

SUGGESTED ANSWERS TO

THE QUESTIONS SET AT

CHARTERED ACCOUNTANCY PROFESSIONAL (CAP)-II LEVEL

December 2021 EXAMINATIONS

Group-I

**The Institute of Chartered Accountants of Nepal
(ICAN)**

ICAN Marg, Satdobato, Lalitpur

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Year and month of Publication: 2022 April

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Paper 1: Advanced Accounting

Attempt all questions. Working notes should form part of the answer.

1. X, Y and Z are in partnership sharing profits and losses in the ratio 2:2:1.
Their Balance sheet as on 31. 03. 2078 as follows:

Liabilities	Rs.	Rs.	Assets	Rs.
Capital accounts:			Fixed assets:	
X	375,000		Plant	787,000
Y	280,000		Current assets:	
Z	225,000	880,000	Stock	103,000
General Reserve		188,000	Debtors	156,000
Creditors		216,000	Bank FD	225,000
			Bank Balance	13,000
		1,284,000		1,284,000

X decided to retire with effect from 1.4.2078.

The remaining partners agreed to share profit and losses equally in future.

The following adjustments were agreed to be made upon retirement of X.

- i) Goodwill was to be valued at 1 year purchase of the average profits of the preceding 3 years on the date of retirement.

The average profits of the past 3 years were as follows:

Year ended	Rs.
31.3.2078	330,000 (as per draft account)
31.3.2077	232,000
31.3.2076	220,000

The partners decided not to raise goodwill account in the books.

- ii) The assets were revalued as follows:

Plant to be depreciated by 10%;

Creditors amounting to Rs. 10,000 were omitted to be recorded;

Rs. 6,000 is to be written off from stock;

Provision for doubtful debts to be created @ 5% of the debtors;

Interest accrued on FD amounting to Rs. 9,000 was omitted to be recorded.

The above adjustments were to be made from the profit for the year ended 31.3.2078 before calculation of goodwill.

- iii) X agreed to take over the bank FD including interest accrued thereon in part payment of his dues and the balance would remain as a loan, carrying interest of 8% p.a.
- iv) Y and Z agreed to bring in sufficient cash to make their capital proportionate and maintain a bank balance of Rs. 150,000.

Required:

- a) Prepare Capital accounts of partners as on 1.4.2078 giving effect to the above adjustments.
- b) Prepare Balance Sheet as on 1.4.2078 after X's retirement.

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Answer

1)

Partners' Capital Accounts as on 1.4.2078

Particulars	X	Y	Z	Particulars	X	Y	Z
To X		22,950	68,850	By Balance b/d	3,75,000	2,80,000	2,25,000
To Revaluation Loss	37,400	37,400	18,700	By General Reserves	75,200	75,200	37,600
To Bank FD	2,34,000			By Y and Z	91,800		
To 8% Loan	2,70,600			By Cash (Bal. fig.)	-	8,600	1,28,400
To Balance c/d*		3,03,450	3,03,450				
	5,42,000	3,63,800	3,91,000		5,42,000	3,63,800	3,91,000

Balance Sheet as on 1.4.2078 after X's Retirement

Equity & Liabilities	Rs.	Assets	Rs.
X's Loan	2,70,600	Plant (90% of Rs. 7,87,000)	7,08,300
Creditors (2,16,000+10,000)	2,26,000	Stock (Rs. 1,03,000-Rs. 6,000)	97,000
Capital Accounts*: (bal. fig.)		Debtors (95% of Rs. 1,56,000)	1,48,200
Y	3,03,450	Bank Balance	1,50,000
Z	3,03,450		
	11,03,500		11,03,500

* Total of capital balance should be Rs. 6,06,900 which is proportioned to individual partners in their profit sharing ratio.

Working Notes:**1. Profit/Loss on revaluation****Revaluation Account**

	Rs.		Rs.
To Plant	78,700	By Interest on FD	9,000
To Creditors	10,000	By Loss on revaluation	93,500
To Inventory	6,000		
To Provision for doubtful debts	7,800		
	1,02,500		1,02,500

2. Calculation of Goodwill**Goodwill Valuation**

Profit of year ended	Rs.
31.3.2078 (Rs. 3,30,000-Rs. 93,500)	2,36,500
31.3.2077	2,32,000
31.3.2076	2,20,000
	6,88,500

Average Profit = $6,88,500/3 = 2,29,500$

Goodwill valued at 1 year purchase amounting Rs. 2,29,500

3. Adjustment for goodwill among partners

X's share of goodwill $(2,29,500 \times 2/5) = 91,800$

Gaining ratio of Y and Z

$Y = 1/2 - 2/5 = (5-4)/10 = 1/10$

$Z = 1/2 - 1/5 = (5-2)/10 = 3/10$

Gaining ratio = 1:3

Entry for adjustment of goodwill

		Rs.	Rs.
Y's Capital A/c	Dr.	22,950	
Z 's Capital A/c	Dr.	68,850	
To X's Capital A/c (Being X's share of goodwill debited to remaining partners in their gaining ratio)			91,800

2.

- a) National Bank Ltd. has the following capital, assets and additional information as on 31st Ashadh 2078.

Capital	Rs. (in million)
Paid up equity share capital	10,315
Statutory general reserve	2,038
Retained earnings	798
Other free reserves	309
Subordinated term debt	1,000
General loan loss provision	1,249
Investment adjustment reserve	118
Deduction from Capital	426
Assets:	Net Value Rs. million
Cash Balance	3,488
Balance with NRB	7,554
Investment with Government securities	14,335
Claims on Government of Nepal	529
Balance with other banks	6,776
Loans to customers	94,936
Other assets	8,670
Off-balance sheet exposures	
Forward exchange contract	4,434
Letter of credit	7,002
Bid Bond and Performance Bond	15,646

The following other information is provided:

- Risk weighted exposure for operational risk 5,266
- Risk weighted exposure for market risk 268
- NRB has directed to add risk weighted exposure at 3% of immediate previous gross income (audited) as capital charge for weak management of operational risk i.e. Rs. 1,436.
- Similarly, the bank is also directed to allocate risk weighted exposure to 3% for unsatisfactory overall risk management policies and procedures of the bank which is calculated at Rs. 3,840.

Required: Compute Risk weighted exposures, Tier 1 and Total Capital Adequacy Ratio of National Bank Ltd. **10**

- b) Mr. Ram Shrestha commenced a contract on Shrawan 1, 2068. The price agreed for the contract, was Rs. 500,000. At the end of FY 2068-69, the contract was in advanced stage of completion and it was decided to arrive at the notional profit on the basis of the total contract. The contract is expected to be completed by the Poush end 2069. Actual expenditure for the Financial Year 2068-69 and estimated expenditure for FY 2069-70 are given below:

Expenses	Actual till Ashadh 31, 2069	Estimated for FY 2069/70 up to Poush end 2069
Materials	140,000	40,000
Labour	80,000	20,000
Plant purchased (at original cost)	40,000	-
Mis. Expenses	25,000	4,000
Plant returned on stores on Ashadh 31, 2068 (at original cost)	10,000	-
Plant returned on stores on Poush 30, 2069 (at original cost)	-	20,000
Materials at site	5,000	-
Work Certified	450,000	500,000
Work uncertified	10,000	-
Cash Received	360,000	500,000

The plant is subject to annual depreciation at 20% on SLM basis.

Required:

Prepare the contract account for the year ended Ashadh 31, 2069.

Working should be part of your answer. **10**

Answer

2 a) i) **Computation of Capital:**

Capital	Rs. (in million)
Paid up equity share capital	10,315
Statutory general reserve	2,038
Retained earnings	798
Other free reserves	309
Deduction from Capital	(426)
Tier 1 Capital	13,034
Subordinated term debt	1,000
General loan loss provision	1,249
Investment adjustment reserve	118
Tier 2 Capital	2,367
Total Capital	15,401

ii) **Computation of risk weighted exposures for credit risks:**

Assets	Net Value	Risk Weight	RWE
Cash Balance	3,488	0%	0

Balance with NRB	7,554	0%	0
Investment with Government securities	14,335	0%	0
Claims on Government of Nepal	529	0%	0
Balance with other banks	6,776	20%	1,355.2
Loans to customers	94,936	100%	9,4936
Other assets	8,670	100%	8,670
Off-balance sheet exposures			
Forward exchange contract	4,434	10%	443.4
Letter of credit	7,002	20%	1,400.4
Bid Bond and Performance Bond	15,646	50%	7,823
Total RWE for credit risks			114,628

iii) **Computation of Total Risk Weighted Exposures:**

Risk Weighted Exposures	Rs. In million
Risk Weighted Exposure for Credit Risk	114,628.00
Risk Weighted Exposure for Operational Risk	5,266
Risk Weighted Exposure for Market Risk	268
Total Risk Weighted Exposures (Before adj. of Pillar II)	120,162
Adjustments under Pillar II	
RWE for operational Risk	1,436.00
RWE for overall risk management	3,840.00
Total Risk Weighted Exposures (After adj. of Pillar II)	125,438

iv) **Computation of Capital Adequacy Ratio**

Tier 1 Capital	13,034.00
Tier 2 Capital	2,367.00
Total Capital	15,401.00
Total Risk Weighted Exposures	125,438
Tier 1 to Risk Weighted Exposure Ratios	10.39%
Total Capital to Risk Weighted Exposure Ratio	12.28%

2 b)

In the books of Ram Shrestha

Contract Account

For the year ended Ashadh 31, 2069

Particulars	Amount	Particulars	Amount
To Materials	140,000	By Plant returned to stores (WN 3)	8,000
To Labour	80,000	By Work in progress:	
To Plant	40,000	Plant at site (WN 4)	24,000
To Mis. Expenses	25,000	Materials at site	5,000
To Profit & Loss a/c (WN2)	129,600	Work certified	450,000
To Work in progress balance c/d	82,400	Work uncertified	10,000
	497,000		497,000
To Work in progress balance b/d	489,000	By Work in progress balance b/d	82,400

Working Notes:

1.

Memorandum Contract Account
For 6 months ended Poush 30, 2069

Particulars	Amount	Particulars	Amount
To Materials	180,000	By Plant returned to stores (WN 3 & 5)	22,000
To Labour	100,000	By Plant at site (WN 6)	7,000
To Plant	40,000	By Contractee's A/c	500,000
To Mis. Expenses	29,000		
To Estimated Profit	180,000		
	529,000		529,000

2. Profit on contract to be taken to statement of profit or loss for the year ending Ashadh 31, 2069

Profit = Estimated profit * cash received/total contract price

$$180,000 * 360,000 / 500,000 = 129,600$$

3. Plant returned to stores on Ashadh 31, 2069

Original cost

10,000

Less: Depreciation @20% for whole year

2000

8000

4. Calculation of plant at site on Ashadh 31, 2069

Original cost

40,000

Less: plant returned

10000

Balance

30000

Less: Depreciation @20% * 30000

6000

Balance

24,000

5. Calculation of plant returned on poush 30, 2069

Original cost

20,000

Less: Depreciation @20% for 18 months

6000

Balance

14,000

6. Calculation of plant at site on poush 30, 2069

Original cost

10,000

Less: Depreciation @20% for 18 months

3000

Balance

7,000

3.

