

Answer Question Nos. 1 and 2 and four from the rest.

Question 1. As a Statutory Auditor, how would you deal with the following:

(a) Mr. Satish is appointed as the auditor of Greenwood Travels Ltd. with audit fees of Rs. 35,000. He purchased air ticket from Delhi to Kolkata and back for Rs. 18,000 from the client for his personal work and the amount remains unpaid at the end of the year as it is a general practice of the client to give credit to all. Mr. Satish claims that he does not incur any disqualification as contained in Section 226(3)(d) of the Companies Act.

**Answer.** Disqualification of auditors: The guidance note on "Independence of Auditors" issued by the ICAI in this context recommends that "a question of indebtedness may also be raised where an auditor of a company purchases goods or services from the company audited by him. In such a case, if the amount outstanding exceeds Rs.

1000, irrespective of the nature of the purchase or period of credit allowed to other customers, the provisions concerning disqualification of auditor as contained in Section 226(3)(d) will be attracted. This is applicable in the case of purchase of air tickets for personal work by the auditor of a company on normal terms and conditions of the business of the company as the amount outstanding at the end of the year exceeded Rs. 1000. Therefore, the contention of Mr. Satish that he does not incur disqualification is not correct as he has purchased a ticket of the value of Rs. 18,000. The provisions concerning disqualifications of auditor as contained in Section 226(3)(d) will be attracted.

(4 Marks)

(b) During the audit for the year ended on 31st March, 2009 of XYZ Ltd. you come across certain personal expenses of employees having been debited to Profit and Loss account.

**Answer.** Personal expenses of employees (debited to profit and loss account) Explanation  
The practice of meeting certain types of personal expenses of employees by the company is considered normal and is being recognised by the statutory authorities also. The charging of such personal expenses of the employees by the company to its profit and loss account is justifiable or not depends upon the terms and conditions of appointment of the employees. If the terms and conditions of employment include payment of expenses of personal nature, then such expenses can be incurred by the company. Where, however the contract of employment does not contain any provision for payment of expenses of a personal nature, then there is no warrant for incurring or re-imburement of such expenses by the company. Illustration of such expenses are medical re-imburement, conveyance for personal use, expenses on leave travel, maternity benefits, provisions of rent free quarters, canteen facilities etc.

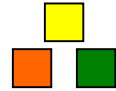
### **Conclusion**

Thus, charging of such personal expenses to profit and loss account either on the basis of company's contractual obligations or in accordance with the accepted business practice is perfectly normal and legitimate and does not call for any comments by the auditor. However, where personal expenses not covered by contractual obligations or by accepted business practice, is charged to profit and loss account, it would be the duty of the auditor to report thereon in terms of Section 227 (IA) of the Companies Act, 1956.

(5 Marks)

(c) Apex Ltd., a well reputed manufacturing public limited company has made a contribution of Rs. 2.5 lacs during the financial year ended 31.3.06 to a political party for running a school, situated in the village, where most of the workers of the company reside. It is admitted that the benefit of the school is mostly for the children of the workers of the company. The company has not made any profits in the last four years.

**Answer.** Restrictions regarding political contribution: Section 293-A of the Companies Act 1956 deals with prohibitions and restrictions regarding political contribution. A non-



Government company which has been in existence for not less than three years may contribute any amount or amounts directly or indirectly to any political party or for any political purpose to any person provided that the aggregate of the amounts which may be so contributed by a company in any financial year shall not exceed 5% of its average net profits determined in accordance with the provisions of Section 349 and 350 during the three immediately preceding financial years. The company in question has not made any profit in last four years and contributed Rs. 2.5 lacs during the year to a political party for running a school. This is violation of the provisions of Section 293-A of the Companies Act although the children of its workers are benefited. The auditor would have to qualify his report stating the contravention of the provisions of the Companies Act.

