Mission May 2010 Phase I

IPCC

Subject: Audit and Assurance

Instructions :

(i) ***All questions are compulsory.***

(ii) ***Total marks : 100***

(iii) ***Total duration : 3 Hours***

(iv) ***In case of fill in the blanks students are advised to write full sentences with the relevant answer in the blank.***

(v) ***Use of two colour pens (black & blue or Black or Pink etc) is NOT allowed. Use only single colour pen.***

(vi) ***Answer all the questions serially.***

Question 1. Fill in the Blanks:

(i) Audit trail enable an auditor to trace the transactions from the source document to the summarized totals in accounting reports or vice-versa.

(ii) Section 293A of the Companies Act, 1956 prohibits Government company from contributing amounts to a political party or to any person for a political purpose.

(iii) Administrative Controls are designed to ensure that an acceptable standard of discipline and efficiency is maintained over the day to day operations of Computer Department.

(iv) Economy audit is concerned with using financial, human and physical resources in appropriate quantity and quality and at minimum cost.

(v) 'Contingency Fund' is established by the Union Government/ state to enable advances to be made by the President / Governor of the state for the purpose of meeting unforeseen expenditure pending its authorization by the Parliament /state legislature.

(vi) The issue of sweat equity shares must be authorised by a special resolution in the general meeting;

(vii) The period to which the accounts of the Company relate may be extended to eighteen months where special permission has been granted in that behalf by the Registrar.

(viii) The auditor under section 227 (3), is required to express his opinion whether, in his opinion, the P& L and Balance Sheet complies with the accounting standards. referred to in sub-section (3C) of section 211.

(ix) The word "fund" in relation to any "Reserve" should be used only where such Reserve is specifically represented by earmarked investments.

(x) If books of accounts are not kept on accrual basis and according to the double entry system of accounting then it will be deemed that proper books of accounts are not kept.

(xi) The words "subject to" are essential to state any qualification in the financial statements in clear and unambiguous manner.

(xii) Where an auditor gives an opinion on the various matters without any reservations, it is an unqualified opinion

(xiii) Where an auditor gives a qualified opinion then he should express clearly the nature of the qualification in the report. And also the reasons for the qualification.

(xiv) Auditor should not date the report earlier than the date on which the financial statements are signed or approved by management.

(xv) A compliance test is a test which seeks to provide audit evidence that the internal control procedures are being applied as prescribed.

(xvi) The main object of window-dressing to present rosy picture of state of financial affairs than it is otherwise.

(xvii) Removal of auditor can be done only by special resolution and only the members of the company have the power to remove the auditor.

(xviii) In case of joint auditors, casual vacancy of one joint auditor will not affect other joint auditors and they can continue to act as auditors during the period of the casual vacancy exists.

(xix) In case the annual general meeting is not held within the period prescribed under section 166, the auditor will continue in office till the annual general meeting is actually held and concluded.

(xx) As per SA 200 the scope of an audit depends upon the terms stated and decides in the Engagement letter, so a Statute can overwrite it.

(10 Marks)

Question 2. State with reasons (in short) whether the following statements are True or False.

(i) A person who has been officer or employee of the company earlier to his appointment as auditor not disqualified for appointment as an auditor u/s. 226.

Answer. A person who has been officer or employee of the company earlier to his appointment as auditor is not disqualified for appointment as an auditor u/s. 226, provided he is able to conduct the audit in an independent manner.

(ii) It is auditor's responsibility to maintain adequate accounting system incorporating various internal controls.

Answer. **False:** As SA 200, it is wholly and solely management's responsibility and not the auditor's responsibility. As per the said SA "the duty of safeguarding the assets of a company and maintaining the adequate accounting system is **primarily** that of the management. Auditor is entitled to rely upon the safeguards and internal controls instituted by the management. But the auditor is expected to examine and evaluate the internal control system.

(iii) Since client pays for the audit, the audit working papers belong to the client.

Answer. **False:** The documents prepared solely for the purpose of carrying out professional duties as an auditor (whether under statutory provisions or otherwise) belong to the professional account. The client does not have a right to access the working papers of the auditor. The auditor may, at his discretion, make portions of or extracts from his working papers available to the client. Hence, working papers are the property of the auditor.

(iv) Capital Reserve and Reserve Capital can be used inter-changeably.