- a) The Receipts and Payments account of Youth Club prepared on 31st Ashadh, 2078 is as follows:

Receipts and Payments Account

Dr.				Cr.
Receipts		Amount Rs	Payments	Amount Rs.
To Balance b/d		450	By Expenses (including payment for sports material Rs 2,700)	6,300
To Annual income from subscription	4,590		By Loss on sale of furniture (cost price Rs. 450)	180
Add: Outstanding of last year received this year	180		By Balance c/d	90,450
Less: Prepaid of last year	4,770	4,680		
To Other fees	(90)	1,800		
To Donation for building		90,000		
		96,930		96,930

Additional information:

Youth club had balances as on 1.4.2077:

Furniture Rs 1,800; investment at 5%` Rs 27,000; Sports material Rs 6,660;

Balance as on 31.3.2078;

Subscription receivable Rs 270; Subscription received in advance Rs 90;

Stock of sports material Rs 1,800

Required:

Do you agree with above receipts and payments account? If not, prepare correct receipts and payments account and income and expenditure account for the year ended 31st Ashadh, 2078 and balance sheet as on that date.

10

- b) A company made a public issue of 200,000 equity shares of Rs. 10 each at a premium of Rs. 2 per share. The entire issue was underwritten by the underwriters L, M, N and O in the ratio of 4:3:2:1 respectively with the provision of firm underwriting of 5,000, 4,000, 2,000 and 2,000 shares respectively.

The company received application for 150,000 shares (excluding firm underwriting) from public, out of which applications for 55,000, 40,000, 42,000 and 8,000 shares were marked in favour of L, M, N and O respectively.

Required:

Calculate the liability of each underwriter as regards the number of shares to be taken up assuming that the benefit of firm underwriting is not given to the individual underwriter.

5

Answer

3 a)

Corrected Receipts and Payments Account of Youth**Club for the year ended 31st Ashadh, 2078**

Receipts		Amount	Payments	Amount
	Rs	R s		R s
To Balance b/d		450	By Expenses (Rs 6,300-Rs 2,700)	3,600
To Subscription Annual income	4,590		By Sports material	2,700
Less: receivable as on 31.3.2078	(270)		By Balance c/d (cash in hand and at bank)	90,720
Add: Advance received for the year 2078-2079	90			
Add: Receivable as on 31.3.2077	180			
Less: Advance received as on 31.3.2077	(90)	4,500		
To Other fees		1,800		
To Donation for building		90,000		
To Sale of furniture		270		
		97,020		97,020

Income and Expenditure Account of Youth club**for the year ended 31st Ashadh 2078**

Expenditure		Amount	Income	Amount
To Sundry expenses		3,600	By Subscription	4,590
To Sports material Balance as on 1.4.2077	6,660		By Other fees	1,800
Add: Purchases	2,700		By Interest on investment (5% on Rs 27,000)	1,350
Less: Balance as on 31.3.2078	(1,800)	7,560	By Deficit: Excess of expenditure over income	3,600
To Loss on sale of furniture		180		11,340
		11,340		

Balance sheet of Youth club as on 31st Ashadh 2078

Equity & Liabilities		Amount (Rs)	Assets		Amount (Rs)
Capital fund	36,000		Furniture	1,800	
Less: Excess of expenditure	(3,600)	32,400	Less: Sold	(450)	1,350
			5% Investment		27,000

over income			Interest accrued on investment		1,350
Building fund		90,000	Sports material		1,800
Subscription received in advance		<u>90</u>	Subscription receivable		270
		<u>1,22,490</u>	Cash in hand and at bank		<u>90,720</u>
					<u>1,22,490</u>

Working Notes:

Balance Sheet of Youth Club as on 1st Shrawan 2077

Liabilities	Amount	Assets	Amount
	Rs		Rs
Subscription received in advance	90	Furniture	1,800
Capital Fund (balancing figure)	36,000	Investment	27,000
		Sports material	6,660
		Subscription receivable	180
		Cash in hand and at bank	<u>450</u>
	<u>36,090</u>		<u>36,090</u>

3 b)

Particulars	No. of shares				
	L	M	N	O	Total
Gross underwriting	80,000	60,000	40,000	20,000	2,00,000
Less: Marked Application (excluding firm underwriting)	(55,000)	(40,000)	(42,000)	(8,000)	(1,45,000)
Balance	25,000	20,000	(2,000)	12,000	55,000
Less: Surplus of N allotted to L, M & O in the ratio of 4:3:1	(1,000)	(750)	2,000	(250)	-
Balance	24,000	19,250	-	11,750	55,000
Less: Unmarked application including firm underwriting (WN)	(7,200)	(5,400)	(3,600)	(1,800)	(18,000)
Net Liability	16,800	13,850	(3,600)	9,950	37,000
Less: Surplus of N allotted to L, M & O in the ratio of 4:3:1	(1,800)	(1,350)	3,600	(450)	-
Balance	15,000	12,500	-	9,500	37,000
Add: Firm Underwriting	5,000	4,000	2,000	2,000	13,000
Total Liability	20,000	16,500	2,000	11,500	50,000

Working Note:

Particulars	No. of shares
Application received from public	1,50,000
Add: Firm underwriting	<u>13,000</u>
Total Applications	1,63,000
Less: Marked application	<u>(1,45,000)</u>
Unmarked application including firm underwriting	18,000

- a) Following particulars are provided for Budhabare Ltd. whose business premises was partly destroyed by fire:

Sum insured (from 31 st Chaitra 2073)	Rs. 400,000
Period of indemnity	12 months
Date of damage 2074	1 st Baishak,
Date on which disruption of business ceased 2074	31 st Magh,

The subject matter of the policy was gross profit not only net profit and insured standing charges are included.

The books of account revealed:

- The gross profit for the financial year 2073 was Rs. 360,000.
- The actual turnover for financial year 2073 was Rs. 1,200,000 which was also the turnover in this case.
- The turnover for the period 1st Baishak to 31st Magh, in the year preceding the loss, was Rs. 1,000,000.

During dislocation of the position, it was learnt that in Falgun - Chaitra 2073, there has been an upward trend in business done (compared with the figure of the previous years) and it was stated that had the loss not occurred, the trading results for 2074 would have been better than those of the previous years.

The Insurance company official appointed to assess the loss accepted this view and adjustments were made to the pre-damaged figures to bring them up to the estimated amounts which would have resulted in 2074.

The pre-damaged figures together with agreed adjustments were:

Period	Predamaged figures	Adjustment to be added	Adjusted standard turnover
	Rs.	Rs.	Rs.
Baishak	90,000	10,000	100,000
Jestha. to Magh	910,000	50,000	960,000
Falgun to Chaitra	200,000	10,000	210,000
	1,200,000	70,000	1,270,000
Gross Profit	360,000	46,400	406,400

Rate of Gross Profit 30% (actual for 2073), 32% (adjusted for 2074).

Increased cost of working amounted to Rs. 180,000.

There was a clause in the policy relating to savings in insured standard charges during the indemnity period and this amounted to Rs. 28,000. Standing Charges not covered by insurance amounted to Rs. 20,000 p.a. The actual turnover for Baishak was nil and for the period Jestha to Magh 2074 Rs. 800,000

Required:

Calculate the amount of claim for Budhabare Ltd. to be lodged with insurance company.

b) From the following information of X Engineering Co.

Sales to net worth	2.3 times
Current liabilities to net worth	42%
Total liabilities to net worth	75%
Current Ratio	2.9 times
Sales to Closing inventories	4.5 times
Average Collection Period	64 days

Proforma Balance Sheet

Liabilities	Rs.	Assets	Rs.
Net worth	?	Fixed Assets	?
Long Term Liabilities	?	Cash	?
Current Liabilities	?	Stock	?
		Sundry Debtors	?
Total		Total	

Computations are to be made on nearest rupee.

Required: Compute the proforma Balance Sheet of the company if its sales are Rs. 1,600,000

5

Answer

4 a)

1. Short sales

Period	Adjusted Standard Turnover	Actual Turnover	Shortage
	Rs.	Rs.	Rs.
Baishakh	1,00,000	-	1,00,000
Jestha to Magh	9,60,000	8,00,000	1,60,000
	10,60,000	8,00,000	2,60,000

2. Gross profit ratio for the purpose of insurance claim on loss of profit

Gross profit - Insured Standing Charges - Uninsured standing charges = Net profit

Or

Gross profit - Uninsured standing charges = Net profit + Insured Standing Charges

$$= 4,06,400 - 20,000 = 3,86,400$$

$$\frac{\text{Rs. } 3,86,400}{\text{Rs. } 12,70,000} \times 100 = 30.425\%$$

3.	Amount allowable in respect of additional expenses
	<p>Least of the following:</p> <p>(i) Actual expenses = 1,80,000</p> <p>(ii) Gross profit on sales during 10 months period = $8,00,000 \times 30.425\%$ = 2,43,400</p> <p>(i) $\frac{\text{Gross Profit on Annual Adjusted Turnover}}{\text{Gross Profit on Annual + uninsured standing Adjusted Turnover charges}} \times \text{Additional expenses}$ $= 3,86,400 / (3,86,400 + 20,000) \times 1,80,000$ $= 1,71,142 \text{ (approx.)}$ Least i.e. = Rs. 1,71,142 is admissible.</p>

4. Amount of Claim

Gross profit on short sales = Rs. 2,60,000 x 30.425/ 100	79,105
Add: Amount allowable in respect of additional expense	1,71,142
	2,50,247
Less: Savings in Insured Standing Charges	(28,000)
	2,22,247

On the amount of final claim, the average clause will not apply since the amount of the policy Rs. 4,00,000 is higher than gross profit on annual adjusted turnover Rs. 3,86,400.

Therefore, insurance claim will be Rs. 2,22,247.

4 b)

Proforma Balance Sheet

Liabilities	Rs.	Assets	Rs.
Net worth	695,652	Fixed Assets	370,086
Long Term Liabilities	229,565	Cash	211,202
Current Liabilities	292,174	Stock	355,555
		Sundry Debtors	280,548
Total	1,217,391	Total	1,217,391

i) Net Worth:

Sales to Net Worth = 2.3 times

Sales = 1600,000

Net Worth = $1600,000 / 2.3 = 695,652$

ii) Current Liabilities

Current Liabilities to Net Worth = 42%

Current Liabilities = $42\% \text{ of } 695,652 = 292,174$

iii) Long term Liabilities

Total liabilities are 75% of net worth = $75\% \text{ of } 695,652 = 521,739$

Long term Liabilities = $521,739 - 292,174 = 229,565$

iv) Current Assets

Current Ratio = 2.9 times

Therefore, current assets = $2.9 \text{ times of CL} = 2.9 \times 292,174 = 847,305$

v) Stock

Sales to Closing Inventories = 4.5 times

Closing Inventories = $1600,000 / 4.5 = 355,555$

vi) Sundry Debtors

Average Collection Period = 64 days

Sundry Debtors/Avg. Daily sales = 64

Sundry Debtors = $1600,000 / 365 \times 64 = 280,548$

vii) Cash

Cash = Current Assets-stock-debtors

= $847,305 - 355,555 - 280,548$

= 211,202

5.

