PRIME ACADEMY

34TH SESSION PROGRESS TEST – FINANCIAL REPORTING

No. of Pages: 9

Total Marks: 75

Time Allowed: 2Hrs

Part A

1. M/s Kani Ltd has included interest and borrowing cost related to overdraft ₹. 45 crores while valuing the inventories. The CFO argues that it will form part of cost of inventories. As per AS 2, which of the following should be the alternative adopted by the company.
   a) Interest on bank O/D will not form part of inventory. And therefore not to be included while valuing the inventory.
   b) The interest cost will be included in the value of inventory.
   c) The interest will be included only with respect to the proportion of inventory amount on the total loan amount.
   d) All of the above

2. Expenditure incurred on construction cost upto 31.03.2011 — ₹. 990 crores
   Total contract price — ₹. 1250 crores
   Estimated additional expenses (including provision for contingencies) — ₹. 60 crores
   Compute the estimated profit in accordance with AS 7.
   a) ₹.200 crores
   b) ₹. 20 crores
   c) ₹.188.57 crores (approx.)
   d) ₹.260 crores

3. On 25.01.2011, X Ltd obtained advertisement right for a cricket match to be held in March & April for ₹. 520 crores. The company received advertising contract for 70% of available time for ₹. 700 crores during the month of January 2011. And for the balance during February 2011 for ₹. 240 crores.40% of the advertisement were telecasted before public on March and the balance 60% appeared before public on April 2011. Determine the profit made out of advertisement contract to be recognized for FY 2011-12 as per AS 9.
   a) ₹.420 crores
   b) ₹.252 crores
   c) ₹.700 crores
   d) ₹.940 crores

4. Durga Ltd sold plant and machinery related to their tumkur plant for ₹. 600 crores and purchased a new

set of boilers and machinery for ₹. 400 crores . Can the cash flows out of the sale and purchases be netted as per para 26 and para 24 of AS 3

a) Yes
b) No
c) Not applicable
d) The surplus can be shown under operating activity

5. In Hari & Co Ltd there was a theft of cash to the extend of ₹. 5 lakhs in January 2011. The theft was detected only in May 2011. The accounts of the company were not yet approved by board of directors. Whether the theft of cash should be disclosed in books of accounts? If so provide the most appropriate way.

a) The event is an adjusting event as per AS 4 and the financial statements required adjustment to the reported values.
b) The event is an non adjusting event requiring no adjustments to the reported values in financial statements.
c) Only disclosure required without any adjustment to the reported values.
d) Mentioned in the director's report without adjusting financial statements.

6. Explain the treatment of non-monetary grant (such as land or other resources) as per AS 12

a) Non-monetary grant given free of cost are recorded at nominal value.
b) No entry made in books of accounts.
c) Capital grant account is credited with value of asset.
d) None of the above

7. Retrospective effect should be given for depreciation for change in

a) Historic cost
b) Method of depreciation
c) Expected useful life
d) Both b and c

8. The cost of a pollution control machinery purchased by Govinda ltd was ₹ 100 crores having an estimated useful life of 10 years against which the Environment ministry of government of India paid a grant of ₹. 30 crores. What shall be the value of the depreciation having reference to the relevant accounting standards issued by ICAI. (assume NIL residual value). Select the most appropriate alternative that is in line with Accounting standard 12.

a) ₹ ..7 crores
b) ₹.10 crores
c) ₹.10 crores depreciation with a grant amortization of ₹. 3 crores to the credit of P & L.
d) Either a or c above

9. In case of integral foreign operations, cost of fixed asset should be recognized at

a) Exchange rate on date of purchase
b) Closing exchange rate on which balance sheet is drawn

c) Opening exchange rate
d) The average rate of closing and opening

10. As per AS 11 loss on account of foreign exchange difference on purchase of fixed assets should be
    a) Debited to asset a/c
    b) Treated as deferred revenue
    c) Debited to Profit &Loss a/c
    d) Either a or b

11. Which of the following will be included as part of the inventory cost in accordance with AS 2

    a) Abnormal amounts of wasted materials, labour or other production costs.
    b) Storage costs unless those costs are necessary in the production process prior to a further production stage.
    c) Administrative overheads that do not contribute to bringing the inventories to their present location and condition
    d) Freight charges paid to bring the inventory to its present location and condition.

12. What is the accounting entry to be passed as per AS 10 for the following situation:
    "Decrease in the value of fixed asset by ₹.30,00,000 on account of revaluation"

	₹	₹
a) Profit & Loss A/c Dr	30,00,000	
To Fixed Assets A/c		30,00,000
b) Revaluation A/c Dr	30,00,000	
To Fixed Assets A/c		30,00,000
c) Profit & Loss A/c Dr	30,00,000	
To Revaluation A/c		30,00,000
c) Fixed Asset A/c Dr	30,00,000	
To Revaluation reserve A/c		30,00,000

13. A change in method of depreciation can be provided only if
    a) required by statute,
    b) for compliance with an accounting standard or
    c) for appropriate presentation of the financial statements.
    d) any of the above
14. Foreign Branch operations functioning independently from the parent, the functional currency will be:
    a) Same as parent
    b) Determined using the guidance for determining the entity's functional currency.
    c) That of the country of incorporation
    d) None of the above

15. Premier ltd made provision for non moving stock regularly based on their estimation. For the financial year 2010-11 the board decided to make provision for non-moving stock based on technical evaluation.
a) This will be a change in accounting policy as per AS 5
b) This will not be a change in accounting policy as per AS 5
c) The provision is made to comply with AS 2 Inventory valuation and not relating to AS 5

d) None of the above.

16. The segment assets defined in AS 17 does not include
a) Deferred tax asset
b) Fixed assets
c) Both the above
d) None of the above

17. Based on relevant accounting standard Royalty income will be recognized based on
a) On receipt basis
b) Based on royalty agreement
c) When mining products are found good
d) When books are published

18. According to para 9.2 of AS 9 on Revenue Recognition, where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, for escalation of price, export incentives, interest etc., revenue recognition is
a) postponed to the extent of uncertainty involved.
b) Not made as there is uncertainty involved
c) Based on estimate partly recognized
d) None

19. An unquoted long term investment is carried in the books at a cost of ₹. 2 lakhs. The published accounts of the unlisted company received in May, 1998 showed that the company was incurring cash losses with declining market share and the long term investment may not fetch more than ₹. 20,000. Which of the following will be more appropriate by virtue of AS 13?
a) provision for diminution should be made to reduce the carrying amount of long term investment to ₹. 20,000
b) Investment taken only at cost
c) Investments are taken at market value basis
d) Either b or c whichever is lower

20. As per AS 19 on Leases, unearned finance income is the difference between
a) gross investment and return in the lease arrangement
b) amount accruing to the lessor, at the interest rate implicit in the lease.
c) operating lease and finance lease
d) the gross investment in the lease and the present value of minimum lease payments under a finance lease from the standpoint of the lessor; and any unguaranteed residual value

21. Balaguru Ltd. entered into a sale deed for its immovable property before the end of the year. But registration was done with registrar subsequent to Balance Sheet date. But before finalization, is it possible to recognize the sale and the gain at the Balance Sheet date?
a) No recognition possible

b) yes it can be recognized
c) only sales should be recorded without recognizing the gain
d) None of the above

22. If two companies have a same subsidiary, then CFS should be prepared by
    a) The company which first becomes the holding company
    b) Both the companies
    c) Two companies cannot have a same subsidiary
    d) The company which becomes the holding company latter

23. If a company ceases to be a subsidiary, then the investment should be be accounted
    a) The company which first becomes the holding company
    b) Both the companies
    c) In accordance with AS 13 from the date it ceases to be subsidiary and not become an associate d
    d) The company which becomes the holding company latter

24. Nature of investment covered in AS 23 for the purpose of associates will be
    a) Small share holding for earning dividend
    b) Both the companies
    c) Substantial holding in another company that allows controlling the other company
    d) Investment that don't meet test of control but are not small either and where there is no joint control of entity

25. In the case of jointly controlled entity
    a) There is no separate legal status
    b) The legal form cannot be partnership
    c) A contractual arrangement exists which determines joint control
    d) Sharing of income and expenses arises

(25x1=25 Marks)

Part B

1.

The Balance Sheets of three companies Angle Ltd., Bolt Ltd., and Canopy Ltd., as at 31st December, 2009 are given below:

Liabilities	Angle Ltd. ₹.	Bolt Ltd. ₹.	Canopy Ltd. ₹.
Share capital			
(Equity shares of ₹.100 each)	15,00,000	10,00,000	6,00,000
Reserves	2,00,000	1,25,000	75,000
Profit and Loss A/c	5,00,000	2,75,000	2,50,000
Sundry creditors	2,00,000	2,50,000	1,00,000
Bills payable	-	-	50,000
Angle Ltd.	-	1,00,000	80,000
	24,00,000	17,50,000	11,55,000

	Angle Ltd. ₹.	Bolt Ltd. ₹.	Canopy Ltd. ₹.
Goodwill	2,50,000	5,80,000	4,50,000
Plant and Machinery	4,00,000	2,50,000	3,25,000
Furniture and Fittings	2,00,000	1,50,000	1,40,000
Shares in-			
Bolt Ltd. (7,500 shares)	9,00,000	-	-
Canopy Ltd. (1,000 shares)	1,50,000	-	-
Canopy Ltd. (3,500 shares)	-	5,20,000	-
Stock in trade	1,00,000	1,50,000	1,60,000
Sundry debtors	1,40,000	70,000	70,000
Bills receivable	50,000	20,000	-
Due from-			
Bolt Ltd.	1,20,000	-	-
Canopy Ltd.	80,000	-	-
Cash in hand	10,000	10,000	10,000
Total	24,00,000	17,50,000	11,55,000

(a) All shares were acquired on 1st July, 2008.
(b) On 1st January, 2008, the balances were:

	Angle Ltd. ₹.	Bolt Ltd. ₹.	Canopy Ltd. ₹.
Reserves	1,00,000	1,00,000	50,000
Profit and Loss account	50,000	(50,000)Dr.	30,000
Profit during 2008 were earned evenly over the year	3,00,000	2,50,000	1,00,000

(c) Each company declared a dividend of 10% in the year 2009 on its shares out of Profits for the year 2008; Angle Ltd. and Bolt Ltd. have credited their Profit and Loss account with the dividends received.
(d) The increase in reserves in case of Angle Ltd., Bolt Ltd., and Canopy Ltd., was

affected in the year 2008.