Answer. **False.** Capital reserve is created out of Capital Profits. It can be used to write off intangible assets, for declaring dividend in certain cases. No resolution is required to be passed to create capital reserve. Whereas Reserve Capital is created out of uncalled capital. It CAN'T BE used to write off intangible assets, and for declaring dividend in certain cases. To create Reserve Capital, special resolution is required to be passed. It can be called up only in the event of its winding up.

(v) Each of the joint auditors is joint and severally responsible for the work not divided and carried out by all of them.

Answer. **True:** Each of the joint auditors is joint and severally responsible when the work is not divided and carried out by all of them. Also when the decisions are taken jointly regarding nature, extent and timing of the audit procedures to be performed by any one of them.

(5 Marks)

Question 3. Cineworld Pvt Ltd. is a in the business of multiplex and restaurant. Restaurant is adjoining to the multiplex. There has been a theft from ticket collection box. State how as an auditor you would conduct the audit of Cineworld Pvt Ltd.

Answer. As an auditor Cineworld Pvt ltd. following must be taken into account:

Constitution: Note the financial powers of the executives and the managing committee; Check the Rules, Regulations and Bye laws applicable to the Theatre; Ascertain the objects for which the license have been issued have been complied with or not;

Minute Books : Scrutinize the minutes of the meetings of Managing committee as regards various financial decisions including various decisions and resolutions affecting accounts requirement etc.

Income Sale of Tickets: Since there has been a theft from the ticket collection box auditor must ensure the effectiveness of the internal control with respect to ticket collection. Surprise physical verification of cash collection must be made at the end of any show to ensure that the collections received are recorded in the books. Other points which must be considered are as follows:

- Ensure that entry to the Cinema Hall during the show is through printed tickets only which are serially numbered and bound into books;
- Verify whether the printed tickets have been endorsed by Commercial Tax Authorities;
- Separate series of tickets is used for Advance Bookings & Free Passes are properly authorized;
- Stock of unsold tickets have been kept in the custody of Responsible Official;
- Vouch the entries in the Cash Book in respect of cash collected on sale of tickets for different shows, based on Daily Statements;
- Reconcile the amount of Entertainment Tax collected with the total number of tickets are issued for each class;

Advertisement Receipts: Verify the advertisement charges collected with reference to the Agreements entered into with the Advertisers; Cross verify the Advertisement Income based on Register of Slides & Shots Exhibited kept at the Cinema Hall;

Refreshment & Restaurant Income: Enquire the arrangement for collection of share in the restaurant income, i.e. fixed % sharing or Fixed Amount charged etc. Ensure whether the income is properly accounted for; Ensure closing stock of food stuffs, cold drinks, etc. have been duly considered and issues and purchases have been properly authorized;

Rental & Investment income: Rental income with Rent receipts and agreements; Dividend and Interest income, verify the securities in respect of investments held; Verify whether purchase and sale of investment have been properly authorized.

Expenditure :Ascertain the operation of internal control system over various heads of expenditure; Vouch the expenditure incurred on advertisement, repair and maintenance; Verify whether proper sanction exists in respect of regular administrative expenditure like salaries, printing, stationery etc.; Verify whether adequate distinction has been made between capital and revenue expenditure; Vouch payments towards film hire, with bills of distributors and underlying agreements;

Taxation & Statutory Compliance: Verify whether proper tax liability has been assessed and Return of Income was filed within due date; All taxes collected have been remitted to proper authorities on timely basis; All statutory obligations have been remitted to proper authorities on timely basis;

General :Verify the fixed assets and ensure that adequate depreciation is provided; Examine unadjusted balances out of advances paid to the distributors against film hire contract, to see they are good and recoverable; Verify that all advances in respect of films already run have been duly adjusted; Ensure that income against advance tickets sold have been duly accounted for and that at the end of year are shown under liability; Verify all the Balance sheet items and verify whether appropriate provisions have been made for replacement of current assets; Compute significant Ratios and seek appropriate explanation for significant deviations; Verify whether the form and manner of presentation of Financial Information conforms to Accounting Standards and applicable legal requirements; Obtain appropriate management representations and certificates in respect of various aspects covered during the course of audit.