- a) Rich Ltd sold Two lakh vacuum pumps during the year 2076-77 with a condition to make good by repair/replacement any manufacturing defects reported within 6 months from the date of sale. Past experience in this

regard showed that there were no replacements carried out, but minor/major repairs were necessitated to the extent of 10%/5% respectively of the units sold. The cost of such minor/major would amount to Rs 1,000/Rs 6,000 respectively. While finalizing the accounts for the year, the company does not reflect provision in this regard. Comment as per Nepal Accounting Standard. **5**

- b) On 20th Ashadh 2076, Kapil sold 100 identical items to a customer for Rs. 2,000 each. The items cost Kapil Rs. 1,600 each to manufacture. The terms of sale are that the customer has the right to return the goods for a full refund within three months. After the three-month period has expired the customer can no longer return the goods and payment becomes immediately due. Kapil has entered into transactions of this type with this customer previously and can reliably estimate that 4% of the products are likely to be returned within the three-month period.

State how these transactions would be reported in the financial statements of Kapil for the year ended 31st Ashadh 2076. **5**

- c) From the following information, prepare the Cash Flow from Financing activities as per NAS 7 'Statement of Cash Flows' as the accountant of ABC Limited is not able to decide and seeks your advice: **5**

- Received Rs. 400,000 as redemption of short-term deposit.
- Proceeds of Rs. 2,000,000 from Issuance of equity share capital.
- Received interest of Rs. 70,000 on Govt. bonds.
- An amount of Rs. 1,300,000 incurred for purchase of goodwill.
- Proceeds of Rs. 500,000 from sale of patent.
- Proceeds of Rs. 120,000 from long term borrowing.
- Amount paid for redemption of debentures of Rs. 2,200,000.
- Underwriting commission of Rs. 40,000 paid on issue of equity share capital.
- Interest of Rs. 144,000 paid on long-term borrowing.

Answer

- 5 a) This problem is based on NAS 37. The standard provides that an entity should recognize a provision only when all of the following conditions are met:

1. There is a **present obligation** as a result of a **past event**;
2. It is probable that an **outflow of resources embodying economic benefits** will be required to settle the obligation; and
3. A **reliable estimate** can be made of the amount of obligation.

In the present case, Rich Ltd fulfils all the above conditions the sale of pumps with a warranty obligation constitutes the present obligation as a result of the past event. It is probable that some outflow will be involved in setting the warranty obligation, satisfy the second condition. As per the details based on past precedence reliable estimate can be made as under:

Provision for major repair = $[6000 \times (5\% \text{ of } 200,000)]$ = Rs.600 lakhs

Provision for minor repair = $[1000 \times (10\% \text{ of } 200,000)]$ = Rs.200 lakhs

Total Provision = Rs.800 lakhs

Thus, Rich Ltd as on 31-03-2076 should make a provision for warranty obligation against sale of vacuum pumps to the extent of Rs. 800 lakhs.

- 5 b) When the customer has a right to return products, the transaction price contains a variable element. Since, this can be reliably measured, it is taken account of in measuring the revenue and the total revenue will be Rs. 192,000 (96 x Rs. 2,000). Rs. 200,000 (100 x Rs.2,000) will be recognised as a trade receivable. Rs. 8,000 (Rs.200,000 – Rs.192,000) will be recognised as a refund liability. This will be shown as a current liability. The total cost of the goods sold is Rs. 160,000 (100 x Rs. 1,600). Of this amount, only Rs. 153,600 (96 x Rs.1,600) will be shown as a cost of sale. The other Rs. 6,400 (Rs. 160,000 – Rs. 153,600) will be shown as a right of return asset under current assets.

5 c) **Statement showing Cash Flow from Financing Activities**

Cash inflow from financing activity	Rs.	Rs.
Proceeds from insurance of equity share capital	20,00,000	
Proceeds from long term borrowings	120,000	
Total cash inflow from financing activity		21,20,000
Less: Cash outflow from financing activity		
Amount paid for redemption of debentures	22,00,000	
Underwriting commission paid	40,000	
Interest paid on long-term borrowings	1,44,000	(23,84,000)
Net cash flow available from (used in) financing activity		(2,64,000)

6. Write short notes on: **(5×3=15)**

- What are the disadvantages of a spreadsheet as an accounting tool?
- Distribution of Management Expense of Insurance Business
- Sinking Fund
- Provisions and contingent liabilities
- Components of PEARLS

Answer

a) Disadvantages of a spreadsheet as an accounting tool are as follows:

- Spreadsheet has data limitations. Depending upon the package, it can accept data only up to a specific limit.
- Simultaneous access on a network may not be possible. Many of the modern software allow locking of the table when update is taking place. This is not possible in a spreadsheet.
- Double entry is not automatically completed in Spread Sheet. Formulas or other means have to be adopted to complete the double entry.
- Reports are not automatically formatted and generated but have to be user controlled. Each time a report has to be printed, settings have to be checked and data range has to be set. In many accountings software that is automatically taken care of by the program.

- b) Distribution of the management expense among the Profit and Loss account and Revenue Account shall be done as per the Directives of the Insurance Board. The separate directives issued for Life Insurer and Non-life Insurer prescribes separate methods for distribution of management expense.

The distribution shall be as follows for Non-Life Insurer.

Method of Distribution of management expenses for Non-Life Insurer

- a) Distribute 10% of the total management expense to the profit and loss account
- b) Distribute the remaining 90% to the each of the revenue account as per the following formula:

$$\text{Management Expense} = \text{Weight/Total Weight} * \text{Total Management Expenses} * 0.9$$

Explanation:

- 1. Weight (Non-Life Insurance Business) = Direct Insurance Premium-Agent commission of concerned category of insurance business the insurer carried out.
- 2. Weight (Life Insurance Business) = Direct Insurance Premium-Agent commission of concerned category of insurance the insurer operating-Medical Fee.
- 3. Total Weight = Sum of Weight of every category of Insurance Business.

- c) The most common method of supplementing capital available to a company is to issue debentures, which are usually redeemable. Redeemable debentures may be redeemed after a fixed number of years or any time after a certain number of years has elapsed since their issue, on giving a specified notice or by annual drawing. Usually, according to the conditions of the issue, the company is required to create a fund by appropriating annually a certain percentage of, or a fixed amount out of, its profit. The fund so created is normally known as Sinking Fund or Debenture Redemption Reserve Fund. The company invests the amount of the fund either in the purchase of securities which are readily saleable or takes a policy that shall mature at the time the debentures will fall due for payment. Such an arrangement would ensure that the company will have sufficient liquid funds for the redemption of debentures at the time they shall fall due for payment. In the case of debentures that are redeemable at premium, the appropriation to the Sinking Fund should be sufficient to pay both the amount of debenture and the premium on redemption. On redemption of debentures, out of the balance lying in the Sinking Fund an amount equal to the debentures so redeemed is transferred to General Reserve.
- d) Provision is a liability of uncertain timing or amount. The liability may be a legal obligation or a constructive obligation. Examples of provisions may include: warranty obligations; legal or constructive obligations to clean up contaminated land or restore facilities; and obligations caused by a retailer's policy to make refunds to customers. An entity recognizes a provision if it is probable that an outflow of cash or other economic resources will be required to settle the provision. If an outflow is not probable, the item is treated as a contingent liability.

Contingent liabilities are possible obligations whose existence will be confirmed by uncertain future events that are not wholly within the control of the entity. Contingent liabilities also include obligations that are not recognized because their amount cannot be measured reliably or because settlement is not probable.

An entity must recognize a provision if a present obligation (legal or constructive) has arisen as a result of past event (the obligating event), payment is probable (more likely than not) and the amount can be estimated reliably.

- e) The PEARLS system is uniquely different. It was first designed as a management tool, and later became an effective supervisory mechanism for credit unions, which are also known as saving & credit cooperatives or financial cooperatives. Each letter of the name "PEARLS" looks at a different, but critical aspect of a credit union:

P = Protection

Protection is measured by 1) comparing the adequacy of the allowances for loan losses against the amount of delinquent loans and 2) comparing the allowances for investment losses with the total amount of non-regulated investments. Protection against loan losses is deemed adequate if a credit union has sufficient provisions to cover 100% of all loans delinquent for more than 12 months.

Inadequate loan loss protection produces two undesirable results: inflated asset values and fictitious earnings. Most credit unions are not anxious to recognize loan losses, and much less, to charge them off against earnings. That unwillingness leads to widespread abuse of the principles of safety and soundness. Reported net income is overstated, asset values are inflated, provisions for loan losses are inadequate, and member savings are not adequately protected.

E = Effective Financial Structure

The financial structure of the credit union is the single most important factor in determining growth potential, earnings capacity, and overall financial strength.

The PEARLS system measures assets, liabilities and capital, and recommends an "ideal" structure for credit unions.

Credit unions are encouraged to maximize productive assets as the means to achieve sufficient earnings.

A = Assets Quality

A non-productive or non-earning asset is one that does not generate income. An excess of non-earning assets affects credit union earnings in a negative way. Non-earning assets are also discouraged because once purchased, they are often difficult to liquidate. The only effective way to maintain the ideal balance between productive and unproductive assets is by increasing the volume of productive assets.

R = Rates of Return and Costs

The PEARLS system segregates all of the essential components of net earnings to help management calculate investment yields and evaluate operating expenses. In this way, PEARLS demonstrates its value as a management tool. Unlike other systems that calculated yields on the basis of average assets, PEARLS calculates yields on the basis of actual investments outstanding. This methodology assists management in determining which investments are the most profitable.

It also permits the credit unions to be ranked according to the best and worst yields. By comparing financial structure with yields, it is possible to determine how effectively the credit union is able to place its productive resources into investments that produce the highest yield. These powerful analysis techniques help management stay abreast of the financial performance of the credit union.

L = Liquidity

Effective liquidity management becomes a much more important skill as the credit union shifts its financial structure from member shares to more volatile deposit savings. In many movements following the traditional model, member shares are very illiquid and most external loans have a long payback period, therefore there is little incentive to maintain liquidity reserves. Liquidity is traditionally viewed in terms of cash available to lend - a variable exclusively controlled by the credit union. With the introduction of withdrawable savings deposits, the concept of liquidity is

radically changed. Liquidity now refers to the cash needed for withdrawals - a variable the credit union can no longer control.

S = Signs of Growth

The only successful way to maintain asset values is through strong, accelerated growth of assets, accompanied by sustained profitability. Growth by itself is insufficient. The advantage of the PEARLS system is that it links growth to profitability, as well as to the other key areas by evaluating the strength of the system as a whole.