(e) All the bills payable appearing in Canopy Ltd.'s Balance Sheet were accepted in favour of Bolt Ltd., out of which bills amounting ₹.30,000 were endorsed by Bolt Ltd., in favour of Angle Ltd.

(f) Stock with Bolt Ltd. includes goods purchased from Angle Ltd., for ₹.18,000. Angle Ltd., invoiced the goods at cost plus 20%.

Prepare consolidated Balance Sheet of the group as at 31st December, 2009. Working should be part of the answer. Ignore taxation including dividend distribution tax, disclose minority interest as per AS 21.

(20 Marks)

2 a)

A company is engaged in the business of ship building and ship repair. On completion of the repair work, a work completion certificate is prepared and countersigned by ship owner (customer). Subsequently, invoice is prepared based on the work completion certificate describing the nature of work done together with the rate and the amount. Customer scrutinizes the invoice and any variation is informed to the company. Negotiations take place between the company and the customer. Negotiations may result in a deduction being allowed from the invoiced amount either as a lump sum or as a percentage of the invoiced amount. The accounting treatment followed by the company is as follows:

(i) When the invoice is raised, the customer's account is debited and ship repair income account is credited with the invoiced amount.

(ii) Deduction, if any, arrived after negotiation is treated as trade discount by debiting the ship repair income account.

(iii) At the close of the year, negotiation in respect of certain invoices had not been completed. In such cases, based on past experience, a provision for anticipated loss is created by debiting the Profit and Loss account. The provision is disclosed in Balance Sheet.

Following two aspects are settled in the negotiations:

(i) Errors in billing arising on account of variation between the quantities as per work completion certificate and invoice and other clerical errors in preparing the invoice.

(ii) Disagreement between the company and customer about the rate/cost on which prior agreement has not been reached between them.

Comment whether the accounting treatment of deduction as trade discount is correct? If not, state the correct accounting treatment.

(6 Marks)

2 b)

A major fire has damaged the assets in a factory of M/s AGNI Limited on 5th April – five days after the year end and closure of accounts. The loss is estimated at ₹.10 crores out of which ₹.7 crores will be recoverable from the insurers. Explain briefly how the loss should be treated in the final accounts for the previous year.

(4 Marks)

3a)

Rose Ltd. had made an investment of ₹.500 lakhs in the equity shares of Nose Ltd. on 10.01.2009. The realizable value of such investment on 31.03.2009 became ₹.200 lakhs as Nose Ltd. lost a case of patent rights. Rose Ltd.

follows financial year as accounting year. How will you recognize this reduction in Financial statements for the year 2008-09?

(3 Marks)

3b)

From the following Profit & Loss Account of Brightex Co. Ltd., prepare a gross value added statement for the year ended 31.12.1998:

Show also the reconciliation between gross value added and profit before taxation.

Profit and Loss Account for the year ended 31.12.1998

	Notes	(₹.'000)	(₹.'000)
Income :			
Sales			6,240
Other Income			55
			6,295
Expenditure:			
Production and operational expenses	1	4,320	
Administration expenses (Factory)	2	180	
Interest & Other charges	3	624	
Depreciation		16	5140
Profit before tax			1155
Provision for tax			55
			1100
Balance as per last balance sheet			60
Transferred to fixed assets replacement reserve		400	
Dividend paid		160	560
Surplus carried to balance sheet			600

Notes:

1. Production & Operation expenses :

Consumption of raw materials	3,210
Consumption of stores	40
Local tax	8
Salaries to administrative staff	620

Other manufacturing expenses	442
	4,320

2. Administration expenses include salaries and commission to directors	5
3. Interest on other charges include :	
(a) Interest on bank overdraft (Overdraft is of temporary nature)	109
(b) Fixed loan from I.C.I.C.I.	51
(c) Working capital loan from I.F.C.I.	20

(d) Excise duties amount to one-tenth of total value added by manufacturing and trading activities.

(7 Marks)

4.

A Ltd. Leased a machinery to B Ltd. on the following terms:

	(₹. in Lakhs)
Fair value of the machinery	20.00
Lease term	5 years
Lease Rental per annum	5.00
Guaranteed Residual value	1.00
Expected Residual value	2.00
Internal Rate of Return	15%

Depreciation is provided on straight line method @ 10% per annum. Ascertain unearned financial income and necessary entries may be passed in the books of the Lessee in the First year.

(10 Marks)

PRIME ACADEMY

34TH SESSION PROGRESS TEST- FINANCIAL REPORTING

SUGGESTED ANSWERS

PART A

Question No:	Answers
1	**a**
2	**c**
3	**b**
4	**b**
5	**a**
6	**a**
7	**d**
8	**d**
9	**a**
10	**c**
11	**d**
12	**a**
13	**d**
14	**b**
15	**b**
16	**a**
17	**b**
18	**a**
19	**a**
20	**d**
21	**b**
22	**c**
23	**c**
24	**d**
25	**c**

PART B

1)

Consolidated Balance Sheet of Angle Ltd. and its subsidiaries Bolt Ltd and Canopy Ltd

as at 31st December, 2009

Liabilities	₹	₹	Assets	₹	₹
Share Capital			Goodwill		
(Equity shares of			Angle Ltd. 2,50,000		
₹.100each)		15,00,000	Bolt Ltd. 5,80,000		
Minority Interest			Canopy Ltd. 4,50,000	12,80,000	
Bolt Ltd. (W.N.6)	3,97,396		Add: Cost of	1,55,833	14,35,833
Canopy Ltd	2,31,250	6,28,646	control(W.N.7)		
Reserves (2,00,000		2,16,927	Plant & Machinery		
+14,844+2083)			Angle Ltd	4,00,000	
Profit and Loss			Bolt Ltd	2,50,000	
account (W.N.4)		7,62,260	Canopy Ltd	3,25,000	
Sundry creditors			Furniture & Fittings		9,75,000
Angle Ltd	2,00,000		Angle Ltd	2,00,000	
Bolt Ltd	2,50,000		Bolt Ltd	1,50,000	
Canopy Ltd	1,00,000	5,50,000	Canopy Ltd	1,40,000	4,90,000
Bills Payable	50,000		Stock-in-trade		
Less: mutually held	50,000	Nil	Angle Ltd	1,00,000	
			Bolt Ltd	1,50,000	
			Canopy Ltd	1,60,000	
				4,10,000	
			Less: Provision for		
			unrealized profit	3,000	4,07,000
			Sundry Debtors		
			Angle Ltd	1,40,000	
			Bolt Ltd	70,000	
			Canopy Ltd	70,000	2,80,000
			Bills Receivable		
			Angle Ltd	50,000	
			Bolt Ltd	20,000	
				70,000	
			Less: Mutually held	50,000	20,000
			Cash in hand		
			Angle Ltd	10,000	
			Bolt Ltd	10,000	
			Canopy Ltd	10,000	30,000
			Cash-in-Transit/dues		
			from Bolt Ltd		20,000
		36,57,833			36,57,833

Disclosure in accordance with AS 21
Amount of Equity attributable to minorities on the date of Investment ie. 01.07.2008

	Bolt ltd	Canopy Ltd
	₹	₹
Share Capital	2,50,000	1,50,000
Share in Capital reserve as on 01.01.08	25,000	12,500
Share in Capital Profits as on 01.01.08	(12,500)	7,500
Share in Capital profits for the period 01.1.08 to 30.6.08	31,250	12,500
	2,93,750	1,82,500
Total amount of Equity attributable to minorities	4,76,250	

Disclosure in accordance with AS21

Minority Interest as on 31.12.2009

	₹
Amount of equity as on the date of investment ie. 01.07.2008	4,76,250
Add: Movement in equity and proportionate share of profit less Dividend from the date of investment upto 31.12.09	1,52,396
	6,28,646

Working Notes:

1. Ascertainment of Profits for the year 2009

	Angle Ltd	Bolt Ltd	Canopy Ltd
	₹.	₹.	₹.
Balance as on 1st January, 2008	50,000	(50,000)	30,000
Add: Profits earned during 2008	3,00,000	2,50,000	1,00,000
	3,50,000	2,00,000	1,30,000
Less: Dividend declared	1,50,000	1,00,000	60,000
	2,00,000	1,00,000	70,000
Less: Transfer to Reserve	1,00,000	25,000	25,000
	1,00,000	75,000	45,000
Add: Profit for the year 2009(B/F)	4,00,000	2,00,000	2,05,000
Balance as on 31st December 2009	5,00,000	2,75,000	2,50,000

2. Undistributed profits for the year 2008

	Bolt Ltd	Canopy Ltd
	₹.	₹.
Profits for the year 2008	2,50,000	1,00,000
Less: Dividends declared	1,00,000	60,000
	1,50,000	40,000
Less: Transfer to Reserves	25,000	25,000
	1,25,000	15,000

3. Analysis of Profits

Particulars	Capital profits ₹.	Revenue reserves ₹.	Revenue profits ₹.
Canopy Ltd.			
Reserves as on 1st January, 2008	50,000		
Transfer to Reserve in the year 2008 [(75000-50000)/2]	12,500	12,500	
Profit & Loss Account			
Balance as on 1st January 2008	30,000		
Profit for 2008 remaining undistributed [(1,00,000-25,000-60,000)/2]	7,500		7,500
Profit for the year 2009 (2,50,000 – 30,000-15,000)			2,05,000
(A)	1,00,000	12,500	2,12,500
Minority Interest [1/4th of (A)]	25,000	3,125	53,125
	75,000	9,375	1,59,375
Share of Angle Ltd. [1/6th of (A)]	16,667	2,083	35,417
Share of Bolt Ltd.	58,333	7,292	1,23,958
BOLT Ltd.			
Reserves as on 1st January 2008	1,00,000		
Transfer to Reserves 2008[(1,25,000-1,00,000)/2]	12,500	12,500	
Profit & Loss Account – Balance (Dr.) as on 1st January 2008	(50,000)		
Undistributed Profits for 2008 [(2,50,000-25,000-1,00,000)/2]	62,500		62,500
Share in profits of Canopy Ltd.	58,333	7,292	1,23,958
Profits for the year, 2009 (2,75,000+50,000-1,25,000)			2,00,000
(B)	1,83,333	19,792	3,86,458
Less: Minority Interest [1/4th of (B)]	45,833	4,948	96,615
Share of Angle Ltd	1,37,500	14,844	2,89,843