(10 marks)

Question 4. Read the following paragraph and answer the question given below:

A limitation on the scope of the auditor's work may sometimes be imposed by the entity, for example, when the terms of the engagement specify that the auditor will not carry out an audit procedure that the auditor believes is necessary. However, when the limitation in the terms of a proposed engagement is such that the auditor believes the need to express a disclaimer of opinion exists; the auditor should ordinarily not accept such a limited engagement as an audit engagement, unless required by statute. Also, a statutory auditor should not accept such an audit engagement when the limitation infringes on the auditor's

statutory duties. A scope limitation may be imposed by circumstances, for example, when the timing of the auditor's appointment is such that the auditor is unable to observe the counting of physical inventories. It may also arise when, in the opinion of the auditor, the entity's accounting records are inadequate or when the auditor is unable to carry out an audit procedure believed to be desirable. In these circumstances, the auditor would attempt to carry out reasonable alternative procedures to obtain sufficient appropriate audit evidence to support an unqualified opinion. When there is a limitation on the scope of the auditor's work that requires expression of a qualified opinion or a disclaimer of opinion, the auditor's report should describe the limitation and indicate the possible adjustments to the financial statements that might have been determined to be necessary had the limitation not existed.

The auditor may disagree with management about matters such as the acceptability of accounting policies selected, the method of their application, or the adequacy of disclosures in the financial statements. If such disagreements are material to the financial statements, the auditor should express a qualified or an adverse opinion.

Questions:
(i) What are the circumstantial instances under which an auditor's scope becomes limited?
Answer. Following are the circumstances under which the scope of auditor becomes limited:

- When the terms of the engagement specify that the auditor will not carry out an audit procedure which auditor otherwise thought was necessary.
- When the entity's accounting records are inadequate and auditor is unable to carry out proper audit to enable him to express an opinion on the financial statements.
- Other circumstances like timing of the appointment of auditor after the end of the financial year as a result of which he is not able to carry out the physical verification of the stock or cash.

(ii) What is the remedy (ies) available to the auditor under (i)?
Answer. If the auditor believes that he will have to express a disclaimer of opinion for the proposed audit assignment then ordinarily he should not accept such a limited engagement audit. But if the audit is required by the Statute then can accept such audit but at the same time should give disclaimer of opinion or adverse opinion, as the case may be. Where an audit which infringes on the auditor's statutory duties the same should **NOT** be accepted. If the limitation in the scope of audit is circumstantial then the auditor must find out an alternative method to form an opinion.

(iii)What if an auditor disagrees with the management in certain matters and what would be his duty?
Answer. It may happen that after the appointment of auditor, the management and auditor differs on some points. The difference of opinion must be resolved before giving the

opinion, if disagreement is not resolved then auditor may, bearing the concept of materiality in mind, give qualified or an adverse opinion (as the case may be).

(6 Marks)

Question 5.Draft an audit report giving qualification for not complying with the requirements of AS 6.

Answer.

Auditors Report

To,
The members of M/s ABC Ltd.

We have audited the attached balance sheet of M/s ABC Ltd. as at 31st March, 2009 and also the profit and loss account and the cash flow statement for the year ended on that date annexed thereto. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the auditing standards generally accepted in India. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As required by the Companies (Auditor's Report), Order,2003 issued by the Central Government of India in terms of sub-section (4A) of section 227 of the Companies Act, 1956, we enclose in the Annexure a statement on the maters specified in the paragraphs 4 and 5 of the said Order.

As stated in Note X of Schedule to the financial statements, no depreciation has been provided for the period in the financial statements. This is contrary to Accounting Standard (AS) 6 on "Depreciation Accounting", issued by the Institute of Chartered Accountants of India and the accounting policy being followed by the entity according to which depreciation is provided on straight line basis. Had this accounting policy been followed, the provision for depreciation for the period would have been Rs….This short provisioning for depreciation has resulted into the profit for the year, fixed assets and reserves and surplus being overstated by Rs……

Further to our comments in the Annexure referred to above, we report that:

a) We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purpose of our audit.
b) In our opinion, proper books of account as required by law have been kept by the company so for as appears from our examination of those books (and proper returns adequate for the purposes of our audit have been received from the branches not visited by us). The Branch Auditor's Report(s) have been forwarded to us and have been appropriately dealt with.

c) The Balance Sheet and Profit & Loss Account and Cash Flow Statement dealt with by this report are in agreement with the books of accounts (and with the audited returns from the branches).
d) In our opinion, the Balance Sheet, Profit and Loss Account and Cash Flow Statement dealt with by this report comply with the accounting standards referred to in sub-section (3c) of section 211 of the Companies Act, 1956;
e) On the basis of written representations received from the directors, as on 31st March 2009 and taken on record by the Board of Directors, we report that none of the directors is disqualified as on 31st March 2009 from being appointed as a director in terms of clause (g) of sub-section (i) of section 274 of the Companies Act, 1956;

In our opinion and to the best of our information and according to the explanations given to us, subject to the effects on (on the financial statements of the matter referred to in the paragraph 4), the financial statements give the information required by the Companies Act, 1956, in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India:
a) In the case of the Balance Sheet of the state of affairs of the company as at 31st March 2009;
b) In the case of the Profit and Loss account of the profit/loss for the year ended on that date; and
c) In the case of the Cash Flow Statement of the Cash Flow for the year ended on that date.

