



**GLOBAL CMA**

COST AND MANAGEMENT AUDIT

Paper-19

Syllabus-2016

Answer of Postal test Paper

Set-2

**Q.1****A. Fill in Blanks**

1. 1965
2. Committed
3. Optimum
4. Application of Cost Audit

**B. True or False**

1. **True.** The Cost audit Report mainly comment on the efficiency of the company namely, utilization aspect of the factors of production)
2. **False.** cas 9 deals with packing material cost.
3. **True.** expenses on account of donations is purely financial in nature, hence excluded from Cost Accounts.
4. **False .** Rules 3 deals with application of Cost Records.
5. **False.** part B of the annexure to cost audit report relates to manufacturing sector.

**Q. 2**

- a. The packing material receipts should be valued at purchase price including duties and taxes, freight inwards, insurance, and other expenditure directly attributable to procurement (net of trade discounts, rebates, taxes and duties refundable or to be credited) that can be quantified at the time of acquisition.
- b. Finance costs directly incurred in connection with the acquisition of Packing Material shall not form part of Packing Material Cost.
- c. Self manufactured packing materials shall be valued including direct material cost, direct employee cost, direct expenses, job charges, factory overheads including share of administrative overheads comprising factory management and administration and share of research and development cost incurred for development and improvement of existing process or product.
- d. The forex component of imported packing material cost shall be converted at the rate on the date of the transaction. Any subsequent change in the exchange rate till payment or otherwise shall not form part of the packing material cost. Explanation: The date on which a transaction (whether for goods or services) is recognised in accounting in conformity with generally accepted accounting principles.

**Q.4**

**A.** Self Manufactured Materials (and self manufactured components and sub assemblies) are valued at cost including direct Material cost, direct employee cost, direct expenses, Factory overheads and share of administrative overheads relating to production. share of other administrative overheads, Finance cost and Marketing overheads are excluded.

**C.** Depot: Depot is the bounded premises / place managed internally or by an agent, including consignment agent and C & F agent, franchisee for storing of materials / goods for further dispatch including the premises of Consignment Agent and C&F Agent for the purpose. Depot includes warehouses, go-downs, storage yards, stock yards etc.

**D.**Packing Material development cost: Cost of evaluation of packing material such as pilot test, field test, consumer research, feedback, and final evaluation cost.

## **Q.5**

**A.** The essential qualities of a management auditor are :-

- (i) Ability to grasp the business problems
- (ii) General understanding of the nature, purposes and objects of the organisation e.g. nationalized or government controlled organisation etc.
- (iii) Ability to determine or assist the progress of the organisation
- (iv) Knowledge of the principles of delegation of authority and control and the preparation of different budgets viz. cash budget, production budget, master budget, etc
- (v) Power of grasping and understanding different internal control devices viz., flow chart, flow of work, analysis of work scheduling, use of computer, etc.
- (vi) Sufficient knowledge about engineering statistical techniques, cost and management accounting, general financial accounting, production planning and control etc.
- (vii) General understanding of different laws viz. company laws, tax laws, FEMA, MRTP, and other economic legislations.
- (viii) Sufficient knowledge and experience in preparing various reports for submission to different levels of management including the top management
- (ix) Tactfulness, perseverance, pleasing and dynamic personality.

**B.** Unlike financial audit or other audits there can be no fixed items of evidence to be checked by a management auditor. A management auditor has to rely more on his experience and acumen to identify areas of review and study, particularly areas of weaknesses to be overcome, strengths to be exploited and risk to be properly covered.

The auditor's evidence comes from his discussions with the people concerned in the organisation, the survey and review of various reports of the organisation, including internal audit reports, inspection reports or any investigation reports, physical inspection, test examination of various transactions, inspection of important departmental files, monthly performance review statements, minutes and notes and above all personal observations.

Evidence can be gathered either by sampling techniques or by going into full details depending upon what the samples reveal. The evidence should be such that an auditor can draw valid conclusions, duly verifying the same with the people concerned. It should be understood that a management auditor does not rely on a voucher as an evidence, but shall fall back on various records, including vouchers as evidence for his audit, if the samples demand so. There is no area of restrictions for obtaining evidence.