4. Consolidated Profit and Loss Account of Angle Ltd

	₹	₹.
Profit & Loss Account balance as on 31.12.2009		5,00,000
Add: Share in revenue profits of Canopy Ltd		35,417

	Share in revenue profits of Bolt Ltd		2,89,843
Less:	Pre-acquisition dividend		8,25,260
	Angle Ltd. ½ (₹. 75,000 + ₹. 10,000)	42,500	
	Bolt Ltd. (½ of ₹. 35,000)	17,500	60,000
			7,65,260
Less:	Unrealised Profit in Closing Stock (20/120 X 18,000)		3,000
			7,62,260

5. Consolidated Reserves of Angle Ltd.

	₹.
Reserves as on 31.12.2007	2,00,000
Add: Share in revenue reserves of Canopy Ltd.	2,083
Add: Share in revenue reserves of Bolt Ltd	14,844
	2,16,927

6. Minority Interest

	Bolt Ltd ₹.	Canopy Ltd ₹.
Share Capital	2,50,000	1,50,000
Share of Capital Profits	45,833	25,000
Share of Revenue Reserves	4,948	3,125
Share of Revenue Profits	96,915	53,125
Total	3,97,396	2,31,250
Grand total		6,28,646

7. Cost of Control / Goodwill

	₹.	₹.
Cost of investments (9,00,000+1,50,000+5,20,000)		15,70,000
Less: Dividend Attributable to Pre-acquisition profits for 6 months ie. [(75,000+45,000)/2]		60,000
		15,10,000
Less: Face value of Shares		
Bolt Ltd.	7,50,000	
Canopy Ltd.	4,50,000	
Capital profits		
Bolt Ltd.	1,37,500	
Canopy Ltd.	16,667	13,54,167
Goodwill		1,55,833

8. Cash in Transit / Dues from Bolt Ltd.

	₹.	₹.

(i)	Due to Angle Ltd.		
	From Bolt Ltd.	1,20,000	
	From Canopy Ltd.	80,000	2,00,000
(ii)	Due By Angle Ltd.		
	To Bolt Ltd	1,00,000	
	To Canopy Ltd	80,000	1,80,000
			20,000

2 (a)

(i) As per AS 9 "Revenue Recognition", revenue is recognized at the time when the invoice is raised to the customers; however the treatment of deduction as trade discount is not as per AS 9. Considering the treatment prescribed by AS 4 "Contingencies and Events occurring after the Balance Sheet Date", the correct treatment of the difference between the invoice amount and finally settled amount should be under:

The adjustment of the difference between the invoiced amount and the amount finally settled against "Ship Repair Income" account is in order. Events occurring up to the date of approval of the accounts by the Board of Directors should be taken into consideration in determining the amount of adjustment to be made in this regard. The description of the difference as "trade discount" is not appropriate.

2 (b)

The loss due to break out of fire is an example of event occurring after the balance sheet date. The event does not relate to conditions existing at the balance sheet date. It has not affected the financial position as on the date of balance sheet and therefore requires no specific adjustments in the financial statements. However, paragraph 8.6 of AS 4 states that disclosure is generally made of events in subsequent periods that represent unusual changes affecting the existence or substratum of the enterprise at the balance sheet date. In the given case, the loss of assets in a factory is considered to be an event affecting the substratum of the enterprise. Hence, as recommended in paragraph 15 of AS 4, disclosure of the event should be made in the report of the approving authority.

3 (a)

Recognition of reduction in value of investment would depend upon the nature of investment and nature of decline as per AS13. If the investments were acquired for long term and decline is temporary in nature, reduction in value will not be recognized and investments would be carried at cost. If the decline is of permanent nature, it will be charged to profit and loss account. If the investments are current investments, the reduction should be recognized and charged to Profit and Loss Account as the current investments are carried at cost or fair value whichever is less.

3 (b)

Brightex Co. Ltd
Value Added Statement
For the year ended 31st December, 1998

Particulars	**₹. In thousands**	**₹. In thousands**	**%**
Sales		6,240	
Less: Cost of bought in material and services:			
Production and operational expenses			
(4,320 – 8 -620)	3,692		
Administration expenses (180-5)	175		
Interest on bank overdraft	109		
Interest on working capital loan	20		
Excise duties (Refer to working note)	180		
Other/miscellaneous charges (444-180)	264	4,440	
Value added by manufacturing and trading activities		1,800	
Add: Other income		55	
Total value added		1,855	
Application of value added:			
To pay Employees:			
Salaries to Administrative staff		620	33.42
To pay Directors:			
Salaries and Commission		5	0.27
To pay Government:			
Local Tax	8		
Income Tax	55	63	3.40
To pay Providers of Capital:			
Interest on Fixed Loan	51		
Dividend	160	211	11.37
To provide For Maintenance and Expansion of the Company:			
Depreciation	16		
Fixed Assets Replacement Reserve	400		
Retained Profit (600-60)	540	956	51.54
		1,855	100.00

Reconciliation Between Total Value Added and Profit Before Taxation:

Particulars	₹. In thousands	₹. In thousands
Profit before Tax		1,155
Add back:		
Depreciation	16	
Salaries to Administrative Staff	620	
Director's Remuneration	5	
Interest on Fixed Loan	51	
Local Tax	8	700
Total value added		1,855

Working Note:

Calculation of Excise Duty

		₹. In thousands
Interest and other charges		624
Less : Interest on bank overdraft	109	
Interest on loan from ICICI	51	
Interest on loan from IFCI	20	180
Excise duties and other/miscellaneous charges		444

Assuming that these miscellaneous charges have to be taken for arriving at Value Added (in the first part of Value Added Statement), the excise duty will be computed as follows.
Let excise duty be x; thus miscellaneous/ other charges = 444 -x
Thus x = 1/10 x [6,240 -{3692+ 175+109+20+x+(444-x)}]
= 1/10 x [6240 - 4440] = 180
Other/ miscellaneous charges = 444 - 180 = 264
The above solution is given accordingly.

However, if other/miscellaneous charges are taken as any type of application of Value Added. (i.e, to be taken in the application part), then excise duty (x) will be computed as follows:

x = 1/10 x [6240 - (3692+175+109+20+x)]
x = 1/10 x [2244 -x]
11x = 2244
x = 204
And thus total value added will be 2040 + 55 (other income) = 2095

And accordingly, application part will be prepared, taking miscellaneous charges. ₹ ('000) 240 [i.e, 444 - 204] as the application of value added.

4:

Computation of Unearned Finance Income

As per AS 19 on Leases, unearned finance income is the difference between (a) the gross investment in the lease and (b) the present value of minimum lease payments under a finance lease from the standpoint of the lessor; and any unguaranteed residual value accruing to the lessor, at the interest rate implicit in the lease.

where :

(a) Gross investment in the lease is the aggregate of (i) minimum lease payments from the stand point of the lessor and (ii) any unguaranteed residual value accruing to the lessor.

Gross investment = Minimum lease payments + Unguaranteed residual value
= (Total lease rent + Guaranteed residual value) + Unguaranteed residual value
= [(₹. 5,00,000 X 5 years) + ₹. 1,00,000] + ₹. 1,00,000
= ₹. 27,00,000

(b) Table showing present value of (i) Minimum lease payments (MLP) and (ii) Unguaranteed residual value (URV).

Year	MLP inclusive of URV ₹.	Internal rate of return (Discount factor 15%)	Present value ₹.	
1	5,00,000	.8696	4,34,800	
2	5,00,000	.7561	3,78,050	
3	5,00,000	.6575	3,28,750	
4	5,00,000	.5718	2,85,900	
5	5,00,000	.4972	2,48,600	
	1,00,000 (guaranteed residual value)	.4972	49,720	
			17,25,820	(i)
	1,00,000 (guaranteed residual value)	.4972	49,720	(ii)
		(i) +(ii)	17,75,540	(b)

Unearned Finance Income = (a) – (b)
= ₹. 27,00,000 – ₹. 17,75,540
= ₹. 9,24,460

Journal Entries in the books of B ltd.

Particulars	Debit ₹.	Credit ₹.
<u>At the inception of lease</u> Machinery A/c Dr. To A Ltd's A/c (Being lease of machinery recorded at present value of MLP)	 17,25,820*	 17,25,820*
<u>At the end of the first year of lease</u> Finance charges A/c (refer working note) Dr. To A Ltd's A/c (Being the finance charges for first year due)	 2,58,873	 2,58,873
A Ltd's A/c Dr. To Bank A/c (Being the lease rent paid to the lessor which includes outstanding liability of ₹. 2,41,127 and finance charges of ₹. 2,58,873)	5,00,000	 5,00,000
Depreciation A/c Dr. To Machinery A/c (Being the depreciation provided @ 10% p.a. on straight line method)	1,72,582	 1,72,582
Profit and Loss A/c Dr. To Depreciation A/c To Finance charges A/c (Being the depreciation and finance charges transferred to profit and loss account)	4,31,455	 1,72,582 2,58,873

Note:

*As per para 11 of AS 19, the lessee should recognise the lease as an asset and a liability at an amount equal to the fair value of the leased asset at the inception of lease. However, if the fair value of the leased asset exceeds the present value of minimum lease payments from the standpoint of lessee, the amount recorded should be the present value of these minimum lease payments. Therefore, in this case, as the fair value of ₹. 20,00,000 is more than the present value amounting ₹.17,25,820, the machinery has been recorded at ₹. 17,25,820 in the books of B Ltd. (the lessee) at the inception of the lease. According to para 13 of the standard, at the inception of the lease, the asset and liability for the future lease payments are recognised in the balance sheet at the same amounts.

Working Note:

Table showing apportionment of lease payments by B Ltd. between the finance charges and the reduction of outstanding liability.