Place of Signature — For XYZ and Co.
Date: — Chartered Accountants

Signature
(Name of the member signing the Audit Report)
Designation
M.No. __________

(7 Marks)

Question 6**.** Short notes on any three of the following :
(i) Option on share capital
Answer. An option on shares arises when a person acquires a right under the agreement with the company to subscribe for share in the company if he so chooses. Such options generally arise under the following circumstances :

- Under the promoter's agreements which is subsequently ratified by the company;
- Collaboration agreement;
- Loan agreements, debenture deeds (Section 81 of the Companies Act);
- Conversion of Preference shares into equity shares; and
- Other contracts, such as for supply of capital goods and/or merchandise.

Schedule VI, Part I, require disclosure of the particulars of any option on unissued share capital. The procedure to be followed broadly in audit of option on unissued share capital is stated below.

(ii) Cut-off procedures relating to inventories
Answer. The auditor should examine whether the entity has adopted appropriate ‘cut -off’

procedure for inventory and the enterprise has made an arrangement to ensure that the transactions entered into at the end of financial year are posted in the relevant period to which they relate. Auditor must ensure the efficacy by the following audit procedures mentioned as below –

(a) Calculate the gross profit percentage, ratio of creditors to purchases and ratio of debtors to sales to assess whether unusual fluctuations exist. If it does, then it implies errors or frauds relating to cut-off may be there, which, in turn necessitate extensive substantive procedures by the auditor.

(b) Examine invoices (relating to purchase and sales) and credit notes relating to raw materials and finished goods posted to the books of account during the last few days preceding the financial year and the first few days following the financial year and should be matched with the entries in the stock records to ensure that they are entered in the correct periods.
(c) Ensure stocks represented by such documents were included or excluded, as appropriate during stocktaking.

(iii) "Subsequent events" as per Standard on Auditing (SA 560).
Answer. Meaning of Subsequent Events: SA 560 on "Subsequent Events", defines the term 'subsequent events" as those significant events which occur between the balance sheet date and the date of the auditor's report. In the case of an audit a branch or division, of an entity, "subsequent events" refers to significant events which occurred up to the date of report of the auditor of that component. Thus, subsequent events are those events which occur after the date of the balance sheet till the audit report is signed by the auditor.
Consideration of Subsequent Events by the Auditor: SA 560 requires that the auditor should consider the effect of subsequent events on the financial statements and the auditor's report. However, the exact manner of treatment would depend upon whether the event falls in the category of 'adjusting event' or 'non –adjusting event'. As per Accounting Standard (AS) 4, events occurring after the date of the balance sheet are of two types, viz., adjusting events which provide further evidence of conditions that existed at the date of the balance sheet; and, non - adjusting events are those which are indicative of conditions that arose subsequent to the date of the balance sheet.

Therefore, an auditor is required to consider all subsequent events while discharging his duties and determine whether those shall have to be adjusted or simply required to be disclosed. However, the auditor should perform work as near as practicable to the date of the auditor's report.

(iii)Propriety Audit:
Answer. Propriety audit brings out the cases of improper, avoidable expenditure, even though the expenditure has been incurred in conformity with the existing rules and regulations. A transaction may satisfy all the requirements in so far as the various formalities regarding rules and regulations are concerned, but may still be highly wasteful.
In Propriety audit following points must be considered:
(1) The expenditure should not be prima-facie more than what occasion demands.
(2) Public money should not be utilised for the benefit of particular person or section of the community.
(3) Sanctioning authority must not exercise its powers to pass expenditure which will directly or indirectly to its own advantage.

(5X3=15 Marks)

Question 7. Comment on the following:

(a)One customer from whom Rs.1.5 lakhs are recoverable for credit sales gives an imported bullet motor-bike in full settlement of dues. The directors estimate that the market value for the motor -bike transferred is Rs.1.75 lakhs. As on the date of the balance sheet the motor -bike has not been registered in the name of auditee.