(4 Marks)

(d) Big Ltd. has borrowed Rs. 30 lakhs from State Bank of India during the financial year 2006-07. The borrowings are used to invest in shares of Small Ltd., a subsidiary company of Big Ltd., which is implementing a new project estimated to cost Rs. 50 lakhs. As on 31st March 2007, since the said project was not complete, the directors of Big Ltd. resolved to capitalize the interest accruing on borrowings amounting to Rs. 4 lakhs and add it to the cost of investments.

**Answer.** Capitalisation of Interest: As per AS 13 on "Accounting for Investments", the cost of investment includes acquisition charges such as brokerage, fees and duties. In the instant case, Big Ltd. has used borrowed funds for purchasing shares of its subsidiary company Small Ltd. Rs. 4 lakhs interest payable by Big Ltd. to State Bank of India cannot be called as cost of investment. The Accounting Standard 16 on "Borrowing Costs" also does not consider investment in shares as qualifying asset that can enable a company to add the borrowing costs to investments. In the instant case, the statutory auditor would qualify his report by stating that the borrowing costs have been wrongly added to the cost of investments rather than charging them to profit and loss account. The effect of the same on the profits for the year would also have to be mentioned

(5 Marks)

Question 2. Comment on the following with reference to the Chartered Accountants Act, 1949, Chartered Accountants (Amendment) Act, 2006 and schedules thereto:

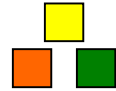
(a) As a Chartered Accountant in practice, you are asked to conduct a review of the "Profit Forecast" prepared by a Company in connection with its application for a Term loans from a bank.

**Answer.** Under Clause 3 of Part I of Second Schedule to The Chartered Accountants Act, 1949, a CA in practice is deemed to be guilty of professional misconduct if he permits his name or the name of his firm to be used in connection with an estimate of earnings contingent upon future transactions in a manner which may lead to the belief that he vouches for the accuracy of the forecast. "The guidance note on accountants' report on profit/financial forecast" provides that profit forecasts can be prepared or reviewed by a CA provided he discloses in his report the sources of information, the basis of forecasts and major assumptions involved and so long as he does not vouch for the accuracy of the forecast. Hence, the offer can be accepted if the above guidance note is complied with.

(4 Marks)

(b) Mr. B, a practicing Chartered Accountant, expressed his opinion on the financial statements of M/s ABC Ltd. for the year ended on 31st March, 2009. It was later found that the closing stock was valued arbitrarily by Management which was accepted by him without verification and large amount of revenue expenditure was capitalised.

**Answer.** Explanation: According to the clause (7) of Part - I of the Second schedule to the Chartered Accountants Act, 1949, a member shall be deemed to be guilty of professional misconduct if "he is grossly negligent in the conduct of his professional duties". It is the duty of an auditor to bring to bear on the work he has to perform that skill, care and



caution which a reasonably competent, careful and cautious auditor would use.

Mr. B. adopted arbitrary valuation of closing stock and accepted the valuation as done by the management without verification. He also failed to point out large amount of revenue expenditure, capitalized, thereby affecting the profitability of the company.

**Conclusion:** In view of the above, Mr. B. is to be held guilty of gross negligence in the conduct of his professional duties.

(5 Marks)

(c) The Chairman of an Audit Committee of a Blue chip Company, who is a chartered accountant asked the firm in which he was previously a partner to quote their fee on a success fee basis so as to ensure that a professional work is assigned to such firm.

**Answer.** Professional services cannot and should not be offered under an agreement which entails that fees shall be payable on a success fee basis. The fees payable, therefore, become contingent in nature. It is obvious that a person who is to receive payment in direct proportion to the benefit received by his client, may be tempted to exaggerate the advantage of his service or may adopt means which are not ethical. It will have the effect of undermining his integrity and impairing his independence. Therefore, the remuneration based on a percentage of the profits or on the happening of a particular contingency such as, the successful outcome of an appeal in revenue proceedings is prohibited. Therefore, the action of the firm to quote fees in such a manner on the advice of the Chairman of the Audit Committee to ensure their appointment could not be accorded approval and the member would be held guilty of professional misconduct under Clause (10) of Part I of the Chartered Accountants Act, 1949.