Year	Outstanding liability (Opening balance) ₹.	Lease rent ₹.	Finance charge ₹.	Reduction in outstanding liability ₹.	Outstanding liability (Closing balance) ₹.
1	17,25,820	5,00,000	2,58,873	2,41,127	14,84,693
2	14,84,693	5,00,000	2,22,704	2,77,296	12,07,397
3	12,07,397	5,00,000	1,81,110	3,18,890	8,88,507
4	8,88,507	5,00,000	1,33,276	3,66,724	5,21,783
5	5,21,783	5,00,000	78,267	5,21,783	1,00,050*
			8,74,230	17,25,820	

* The difference between this figure and guaranteed residual value (₹. 1,00,000) is due to approximation in computing the interest rate implicit in the lease.

PRIME ACADEMY

34TH SESSION PROGRESS TEST – STRATEGIC FINANCIAL MANAGEMENT

No. of pages – 6 Total Marks – 75
Time allowed –
2 Hours

PART – A

1. Risk in Capital budgeting implies that the decision-maker knows the_______of the cash flows
    a. Variability
    b. Probability
    c. Certainty
    d. None of the above

2. In certainty-equivalent approach, adjusted cash flows are discounted at:
    a. Accounting rate of return
    b. Internal rate of return
    c. Hurdle rate
    d. Risk-free rate

3. Which of the following is a risk factor in capital budgeting?
    a. Industry specific risk factors
    b. Competition risk factors
    c. Project specific risk factors
    d. All of the above

4. In risk-adjusted discount rate method, the normal rate of discount is:
    a. Increased
    b. Decreased
    c. Unchanged
    d. None of the above

5. In risk adjusted discount rate method, which of the following is adjusted?
    a. Cash flows
    b. Life of the proposal
    c. Rate of discount
    d. Salvage value

6. NPV of a proposal, as calculated by RADR method and CE approach will be:
    a. Same

b. Unequal
c. Either a or b depending on the project
d. Both a and b

7. Risk of a capital budgeting can be incorporated by:
    a. Adjusting the cash flows
    b. Adjusting the discount rate
    c. Adjusting life
    d. All of the above

8. In CE approach, the CE factors for different years are:
    a. Generally increasing
    b. Generally decreasing
    c. Generally same
    d. None of the above

9. Which of the following is correct for RADR?
    a. Accept a project if NPV at RADR is negative
    b. Accept a project if IRR is more than RADR
    c. RADR is overall cost of capital plus risk-premium
    d. All of the above.

10. If payback period approach to risk the target payback period is:
    a. Not adjusted
    b. Adjusted upward
    c. Adjusted downward
    d. b or c

11. In sensitivity analysis, the emphasis is on assessment of sensitivity of:
    a. Net economic life
    b. Net present value
    c. Both a and b
    d. Overall life

12. Most sensitive variable as given by the sensitivity analysis should be:
    a. Ignored
    b. Given least importance
    c. Given maximum importance
    d. None of the above.

13. Dividend pay-out ratio is:
    a. PAT ÷ Capital

b. DPS÷EPS
c. Preference dividend ÷ PAT
d. Preference dividend ÷ Equity dividend

14. Shares of face value ₹.10 are 80% paid up. The company declares a dividend of 50%. Amount of dividend per share is:
    a. ₹.5
    b. ₹.4
    c. ₹.80
    d. ₹.50

15. Which of the following generally not result in increase in total dividend liability?
    a. Share-split
    b. Right issue
    c. Bonus issue
    d. All of the above

16. Walter's model suggests for 100% DP ratio when:
    a. Ke =
    b. Ke < r
    c. Ke > r
    d. Ke = 0

17. If a firm has Ke< r, the Walter's model suggest for:
    a. 0% payout
    b. 100% payout
    c. 50% payout
    d. 25% payout

18. Dividend irrelevance argument of MM model is based on:
    a. Issue of debentures
    b. Issue of Bonus shares
    c. Arbitrage
    d. Hedging

19. Residuals theory argues that dividend is a
    a. Relevant decision
    b. Active decision
    c.]passive decision
    d. Irrelevant decision

20. Which of the following stresses on investor's preference for current dividend that higher future capital gains?
    a. Walter's Model
    b. Residuals Theory
    c. Gordon's Model
    d. MM Model

21. Which of the following represents passive dividend policy?
    a. That dividend is paid as a % of EPS
    b. That dividend is paid as a constant amount
    c. That dividend is paid after retaining profits for reinvestment
    d. All of the above

22. In case of Gordon's model, the MP for zero payout is zero. It means that:
    a. Shares are not traded
    b. Shares available free of cost
    c. Investors are not ready to offer any price
    d. None of the above

23. Gordon's model of dividend relevance is same as:
    a. No-growth model of equity valuation
    b. Constant growth model of equity valuation
    c. Price-earnings ratio
    d. Inverse of price earnings ratio

24. If r= Ke, than MP by Walter's model and Gordon's model for different payout ratios would be:
    a. Unequal
    b. Zero
    c. Equal
    d. Negative

25. Which of the following is not considered in Linter's Model?
    a. Dividend payout ratio
    b. Current EPS
    c. Speed of adjustment
    d. Preceding year EPS

(25x1=25 Marks)

PART- B

Answer all questions

1. Following are the details for three companies A ltd, B ltd and C ltd.

	A ltd	B ltd	C ltd
R	20%	15%	10%
K_e	15%	15%	15%
E	₹.4	₹.4	₹.4

Calculate the value of an equity share using Gordon Model if dividend payout ratio is 75%

(10 marks)

2. Subhadra Ltd had a net profit of ₹. 10,00,000 in the year 2010-11. The company had been following a payout ratio of 0.25. The income has been growing at an annual rate of 6% over past so many years and dividend is linearly related with net income. The year 2011-12 was an abnormal year and the company made a net profit of ₹.15,00,000. This abnormal growth in profit is not expected in coming years.

   a. What should have been the amount of dividend if 2011-12 was a normal year?
   b. What shall be the amount of dividend for year 2011-12 if payout ratio for this year is 40%?
   c. The company follows residual theory of dividend. The investment in the year 2011-12 has been budgeted at ₹.20,00,000. The company wants to maintain its debt equity ratio of 3. What should be the amount of dividend for the year 2011-12?

(10 marks)

3. Beta of equity share of Kartik ltd. Is ₹1.20. The company follows a payout ratio is 40%. The EPS of the year just concluded is ₹.9. return on market portfolio is 15% and risk free rate is 7%. Rate of return on reinvestment of the retained earnings is 20%
   a. Calculate P/E ratio
   b. What is the value per share on account of growth opportunities (i.e. for 'rate of return on reinvestment of the retained earnings' exceeds the 'return expected by equity shareholders')?
   c. What will be the P/E ratio, if the company announces that in future it will follow a payout ratio is 60%?

(10 marks)

4. Sunlight corporation is considering an investment in one of the two mutually exclusive proposals:
   Project A: It requires initial outlay of ₹.1,70,000
   Project B: It requires initial outlay of ₹.1,50,000

The certainty equivalent approach is employed in evaluating risky investments. The current yield on treasury bills is 5% and the company uses this as riskless rate. Expected values of net cash inflows with their respectively certainty-equivalents are:

Year	Project A		Project B	
	Cash Inflows ₹	Certainty equivalent	Cash Inflows ₹	Certainty equivalent
1	90,000	0.8	90,000	0.9
2	1,00,000	0.7	90,000	0.8
3	1,10,000	0.5	1,00,000	0.6

(i) Which project should be acceptable to the company?

(ii) Which project is riskier and why? Explain.

(iii) If the company was to use the risk-adjusted discount rate method, which project would be analysed with higher rate?

(10 marks)

5. A project under evaluation is thought to involve a medium degree of risk. The risk-free discount rate is 4% and the appropriate risk premium is believed to be 6%. The project costing ₹.1,000 has the following estimated NPV and the probabilities of different economic conditions:

Market conditions	NPV at 4%	NPV at 10%	Probability
Good	1,775	1,487	0.10
Average	1,220	989	0.20
Medium	665	492	0.40
Poor	110	-5	0.20
Bad	-445	-503	0.10

Analyze the expected NPV and its variability.

(10 marks)

PRIME ACADEMY

34th SESSION PROGRESS TEST – STRATEGIC FINANCIAL MANAGEMENT

SUGGESTED ANSWERS

PART-A

1	b
2	d
3	d
4	a
5	c
6	b
7	d
8	b
9	c
10	c
11	b
12	c
13	b
14	b
15	a
16	c
17	a
18	c
19	c
20	c
21	c
22	c
23	b
24	c
25	d

PART B

1. A Ltd. $P = \frac{3}{(0.15)-(0.25x0.20)} =$ ₹.30

B Ltd. $P = \frac{3}{(0.15)-(0.25x0.15)} =$ ₹.26.67

C Ltd. $P = \frac{3}{(0.15)-(0.25x0.10)} =$ ₹.24

2.

a) Dividend for the year 2010-2011 (Had 2011-2012 been a normal year)
= 10,00,000 (1.06)(0.25) = ₹.2,65,000 (including of CDT)

b) Dividend for year 2011-2012 = 15,00,000 x 0.40 = ₹.6,00,000
(including of CDT)

c) Budgeted investment for year 2011-2012 = ₹.20,00,000.
This will be financed through debt of ₹.15,00,000 and retained profit of ₹.5,00,000.

Total Distribution Dividend ₹.10,00,000 subject to CDT.