Answer. As per AS – 10, Accounting for Fixed Assets, when fixed asset is acquired in exchange or in part exchange for another asset, the cost of asset acquired should be recorded either at fair market value or at the net book value of the asset given up. In the present case the latter is more evident (Rs.1.5 lakhs given up) than the fair value of motor bike (Rs.1.75 lakhs estimated by the directors). Hence, the Customer's account should be credited with Rs. 1.5 lakhs and the motor –bike recorded at the same account.

At the same time as per AS – 1, Disclosure of Accounting Policies, the accounting treatment and presentation of the transactions and events should be governed by their substance and not merely by legal form. The motor -bike has not been registered in the name of the company on the date of the balance sheet in the present case. Taking into consideration the accounting principle of substance over form the auditor must ensure that the bike's acquisition is recorded in the present year even though the bike is not registered in the name of the auditee.

(b) While doing audit of a concern, you observe that there are some cheques received by the concern in the last one week of the financial year which has not been deposited with the bank even on the last day of the financial year. No entry is passed for these cheques received by the auditee on the last day of the year.

Answer. Business entity may at times receive cheques from the customers on the last day of the accounting year. It is quite likely, that cheques received on the last day of the accounting year could not be deposited in the bank account. Though normally speaking, it is expected that all cheques should be deposited in the bank daily. But there may be a possibility that such cheques which are received particularly during the late hours could not be deposited in the bank. Therefore, it is quite important to ensure that the system of internal control is effective and such cheques are properly accounted to avoid any frauds and that the financial statements reflect a true and fair view. As far as internal control system is concerned, it should be ensured that a list of such cheques is prepared in duplicate and a copy of the same has been sent to person controlling the debtors' ledger and a second copy is handed over to cashier along with the cheques received. The person who is controlling the debtors' ledger should ensure that proper accounting entries have been passed by crediting respective debtors' accounts. Cheques-in-hand, cash and bank balances should be disclosed in the financial statements.

(5X2 = 10 Marks)

Question 8. Answer the following:

(a) AB Ltd. is a company in which 20% of the paid up share capital is held by a State Government and 31% of the paid up share capital is held by a Government Company. Who will appoint the auditor of AB Ltd? Also state other categories of companies to which provision of section 619B is applicable.

Answer. Section 619 of the Companies Act, 1956,the auditor of a government company shall be appointed or re-appointed by the Comptroller and Auditor General of India. The provision applicable to the appointment of auditor of government companies also apply to another category of companies, even though they are not government companies as contained in section 619B of the Act. As per section 619B of the Companies act 1956 the provisions of section 619 apply to a company in which not less than 51% of the paid-up share capital is held by one or more of the following or any combination thereof:

i) the Central Government and one or more government companies;
ii) any State Government or Governments and one or more government companies;
iii) the Central Government, one or more State Governments and one or more government companies;
iv) the Central Government and one or more corporations owned or controlled by the Central Government;
v) the Central Government, one or more State Governments and one or more corporations owned or controlled by the Central Government;
vi) one or more corporations owned or controlled by the Central Government or the State Government;
vii) more than one government company; the auditor of such a company shall be appointed by the Central Government on the advice of the Comptroller and Auditor General of India.

Therefore provisions of section 619 will be applicable to AB Ltd. as a Government Company and the State Government hold 51% of the paid-up share capital of AB Ltd. together.

(b) No depreciation has been charged, in respect of a spare Bus purchased during the year and kept ready by the company for use as a stand-by on the ground that it was not used during the year. State the duty of an auditor with regard to the above.
Answer. As per AS-6, "Depreciation Accounting", "Depreciation is a measure of wearing out, consumption or other loss of value of depreciable asset arising from use, efflux of time or obsolescence through technology and market changes."
Hence, it is very clear that depreciation arises due to passage of time and therefore should be provided irrespective of whether the assets were put to use at all during the year.

→ It would be necessary to deduct depreciation in respect of idle assets since depreciation arises due to efflux of time.
→ Non utilization of any asset is not an acceptable ground to exclude depreciation, if there is an intention to use, it is considered as a constructive or passive usage.

Auditor will have to explain the management for providing appropriate depreciation, if not accepted he needs to qualify the audit report.