In the instant case, the Chairman of Audit Committee who also happens to be a chartered accountant would also be guilty of misconduct under the Chartered Accountants Act, 1949.

(4Marks)

(d) A Chartered Accountants firm pays share in the profits to a widow of its deceased Partner.

**Answer.** Explanation: Clause 2, Part I of the first schedule to the Chartered Accountants Act, 1949, is applicable. This clause says that a legal representative or widow of a deceased partner would be entitled to share the profits only where the partnership agreement contains a provision that on the death of the partner, his widow or legal representative would be entitled to such payment by way of sharing of fees or otherwise, for some specified period. The widow of a partner, when the partnership agreement does not contain such provision, entitling her to share in profits, would not be entitled to such profits.

**Conclusion:** In the given case, if such a clause is present in the partnership deed, the sharing is permissible, otherwise not. If no such clause exists, and if the firm still pays share in the profits to a widow of the deceased partner, the firm shall be considered as guilty of professional misconduct.

(5 Marks)

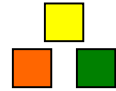
Question 3 Answer the following:

(a) Elaborate under clause 49 of the listing Agreement, who is an independent Director?

**Answer.** Clause 49 of the listing agreement on Independent Director: As per Clause 49 of the listing agreement, an Independent Director shall mean a non-executive director of the company who:

(i) apart from receiving director's remuneration, does not have any material pecuniary relationship or transactions with the company, its promoters, its directors, its senior management or its holding company, its subsidiary(s) and associates which may affect independence of the director;

(ii) is not related to promoters or persons occupying management positions at the board level or at one level below the Board;



(iii) has not been an executive of the company in the immediately preceding three financial years;

(iv) is not a partner or an executive or was not partner or an executive during the preceding three years, of any of the following:

(a) The statutory audit firm or the internal audit firm that is associated with the company, and

(b) The legal firm(s) and consulting firm(s) that have a material association with the company.

(v) is not a material supplier, service provider or customer or a lessor or lessee of the company which may affect independence of the director and

(vi) is not a substantial shareholder of the company i.e. owning two per cent or more of the block of voting shares.

(6 Marks)

(b) What are the methods an auditor may employ in the performance of statistical sampling tests ?

**Answer.** The auditor may use a computer to render considerable assistance in the performance of statistical sampling tests, employing the following methods:

(a) Interval sampling: The computer is programmed to select every *n*th item stored on magnetic tape, and the items so selected can be copied on to a separate tape and printed out in the form required by the auditor.

(b) Random number selection: The technique of random number selection can be computerised, the random numbers being stored on tape or generated by the computer separately for each application.

(c) Random Interval selection: The dangers of selecting a biased example by the use of a uniform interval can be avoided through the use of random variation of the interval between successive items. Random intervals are selected from random number tables maintained on magnetic tape, or produced by means of a random number generator program.

While applying statistical sampling, it should be remembered that materiality is one of the major considerations to decide whether or not a sample should be selected. For instance in case of certain enterprises like real estate builders, agents, merchant houses, etc. the total number of transactions may be relatively very small and hence are not appropriate for the selection of a sample. Even in case of major enterprises, there are certain items which are so significant that the records relating to them should be scrutinized by the auditor at new item by item basis. For example, the year end closing entries in the journal may be manipulated and, therefore, each entry must be carefully examined and authenticated by the auditor. In actual practice many firms of Chartered Accountants have found limited use of statistical sampling than anticipated by them. The various reasons which may be attributed to this state of affairs are as under:

(i) Audit has never been a mathematical discipline,

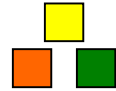
(ii) Designing and sampling schemes properly take unduly long time.

(iii) To draw valid conclusions on the basis of statistical sampling, all members of the audit team should have an excellent grasp of the statistical principles involved.

(6 Marks)

(c) Enumerate the Advantages of Cost Audit to Government.