Dividend = ₹.10,00,000 x 100/115 = ₹.8,69,565

CDT = ₹.1,30,435

3.

a) g = b.r = 0.60 x 0.20 = 0.12

Expected EPS = 9(1.12) = 16.60

Ke = 7 + 1.20(15-7) = 16.60

$$P = \frac{D_1}{Ke-g} = \frac{10.08x0.40}{0.166-0.12} = ₹.87.65$$

PE ratio = 87.65 / 10.08 = 8.70

b) Had r = Ke = 0.1666 : g = 0.60 x 0.166 = 0.0996

$$P = \frac{D_1}{Ke-g} = \frac{9(1.0996)x0.40}{0.166-0.0996} = \frac{3.95856}{0.0664} = ₹.59.62$$

Value per share on account of growth opportunities = 87.65 – 59.62 = ₹.28.03

c) g = b.r = 0.40 x 0.20 = 0.08

Expected EPS = 9(1.08) = 9.72

Ke = 7 + 1.20(15-7) = 16.60

$$P = \frac{D_1}{Ke - g} = \frac{9.72x0.60}{0.166 - 0.08} = ₹.66.27$$

PE ratio = 66.27 / 9.72 = 6.8

4. Determination of NPV of project A:

Year	Cash inflows ₹	Certainty equivalent	Adjusted cash inflows ₹	$PVF_{(5,n)}$	Total PV ₹
1	90,000	0.8	72,000	0.952	68,544
2	1,00,000	0.7	70,000	0.907	63,490
3	1,10,000	0.5	55,000	0.864	47,520
					1,79,554

NV = ₹. 1,79,554 - 1,70,000 = ₹. 9,554

Determination of NPV of project B:

Year	Cash inflows ₹	Certainty equivalent	Adjusted cash inflows ₹	$PVF_{(5,n)}$	Total PV ₹
1	90,000	0.9	81,000	0.952	77,112
2	90,000	0.8	72,000	0.907	65,304
3	1,00,000	0.6	60,000	0.864	51,840
					1,94,256

NPV = ₹. 1,94,256 – 1,50,000 = ₹.44,256

Decision:

(i) Project B should be acceptable as its NPV is greater
(ii) Project A is riskier because its certainty equivalent are lower
(iii) Project A being more risky, it would be analysed with higher discount rate.

5. Calculation of expected NPV and standard deviation at discount rate of 4%

Market conditions	Prob	NPV ₹	Exp.NPV	Prob x (NPV – ENPV)^2 ₹
Good	0.10	1,775	177.5	$(1,775-665)^2$ x 0.10 =1,23,210
Average	0.20	1,220	244.0	$(1,220-665)^2$ x 0.20 = 61,605
Medium	0.40	665	266.0	$(665-665)^2$ x 0.40 = 0
Poor	0.20	110	22.0	$(110-665)^2$ x 0.20 = 61,605
Bad	0.10	-445	-44.5	$(-445-665)^2$ x 0.10 = 1,23,210
				3,69,630

The expected NPV of the project is ₹.665 and the the standard deviation is $(3,69,630)^{1/2}$ =₹. 608

Calculation of expected NPV and standard deviation at discount rate of 4%+6% =10%

Market conditions	Prob	NPV ₹	Exp.NPV	Prob x (NPV – ENPV)^2 ₹
Good	0.10	1,487	148.7	$(1,487-492)^2$ x 0.10 = 99,002
Average	0.20	989	197.8	$(989-492)^2$ x 0.20 = 49,402
Medium	0.40	492	196.8	$(492-492)^2$ x 0.40 = 0
Poor	0.20	-5	-1.0	$(-5-492)^2$ x 0.20 = 49,402
Bad	0.10	-503	-50.3	$(-503-492)^2$ x 0.10 = 99,002
				2,96,808

The expected NPV of the project is ₹.492 and the standard deviation is $(2,96,808)^{1/2}$ =₹. 545

PRIME ACADEMY

34th SESSION PROGRESS TEST – ADVANCED AUDITING

No of pages: 5 Total Marks: 75

Time Allowed: 2 hrs

PART-A

1. To which of the following companies CARO 2003 does not apply.
    a. Foreign Company
    b. Public Company
    c. Companies licensed to operate u/s 25 of the companies act, 1956
    d. A Company with aggregate of paid up capital and reserves of `₹ 55 Lakhs

2. Which of the following matters are not reported by an auditor in his audit report under CARO 2003?
    a. Substantial changes in the share holding pattern
    b. Whether company is regular in depositing undisputed statutory dues
    c. Whether particulars of contracts referred u/s 301 of Companies Act,1956 have been entered in the register to be maintained under the said section
    d. Whether or not adequate security or charge has been created in respect of debentures issued.

3. *XYZ Co Ltd* has sold during the year 35% of its fixed assets used for production. As an auditor which of the following is the best way to substantiate the going concern of the company.
    a. Exercise judgment whether 35% constitutes substantial portion and ensure whether it has affected the going concern.
    b. Obtain representation from management to such an effect
    c. Both a & b
    d. None of the above

4. Which of the following type of modified audit report does not affect the auditor's opinion on true and fairness of the financial statement?
    a. An audit report with qualified opinion
    b. An audit report with disclaimer of opinion
    c. An audit report with adverse opinion
    d. An audit report with emphasis of matter paragraph

5. Under which of the following circumstances a qualified audit report is not obligatory
    a. If the information required by law is not furnished
    b. There exists significant uncertainty, other than going concern, the resolution of which is dependent upon future events which may affect financial statements
    c. If there is a contravention of the provision of companies act having a bearing on the accounts and transactions of the company
    d. If proper books of accounts has not been kept by the company in accordance with law

6. Under which of the following circumstance a person can be appointed as a statutory auditor of a company
    a. Where such person holds a very near relationship with managing or whole time director
    b. Where such person is already appointed as an Internal Auditor of the company

c. Where the person indebted to the company for an amount of ₹ 4900/-
d. Where such person provides services in relation to valuation of shares.

7. A company before appointing the statutory auditors of the company should:
   a. Ensure that audit fees has been fixed
   b. Ensure that the scope and terms of engagement have been mutually agreed
   c. Obtain a certificate to the effect that appointment will be within the statutory limits
   d. None of the above

8. A partnership firm XY & Co has two partners X & Y and the firm already holds audit of 43 companies of which 2 are Joint audits, 2 are audit of section 25 companies and 3 of foreign companies. How many more audit of public companies the firm can take assuming all such public companies have paid up capital of less than `₹ 25 Lacs
   a. 4
   b. 0
   c. 2
   d. 3

9. Under which of the following circumstance the Board of Directors of the company are not entitled fill up a casual vacancy.
   a. Dissolution of the partnership firm which was appointed as the statutory auditor of the company
   b. Where the person appointed ceases to be a member of ICAI
   c. Where the person appointed is disqualified to be an auditor u/s 226(3) of the company's act,1956
   d. Where the casual vacancy is on account of resignation of the auditor

10. Which of the following statement is true
    a. Branch auditors of the company can be appointed only by the board of directors
    b. Branch auditors can be appointed only by shareholders in general meeting
    c. Branch auditors can be appointed at general meeting or the board can be authorised to appoint the branch auditor in consultation with statutory auditor
    d. Only statutory auditors can be appointed as branch auditors

11. Which of the following is not a duty of statutory auditor of the company
    a. To provide reasons for qualification in the audit report
    b. To report whether or not he has obtained all information and explanation for the purpose of audit
    c. To certify the statutory report issued to the members u/s 165 of companies act, 1956
    d. To circulate the audit report and financial statements to the members of the company.

12. Tenure of office of an auditor refers to
    a. The period between AGM of his appointment and to the conclusion of next AGM
    b. The financial year for which he is appointed as an auditor
    c. The period as determined by the shareholder in general meeting
    d. None of the above

13. As per SA 230 what is the minimum period for retention of audit documentation
    a. 8 years from the date of auditor's report
    b. 8 years from the end of financial year

c. 10 years from the end of financial year
d. 10 years from the date of auditor's report

14. In cases where there is a disagreement between the Joint Auditors of the company then
    a. Joint auditor who has different opinion can report separately and other joint auditors can report jointly
    b. The rule of majority prevails
    c. Each of the Joint auditors should report separately
    d. None of the above

15. PQR Mining Limited is engaged in extraction of copper ore and production of copper. The auditor of the company has assessed the risk of material misstatement in inventory and ore extracting assets, which in his judgment requires special audit considerations. Such risk is called as
    a. Audit Risk
    b. Inherent Risk
    c. Assessed Risk
    d. Significant Risk

16. Which of the statement is false: The concept of materiality is applied by the auditor
    a. In planning and performing the audit
    b. In evaluating the effectiveness and appropriateness of Internal Controls
    c. In evaluating the effect of identified misstatements and of uncorrected misstatements
    d. In forming an opinion in the Auditors Report.

17. A third party consignee provides an external confirmation of the goods held on consignment. Which of the following assertions are not provided by such external confirmation
    a. Valuation
    b. Existence
    c. Rights & Obligation
    d. All of the above

18. An accounting estimate is
    a. An amount selected by the management for recognition or disclosure in the financial statements
    b. An amount or range of amount, derived from audit evidence for use in evaluating management point estimation
    c. An approximation of a monetary amount in the absence of precise means of measurement
    d. None of the above

19. Which of the following risks are reduced by Test of Controls and Analytical Procedures
    a. Audit Risk
    b. Control Risk
    c. Detection Risk
    d. Inherent Risk

20. An audit which is aimed at determining whether or not corporate plans have been effectively executed and deals with utilization of resources in an economic and productive manner is called as
    a. Operations Audit
    b. Efficiency Audit
    c. Management Audit
    d. Compliance Audit

21. During an audit engagement an auditor performs detailed analysis on controls of computerized financial application that affect financial statements and included the same in working papers. The working papers are considered to be
    a. A client owned records of conclusions reached by the auditors who perform the audit
    b. Evidence supporting the financial statements
    c. Support for the auditors representation as to compliance with generally accepted auditing standards
    d. A record to be used as a basis for next year's engagement

22. Which of the following is not true: Requirements of an auditor as per SA 620 are
    a. Auditor can seek audit evidence from an expert independently
    b. Where the experts opinion is inconsistent with provision of law, then auditor should deal with it accordingly by discussing with client or expert
    c. Auditor should ensure that experts opinion is prima facie dependable before relying on the same
    d. The auditor should refer to the work of an expert in his unqualified report.