**Q.8** The evaluation of internal controls including internal accounting controls gives an opportunity to the auditor to a clearer insight into the operational systems and an overall view of the organizational workings to spot weaknesses in the systems and procedures both in respect of financial and operational areas of the business. The audit process effectively evaluates the auditee's existing internal controls through the use of questionnaires and flow charts. The internal control questionnaire is a list of systematically and logically prepared questions designed to find out and evaluate the effectiveness of internal control systems regarding various aspects and accounting transactions of an organization. The questionnaires are to be comprehensive in nature to ensure that all aspects and accounting transactions are covered which are to be replied by the officials of the department or division concerned. The criteria for replies against each question are "yes", "no", "not applicable", "explanatory notes" and comments". Normally the affirmative answers suggest satisfactory internal controls while negative answers suggest weaknesses of internal controls.

#### **Q.9**

Successful personnel development concepts must meet company-specific requirements and targets. Also, they should be efficient, economical and lean. Personal development teaches the staff as to how to become more productive and effective at work. Essentially, personal development is about having more control of self actions and emotions and staying motivated irrespective of situation or environment. Evaluation of personnel development may include the following criteria –

- (a) Pre-planning as an essential feature of human resource development.
- (b) Ascertaining manpower needs for appropriate education, training and development.
- (c) Ascertaining the difference between future needs and existing talent i.e. gap or imbalance.
- (d) Adopting a suitable programme of recruitment, selection, training and development to close the gap of imbalance.
- (e) Adequate manpower planning with an appropriate blending of manpower management policies and manpower management programme.

The functional areas along with the scope of human resources management and development indicated below may be identified as the component of personnel function –

- (a) Organization review and analysis : Continuous review and analysis of organization's operation may be necessary in order to determine and develop appropriate work structure, roles and responsibilities, inter and intra-department relationship, and levels of authority.
- (b) Manpower, planning, recruitment and selection : Forecasting and planning is essential to needs an organization for a sufficient number of qualified personnel for manning its operations.
- (c) Manpower training and development : Appropriate methods and techniques of training and development may be adopted. Proper facilities and opportunities are to be provided for personnel to enable them to acquire necessary skills and knowledge to perform the jobs for which they are employed.
- (d) Performance appraisal : There should be proper measuring, rating and evaluation of performance of personnel, guiding employee development and promoting motivation, communication and equity.
- (e) Employee remuneration : This function includes developing and administering appropriate system of remuneration including job evaluation, wage and salary structure, incentive payments, fringe benefits and non-financial rewards.

#### **Q. 11**

**A. Value chain** — many company attempts to gain competitive advantage by appropriately linking its own activities with those of the suppliers, channels or customers. Vertical-integration, quality controls on inputs from suppliers, total quality management strategies, controlling distributors' performance through training/financing etc., collaborative arrangements etc. are some of the ways in which company's own activities are beneficially linked to other organizations. this provides an avenue for reporting under performance analysis report. What has been the cost of such coordinating strategies and how much of competitive advantage of the company has improved or strengthened at present level? if such linkages with other companies are established as a matter policy, every year, then performance as to the cost efficiency in such coordinating/ cooperating linkages can be an area for appraisal for the cost auditor.



B.

Budget-Ratios can be easily computed using the FOH Variance Computation Chart, given below:-

When FOH Volume Variance related ratios are to be computed, the working notes are as under -

WN	(1)	(2)	(3)	(4)	(5)
Cost Factor	AO x SR	AH x SR	PFOH	BFOH	AFOH
Time Factor included in above	SH = Standard Hours	AS = Actual Hours	PH = Possible Hours	BH = Budgeted Hours	
Hours	(1,200 x 8) + (800 x 12) = 19,200 hours	22 days x 8 hours x 100 men = 17,600 hours	(Not Applicable in this question.)	$\frac{1,86,000}{12 \text{ months}} = 15,500 \text{ hours}$	Not Applicable for Ratio Computation