Paper 2: Audit and Assurance

Attempt all questions.

1. As an auditor, give your opinion with explanations on the following cases: (4×5=20)

- a) The management tells you that the work-in-process is not valued since it is difficult to ascertain the same in view of the multiple processes involved and in any case the value of opening and closing work-in-process would be more or less the same.

Answer:

According to NAS 2, *Inventories*, the inventories also include (para 6) those assets which are in the process of production for sale in the ordinary course of business apart from finished goods. The materials or supplies are consumed in such production process. It is, thus, necessary for a company to ensure that each and every component of inventory is measured and valued properly. The argument advanced by the company that it is difficult to ascertain the same in view of the multiple processes involved is not acceptable. In general, the audit procedures regarding work-in-process are similar to those used for raw materials and finished goods. The auditor has to carefully assess the stage of completion of the work-in-process for assessing the appropriateness of its valuation.

The argument that the opening and closing work-in-process would be more or less the same is also not justified because the omission of those would lead to distortion of true and fair view. Further, costs incurred for raw materials and the overheads would normally be different and would give rise to different values of opening and closing inventory. In view of the above, the auditor shall consider its overall impact on financial statements and conclude as to how it should be reported in his audit report.

- b) ABC Limited with paid up capital of Rs.1 crore has appointed an individual firm, Suresh Associates, Chartered Accountants, as auditor of the company at the Annual General Meeting held on 30th Poush, 2076. Mrs. Kamala, wife of Mr. Suresh, invested in the equity shares having face value of Rs.1 lakh of ABC Limited. However, Suresh & Associates accepted engagement and continued to function as statutory auditors of the company.

Answer:

According to section 112(1)(e) of Companies Act 2063, a substantial shareholder of the company or a shareholder holding 1% or more of the paid-up capital of the company or his close relative shall be disqualified for being appointed as an auditor of the company. In this case, Mr. Suresh, Chartered Accountant, did not hold any shares in the company. However, his wife held equity shares of ABC Limited of face value of Rs.1 lakh which is 1% of paid up capital of the company.

Further, section 112(2) provides that the auditor shall, prior to his appointment, give information in writing to the company that he is not disqualified for being appointed as an auditor of the company. Where any auditor becomes disqualified to audit the accounts of a company or there arises a situation where he becomes disqualified for appointment or can no longer continue to act as an auditor of the company, he shall immediately stop performing audit which is required to be performed or is being performed by him and give information thereof to the company in writing. The audit performed by an auditor who has been appointed in contravention of this Section shall be invalid.

Hence, Suresh & Associates cannot continue to function as auditor of the company with the investment made by his wife in the equity shares of ABC Limited which is 1% of the paid-up capital of the company.

- c) Chitle International Ltd.'s total turnover for the FY 2075/76 is Rs.1crore and it includes Rs. 2.7 lakhs from sale of by-products. Whereas, the by-product sales are included under the miscellaneous income in the financial statements and is not separately disclosed in the income head.

Answer:

As per NAS 1, *Presentation of Financial Statements* information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on size of the item or error judged in the particular circumstances of its omission or misstatement. Thus, materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic which information must have if it is to be useful.

As per NAS 1, each material item shall be presented separately in the financial statements. Immaterial amounts shall be aggregated with amounts of a similar nature or function and need not be presented separately.

In this case, income from sale of by-product shall be disclosed separately in the revenue item as the income from by-product is considered material items since it is more than two percent of total turnover of the company. Similarly, the auditor has to ensure that a material item is disclosed separately and distinctly or at least clear information about the item is available in the financial statements. In this case, he is required to request company to disclose information about revenue from sale of by-product, as the income from by-product is material in giving or distorting a true and fair view of financial statements.

- d) During the financial year 2077/78, SR Private Limited, a service providing company purchased generator of Rs.20 lakhs for smooth functioning of its office. The accountant claims that there is no necessity to provide for depreciation in respect of generator as it was kept standby but not used at all during the financial year.

Answer:

As per NAS 16, *Property, Plant and Equipment*, depreciation of assets begins when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by the management. Depreciation is the systematic allocation of the cost of an item of property, plant & equipment (less its residual value) over its useful life. Thus, depreciation has to be charged even in case of these assets which are not used at all during the year but by mere efflux of time provided such assets qualify as depreciable assets.

When the generator was kept ready for use as stand-by, it means it was intended to be used for the purpose of business. Depreciation in respect of this generator would have been provided in the accounts for the year ended 31st Ashadh 2078. If there is an intention to use an asset, though it may not have actually been used, it is a 'constructive' or 'passive' use and eligible for charging depreciation.

2. Give your comments on the following cases: (4×5=20)

- a) Mr. T Pandey, Senior Accountant of M/s Preeti Finance Co. Ltd. produced the photocopies of fixed deposit receipts of Rs. 5,05,000/- to the auditor during the course of

audit as the managing director who kept original receipts in safe vault was presently out of the country to attend the seminar abroad.

Answer:

An auditor should obtain sufficient appropriate audit evidence, evaluate the same and draw reasonable conclusions therefrom as required by NSA 500, *Audit Evidence*. In the given case, photocopies of fixed deposit receipts were made available by Mr. T Pandey, Senior Accountant to the auditors as the original receipts could not be verified, which were kept in the safe vault.

The auditor is generally required to inspect and physically verify the fixed deposit receipts (FDRs) representing the assets. Such verification is necessary to ensure that no unauthorized charge has been created or the fixed deposits receipts have been lodged with a bank to secure a loan or an overdraft. Thus, the photocopies of FDRs cannot serve the desired purpose. Alternatively, reliance can be placed by the auditor on such evidence provided photocopies are certified as true copies by the management as also backed by a letter of representation. Managing director may also be asked to confirm in writing from abroad that no unauthorized charge has been created on the fixed deposits receipts and same shall be produced to auditors as soon as he returns from seminar abroad. The auditor may also obtain independent confirmation from the respective bank that no charge has been created on such fixed deposit receipts.

The auditor should consider the materiality of the amount involved and its overall impact on the financial statements while forming an opinion. In case the auditor is satisfied after extending the substantive audit procedure and if amount involved is reasonable in his opinion, he need not state anything in his report after getting appropriate confirmation in writing from managing director about the status of fixed deposit receipts.

- b) The financial statements of Everest Ltd. for the FY 2076/77 has been approved by its Board of Directors on 1st Kartik 2077, however, auditor has issued his audit report on 25th Aswin 2077.

Answer:

As per NSA 700, *Forming an Opinion and Reporting on Financial Statements*, the auditor should date the report as of the completion date of the audit. This informs the reader that the auditor has considered the effect on the financial statements and on the reports of events and transactions of which the auditor become aware and that occurred up to that date. Since the auditor's responsibility is to report on the financial statements as prepared and presented by management, the auditor should not date the report earlier than the date on which the financial statements are signed or approved by Board of Directors. So, the act done by the auditor in this case is not appropriate in line with provision of NSA 700.

- c) While reporting on the consolidated financial statements, the principal auditor has to evaluate the financial statements of the subsidiary company also. At times when such financial statements were audited by other auditors, the principal auditor relied on the audit reports submitted by the company without further audit procedures.

Answer:

As per NSA 600, *Special Considerations – Audits of Group Financial Statements (including the work of Component Auditors)*, when the principal auditor (group

engagement partner) uses the work of another auditor, the principal auditor should determine how the work of the other auditor will affect the audit of group financial statements. The principal auditor should perform procedures to obtain sufficient appropriate audit evidence, that the work of the other auditor is adequate for the principal auditor's purposes, in the context of the specific assignment.

The principal auditor may conclude that it is not necessary to apply any substantive or quality check procedures because sufficient appropriate audit evidence previously obtained that acceptable quality control policies and procedures are complied with in the conduct of the other auditor's practice.

In the given case, the principal auditor has to ensure that other auditor has complied with applicable ethical and technical requirements while conducting audit.

- d) As statutory Auditor of XYZ Pvt., Ltd. you requested your client for sending letter for balance confirmations from certain debtors. The client argued that since the said balances with debtors were under dispute and the matter was pending in the court, it was not necessary to ask balance confirmation.

Answer:

NSA 505, *External Confirmations*, establishes standards on the auditor's use of external confirmation as a means of obtaining audit evidence. It requires that the auditor should employ external confirmation procedures in consultation with the management. The auditor may come across certain situations in which the management may request him not to seek external confirmation from certain parties because of dispute with the debtors, etc. The management, for example, might make such a request on the grounds that due to a dispute with the particular debtor, the request for confirmation might aggravate the sensitive negotiations between the entity and the debtor. In such cases, when an auditor agrees to management's request not to seek external confirmation regarding a particular debtor, the auditor should consider validity of grounds for such a request and assess management's integrity and obtain other evidence to support the same. The auditor should also ask the management to submit its request in a written form, dealing therein the reasons for such a request. When auditor agrees to management's request not to seek external confirmation regarding a particular matter, the auditor should document the reasons for accepting to the management's request and should apply alternative procedures to obtain sufficient appropriate evidence regarding that matter. While considering the validity of request, in case the auditor reaches at a conclusion that the same was not valid, he may appropriately modify the report.

3. Answer the following: (3×5=15)

- a) List out the analytical procedures that you would adopt in audit of revenue of an entity. What are the factors that determine the extent of reliance on such analytical procedures?

Answer:

Analytical procedures are one of audit procedures which help an auditor to understand the client's business and changes in the business, and to identify potential risk areas to plan other audit procedures. It includes comparison of financial information, relating financial and nonfinancial information and consideration of predictable relationship of data.

The analytical procedures that will be adopted in obtaining audit evidence regarding the various assertions relating to revenue are as follows:

- i. Comparison of Gross-profit ratio to sales for the current year with the corresponding figures of the previous years.

- ii. Comparison of ratio of sales returns to sales for the current year with the corresponding figures for previous years.
- iii. Comparison of trade discount to sales for the current year with previous year.
- iv. Review of Reconciliation of Excise/VAT booked during the year with Excise/VAT returns submitted with the total sales booked.
- v. Comparison of dividend/interest/royalty for the current year with the corresponding figures for previous years.
- vi. Comparison of ratio of income on investments to average investment for the current year with corresponding figures for the previous year.

The factors that affect the extent of reliance on analytical procedures are as follows:

- i. **Materiality:** When items are material, the auditor doesn't solely rely on the analytical procedures in forming conclusions but will carry other substantive procedures also.
- ii. **Other procedures:** When other procedures are also directed towards the same objective, it might confirm or dispel the questions raised from the application of analytical procedures.
- iii. **Weak controls:** When internal controls are weak, greater reliance is placed on tests of balances and tests of details of transactions rather than on analytical procedures.
- iv. **Accuracy:** The accuracy with which expected results of analytical procedures can be predicted. For example, greater reliance is placed on gross profit ratio compared to previous year than in comparing discretionary expenses such as donation.

- b) Briefly discuss about the limitations of Internal Controls.