23. Non disclosure of information to a third party without specific authority or legal or professional necessity is called as
    a. Confidentiality
    b. Integrity
    c. Objectivity
    d. All of the above

24. A written representation of the accuracy of facts stated therein without any estimates is called as an
    a. Audit report
    b. Audit certificate
    c. Statement of Facts
    d. Management representation letter

25. On which of the following items an auditor is not required to make an enquiry under section 227(1A) of the companies act
    a. Where an asset has been sold at a price lesser than its cost on which a charge has been created
    b. Whether loans and advances have been properly secured
    c. Transactions which are represented merely by book entries are nor prejudicial to the interest of the company
    d. Personal expenses, if any, has been charged to revenue account

(25x1=25 Marks)

PART-B

I. Answer the following in brief:

1. Explain any three features of a Qualified Audit Report?
2. Loser Ltd has taken a term loan from a nationalised bank in 2006 for ₹ 200 Lakhs repayable in five equal annual instalments of `₹ 40 Lakhs from 31st March 2007 onwards. It had repaid the loans due in 2007 & 2008 but defaulted in 2009, 2010, & 2011. As the auditor of the company what is your responsibility assuming that company has sought reschedulement of loan?
3. Mr. Suresh is appointed as the auditor of Chennai Travels Limited with audit fees of `₹. 50,000/-. He purchased Air-ticket from Chennai to Delhi and back for `.₹ 12,000/- from the client for his personal work and the amount remains unpaid as at the end of the year as it is a general practice of the client to give credit to all. Mr. Suresh claims that he does not incur any disqualification as contained in section 226(3)(d) of the companies act. How would you deal with the above situation?
4. As an auditor of a company what are the procedures to be followed with respect to Direct Confirmation from Debtors?
5. Write a short note on sampling risk? (5x3=15 Marks)

II. Explain the following

1. Director of T Ltd draws an advance of US$ 200 per day in connection with the foreign trip undertaken on behalf of the company. On his return he files a declaration stating that entire advance was expended without any supporting evidence. T Ltd books the entire expense on the basis of such declaration. As the auditor of T Ltd how do you deal with this
2. You have been reappointed as a sole auditor of a company where you were one of the joint auditors in the immediately preceding year. The concerned joint auditor has not been re-appointed. What are the various steps you would take to ascertain the compliance of the requirements of the Companies Act, 1956 before accepting the audit?
3. What are the difficulties encountered in the course of management audit?
4. Explain what is meant by written representation and indicate to what extent an auditor can place reliance on such representation?
5. Write short notes on objective of operational auditing? (5x5=25 Marks)

III. Explain in detail

1. Briefly describe the auditor's responsibility regarding subsequent events as per SA 560?

(10x1=10 Marks)

PRIME ACADEMY

34th SESSION PROGRESS TEST – ADVANCED AUDITING

SUGGESTED ANSWERS

PART-A

1	C	18	C
2	A	19	C
3	A	20	B
4	D	21	C
5	B	22	D
6	D	23	A
7	C	24	B
8	B	25	A
9	D		
10	C		
11	D		
12	A		
13	D		
14	A		
15	D		
16	B		
17	A		

PART-B

I.

1.

a. Clarity: The auditor must express the nature of qualification, in a clear and unambiguous manner

b. Explanation: Where the auditor answers any of the statutory affirmation in the negative or with a qualification his report shall states the reasons of such answer

c. Placement: All qualifications should be contained in the auditors report. When there are notes which are subject matter of qualification, the same should preferably be annexed to the auditors report. However a reference to the notes to accounts in the auditors report does not automatically become a qualification

d. Subject To: the words 'Subject To' are essential to state any qualification. The qualification should be preceded by the words such as subject to or 'except that' to make it clear that he is making an exception

e. Quantification: It is also necessary that the auditor should quantify, wherever possible, the effect of individual as well as total effect of all qualifications in profit or loss and/or state of affairs of these qualifications in the financial statements in a clear and unambiguous manner. In circumstance where it is not possible to quantify the effect of qualifications accurately the auditor may do so on the estimates made by the management after carrying out such audit tests as are possible to clearly indicate that the figures given are based on the estimates of the management

f. Nature of qualification: Vague statements the effect of which on accounts cannot be ascertained like 'the debtors balance are subject to confirmation', 'no provision for taxation has been made in view of the loss during the year' etc., should be avoided.

g. Violation of Law: Where the company has committed an irregularity resulting in a breach of law, the auditor should bring the same to the notice of the shareholders by properly qualifying his report

h. Notes: Report relationship**-** Where notes of a qualificatory nature appear in the accounts the auditors should state all qualifications independently in their report so that user can access the significance of the qualifications

i. Draft Report: The auditor may discuss the matters of qualifications with the management of the company to acquire their views. It is not necessary that auditor should accept the management's views and modify his opinion. But it would enable the auditor to accurately draft the qualification in his report.

2. As per Para 4 (xi) of CARO, 2003 the auditors of the company has to state in his report that whether the company has defaulted in repayment of its dues to financial institutions or banks or debenture holders and if yes the period and amount of default to be reported

   In this case Loser Ltd has defaulted in repayment of dues for three years. Application for rescheduling will not change the default position. Hence the auditor has to report in his audit report that the company has defaulted in its repayment of dues to the bank to the extent of ₹ 120 Lakhs

3. A question of indebtedness may 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 ₹. 1,000/-, irrespective of the nature of the purchase or period of credit allowed to other customers, the provision concerning disqualification of auditor as contained in section 226(3)(d) will be attracted. This is applicable for 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 as at the end of the year exceeds ₹. 1,000/- . Therefore that the contention of Mr. Suresh that he does not incur disqualification is not correct as he has purchased a ticket of ₹. 12,000/-. The provision concerning disqualifications of auditor as contained in section 226(3)(d) will be attracted

4.

a. Based on the relevant factors, the auditor should determine the following –
   - Confirmation date: Either Balance Sheet date or any other reasonably close date
   - Form of requesting confirmation – Either positive or negative request
   - Debtors from whom the balance confirmation has to be obtained

b. The auditor should maintain strict control to ensure correctness and proper dispatch of letters, confirmations as well as any undelivered letters should be returned

c. When management requests the auditor not to seek any confirmation from certain debtors, the auditor should examine available evidence to support managements justification and explanation. In such case alternative procedures should be applied

d. Where necessary, the auditor may request the entity to follow up with those debtors from whom responses have not been received, In exceptional cases, the auditor may correspond directly with significant debtors

e. If responses received are inadequate, the auditor should increase the examination of the records and analytical procedures, than planned originally

f. Discrepancies revealed based on balance confirmation should be investigated and reconciled. Satisfactory explanations should be obtained to ensure the correctness of the amount of debtors.

5. As per SA 530 "Audit Sampling" The risk that the auditors conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. Sampling risk can lead to two types of erroneous conclusions

a. In the case of test of controls, that controls are more effective than they actually are, or in the case of a test of details, that a material misstatement does not exist when in fact it does. The auditor is primarily is concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion

b. In case of test of controls, that controls are less effective than they actually are, or in the case of test of details, that a material misstatement exists when in fact it does not. This type of erroneous conclusion affects the audit efficiency as it would lead to additional work to establish that initial conclusions were incorrect.

II.

1. SA 500 " Audit Evidence states that an auditor should obtain sufficient appropriate audit evidence to be able to draw reasonable conclusion on which to base his option

   Section 227(1A)(e) of the Companies Act, 1956 requires an auditor to report when personal expenses have been charged to revenue account

   In the context of the facts of the case, ascertain whether the payment made by the company for the foreign trip form an "allowance" or "reimbursement". An allowance is a fixed sum of money allowed or the basis of specified criteria. No evidence supporting the expenditure is required for payment of allowance to the director. On the other hand, if the pay is reimbursement then it should be against actual expenditure.

   The director concerned should provide proof of expenditure. Since the director has given only a declaration, the auditor should ascertain other relevant facts as to whether the advance paid is pursuant to the policy of the company which is based on approximate estimation of the expenditure normally incurred by a person of the status of a director and the same is applicable to persons of a similar status within the company. If the auditor considers the advance taken is reasonable then the declaration can be considered adequate, otherwise he may have to call for additional documentary evidence.

2. When one of the joint auditors of the previous year is appointed as the sole auditor for the next year, it is similar to new re-appointment of one of the retiring joint auditors. The provision of section 225 of the companies act, 1956 relating to non-reappointment of the other person also need to be considered. The following points should be taken into account

   a. Special notice u/s 225(1) was duly received by the company from a member at least 14 days before AGM containing a proposal for appointing a sole auditor expressly
   b. Verify notice to all the members at least 7 days before the AGM [u/s 190(2)]
   c. Verify that the special notice has been sent to the retiring auditor forthwith [u/s 225(2)]
   d. Any representation received from the retiring auditor was sent to the members [u/s 225(3)]
   e. Verify from the minutes whether the representation received from the retiring joint auditor was considered at the AGM
   f. Examine whether the proposed resolution was properly passed
   g. Ensure that provision of section 224(2) are complied fully

h. Ascertain special resolution u/s 224A, if any, is passed accordingly

i. Obtain certified copy of the relevant minutes of AGM and a written communication of appointment within 7 days.

3.

a. Resistance to change: People working in the organization are amenable to change, but at the time of actual implementation they come up with stiff resistance to proposals
b. Fear of shuffling or adverse actions: There is an inherent fear in the executives, that management auditors recommendations may lead to their removal or re-shuffling
c. Perception of auditee: There is a general image that management auditor is a criti, fault finder or private spy9ing authority of the top management
d. Expertise of the auditor: When management auditor performs comprehensive audit operations, they cannot be well informed about such operations. Any suggestions made by them may not be accepted or if forcibly implemented, attempts are likely to be made to make them failure
e. Line-staff conflict: The line-staff relationship has inherent conflicting tendency. Management auditors being specialist in their field, may think that their approach and solutions are the only answers, They must pinpoint all defects to prove themselves to top management
f. Control aspect: People are generally reluctant to accept external control mechanism like management audit. This arises due to factors like
    i. Fear of criticism stemming from adverse audit findings
    ii. Fear of changes in day0to-day working habits due to changes resulting from audit recommendation
    iii. Punitive action by supervisors prompted by reporting deficiencies.
g. Insensitive audit practices: Reports that are overly critical, or which focuses on deficiencies only, the air of mystery cloaking some audits and the perception that auditors gain personally from reporting deficiencies- all these reasons contribute to cold war between auditor and auditee

4. A written statement by management provided to the auditor to confirm certain matters or to support other audit evidence. Written representations in this context do not include financial statements, the assertions therein, or supporting books and records

Audit evidence is all the information used by an auditor in arriving at the conclusion on which the audit opinion is based. Thus written representation are necessary information that the auditor requires in connection with the audit of the entity's financial statements. Accordingly, similar to responses to inquiries, written representation are audit evidence. Although written representation provides necessary audit evidence, they do not provide sufficient appropriate audit evidence on their own about any of the matters with which they deal. Furthermore, the fact that management has provided reliable written representations does not affect the nature or extent of other audit evidence that the auditor obtains about the fulfillment of managements responsibilities, or about specific assertions.