**Answer.** Advantages of Cost Audit to Government: Cost auditor's approach is to ensure that the cost accounting plan is in consonance with the objectives set by the organisation and the system of accounting is geared towards the attainment of the objectives. A cost accounting system designed to exercise control over cost may be different from the one if the objective is to fix price. Accordingly, over a period of time particularly in view of



administered pricing system the cost accounting becomes quite important. Some of the specific advantages which can be reaped by the Government are:

- (i) It helps in the fixation of selling prices of essential commodities and thereby avoiding undue profiteering.
- (ii) In the case of cost plus contracts of Government, it helps to fix the price at reasonable level.
- (iii) It enables the Government to focus the attention on inefficient units.
- (iv) It enables the Government to lay down policies in favour of protecting certain industries.
- (v) It facilitates the settlement of disputes brought to the Government.
- (vi) It creates healthy competition in the industry.

(4 Marks)

Question 4 Answer the following:

(a) Discuss the design & control procedures which the auditor should adopt in applying CAAT in an audit under EDP environment.

**Answer.** The different design and procedural aspects of EDP systems are as follows:

(i) **Consistency of Performance:** EDP systems perform functions exactly as programmed and are potentially more reliable than manual systems, provided that all transactions type and conditions that could occur are anticipated and incorporated into the system.

(ii) **Programmed Control Procedures:** The nature of computer processing allows the design of internal control procedures in computer programs. These procedures can be designed to provide controls with limited visibility (e.g., protection of data against unauthorized access may be provided by passwords) Other procedures can be designed for use with manual intervention, such as review of reports printed for exception and error reporting and reasonableness and limit checks of data.

(iii) **Single Transaction Update of Multiple or Data Base Computer Files :** A single input to the accounting system may automatically update all records associated with the transaction (e.g., shipment of goods documents may update the sales and customers' accounts receivable files as well as the inventory file). Thus, an erroneous entry in such a system may create errors in various financial accounts.

(iv) **System Generated Transactions:** Certain transactions may be initiated by the EDP system itself without the need for an input document. The authorisation of such transactions may neither be supported by visible input documentation nor documented in the same way as transactions which are initiated outside the EDP system (e.g., interest may be calculated and charged automatically to customers' account balances on the basis of pre-authorised terms contained in a computer program).

(v) **Vulnerability of Data and Programme Storage Media:** Large volumes data and the computer programs used to process such data may be stored on portable or fixed storage media, such as magnetic discs and tapes. These media are vulnerable to theft, or intentional or accidental destruction.

(8 Marks)

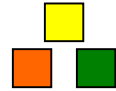
(b) State the internal controls in the area of Loans and Advances of Banks.

**Answer.** Internal controls in the area of loans and advances of banks:

(i) The bank should make advances only after satisfying itself as to the creditworthiness of the borrowers and after obtaining sanction from the proper authorities of the bank.

(ii) All the necessary documents (e.g. agreements, demand promissory notes, letters of hypothecation etc) should be executed by the parties before advances are made.

(iii) Sufficient margin should be kept against securities taken so as to cover any decline in the value thereof and also to comply with Reserve Bank directives. Such margins should be determined by the proper authorities to the bank as a general policy or for particular accounts.



- (iv) All the securities should be received and returned by responsible officer. They should be kept in the joint custody of two such officers.
- (v) All the securities requiring registration should be registered in the name of the bank or otherwise accompanied by the documents sufficient to give title to the bank.
- (vi) In the case of goods in the possession of the bank, contents of the packages should be test checked at the time of receipts. The godowns should be regularly and frequently inspected by a responsible officer of the branch concerned, in addition by the inspectors of the bank.
- (vii) Surprise checks should be made in respect of hypothecated goods not in possession of the bank.
- (viii) Market value of goods should be checked by officers of the bank by personal enquiry in addition to the invoice value given by the borrowers.
- (ix) As soon as any increase/decrease takes place in the value of securities proper entries should be made in the Drawing Power Book. These entries should be checked by an officer.
- (x) All the accounts should be kept within both the drawing power and the sanctioned limit at all times.
- (xi) All the accounts which exceed the sanctioned limit or drawing power or are against unapproved securities or are otherwise irregular should be brought to the notice of the H.O. regularly.
- (xii) The operation in each advance should be reviewed at least once every year.