Ratio	Time-based Computation	Output-based computation	WN Reference and Answer	
1. Efficiency Ratio	$\frac{\text{Standard Hours}}{\text{Actual Hours}}$	$\frac{\text{Actual Output}}{\text{Standard Output}}$	WN1 $\frac{19,200 \text{ hours}}{17,600 \text{ hours}} = 109.09\%$	
2. Capacity Ratio	$\frac{\text{Actual Hours}}{\text{Budgeted Hours}}$	$\frac{\text{Standard Output}}{\text{Budgeted Output}}$	WN2 $\frac{17,600 \text{ hours}}{15,500 \text{ hours}} = 113.55\%$	
3. Volume or Level of Activity Ratio	$\frac{\text{Standard Hours}}{\text{Budgeted Hours}}$	$\frac{\text{Actual Output}}{\text{Budgeted Output}}$	WN1 $\frac{19,200 \text{ hours}}{15,500 \text{ hours}} = 123.87\%$	

Relationship: Activity Ratio = Capacity Ratio x Efficiency Ratio = 113.55% x 109.09% = 123.87%.



Q. 12

- (i) Difference in Absorption = Absorbed OH (-) Actual OH  
 $= (\text{₹}1.25 \text{ per hour} \times 2,93,104 \text{ hours}) - \text{₹}4,46,380 = \text{₹}80,000 \text{ (under absorption)}$   
 Normal Increase in OH Costs 50% = ₹40,000

Treated as Cost and apportioned to -

Units Sold (7,000 units) = ₹35,000  
 Closing Stock of Finished Goods (800 units) = ₹4,000  
 Closing Stock of WIP 200 units (equivalent Units) = ₹1,000

So, Supplementary OH Recovery Rate = ₹5 per unit.

Abnormal Items	₹
Factory In-efficiency	40,000
Treated as LOSS and debited to Costing P&L	

Notes:

- Supplementary OH Recovery Rate =  $\frac{\text{Total OH}}{\text{Total Output Qty.}} = \frac{\text{₹}40,000}{8,000 \text{ Units}} = ₹5 \text{ per unit.}$

This calculation can be based on either Units Sold, (or) Closing Stock of FG, (or) Closing Stock of WIP, (or) Total of all these.

(ii) Journal Entries

(₹ in rupees)

Transaction/Narration	Particulars	Dr.	Cr.
1. Production OH incurred	Production OH Control A/c To General Ledger Adjustment A/c.	Dr. 4,46,380	4,46,380
2. Production OH absorbed (₹1.25 per hour × 2,93,104 days)	WIP Control A/c To Production OH Control A/c.	Dr. 3,66,380	3,66,380
3. Treatment of Under absorption	Cost of Sales A/c Finished Goods Control A/c WIP Control A/c Costing P&L A/c To Factory OH Control A/c	Dr. 35,000 Dr. 4,000 Dr. 1,000 Dr. 40,000	80,000

(iii) Impact on Profit

- OH absorbed into production is only ₹3,66,380 whereas OH actually incurred is ₹4,46,380. Hence, before passing the Journal Entry for under absorption, profit would have been wrongly over-stated (due to under-absorption / under-statement of costs) by ₹80,000.
- The above wrong over statement of profits is rectified by the Under absorption entry, in the following manner -

Under absorption Amount, (i.e., Profit over-statement amount) = ₹80,000				
Transfer to	Cost of Sales A/c	FG Control A/c	WIP Control A/c	Costing P&L A/c
Amount Transfer	₹35,000	₹4,000	₹1,000	₹40,000
Treatment	Finally transferred to Costing P&L A/c	Included in Value of Closing Stock of FG	Included in Value of Closing Stock of WIP	Transferred to Costing P&L A/c
	Profits of current period will be reduced by ₹35,000	Profit of next period will be reduced by ₹5,000, since Opening Stock will be valued at higher amount.		Profits of current period will be reduced by ₹40,000

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