Answer:

Limitations of Internal Control:

Internal control can provide only reasonable assurance. Internal control, no matter how effective, can provide an entity with only reasonable assurance about achieving the entity's compliance, operational and financial reporting objectives. The likelihood of their achievement is affected by inherent limitations of internal control. Such limitations are discussed as below:

- (i) Human judgment in decision-making: Realities that human judgment in decision-making can be faulty and that breakdowns in internal control can occur because of human error.
- (ii) Lack of understanding the purpose: Equally, the operation of a control may not be effective, such as where information produced for the purposes of internal control (for example, an exception report) is not effectively used because the individual responsible for reviewing the information does not understand its purpose or fails to take appropriate action.
- (iii) Collusion among people: Additionally, controls can be circumvented by the collusion of two or more people or inappropriate management override of internal controls. For example, management may enter into side agreements with customers that alter the terms and conditions of the entity's standard sales contracts, which may result in improper revenue recognition. Also, edit checks in a software program that are designed to identify and report transactions that exceed specified credit limits may be overridden or disabled.

- (iv) Judgements by Management: Further, in designing and implementing controls, management may make judgments on the nature and extent of the controls it chooses to implement, and the nature and extent of the risks it chooses to assume.
- (v) Limitations in case of small entities: Smaller entities often have fewer employees due to which segregation of duties is not practicable. However, in a small owner-managed entity, the owner-manager may be able to exercise more effective oversight than in a larger entity. This oversight may compensate for the generally more limited opportunities for segregation of duties.

On the other hand, the owner-manager may be more able to override controls because the system of internal control is less structured. This is taken into account by the auditor when identifying the risks of material misstatement due to fraud.

- c) Describe the necessity of "Other Matter Paragraph" and how it is presented in the Auditor's Report?

Answer :

NSA 706, *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report* deals with additional communication in the auditor's report when the auditor consider it necessary to:

- (i) Draw users' attention to a matter or matters presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements; or
- (ii) Draw users' attention to any matter or matters other than those presented or disclosed in the financial statements that are relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

The other matter paragraph is used in second scenario discussed above where it relates to a matter other than those presented or disclosed in the financial statements.

The "Other Matter Paragraph" is presented in the Auditor's Report as follows:

- i. When a Key Audit Matters section is presented in the auditor's report and an Other Matter paragraph is also considered necessary, the auditor may add further context to the heading "Other Matter", such as "Other Matter – Scope of the Audit", to differentiate the Other Matter paragraph from the individual matters described in the Key Audit Matters section.
- ii. When an Other Matter paragraph is included to draw users' attention to a matter relating to Other Reporting Responsibilities addressed in the auditor's report, the paragraph may be included in the Report on Other Legal and Regulatory Requirements section.
- iii. When relevant to all the auditor's responsibilities or users' understanding of the auditor's report, the Other Matter paragraph may be included as a separate section following the Report on the Audit of the Financial Statements and the Report on Other Legal and Regulatory Requirements.

4. Answer/Comment on the following:

(3×5=15)

- a) R Baral & Associates has been operating a separate bank account for keeping client's fund in course of providing fund manager service to the client. The interest

earned on such account during financial year 2077/78 amounting Rs. 85,000 has been transferred to firm's bank account and booked as miscellaneous income, subsequently with corresponding miscellaneous income in client's account and miscellaneous expenditure in firm's account.

Answer:

As per Section 350 "Custody of Client Assets" of Code of Ethics of the Institute of Chartered Accountants of Nepal, and Guidelines on assuming custody of clients' money by professional Accountants in public practice, it is necessary that "All interest earned on clients' monies should be credited to the client's account".

The accounting entries made by R Baral & Associates for interest income transferring to firms account is incorrect. However, subsequent transfer of interest income to client's account by booking as miscellaneous expense in firm's account is correct.

In the light of the provision contained in Section 350 of Code of Ethics, a professional accountant in public practice entrusted with money (or other assets) belonging to others shall therefore:

- (i) Keep such assets separately from personal or firm assets;
- (ii) Use such assets only for the intended purpose;
- (iii) Be ready to present accounting of those assets and any income generated from such assets at all time to the client; and
- (iv) Comply with all the relevant laws and regulations applicable for the custody of client's assets.

Hence, R Baral & Associates should comply with the code of ethics as prescribed by ICAN and save the firm away from the disciplinary action for non-compliance of ICAN code of ethics.

- b) A partner of a firm of Chartered Accountants during a T.V. interview handed over a bio-data of his firm to the chairperson. Such bio-data detailed the standing of the international firm with which the firm was associated. It also detailed the achievements of the concerned partner and his recognition as an expert in the field of taxation. The chairperson read out the said bio-data during the interview.

Answer:

Code of Ethics and related Guidelines on marketing professional services issued by the Institute prohibits solicitation of client or professional work either directly or indirectly by circular, advertisement, personal communication or interview or by any other means because it shall constitute professional misconduct. The bio-data was handed over to the chairperson during the T.V. interview by the Chartered Accountant which included details about the firm and the achievements of the partner as an expert in the field of taxation. The chairperson read out the same in detail about association with the international firm as also the achievements of the partner and his recognition as an expert in the field of taxation. Professional accountants in practice while participating in such interview should be careful in giving details about firm and himself/ herself that may be considered as publicity. When such publicity attracts non-compliance with code of ethics and related Guidelines, such act would lead to professional misconduct attracting the penalty there of.

- c) How the concept of "related party" has been defined in Nepal Standards on Auditing (NSA)?

Answer:

NSA 550, in para 10 (b) provides the definition of related party as a party that is either:

- (i) A related party as defined in the applicable financial reporting framework; or
- (ii) Where the applicable financial reporting framework establishes minimal or no related party requirements:
 - i. A person or other entity that has control or significant influence, directly or indirectly through one or more intermediaries, over the reporting entity;
 - ii. Another entity over which the reporting entity has control or significant influence, directly or indirectly through one or more intermediaries; or
 - iii. Another entity that is under common control with the reporting entity through having:
 - a. Common controlling ownership;
 - b. Owners who are close family members; or
 - c. Common key management.

However, entities that are under common control by a state (that is, a national, regional or local government) are not considered related unless they engage in significant transactions or share resources to a significant extent with one another.

5. Answer/Comment on the following: (2×5=10)
- a) Explain the Propriety aspect of Audit in line with Section 9 of Audit Act, 2075.

Answer:

Section 9 of the Audit Act, 2075 requires the Auditor General to audit following matters considering the propriety thereof:

- (1) The Auditor General shall, as required, audit the following matters in view of the propriety thereof:
 - (a) If it is seen that any expenditure, though it conforms to the authorization, has been made unreasonably or in a manner to cause loss and damage to the national property, with respect to such expenditure and its authorization,
 - (b) With respect to any grant of national property whether movable or immovable or underwriting of revenue or any lease, permit, license or rights relating to mining, forest, hydropower etc. and all authorizations issued in a manner to abandon any revenue or national property, whether movable or immovable,
 - (c) With respect to the subject-matters of various financial transactions including contracts and agreements relating to public works, repair and maintenance, procurement and supply, consultancy service, service delivery, public expenditure and revenue mobilization.
- (2) The Auditor General may, if he or she deems it appropriate, examine, in accordance with the recognized principles of accounting, as to whether or not any official within his or her scope of competence has borne financial accountability.
- (3) The Auditor General may not include in his or her report minor items of irregular amounts or other items deemed

- b) Annual General Meeting of Surya Ltd. could not appoint the auditor for the FY 2077-78. Suggest how Surya Ltd. can appoint the auditor for the FY 2077-78?

Answer:

Section 113 of the Companies Act, 2063 empowers the Office of Company Registrar (OCR) to fill a vacancy in case no auditors are appointed or reappointed at an annual

general meeting. Since the auditor could not be appointed in AGM, OCR at the request of the board of directors shall appoint a person to fill the vacancy as provided in Section 113. The non-appointment of auditor by AGM does not result in any casual vacancy.

Moreover, even if the auditor is existing one would not make any difference since the appointment has to be made at each AGM and the auditor must accept the same. As a general principle, the shareholders have to exercise this power in all cases, except in the case of filling a casual vacancy or appointing the first auditors.

Thus, as per the provision of Companies Act as stated above, Surya Ltd. have to follow the required procedures for appointing the auditor for the FY 2077-78.

6. Write short notes on the following:

(4×2.5=10)

a) Uses of Negative External Confirmation Requests

Answer:

A negative external confirmation request asks the respondent to reply only in the event of disagreement with the information provided in the request. However, when no response has been received to a negative confirmation request, the auditor remains aware that there will be no explicit evidence that intended third parties have received the confirmation requests and verified that the information contained therein is correct. Accordingly, the use of negative confirmation requests ordinarily provides less reliable evidence than the use of positive confirmation requests, and the auditor considers performing other substantive procedures to supplement the use of negative confirmations. Negative confirmation requests may be used to reduce audit risk to an acceptable level when:

- i. the assessed level of inherent and control risk is low;
- ii. a large number of small balances is involved;
- iii. a substantial number of errors is not expected; and
- iv. the auditor has no reason to believe that respondents will disregard these requests.

b) Professional Skepticism

Answer:

Professional skepticism is an attitude which means that the auditor should recognize the fact that circumstances may exist that may cause the financial statements to be materially misstated. It includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.

c) Computer Assisted Audit Techniques

Answer:

Computer assisted audit techniques (CAATs) includes tools used by auditors during their work. These tools allow auditors to receive data in any form and analyze it better. CAATs include various methods that can help auditors in many ways. For example, auditors can use them to identify trends or signal out anomalies in the provided information. These tools are available for both external and internal audit uses. In essence, computer-assisted audit techniques refer to the use of technology in auditing. Using these tools, auditors can assess several aspects of their audit engagement. Whether it is evaluating the client's internal controls or extracting specific information, CAATs can be significantly valuable. While some people assume CAATs apply to large audits only, these tools are beneficial in any size audits. Traditionally, auditors spend most of their time analyzing data. With CAATs, they don't have to take the same time. Instead, they can focus on other more prominent audit matters.

d) Teeming and Lading

Answer:

Teeming and lading is a term that describes a practice whereby organizations attempt to hide an information in one customer's account by moving in money from another customer's account. It is sometimes referred to as lapping, short banking, or delayed accounting. Essentially, teeming and lading is a strategy that delays a payment deficit from showing up on a customer's account by moving money around. Hence, older payments appear to have been covered before customers, or other organization members might notice any disparity. Most often, teeming and lading is a strategy used by employees who have used a customer's money for personal purposes to cover their tracks. It may also be used by an employee that has used one customer's money for another customer's benefit. In both examples, teeming and lading helps keep the activity from being found out by delaying a deficit from showing up in the books and manipulating the company accounts.

7. Distinguish between:

(2×5=10)

a) Audit, Review and Compilation Level of assurance :

Answer:

The level of assurance that the financial statements of a client are fairly presented is at its highest for an audit and at its lowest (none at all) for a compilation, with a review somewhere in between.