(8 Marks)

Question 5 Answer the following:

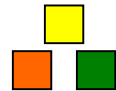
(a) As an internal auditor of a Cement Manufacturing Company, draft an audit programme for verification of transportation charges for despatches from the factory.

**Answer.** Procedure for Audit of Transportation Charges

- (i) Check rates contracted with transporters for carriage of goods.
- (ii) Check whether the rates mentioned as per the contract are correctly taken in the transporter's invoice.
- (iii) In case of discrepancy, check whether the same is authorised by the appropriate sanctioning authority.
- (iv) Check that the transporter's invoice includes a delivery challan which has customers stamp indicating the receipt of goods.
- (v) In case there is no stamp on the delivery challan, check whether the goods are received back and there is a corresponding inward note.
- (vi) Check whether all the goods to be dispatched have a transport booking order reference.
- (vii) Check whether each transporter's invoice mentions the transport booking order reference.
- (viii) Check whether all the transport booking orders have corresponding transporters names.
- (ix) Check whether the transport booking orders are prenumbered.
- (x) Check whether all the invoices are correctly booked in the books of accounts.
- (xi) In case there is an additional charge by the transporter due to extra carriage, check for the relevant supporting records (like material inward note/customer rejection note) and necessary authorisation by the sanctioning authority.
- (xii) Check whether service-tax on the transporters is correctly calculated and accounted.
- (xiii) Verify that there is a mechanism for linking all the transport bills to the sale invoices.

(8 Marks)

(b) Under CARO, 2003 how, as a statutory auditor would you comment on "A Term Loan obtained from a bank for Rs.75 lakhs for acquiring R&D equipment, out of which



Rs.12 lakhs was used to buy a car for use of the concerned director, who was overlooking the R&D activities”.

Answer. Utilisation of Term Loans: Under CARO, 2003, an auditor is required to comment whether term loans were applied for the purpose for which the loans were obtained.

The auditor should examine the terms and conditions of the term loan with the actual utilisation of the loans. If the auditor finds that the fund has not been utilized for the purpose for which they were obtained, the report should state the fact.

In the instant case, since term loan taken for the purpose of R&D equipment has been utilized for purchase of car which has no relation with R&D equipment. Therefore, car though used for R&D Director cannot be considered as R&D equipment. The auditor should state the fact in his report that the out of term loan of R&D lack, Rs.12 lakhs was not utilised for the purpose of acquiring the R & D equipment.

(8 Marks)

Question 6 Answer the following:

(a) A leading jewellery merchant used to value his inventory at cost on LIFO basis. However, for the current year, in view of requirements of A AS-2 (SA 200 A), he changed over to FIFO method of valuation. The difference in value of stock amounted to Rs.55 lakhs which is higher than that under the previous method. In such a situation, what are the reporting responsibilities of a Tax Auditor under Section 44AB of Income Tax Act, 1961.

**Answer.** The change in the method of valuation of stock is not a change in method of accounting, as it is only a change in accounting policy. However in the Income Tax Act, 1961 this is considered under method of accounting. Under the Income-Tax Act, 1961 if the change in method of valuation is bonafide, and is regularly and consistently adopted in the subsequent years as well, such change would be permitted to be made for tax purposes. In the instant case, the change in the valuation of stock from LIFO basis to FIFO basis is pursuant to mandatory requirements of the AS -2 ‘Valuation of Inventories’ and therefore should be viewed as bonafide change.

This apart, the tax auditor in his report has to specifically refer to the method of valuation of stock under Clause 12 in Form 3CD.

(a) Method of valuation of closing stock employed in the previous year.

(b) Details of deviation, if any, from the method of valuation prescribed under section 145A and the effect thereof on profit or loss.