(c) Raman, a practicing C.A. is attending the taxation related matters of Ayushman Ltd., and he has to regularly visit the company from 12.00 P.M. to 2.30 P.M. on all working days. He is paid Rs. 4,500 p.m. for the same. Ayushman Ltd., is eager to appoint Raman as its auditor at the next general meeting. Advise whether Raman can accept the appointment.
Answer. According to Section 226(3), an employee or an officer of a Company cannot be appointed as its Auditor. An auditor may render services to the Company in matters relating to Taxation, Management Consultancy or other related area as long as his contract is a "Contract **for** services" (retainer ship) and not a "Contract **of** service" (i.e. employment). There is no prohibition for charging fee on monthly basis.
In the given case, Raman attends office regularly from 12.00 P.M. to 2.30 P.M. on all working days. Assuming he is not bound by the office timings but is attending to tax matters regularly during office working hours as per his own convenience. If he is under part-time service contract then he cannot be appointed. But if his appointment is on retainer ship, he may be appointed.

(5X3=15 Marks)

Question 9. ABC Ltd. has raised money by issue of shares to meet the cost of construction of Plant & Machinery of Rs 50 Lacs. Plant & Machinery cannot be made profitable for a long time. ABC Ltd. wants to pay interest on paid up share capital during construction period. State the provision in the Companies Act, 1956 under which it can pay interest on paid up share capital during construction period?

Answer. Under section 208 of the Companies Act 1956, a company which has raised money by issue of shares to meet the cost of construction of any work or building or provision of any plant which cannot be made profitable for a long time, can pay interest on paid-up capital for a period and subject to conditions specified in sub-sections (2) to (7) of section 208. Accordingly, the payment of interest should be verified as follows:

(a) The payment is authorised by the Articles or by a special resolution.

(b) Previous sanction of the Central Government for making such payment must be obtained.

(c) The interest must be paid only for such period as has been authorised by the Central Government and does not extend beyond the half- year next following during which the construction was completed or the plant was provided.

(d) Rate of interest shall, in no case exceed such rate as the Central Government may, by notification in official Gazzette.

(e) The amount of interest paid must be added to the cost of assets created out of the capital.

The interest paid being a part of the capital expenditure incurred in bringing into existence assets, it should be added thereto. Until so added, it must be shown as a separate item in the Balance Sheet under the head 'Miscellaneous Expenditure'. Therefore, ABC Ltd. can pay interest on paid up share capital during construction period under section 208 of the Companies Act, 1956.

(7 Marks)

Question 10. How would you vouch / verify the following items :

(i) Trademarks and Copyright :

Answer. The existence of a trademark must be verified by an inspection of the certificate as regards grant of the trademark. If the same has been purchased, then the agreement surrendering it in favour of the auditee should be examined. Right must be legally enforceable. Copyrights acquired (by surrender of rights) must be verified in the similar manner. The auditor should obtain a schedule of trademarks and copyrights and must verify that the renewal fees have been paid and charged to revenue. The last renewal receipt should, in each case, be examined to ascertain that the trade mark has not lapsed. Copyrights and trademarks are revalued at cost less amortisation charges till date. If copyright and trademarks are purchased, the cost includes purchase price and registration charges. If it has been developed by the client, the cost should include cost of developing outlays, design costs and other associated direct cost. The cost of trademarks and copyright should be amortised over the period of legal validity or useful commercial life, whichever is shorter. If in the course of audit, auditor finds that any publication has ceased to command sale, then the balance of amount in the copyright account must be written off to revenue.AS-26 has suggested for every intangible assets useful life of ten years unless and until there is clear evidence that useful life is longer than ten years.

(ii) Sale of Scrap

Answer. Following points must be considered:

(a)Review of internal control with respect to generation, storage and disposal of scrap.

(b)Check whether the organization is maintaining reasonable record for generation of Scrap.

(c) Analyze the raw material used, production and generation pattern of scrap and compare the same with figures of earlier year.
(d)Check the rates at which scrap has been sold and compare the rate with previous year.
(e)Vouch sales invoices, advertisement for tender, rate contract with scrap dealers.
(f)Ensure that there exists a proper control procedure to identify scrap and good units and they are not mixed up and sold as scrap.
(g)Make an overall assessment of the value of realization from scrap as to its reasonableness.

(iii)Payment of Retirement Gratuity to employees.
Answer. This may be vouched in the following manner :
(i) Ensure that the enterprise has complied with the requirements of AS-15 (revised).
(ii)Examine the basis on which gratuity payable is worked out (actuarial agreement or on the assumption that all employees retire on the balance sheet date).
(iii) Verify computation of liability of gratuity.
(iv) Check the amount of gratuity paid to employees who retired during the year with reference to the no. of years of service rendered by the retiring employees.
(v) If the enterprise has taken an insurance policy verify that the annual premium has been charged to Profit & Loss account.

(5X3=15 Marks)