- i. Reliance on management: In all three cases, the auditor begins with the account balances provided by management, but an audit requires in a significant amount of corroboration of this information. A review requires some testing of the information, while a compilation almost entirely relies on the presented information.
- ii. Understanding of internal controls: The auditor only tests the internal controls of the client in an audit; no testing is conducted for a review or a compilation.
- iii. Work performed: An audit requires a significant number of hours to complete, since there are many audit procedures to be performed. A review requires substantially fewer hours, while the effort associated with a compilation is relatively minor.
- iv. Price: It requires vastly more effort for an auditor to complete an audit, so audits are much more expensive than a review, which in turn is more expensive than a compilation.

Another issue is the level of demand for each of these services. The users of financial statements, such as investors and lenders, nearly always demand an audit, since it provides the greatest assurance that what they are reading is a fair representation of the financial results, financial position, and cash flows of the reporting entity.

b) Differentiate between Performance audit and Propriety audit.

Answer:

No.	Performance Audit	Propriety Audit
Meaning	Performance audit is an independent examination of the economy, efficiency and effectiveness of government undertakings, programmes or organisations, with due regard to economy, and the aim of leading to improvements.	Propriety audit has been described as an audit of the actions and decisions of the executives.

Focus	Performance audit is focused to improve the system of management to ensure genuine output/outcome from resources employed.	The focus of such an audit is on the financial discipline, the authority structure, efficiency, rules and regulations and the protection of public interest.
Objective	In this, auditor focus on whether the operations of audit entities were conducted in a way that ensures the best possible use of resources or considering the 3Es and officials in the public sector have met their accountability obligations.	In this, auditor focus on whether the expenditure is improper, avoidable, or infructuous expenditure even though the expenditure has been incurred in conformity with the existing rules and regulations.
Scope	This type of audit examines: a) the economy in the acquisition of the appropriate quality and quantity of human, financial, physical and information resources at the appropriate times and at the lower cost; b) “Efficiency” of utilization of human, financial, physical and information resources such that the output is maximized for any given set of resource inputs, or input is minimized for any given quantity and quality of output and c) “Effectiveness” in the achievement of the objectives or other intended effects of activities whether policy objectives or goals have been met and whether this can be attributed to the policy pursued.	Audit against propriety seeks to ensure that expenditure conforms to principles of a) the expenditure should not be prima facie more than the occasion demands; b) every public officer is expected to exercise the same vigilance in respect of expenditure incurred from public moneys as a person of ordinary prudence would exercise in respect of expenditure of his own money; c) no authority should exercise its powers of sanctioning expenditure to pass an order which will be directly or indirectly to its own advantage and d) public moneys should not be utilized for the benefit of a particular person or section of the community.

Paper 3: Corporate and Other Laws

1. Answer the following question.

(5×5=25)

- a) ABC public Company decided to hold election for constituting a new Board of Directors of the company. The Articles of Association of the company is silent about the number of shares required to be held by a person for his appointment as director of the company. Mr. Aswin having 90 shares of the company filed his candidacy for the appointment of director of the company. The election officer refused his application. State the required numbers of the Directors to constitute Public Company and how far the decision of the election officer is valid. Write your answer with reference to the Companies Act, 2063.
- b) Indrawati Hydro Company having its registered office in Kathmandu, calls its Annual General Meeting at Kathmandu. A notice was published by the company in the national daily newspaper on 15th Oct. 2021, calling the meeting will held on 8th Nov. 2021. No other public notice was made by the company for its Annual General Meeting. Due to Covid new variant, seven percent of the shareholders of the company attended the meeting in person and decided on the agenda. Considering that the meeting was not an adjourned meeting, state your findings on the following issues referring to the provisions of the Companies Act, 2063.
- i) Irregularities committed by the company on entire proceedings of the meeting as mentioned above.
 - ii) Validity of the resolutions passed by the meeting.
- c) Mr. A is appointed as an auditor of Prime Development Bank Ltd. in this Fiscal Year 2077/2078. He is willing to be continued in this company for Fiscal Year 2078/2079. Mr. B, who had been a partner of A before 3 years, is also willing to be an auditor in this company. In spite of this, company is planning to substitute another auditor. In this circumstance, if the willingness of A and B is justified? If the company has planned to remove Mr. A then how it can be removed? Justify your answer with reference to the Companies Act, 2063.
- d) Heritage Nepal Pvt. Ltd. dismissed its CEO, Pradip, as against the service contract between them. He filed a case for compensation as against the wrongful dismissal. Shortly thereafter, Heritage Nepal ceased trading. The company paid of all its creditors and then transferred its remaining assets to another company National Builders Ltd. Pradip Sharma obtained a default judgment against the company, Heritage Nepal, but by that name it had no assets and stood dissolved. Therefore, he charged against the transferee company, National Builders. Decide whether the transferee company is liable to pay compensation to Pradip.
- e) Mr. Y was convicted of property embezzlement while he was managing director of Fresh and Refreshing Ltd. and sentenced four years ago. Mr. Y has recently purchased shares of Old and Gold Ltd. and wants to be

appointed as director of the company. State the circumstances in which one is disqualified to be appointed as a director under Companies Act, 2063 and also state if Mr. Y is eligible for appointment in the given issue.

Answer:

- a) Section 86 (2) the Companies Act, 2063 provides for the constitution of a board of directors in a public Company. Accordingly, every public company shall have a board of directors consisting of minimum three to maximum of eleven directors.

Section 88 of the Companies Act, 2063 contains provision regarding share qualification of directors. According to which if the Articles of Association of a company specify any number of shares required to be held by a person for his appointment as director of the company, the person who becomes director shall hold such number of shares. If such number of shares to be held by any person is not specified, one hundred shares should be held by the person willing to become a director.

On the basis of above provision, the refusal of election officer is valid, as Mr. Aswin doesn't hold one hundred shares.

b)

- i) Indrawati Hydro Company must follow the legal procedures for convening its AGM pursuant to the Companies Act, 2063. The notice must be provided by the proper authority which would normally be the Board of Directors following proper procedures.

Section 67 (2) of the Companies Act, 2063 a general meeting of a public company may be called by providing not less than 21 days prior notice in writing with mentioning the Venue, Date, Time and Agenda, at least two times general notice in the National daily newspaper which is mandatory.

In this case, only one time notice was published, i.e. only on 15th Oct. 2021 calling the meeting will be held on 8th Nov. 2021. At least another notice was not published in any national daily newspaper. So, there is a mistake on the part of this company not to publish another public notice.

So, there is an irregularity committed by the Company for not issuing at least another notice calling for AGM, so it is an invalid AGM.

- ii) Further, only seven percent out of total of the shareholders of the company attended in the meeting. As per the legal provision under Section 73 of the Act, there must be at least three shareholders of the total shareholders representing more than 50 percent out of total distribution of the shares of the company. If the quorum is not fulfilled, then the entire proceedings of the company cannot go ahead by the meeting. It becomes a mistake of procedure for AGM.

In given case, only seven percent were present in the meeting, whereas, as legal provision under Section 73 of the Act provides for a large number at least three

members or shareholders must represent more than fifty percent of total allotted shares in person or by proxy in the case of public company. Therefore, the meeting was invalid for the want of required quorum. Hence, the meeting was against the legal provision, the resolutions so passed were invalid for that reason.

- c) Under Section 110 of the Companies Act, 2063, every company must appoint an auditor to audit its accounts.

Section 111 states different rules as to appointment of auditor. An auditor, from the amongst the auditors registered or licensed under the existing law, can be appointed, in case of a public company, by the General Meeting and in the case of a private company as provided in its MOA, AOA and consensus agreement or by the General Meeting in the absence of such arrangements.

The prime authority to appoint an auditor is general meeting. The company registrar office also performs an appointing authority on the request of Board of Director when there is a failure to appoint an auditor by AGM or AGM could not be held or an auditor appointed as per the Act ceases to hold the office for any reason.

The auditor appointed as such remains in the office until next AGM is held. No auditor or his /her partner or ex-partner or employee or ex-employee shall be appointed as auditor for more than three consecutive terms to perform the audit of a public company.

Solution:

Both candidates are eligible as per law. With regard to the willingness of Mr. A, he can be continued up to three consecutive terms. However, the issue is subject to the approval and consent of the shareholders' general meeting. Further, Mr. B is also eligible to be appointed as an auditor of the said company. He has fulfilled requirement like Mr. A.

Regarding the removal process of an auditor, u/s 119 of the Companies Act, 2063 has mentioned, that, an auditor should be removed after completion of the audit of accounts of such F/Y. Auditor can be removed after fulfilling following conditions.

- When the auditor breaches the code of conduct of auditors or does any act against the interest of the company which has appointed him as the auditor or commits any act contrary to the prevailing law.
 - Auditor may be removed through the same process whereby he/she was appointed as auditor.
 - Prior information should be provided to the Institute of Chartered Accountants of Nepal.
 - Approval should be taken from regulatory authority as provided by the prevailing law. Approval from the office in the time while failing such authority.
 - The auditor should be provided with a reasonable opportunity to defend his/herself.
- d) When a company is incorporated, it is treated as a separate legal person than of its shareholders. This corporate personality can be lifted and the natural person behind it can be made liable where the separate legal existence of company has been used to commit some fraud or misconduct. In other words, the separate legal existence of a company cannot be used as a means to achieve some illegal or fraudulent purposes. The courts will refuse to

uphold the separate existence of the company where it is formed to defeat or circumvent law, to defraud creditors or to avoid legal obligations.

In **Creasey vs. Breachwood Motors Ltd. 1993 BCLC 480**, it has been decided by court that if the takeover of the company's assets had been carried out with an intention to avoid legal duty and as against the interest of its creditors, the court can disregard the separate entity of the company.

In this case, therefore, the transferee company is liable to pay compensation. As being created unjust result to the interest of the plaintiff, Mr. Pradip, the transferee company National Builders Ltd. cannot be treated as a separate legal person than its transferor company Heritage Nepal Pvt. Ltd. It means that the two companies not treated as separate entities but same and single.