The auditor has to see that the method of stock valuation is followed consistency from year to year. It is also necessary to ensure that method followed for valuation of stock results is correct profits or gain 2001. The change from LIFO to FIFO is bonafide, the disclosure of which would have to be made the financial statements. As far as section

145A is concerned, the tax auditor need not change the method of valuation of purchases, sales and inventories which is regularly employed by the assessee. All that he has to do is to adjust the valuation for any tax, duty, cess or fee actually paid or incurred by the assessee, if the same had not already been adjusted.

(8 marks)

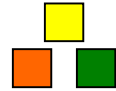
(b) What are the areas in which Due Diligence can take place ?

Answer. Areas in which Due Diligence can take place :

1. Commercial/operational due diligence: It is generally performed by the concerned acquire enterprise involving an evaluation from commercial, strategic and operational perspectives. For example, whether proposed merger would create operational synergies.

2. Financial Due Diligence: It involves analysis of the books of accounts and other information pertaining to financial matters of the entity. It should be performed after completion of commercial due diligence.

3. Tax Due diligence: It is a separate due diligence exercise but since it is an integral component of the financial status of a company, it is generally included in the financial due diligence. The accountant has to look at the tax affect of the merger or acquisition.



4. Information systems due diligence: It pertains to all computer systems and related matter of the entity.

5. Legal due diligence: This may be required where legal aspects of functioning of the entity are reviewed. For example, the legal aspects of property owned by the entity or compliance with various statutory requirements under various laws.

6. Environmental due diligence: It is carried out in order to study the entity's environment, its flexibility and adaptiveness to the acquirer entity.

7. Personnel due diligence: It is carried out to ascertain that the entity's personnel policies are in line or can be changed to suit the requirements of the restructuring.

(4 marks)

Question 7 Answer the following:

(a) Draft audit report u/s 227(3)(f) of the Companies Act, 1956 for XYZ Ltd. as on 31.3.2008 Where one of the directors, Mr. Flexible has failed to produce written representation that he has not defaulted u/s 274(1)(g) of the Companies Act, 1956.

**Answer.** Draft audit report u/s 227 (3) (f): Where one of the directors failed to produce written representation.

“Mr. Flexible who is also a director of XYZ Ltd. has not produced any written representation to the company as to whether XYZ Ltd. as at 31.03.06 had not defaulted in terms of Section 274(1)(g) of the companies Act. In the absence of the representation we are unable to comment whether Mr. Flexible is disqualified from being appointed as director in terms of section 274(1)(g). As far as other directors are concerned on the basis of the written representation received from such directors and taken on record by the Board, we report that none of the remaining directors is disqualified as on 31.3.2006 from being appointed as a director in terms of Section 274(1) (g) of the Companies Act, 1956”.

(6 Marks)

(b) In an operational audit performance evaluation, what factors can cause unsatisfactory production performance?

**Answer.** Factors which can cause unsatisfactory production performance in an operational audit performance evaluation

- (i) Non-availability of raw materials
- (ii) Inadequate or unskilled personnel
- (iii) Lack of proper supervision
- (iv) Lack of proper machine maintenance
- (v) Strikes and/or lock out
- (vi) Problems of power supply
- (vii) Non-availability of essential machine spares
- (viii) Lack of proper quality control
- (ix) Poor quality of raw materials
- (x) Other causes like fire, earthquake etc.

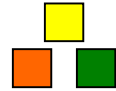
(8 Marks)

Question 8 Write short notes on:

(a) Walk Through Tests.

**Answer.** Walk Through Tests: A walk through is a procedure in which an auditor traces a transaction from its initiation through the company's information systems to the point when it is reflected in the financial reports. The auditor should perform one walk through, at a minimum, for each major class of transactions. A walk-through provides evidence to confirm that the auditor understands:

- (1) the process flow of transactions,
- (2) the design of identified controls for internal control components, including those related to preventing and detecting fraud, and



(3) whether all points in the process have been identified at which misstatements related to relevant financial statement assertion could occur. Walk throughs also provide evidence to evaluate the effectiveness of the controls' design and confirm that the controls have been placed in operation.