The auditor shall request the management to provide a written representation that it has fulfilled its responsibility for the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation, as set out in terms of audit engagement. Other SAs require the auditor to request written representations. If, in addition to such required representations, the auditor determines that it is necessary to obtain one or more written representations to support other audit evidence relevant to the financial statements or one or more specific assertions in the financial statements, the auditor shall request such other written representation. The date of representation should be as near as practicable to, but not after, the date of auditors report on the financial statements. The written representation shall be for all financial statements and period(s) referred to in the auditors report.

SA 580 states that if the auditor has concerns about the competence integrity, ethical values or diligence of management, or about its commitment to or enforcement of these, the auditor shall determine the effect that such concerns may have on reliability of presentations and audit evidence in general.

In particular, if written representation are inconsistent with other audit evidence the auditor shall perform audit procedure to attempt to resolve the matter. If the matter remains unresolved, the auditor shall reconsider the assessment of the competence, integrity, ethical values of diligence of management, or of its commitment to or enforcement of these, and shall determine the effect that this may have on the reliability of representations (oral or written) and audit evidence in general. If the auditor concludes that written representation are nor reliable, the auditor shall take appropriate actions, include determining the possible effect on the opinion in the auditors report.

5.

The general objective of operational audit are as follows

a. Appraisal of controls:
    i. Internal control provide the essential tool to ensure proper performance in each functional or organizational area for accomplishing the desired organizational objectives
    ii. The purpose of operational audit is to determine whether the controls are adequate and effective in accomplishing management objective
    iii. The operational auditor reviews internal control and reports to ascertain whether they bring performance, qualitative and quantitative, to the notice of the management, also within the organizations policies and plans are being carried out
b. Evaluation of performance: In the area of performance appraisal, the operational auditor is basically concerned with
    i. Analysing the technical efficiency of the operations
    ii. Accumulating information and evidence to measure the effectiveness, efficiency and economy of operations
    iii. Comparing the actual performance with applicable standards, procedures, rules, policies and plans
    iv. Performance evaluations is generally based on – Productivity, Personnel, workload, cost and quality

c. Appraisal of management objectives and plans
    i. Every act in an organization is the product of basic plans and objectives set by the management, Hence, the management policies and objectives should be evaluated properly
    ii. The aim of operational audit is to appraise operations and controls and adherence to prescribed and laid-down policies and not to go into questions of appropriateness of plans and objectives.

d. Appraisal of organisation structure:
    i. Organisational structure an essential element of internal control design, provides the line of relationships and delegation of authority and tasks.
    ii. The operational auditor should consider the following in evaluating the organizational structure
        1. Conformity with management objectives
        2. Proper match between responsibility and authority
        3. Clear definition of scalar line of authority from top to bottom and
        4. Possibility of defective delegation, overlapping or duplication of work.

III

1. When the auditor draws up his audit plan, checking of subsequent events is an important audit procedure irrespective of the level of test checks employed for the checking of transactions during the year. In fact more detailed check is normally required for subsequent events to confirm certain assertions contained in the financial statements, e.g. the payment made by debtors after the close of accounting period would confirm that outstanding debtors on the date of balance sheet have been realised. SA 560 on "Subsequent Events" establishes standard on the auditors responsibility regarding subsequent events. SA 560 states that the term subsequent events refers to event occurring between the date of the financial statements and the date of the auditors report, and the facts that become known to the auditor after the date of the auditors report. AS 4 deals with all those significant events, both favourable and un favourable , that occur between the balance sheet date and the date on which the financial statements are approved by the board of directors. As per AS 4 two types of events can be identified (a) those which provide further evidence of conditions that existed at the balance sheet date (b) those which are indicative of conditions that arose subsequent to the balance sheet date. SA 560 lays down that auditor should consider the effect of subsequent events on the financial statements and on the auditors report.

   SA 560 further requires that the auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of financial statements and date of audit report that require adjustment of, or disclosure in, the financial statements have been identified. The auditor is not, however, expected to perform additional audit procedures on matters to which previously applied audit procedures have proved satisfactory conclusions.

   The auditor shall take in to account the auditors risk assessment in determining the nature and extent of such audit procedures which shall include the following

a. Obtaining an understanding of any procedures management has established to ensure that subsequent events are identified
b. Inquiring of management and , where appropriate , those charged with governance as to whether any subsequent events have occurred which might affect the financial statements.
c. Reading minutes, if any, of the meetings, of the entity's owners, management and those charged with governance, that have been held after the date of financial statements and inquiring about matters discussed at any such meetings for which minutes are not yet available
d. Reading the entity's latest subsequent interim financial statements, if any

When, as a result of the procedures performed above, the auditor identifies events that require adjustment of, or disclosure in, financial statements, the auditor shall determine whether each such event is appropriately reflected in those financial statements.

PRIME ACADEMY

34TH SESSION PROGRESS TEST – CORPORATE AND ALLIED LAWS

No. of pages – 4

Total Marks – 75
Time allowed – 2 Hours

PART A

1. Following can be a Director of a Company
    a. Individual
    b. Body Corporate
    c. Firm
    d. Association of persons
2. ________name the first Directors of a company
    a. Certificate of incorporation
    b. Articles of Association
    c. Memorandum of Association
    d. General meeting
3. Appointments in case of proportional representation will be made once in every
    a. One year
    b. Two years
    c. Three years
    d. Four years
4. Public companies appointing Small Shareholder as Director must have paid-up capital of ____or more
    a. Two crores
    b. Five crores
    c. Eight crores
    d. Ten crores
5. Small Shareholder means, Shareholder holding shares of nominal value of ₹.______
    a. 10,000
    b. 20,000
    c. 30,000
    d. 25,000
6. ___________company can provide for additional grounds for disqualification of Directors
    a. Public company
    b. Private company
    c. Private subsidiary of Public company
    d. Both a & b
7. _________ Directors need not hold qualification shares
    a. Director appointed by central government
    b. Nominee directors representing financial institution established by separate act of parliament
    c. Small Shareholder director
    d. All of the above
8. The time limit for obtaining qualification shares for directors
    a. One month
    b. Immediately after appointment
    c. Two months

d. No time limit

9. Managerial remuneration includes
   a. Expenditure incurred by company in providing rent free accommodation
   b. Remuneration payable for acting as technical expert
   c. Sitting fees
   d. Attendance fees
10. Compensation for loss of office is not provided when _____
    a. Director resigns due to amalgamation of the company
    b. Voluntary winding up
    c. Compulsory winding up
    d. All of the above
11. In how many companies can a person hold directorship at a time
    a. 10
    b. 15
    c. 20
    d. 5
12. A Company may appoint or re-appoint a manager for a period not exceeding ____at a time
    a. 2 years
    b. 3 years
    c. 4 years
    d. 5 years
13. Can a company appoint at the same time a managing director and a manager
    a. Yes
    b. No
    c. Yes, with the consent of Directors
    d. Yes, with the consent of shareholders
14. __________ means any director whose presence cannot by reason of Sec.300 count for the purpose of forming quorum at a meeting of the Board, at the time of the discussion or vote on any matter
    a. Professional Director
    b. Nominee Director
    c. Interested Director
    d. Independent Director
15. Who shall be paid compensation for loss of office
    a. Managing Director
    b. Whole-time Director
    c. Manager
    d. All of the above
16. Companies having a paid-up capital and free reserves of ₹ .10 crores and above shall pay sitting fees of upto
    a. ₹ .5000
    b. ₹.10,000
    c. ₹.15,000
    d. ₹.20,000
17. Mr .A, Mr. B & Mr. C was appointed as the director of XYZ India Pvt Ltd by passing a single resolution without obtaining the unanimous consent of the meeting. The appointment is valid.
    a. True
    b. False

18. Sec 193 (1) of the Companies Act, 1956 provides that every company shall cause minutes of all proceedings of every meeting of its Board of directors, to be kept by making within ____ of the conclusion of every such meeting concerned
    a. 10 days
    b. 20 days
    c. 30 days
    d. One week
19. The quorum for meeting of the board of directors of a company shall be ___of its total strength
    a. 1/3
    b. 2/3
    c. 2
    d. 100%
20. Board of directors of every company shall meet at least once in every______
    a. Three months
    b. Four months
    c. Six months
    d. One year
21. The Board of directors of a public company are restricted from
    a. investing, otherwise than in. trust securities
    b. borrowing moneys
    c. contributing to charitable and other funds not directly relating to company's business
    d. All of the above
22. Can the remuneration of Directors of Public Company be increased?
    a. Yes
    b. No
23. State in which of the following cases disqualification under Sec274(1)g will not apply
    a. failure to file annual accounts and annual returns for three consecutive financial years
    b. failure to redeem debentures for one year or more
    c. failure to pay interest on debentures for one year or more
    d. fails to repay deposits for one year or more
24. Shareholders shall remove directors of a company by passing
    a. Ordinary resolution
    b. Special resolution
    c. Central government approval
    d. Both a and c
25. Every director who fails to disclose his interest in the prescribed manner shall be punishable with fine which may extend to______
    a. ₹. 5000
    b. ₹. 10,000
    c. ₹. 20,000
    d. ₹ .50,000

(25x1=25 Marks)

PART B

Answer any five questions

1. (a) ABC Ltd. Wishes to appoint an alternate director in place B, who has gone to USA for one year. Advise the procedure to be followed by the company.