2. Answer the following questions:

- a) CA. Jagadishwor Uthak was appointed as statutory auditor for Synergy Bank Ltd. with paid up capital of NRs 10 billion for FY 2077/78. Mr. Uthak holds share of Synergy Bank Ltd. of total amount of NRs. 80 million. After his appointment, a complaint was filed challenging his appointment stating that he should not have been eligible for appointment. Referring to provisions in regard to eligibility of appointment of auditor under Banks and Financial Institution Act, 2073 give your opinion, if Mr. Uthak can be appointed as Statutory Auditor of the Bank. **5**
- b) A new bank with name Fund Finance Limited applied with the Nepal Rastra Bank for the license. However, Nepal Rastra Bank denied issue of license specifying that Fund Finance Limited has no adequate infrastructure to conduct banking or financial transactions. Critically examine the reason of Nepal Rastra Bank for denial of license mentioning the grounds under which Nepal Rastra Bank has power to refuse to issue license under provisions of the BAFIA, 2073. **5**
- c) Bright Bank Ltd. established in 20XX November and commenced financial transactions from 20XX December and need to be formed BoDs. Explain, How the Board of Director of a Banks and Financial Institutions be formed? Explain, the circumstances for ineligibility to remain in the office of Director as per the Banks and Financial Institution Act, 2073. **5**

Answer:

a) **Issue:**

CA. Jagadishwor Uthak is appointed as a statutory auditor of Synergy Bank Ltd. He holds share of total amount of NRs. 80 million out of paid up capital of NRs 10 billion for FY 2077/78. Assessment of the validity of the appointment of CA. Jagadishwor Uthak as a statutory auditor of Synergy Bank Ltd. can be discussed as follows:

Legal Provision:

Section 64 – “Ineligibility for Appointment as Auditor” of Bank and Financial Institution Act, 2073 has mentioned criteria regarding ineligibility of appointment as auditor as follows:

Section 64 subsection (1) states that any of the following persons or any firm, company or institution in which such person is a promoter or partner shall not be eligible to be appointed as an auditor of a bank or financial institution:

- (a) A promoter, Director, Chief Executive of a bank or financial institution or his\her family member,
- (b) An official, employee or internal auditor of the bank or financial institution,
- (c) A person working as a partner of any promoter, Director or employee of the bank or financial institution,
- (d) A borrower of the bank or financial institution, a person with significant ownership or relevant person or person having financial interests,
- (e) A person who has been declared bankrupt in Nepal or abroad,
- (f) A person, firm, company or institution having subscribed one percent or more shares of the bank or financial institution,
- (g) A person, who has been punished in any criminal offense by the court and a period of five years has not been lapsed after he\she has served the punishment,
- (h) A person, who is disqualified to become an auditor according to prevailing laws.

Conclusion:

Mr Pathak owns NRs. 80 million of shares out of total NRs. 10 billion shares of Synergy Bank Ltd. which is 0.8% of total share. His holding of shares is within the threshold of 1%. Hence, CA Jagadishwor Uathak is eligible for appointment as auditor of Synergy Bank Ltd. if he is not disqualified under other points mentioned.

b) Issue:

Nepal Rastra Bank (NRB) denied license to proposed bank Fund Finance Limited on the ground of having no adequate infrastructure to conduct banking or financial transactions. Review on the validity of decision of NRB as per BAFIA, 2073 can be summarize as follows:

Legal Provision:

Section 35 – “Issuance of License may be denied” subsection (1) of BAFIA, 2073 states that notwithstanding anything contained in Section 34 – “License may be granted for carrying out Banking and Financial Transactions”, the Rastra Bank may deny to issue license to operate banking and financial transactions to a bank or financial institution in any of the following circumstances:

- (a) If it causes adverse effects on the stability, fair competition and credibility of the financial system of Nepal,
- (b) If it is not reasonable and appropriate to issue license for operation of financial transaction for protection of interests of depositors,
- (c) If the infrastructure to operate banking and financial transactions are not completed,
- (d) If other particulars or conditions pursuant to this Act are not found to be completed.

Section 35 subsection (2) states that the Rastra Bank shall, in case there is a situation that the license to operate banking and financial transactions could not be issued according to

this Section, inform to the concerned bank or financial institution stating the reasons thereof within ninety days of the date of filing of the application.

Conclusion:

The decision of the NRB to deny issue of license to proposed Fund Finance Limited on ground of inadequate infrastructure to operate banking and financial transactions is valid under BAFIA, 2073.

- c) Section 14 of BAFIA Act, 2073 provides, any bank or financial institution shall have a Board of Directors comprising of at least five Directors and not exceeding seven Directors. Subject to this Act, and the Articles of Association, the General Meeting of the Bank or Financial institution shall appoint Directors.

Provided that, until the first Annual General Meeting of the bank or financial institution is held, promoters shall appoint the directors. In case of the position of any Directors falls vacant before the holding the Annual General Meeting, the Board of Directors may appoint the director for time being.

A Director chosen by the Directors from among themselves by majority decision shall be the Chairperson of the BoDs and any company, corporate body, foreign bank or financial institution which has subscribed shares of the bank or financial institution may, while appointing a director proportionate to the shares as it has subscribed, appoint an Alternate Director to work in absence of the Director.

Section 19 of the BAFIA Act 2073 defines; no person shall be remained in the office of Director of the bank or financial institution in any of the following circumstances:

1. No qualifications meet section 16 or 17 or ineligible under section 18 of the act,
2. The motion to remove from the office of a director is passed by majority of the general meeting
3. Resignation given by a director from him/her position is approved,
4. In case of commission of any act that is not supposed to be committed under this act or directives of Rastra Bank

In case the Rastra Bank directs to remove from the office due to he/she has committed acts against rights and interests of the bank or financial institution or the depositors and since he/she is not competent to carry out works as in the of a director of the bank or financial institution.

3. Answer the following questions: (2×5=10)

- a) Mr. MN, Chairperson of the Securities Board of Nepal was observed to be involved in the activities in contrary to interest of investors in the securities. Government of Nepal wants to remove him from the office. Suggest the government officials elaborating the circumstances of removal of Chairperson of Securities Board of Nepal pursuant to the Securities Act, 2063.
- b) Mr. Radha Krishna Sah was appointed as the Chairperson of the Insurance Board. He as the newly appointed Chairperson asked you to

submit a note on the procedures how the meeting of the Insurance Board is held as per Insurance Act, 2049. Suggest Radha Krishna in this respect.

Answer:

a) Issue:

Mr MN, Chairperson of the Securities Board of Nepal was observed to be involved in the activities in contrary to interest of investors in the securities. Circumstances of removal of Chairperson of Securities Board of Nepal in pursuant to Securities Act, 2063 can be discussed as follows:

Legal Provision:

Section 12 of the Securities Act, 2063 mentions the provision in regard to the circumstances of the removal of chairman or member of the Securities Board of Nepal.

Section 12 subsection (1) states that where there arises a situation for removal of the Chairperson or the member referred to in subsection (2) of this Section, the Government of Nepal shall remove the Chairperson and member, as the case may be.

Provided that prior to making such a removal, the Government of Nepal shall not deprive the concerned person of a reasonable opportunity to defend himself/herself.

Section 12 subsection (2) states that the Chairperson, as the case may be, shall be removed from his or her office in any of the following circumstances:

- (a) If he or she is disqualified to be a chairperson and a member, as the case may be, pursuant to Section 11 – “Disqualification of Chairperson and member”;
- (b) If he/she commits any act contrary to the interest of investors in securities or any act that may cause loss or damage to the development of capital market;
- (c) If he or she suffers from lack of competence to implement, or cause to be implemented, such functions required to be performed by the Board to attain the objectives of the Board pursuant to this Act or the rules framed under this Act;
- (d) If he or she has been held disqualified to carry on any occupation or business by the reason of misconduct and his or her certificate has been revoked or he or she has thus been restricted to carry on a business;
- (e) If he or she remains absent from three consecutive meetings of the Board without giving a notice.

Conclusion:

As, Mr. MN Chairperson of the Securities Board of Nepal was observed to be involved in the activities in contrary to interest of investors in the securities, Government of Nepal shall remove the Chairperson as per Securities Act, 2063. However, Mr. MN shall be provided reasonable opportunity to defend himself before removal.

- b) Section 5 of the Insurance Act 2049 has prescribed procedures for holding meeting and reaching to decision of the Insurance Board. Such procedures of the meeting are as follows:
 - 1. The meeting of the Insurance Board shall be held on the date, time and venue as prescribed by the Chairperson.
 - 2. The meeting of the Insurance Board shall be held at least eight times per year and not less than twice within three months.

3. The meeting of the Insurance Board shall be presided by the Chairperson. In the case of his/her absence, the meeting shall be presided by the person selected from among the Members themselves.
4. The quorum for the meeting of the Insurance Board shall be fulfilled in the presence of fifty percent of the total Members of the Insurance Board.
5. The opinion of majority shall prevail in the meeting of the Insurance Board and in case of tie, the chair person may cast decisive vote.
6. The decision of the Insurance Board shall be certified by the Secretary.
7. Other procedures relating to the meeting of the Insurance Board shall be as determined by the Insurance Board itself.

4. Answer the following questions: (2×5=10)

- a) State and elaborate the types of employment as per the legal provisions prescribed by the Labour Act, 2074.
- b) Industrial Enterprises Act, 2076 has been enacted for the protection and promotion of industrial establishments and also for the promotion of investment with a view to speed up of the industrialization by making the simple policy in Nepal. State the legal provisions regarding the registration and regulation of an industry under the Industrial Enterprises Act, 2076.

Answer:

- a) Section 10 of the Labour Act 2074 prescribes– “Classification of Employment”. It has categorized employment into 5 various types. They are as follows:
 - (1) **Regular employment:** Employment of any type whatever other than that is work-based, time-based and casual employment.
 - (2) **Work-based employment:** Employment that the employer provides or has provided specifying any particular work or service for performance.
 - (3) **Time-based employment:** Employment that the employer provides or has provided to the labour specifying a certain period on the condition that the labour has to provide any service or perform any work within that period.
 - (4) **Casual employment:** Employment that the employer provides or has provided to the labour on the condition that the labour has to provide any service or perform any work, for seven days or less within a period of one month.
 - (5) **Part-time employment:** Employment that the employer provides or has provided to the labour on the condition that the labour has to perform a work in thirty-five hours or less than thirty-five hours in a week.

If there arises a question as to whether any employment is regular or not, it shall be determined as prescribed on the basis of the nature of the work, notwithstanding anything contained in the employment contract.

- b) According to Section 3 of the Act, no one can establish or cause to establish industry or operate it without its registration.

For registration of industry, it has to fulfill all the requirements as similar to the registration of a company, by making an application either manually or online service with required documents and fees. The new enactment permits to make an application by online.

Section 4 of the Act prescribes the process of registration of industry. According to it, an application is to be made for registration of Industry. Under Section 4(1) any person desirous of establishing any industry under the Act, an application is required to be made to the concerned registering office for its registration setting out the nature, documents, and particulars in a prescribed manner. Documents to be attached can be submitted with digital attestation through electronic means.

Section 5 prescribes the provision relating to grant of certificate of registration. According to it, on receipt of the application pursuant to Section 4 for the registration of industry the concerned registering office will, after making necessary examination regarding the compliance of required documents as per Act and regulation thereof, issue certificate of registration as prescribed.

While issuing the certificate of registration in addition to others the registering office is required to mention the following matters:

1. Date of issue of the certificate
2. Date by when the production or the transaction shall be had to be commence
3. The terms and condition to be complied with by the industry
4. Other terms and conditions as prescribed by the registering office as per the nature of the industry

Notwithstanding anything mentioned in sub-section (1) in case of micro enterprise the application for their registration can be made within one year from the date of its operation as per Section 5(3) of Act.