When performing a walk-through, the auditor should:

- (i) Be sure that the walk-through encompasses the complete process (initiation, authorization, recording, processing and reporting) for each significant process identified, including controls intended to address fraud risk.
- (ii) Ask the entity's personnel, at each of key stage in the process, about their understanding of what the company's prescribed procedures require.
- (iii) Determine whether processing procedures are performed as expected on a timely basis, and look for any exceptions to prescribed procedures and controls.
- (iv) Evaluate the quality of evidence provided and perform procedures that produce a level of evidence consistent with the auditor's objectives. The auditor should follow the whole process, using the same documents and technology that company staff use, asking questions of different personnel at each significant stage and asking follow-up questions to identify any abuse of controls or fraud indicators.

Once a walk-through is performed, the auditor may carry forward the documentation, noting updates, unless significant changes make preparation of new documentation more efficient. If such significant changes occur in the process flow of transactions or supporting computer applications, the auditor should evaluate the nature of changes and the effect on related accounts. The auditor should determine whether it is necessary to walk through transactions that were processed both before and after the change.

**(b) Powers and duties of an auditor of a Multi-state Cooperative Society.**

**Answer.** Powers and duties of an auditor of a Multi-state Cooperative Society: Under Section 73 of the Multi-State Cooperative Societies Act, 2002 every auditor of a multi – State Co-operative Society shall have a right of access at all times to the books, accounts and vouchers of the Multi-State Co-operative Society whether kept at the head office of the Multi-State Co-operative Society or elsewhere and shall be entitled to require from the officers or other employees of the Multi-State Co-operative Society such information and explanation as the auditor may think necessary for the performance of the duties as an auditor.

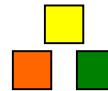
As per section 73 (2) the auditor shall make the following inquiries:

- (a) Whether loans and advances made by the Multi-State Co-operative Society on the basis of security have been properly secured and whether the terms on which they have been made are not prejudicial to the interests of the Multi-State Co-operative or its members;
- (b) Whether transactions of the Multi-State Co-operative Society which are represented merely by book entries are not prejudicial to the interest of the Multi-State Co-operative Society;
- (c) Whether personal expenses have been charged to revenue account; and
- (d) Where it is stated in the books and papers of the Multi-State Co-operative Society that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading.

**(c) Solvency margin in case of an insurer carrying on general insurance business.**

**Answer.** Solvency margin in case of an insurer carrying on general insurance business: In case of an insurer carrying on general insurance business, the solvency margin should be the highest of the following amounts :

- (i) fifty crore rupees (one hundred crores of rupees in case of reinsurer), or
- (ii) a sum equivalent to twenty percent of the net premium income; or
- (iii) a sum equivalent to thirty percent of net incurred claims.



Subject to credit for reinsurance in computing net premiums and net incurred claims being actual but a percentage, determined by the regulation but not exceeding fifty percent. It may be noted that conditions regarding maintenance of the above mentioned solvency margin may be relaxed by the authorities in certain special circumstances.

If, at any time, an insurer does not maintain the required solvency margin, the insurer is required to submit a financial plan to the authority indicating the plan of action to correct the deficiency in the solvency margin. If, on consideration of the plan, the authority finds it inadequate the insurer has to modify the financial plan.

Sub-section (2c) of Section 64 A states that if an insurer fails to comply with the requirements of the insurance Act, 1938, it shall be deemed to be insolvent and may be wound up by the court.

**(d)** Types of market under NEAT (National Exchange Automated Trading).

**Answer.** Type of markets under NEAT

(i) Normal Market: All orders of regular lot size or multiples thereof are traded in the normal market. Normal market consists of regular lot orders, special term orders, negotiated trade order and stop loss order depending on their order tributes.

(ii) Odd Lot Market: If the order size is less than the regular lot size such orders are traded in the odd lot market. In an odd lot market both the price and quantity of both the orders (buy and sell) should exactly match for the trade to take place.

(iii) Spot Market: Spot orders are similar to normal market orders except that spot orders have different settlement periods vis-a-vis normal market.

(iv) Auction Market: In the auction market, auctions are initiated by the exchange on behalf of trading members, for completing the settlement process.

(4X4= 16 Marks)