   (b) A Public limited company has 10 directors as under:

Non-retiring directors	2
Directors liable to retire by rotation	4
Additional directors	4

   State the number of directors retiring by rotation at the next annual general meeting and the number of directors vacating office. (5+5=10 marks)

2. PQR Ltd. Is a deemed public company. The present strength of the board of Directors of PQR Ltd. Is 12. The Company wishes to increase the strength beyond 12. Advise PQR ltd. The procedure to be followed for increasing the strength of the Board of Directors beyond 12. (10 marks)

3. (a) Surya Ltd. Proposes to appoint X, a relative of one of the directors of the company, as general manager on a monthly remuneration of ₹.30,000

   (b) X was appointed as an additional director in the board meeting held on 15th January 2011 of ABC ltd. and was to hold office until the next annual general meeting of the said company. The next annual general meeting which should have been held on 30th September, 2011could not be held due to circumstances beyond control. The Board desires that X should continue on the Board after 30th September, 2011. Advise the board. (5+5=10 marks)

4. (a) Ajeesh Ltd. having paid-up capital of ₹.50 lakh, entered into a contract with company XYZ ltd., in which director D was holding 20% shares. The director did not disclose his interest at the time of approval of the contract by the Board.

   (b) Rajiv is already a director of 15 companies. He is being appointed as a director of another company, Biju ltd. Explain:
   (i) whether he can accept the new appointment; &
   (ii) if he wishes to accept, explain the procedure that he must adopt? (5+5=10marks)

5. Advise Board of Directors of a public company about their powers in respect of the following proposals explaining the relevant provisions of the companies act, 1956.
   i. Donations of ₹.5,00,000 to a hospital established exclusively for the benefit of employees
   ii. Buy-back of shares of the company for the first time upto 10% of the paid-up equity share capital
   iii. Delegating to the managing director of the company, the power to invest surplus funds of the company in the shares of some companies (10 marks)

6. Ranbir was appointed as the sole selling agent of S ltd. for a period of five years in a general meeting of the company. Exactly after one and half years, S Ltd. was amalgamated with another company A Ltd. Ranbir was not appointed as the sole selling agent of A Ltd. S Ltd. paid Ranbir ₹.6lacs as selling agency commission during the said one and half years. Is Ranbir entitled to any compensation and if yes, what is the quantum? (10 marks)

PRIME ACADEMY

34TH SESSION PROGRESS TEST- CORPORATE AND ALLIED LAWS

SUGGESTED ANSWERS

PART A

1	a	Individual
2	b	Articles of association
3	c	Three years
4	b	Five crores
5	b	20,000
6	b	Private company
7	d	All of the above
8	c	two months
9	a	Expenditure incurred by company in providing rent free accommodation
10	d	All of the above
11	c	20
12	d	5 years
13	b	No
14	c	Interested Director
15	d	All of the above
16	d	20,000
17	B	False
18	c	30 days
19	a	1/3
20	a	three months
21	d	All of the above
22	a	Yes
23	c	failure to pay interest on debentures for one year or more
24	b	special resolution
25	a	5000

PART B

1. (a) The Board of directors of a company may, if so authorised by its articles or by a resolution passed by the company in general meeting, appoint an alternate director, in accordance with sec 313, to act for a director during his absence for a period of not less than three months from the state in which meetings of the board are ordinarily held.
   An alternate director may be appointed as a managing or whole-time director. Therefore, no new office of the director is created by his appointment. Provisions of the act not applicable to the alternate director are as follows:
   (i) Appointment of an alternate director is not considered as an increase in the strength of the Board of directors.
   (ii) Alternate directorship held by a person cannot be counted fir maximum number of directorships, which a person can hold.
   (iii) An alternate director is not required to hold any qualification shares.

Vacation of office of alternate director: An alternate director shall not hold office as such for a period longer than that 'permissible' to the original director in whose place he has been appointed and shall vacate office as and when the original director returns to the state in which meetings of the board are ordinarily held.

(b) Section 255 of the companies act, 1956 provides that links the Articles provides for retirement of all directors at every annual general meeting, not less than two-third of the total number of directors of public company or of a private company which is a subsidiary of a public company, shall retire by rotation, in terms of Sec 256 of the act, one-third of the directors liable to retire by rotation, shall retire at the Annual general meeting of the company. If the number of directors liable to retire by rotation is not three or multiple of three, then the number nearest to one-third shall retire from the office of director.

Above case, 10 directors mentioned in the question, two directors are non-retiring directors and are not liable to retire. The position in regard to the remaining eight is:

Four directors who were appointed as additional directors, shall vacate the office at the AGM because additional directors hold office only upto the date of the next AGM as per sec 260 of the Act. Of the four rotational directors, one director who constitutes nearest to one-third and who have been longest in office is liable to vacate office.

Thus total number of directors vacating the office is five. The retiring director would be eligible for re-appointment if he is otherwise qualified.

2. The following procedure is required to be adopted for increasing the strength of the board of directors beyond 12.

   (i) A board meeting is to be convened to:

      a. Fix date for a general meeting of the company to consider and approve the resolution for increasing the number of director beyond 12
      b. To approve notice for the general meeting and

c. To authorise the company secretary to issue notice for the meeting on behalf of the board

(ii) Notice for the general meeting is to be issued atleast 21 clear days before the date of the meeting.

(iii) If the shares are listed, the concerned stock exchanges have to be informed about the proposed increase in the strength of the directors and copies of the notice convening the general meeting are to be sent to them.

(iv) Hold the general meeting and get the necessary resolution passed which is subject to the approval of the central government. If the articles have to be altered for this purpose, a special resolution has to be passed at the meeting to that effect.

(v) After the meeting, a copy of the proceedings of the general meeting are required to be forwarded to the stock exchanges, along with 6 copies of the memorandum and articles of the company, if altered.

(vi) Within 30 days of passing special resolution, Form no.23 along with a copy of the special resolution and the explanatory statement has to be filed with, the registrar of Companies.

(vii) An application has to be made to the central government in Form no.24 of the companies (central government's) general rules and forms along with the following:

- Copy of the resolution passed at the meeting and a copy of the proceedings of the meeting
- A copy of the general notice published pursuant to Sec 640B of the Companies act
- A copy of the memorandum and articles of association of the company
- A certificate from the company for the due publication of notice
- Evidence of payment of prescribed fee.

3. (a) As per Sec 314, no relative of a director of a company shall hold any office or place of profit carrying a total monthly remuneration of a sum which is not less than ₹.20, 000 except with the prior consent of the company by a special resolution and the approval of the central government.

Therefore, in the present case, Surya Ltd. proposes to appoint X, a relative of one of its directors of the company, as general manager on a monthly remuneration of ₹.30, 000 and this amount exceed the prescribed limit. Surya ltd will have to get the prior consent of the company by convening a general meeting and getting a special resolution passed for the appointment and also get the approval of the central government before appointing X as the general manager.

(b) The Board of directors of a company may appoint additional directors if they are authorised by Articles of Association. Sec 260 of the Act lays down that if the articles of association of a company empower its directors to appoint additional directors, the board may exercise such powers and they shall hold office only upto the date of the next annual general meeting of the company.

In the present case, X will cease to be additional director on 30th September 2011. However, since the company desires that Mr.X should continue on the board, it is suggested that the company calls for a Board meeting on 1st October 2011 and appoint Mr X afresh as an additional director. Mr X will however, continue as additional director until the next AGM

4. (a) Sec 299 requires every director to disclose his direct or indirect interest in any contract entered by the company or proposed to be entered by the company. Disclose required to be made by a director in the Board meeting where the said contract or proposed contract is being first approved or considered. If the Director was not interested at the time the contract was entered he should make such disclosure, in the first board meeting held after he become interested. Every director who fails to disclose his interests in any contractor arrangement shall be punishable with fine upto ₹.5000.

   It is further provided that nothing contained in sec 299 shall apply to contract between two companies where the director of one company or two of them holds or hold not more than 2% of the paid-up share capital of the company.

   (b) No director shall hold office at the same time as director in more than 15 companies. For calculating the limit certain companies are to be excluded as provided in section 278(1)
   Any person holding office as Director in more than 15 companies has to make choice of 15 companies in which he wishes to continue as director. He has to make this choice within 2 months from the commencement of the Companies Act, 2000. No such person shall act as a director in more than 15 companies after the expiry of 2 months from the commencement of Companies (Amendment) Act, 2000.

   In the view of above, it is not possible for Mr. Rajiv to be a director in 19 companies after excluding the companies listed in sec 278. In the absence of information about companies, it is not possible to ascertain the exact number of directorship held by Mr. Rajiv for the purpose of Sec 275.

5. (i) The limit of 5% of average net profits during the last 3 financial years is applicable only to contributions to charitable and other funds not directly relating to the business of the company or the welfare of its employees [Sec 293(1)(e), companies act,1956]. Hence the board is empowered to make the proposed donation to the hospital.

   (ii) Sec 292 has been amended by Companies (Amendment) Act 2001 to facilitate buy back of shares upto 10% of the total paid-up equity capital and free reserves (Sec 292(i)(aa)). Hence Special resolution in general meeting of the company is not required. Hence the proposed buy back of shares is in order provided other conditions laid down on sec 77A are fulfilled.

   (iii) Sec 292 of the Companies Act, 1956 empowers the Board of directors to delegate to The M.D the power to invest in general terms. But sec 372(A) provides that no investment shall be made, unless it is sanctioned by a resolution passed at a meeting of the Board with the consent of all the directors present sec 372 A does not provide for delegation. Hence the proposed delegation of power to invest to The M.D is not in order.

6. Sec 294 A prohibits payment of compensation to the sole selling agent for the loss of his office in the following cases:

a. Where the appointment of the sole selling agent ceases to be valid by virtue of sec 294(2A)
b. Where he resigns his office as a result of reconstruction or amalgamation of the company and is appointed as the sole selling agent of the reconstructed company or the body corporate resulting from the amalgamation.
c. Where he resigns his office otherwise than in the circumstances envisaged in the foregoing clause (ii)
d. Where he has been guilty of fraud or breach of trust in relation to, or of gross negligence in the conduct of his duty as the sole selling agent and
e. Where he has instigated or taken part directly or indirectly in bringing about the termination of the sole selling agency.

In this case, Ranbir has not been appointed as the sole selling agent of A Ltd. none of the other prohibitions also apply. Hence Ranbir would be entitled to compensation.