctly recorded in the financial books.

Q.No.8. "The duties of auditors are limited to the verification of the arithmetical accuracy of the books of accounts". (C)

The duties of auditors are not limited to the verification of the arithmetical accuracy of the books of accounts kept by his client.

Simply because, the verification of arithmetical accuracy would amount to certification of accounts only which would not serve much purpose since the auditor is required to report on

- a) The manner of selection of accounting policies and
- b) To assess the judgement made by the enterprise on arriving at certain accounting estimates or
- c) How the final accounts have been ultimately prepared to portray the financial statements.

The auditor must satisfy himself by performing substantive audit procedures to vouchers, invoices, minutes of meetings, correspondence and the documentary evidence must verify that there exists a proper authenticity of the transactions.

Furthermore, he must verify that there exists a proper authority in respect of each transaction and that they are properly recorded.

An important aspect would involve valuation of different assets and liabilities shown in balance sheet.

Finally, the auditor must verify that the form in which the final accounts have been drawn up is the one prescribed by law and as per professional pronouncements and exhibit a 'true and fair view'.

In case of companies, Section 143 of the Companies Act, 2013, requires auditors to make a report to members of the companies on the accounts examined by him.

Conclusion: Thus, the duty of the auditor is just not restricted to mere checking arithmetically accuracy of accounts but to report on the same.

Q.No.9. The auditor is entitled to rely on work performed by others. Comment (C)

Work performed by others: The auditor should consider the following matters.

Work Done by	Auditors Duties
Assistants (SA-220)	The auditor should carefully direct, supervise and review work delegated to assistants. He will continue to be responsible for forming his independent opinion.
Experts (SA-620)	The auditor should seek reasonable assurance that the experts work constitutes appropriate audit evidence in support of the financial information. He should evaluate the work of an expert independently to conclude whether or not to rely upon the expert's certificate.
Another Auditors (SA-600)	The principal auditor should perform procedures to obtain sufficient & appropriate audit evidence, that the work of the other auditor is adequate for the principal auditor's purposes in the context of the specific assignment. The principal auditor should consider the significant findings of the other auditor [AAS-10]
Internal Auditor (SA-610)	The means of achieving the objectives are very similar for the internal auditor and external auditor. Hence much of the work of the internal auditor may be useful for the external auditor in determining the nature, timing and extent of his procedures.
Joint Auditors (SA-299)	Each joint auditor is entitled to assume that the other joint auditors have carried out their part of the audit work in accordance with the generally accepted auditing procedures. Each Joint Auditor is entitled to rely upon the other joint auditors for bringing to his notice, any department from Accounting Standards or material errors discovered during audit.

Q.No.10. "An opinion expressed by the auditor is neither an assurance as to the future viability of the enterprise nor the efficiency or effectiveness with which management has conducted the affairs of the enterprise". (Or) generally an audit is not concerned with the propriety of business conduct. Comment. (B)

The objective of an audit of financial statements is to enable an auditor to express an opinion on such financial statements.

In fact, it is the auditor's opinion, which helps determination of the true and fair view of the financial position and operating results of an enterprise.

As per SA-200, "Overall objectives of the independent auditor and the conduct of an audit in accordance with standards on auditing", such an opinion expressed by the auditor is

- a) Neither an assurance as to the future viability of the enterprise
- b) Nor the efficiency or effectiveness with which management has conducted affairs of the enterprise.

It must also be appreciated that the process of auditing suffers from certain inherent limitations, i.e., the limitation which cannot be overcome irrespective of the nature and extent of audit procedures.

It may however be noted that over a period of time, the scope of audit extended quite considerably by inclusion of certain matters of propriety nature in section 143 and CARO 2016 issued under section 143(11) of the Companies Act, 2013. Basically, the auditor has been primarily concerned with carrying out what may be termed as verifactory audit.

CONCLUSION: Thus, the auditor did not make judgement on management decisions, policies or the commercial prudence of transactions. However, with the introduction of aforesaid provisions, the auditor is required to express opinion on certain aspects of management decisions involving propriety aspects as well.

Q.No.11. Write a short note on - operational audit.

(PM)

1. **MEANING:** Operational Audit involves examination of all operations and activities of the entity.
2. **OBJECTIVE:**
 - a) The objects of operational audit include the examination of the control structure and of the relation of department controls to general policies.
 - b) It provides an appraisal of whether the department is operating in conformity with prescribed standards and procedures and whether standards of efficiency and economy are maintained.
 - c) It is concerned with formulation of plans, their implementation and control in respect of production and marketing activities.
3. **INTERNAL AUDIT VS. OPERATIONAL AUDIT:**
 - a) Internal audit focused on accounting operations of the entity.
 - b) Operational audit covers all other operation such as marketing, manufacturing, etc.
 - c) Thus, operational audit in its initial stages developed as an extension of internal auditing.
4. **NEED:**

The need for operational auditing has arisen due to the inadequacy of traditional sources of information for an effective management of the company where the management is at a distance from actual operations due to layers of delegation of responsibility, separating it from actualities in the organization.

THE END