Section 6 prescribes the provision regarding the appeal against the refusal of the registration of industry. According to it, dissatisfied party, pursuant to section 4(7) of the refusal of the registration of the industry by the DOI, may make an appeal with the Ministry of Industry (MOI) within thirty days from the receipt of issue of notice of refusal, and in case refusal by the provincial authority the appeal is to be made with MOI of the concerned province.

Where appeal has been made, the concern appellant authority has to decide the matter after necessary examination against the appeal, within thirty days of the receipt of it. Other process of appeal will be as prescribed.

5. Answer the following questions: (2×5=10)

- a) State the various categories of memberships that the Council of Institute of Chartered Accountants of Nepal offers. Mention a person's credentials to hold such membership under the Nepal Chartered Accountants Act, 2053.
- b) State the legal provisions regarding punishment as prescribed by the Nepal Chartered Accountants Act, 2053?

Answer:

- a) Pursuant to section 16 (1) of the Nepal Chartered Accountants Act 2053, there are two types of membership which are issued by the Council of Institute of Chartered Accountants of Nepal, firstly, chartered accountants and secondly, registered auditor.

The following persons are disqualified to be a member of the ICAN

1. Persons not possessing qualification under sub section 2 & 3 of the section 16 of the Nepal chartered Accountants Act, 2053

2. Persons not attaining the age of 21 years of old
3. Insolvent person
4. Person punished by a competent court on the charge of committing crime of moral turpitude.
5. Person of unsound mind

b) Provisions regarding punishment as provided in the Section 41 of ICAN Act, are as follows:

- (1) A person, who carries out audit without obtaining a Certificate of Practice, pursuant to this Act, shall be liable of punishment with a penalty of maximum two thousand rupees or with an imprisonment for a maximum period of three months or with both.
- (2) A person, who in contravention of Section 6 uses the name or the seal of the Institute or exercises any type of authority bestowed to the Institute, shall be punished with a penalty of one thousand rupees maximum on first conviction, and on any subsequent conviction thereafter, a maximum penalty of five thousand rupees or imprisonment for a maximum period of six months or both.

Provided that this sub-section shall not apply to the organizations or university established under their own legislation or the units within the Institute.

- (3) A person, who has not obtained a Certificate of Practice and is proved to have signed any document in capacity of the member holding Certificate of Practice, shall be liable to punishment with a penalty up to two thousand rupees or imprisonment for a period of up to three months or both.
- (4) A member, who commits any act contrary to the provisions of this Act or Regulations framed under this Act other than the provisions of this section, shall be suspended for a maximum period of five years and shall be liable of punishment with a maximum penalty of two thousand rupees or imprisonment for a maximum period of three months or both.
- (5) A complainant who lodges a complaint, without any reasonable cause to make complaint and it is proved that the complaint was made with an intention to harass a member, shall be liable to punishment with fine up to one thousand rupees.
- (6) The complaint cases, except those to be heard under Section 14, lodged in the Council against any member, pursuant to Section 35, shall be instituted in the concerned Appellate Court.

6. Answer the following questions: (5×4=20)

- a) State the legal provisions regarding the settlement of dispute between the employees and management in respect of bonus payment as per the Bonus Act, 2030.
- b) State the conditions where the Social Welfare Council can suspend or dissolve the executive committee of the social organization.
- c) Mr. 'G' delivered a shopkeeper to repair a watch on the payment of Rs. 100. Subsequently the shopkeeper refused to repair it for the Rs. 100 and also claimed to retain the watch until he is paid for the work done. Decide the right of 'G' by examining the provision of the Nepal Civil Code, 2074.
- d) Mr. 'A' gives a cheque to Mr. 'B' with "not negotiable" crossing. Mr. 'C' steals Mr. B's cheque and gives it to Mr. 'D' for consideration. Mr. 'D' takes the cheque without knowing fact that cheque has been stolen cheque. Suggest Mr. 'D' referring Negotiable Instruments Act, 2034.

- e) Point out the duties of employees regarding the occupational health and safety under the Labour Act, 2074.

Answer:

- a) Section 16 of the Bonus Act 2030 contain the following provisions regarding the settlement of dispute between employee and management regarding bonus payment.

In case any dispute arises between the employee and the management on the issue of bonus to be paid under this Act, the labor office shall resolve such by negotiation having invited both the parties.

In case the dispute fails to be resolved through the negotiation, the labor office may direct the concerned establishment and the employees to submit necessary documents and statement of accounts, the office shall give decision on the basis of such documents and statement of accounts.

Any side which is dissatisfied with the decision taken by the Labor office may appeal to the Labor court within 35 days from the date of receipt of a notice thereof. The decision taken by the Labor court shall be final.

- b) Section 20 of the Social Welfare Council Act, 2049 has authorized the Government of Nepal on the recommendations of the Social Welfare Council to suspend or dissolve the executive committee of those social organizations or institutions affiliated with the council or, receiving economic assistance from the Council, if they do their business against, prevailing laws or their own constitutions. While doing so, a reasonable opportunity, to give their clarification shall be given to the executive committees before their suspension or dissolution.

Similarly, under Sub-section (2) of Section 20 of the Act, the Government of Nepal may constitute an *Ad hoc* committee from the general members of that organization and institution to carry out the business of that organization and institution until the suspension of that organization and institution lifted, when suspended and until the constitution of new executive committee, when dissolved.

Further, Sub-section (3) provides that the *Ad hoc* committee formed pursuant to Sub-section (2) in the condition of dissolution of any social organization and institution, shall constitute new executive committee within the period of three months of its formation, in accordance with the constitution of those organization and institution.

- c)
1. This given problem is related to the Bailment given in the Nepal Civil Code, 2074
 2. The provision lays down that where the bailee has rendered any service involving the exercise of labour /skill in respect of the goods bailed, there he has a right to retain such goods in his possession until he receives due remuneration for the services, he has rendered in respect of them.
 3. This right of bailee is termed as particular lien. This right can be exercised when the services have been performed entirely and the remuneration has become due.
 4. Bailee's particular lien in contracts of service may be lost if he does not complete the work within the agreed time or reasonable time.
 5. Accordingly in the given case, it is clearly expressed by the shopkeeper to repair the watch on the payment of Rs. 100. However, later his refusal to repair the watch, does

not complete the work for which he has promised and therefore, he loses his right to exercise particular lien and nothing could be claimed under it.

6. Thus, the shopkeeper was not entitled to retain the watch.

- d) Section 2 (d) of Negotiable Instrument Act, 2034 defines 'Negotiation' as the act of transfer of negotiable instrument to any person so as to constitute that person the holder thereof. "Not negotiable" crossing does not make negotiable instrument not transferable. Any instrument with "not negotiable" crossing means that it is negotiable until its title is good. Section 89 of Negotiable Instrument Act 2034 make provision regarding Cheque bearing "not negotiable". A person taking a cheque crossed generally or specially bearing in either case the words "not negotiable" shall not have, and shall not be capable of giving a better title to the cheque than that which the person from whom he took it had.

In general rule, a holder in due course obtains better title than the transferor. However, in case of negotiable instrument having "Not negotiable" crossing does not obtain better title than the transferor.

Principle of "*Nemo dat quod non habet*" i.e., "No one can transfer title better than he himself had" is applicable in case of negotiable instrument having "Not negotiable" crossing.

So, in the given case Mr. 'D' is holder in due course, but as the negotiable instrument is having "Not negotiable" crossing he cannot get better title than Mr. 'C'. As Mr. 'C' has no title over the instrument being stolen by him and accordingly Mr. 'D' also does not have title over the instrument.

Person taking the Negotiable Instrument having "Not negotiable" crossing should inquire and assure the title of the transferor over Negotiable Instrument.

- e) Section 73 of the Labour Act, 2074 has imposed the various duties to be followed by the employees to the matter of occupational health and safety. The duties are as under:
1. Not to do such act at the workplace knowingly or recklessly causing adverse effect to safety and health of oneself or others.
 2. To provide necessary help to the employer or concerned person to fulfill the duties stated under this legal provision.
 3. To get directives, advice and other information for the purpose of using or operating safely and cautiously the materials, goods and equipment to be used and operated at the work place.
 4. To operate and use those workplace, materials, goods and equipment safely and carefully as per the directives, advice and other information made for the safety use and handling of the workplace, materials, goods and equipment.
 5. To use the personal safety equipment provided by the employer.

7. Write short notes:

(2×5=10)

- a) Establishment of World Trade Organization (WTO) and its objectives.
- b) State the functions, duties and powers of the Accounting Standard Board pursuant to the Nepal Chartered Accountants Act, 2053.

Answer:

- a) World Trade Organization (WTO) is an international organization established to supervise and liberalize world trade. The WTO is the successor to the General Agreement on Tariffs and Trade (GATT), which was created in 1947. GATT proved remarkably successful in liberalizing world trade. By the late 1980s there were calls for a stronger multilateral organization to monitor trade and resolve trade disputes. Following the completion of the Uruguay Round (1986–94) of multilateral trade negotiations, the World Trade Organization (WTO) began operations on January 1, 1995.

The WTO has six key objectives:

- (1) to set and enforce rules for international trade,
 - (2) to provide a forum for negotiating and monitoring further trade liberalization,
 - (3) to resolve trade disputes,
 - (4) to increase the transparency of decision-making processes,
 - (5) co-operate with other major international economic institutions involved in global economic management, and
 - (6) to help developing countries benefit fully from the global trading system.
- b) The fundamental function, rights and duties of the Accounting Standards Board is to develop accounting standards in order to govern and regulate the financial reporting and accounting profession. Section 15B of the Nepal Chartered Accountants Act, 2053 has prescribed the rights and duties of Accounting Standards Board shall be as follows:
- To develop accounting standards, on the basis of relevant International Accounting Standards, in order to govern and regulate financial reporting and accounting profession.
 - To evolve appropriate process of development of accounting standards and publish material related to accounting standards.
 - To redraft, improvise and revise standards.
 - To interpret the standards.
 - To undertake other related tasks related to accounting standards.

Examiner's Commentary on Students' Performance in December 2021 Examinations

Subject: Advanced Accounting

List of Questions	Specific Comments on the Performance of the Students
Question no. 1	Overall Satisfactory performance.
Question no. 2	Satisfactory performance.
Question no. 3	Lack of Conceptual clarity.
Question no. 4	Satisfactory performance.
Question no. 5	Lack of concept of NFRS provision for answering questions.
Question no. 6	Many students do not know about spread sheet.

Subject: Audit and Assurance

List of Questions	Specific Comments on the Performance of the Students
Question no. 1	Satisfactory performance
Question no. 2	Satisfactory performance
Question no. 3	Other Matter paragraph is not properly understood by the students.
Question no. 4	Poor Performance; weak preparation
Question no. 5	Most of the students were not known about proprietary audit.
Question no. 6	Satisfactory performance
Question no. 7	Students are confused on 7(a) question

Subject: Corporate and Other Laws

List of Questions	Specific Comments on the Performance of the Students
Question no. 1	Satisfactory performance
Question no. 2	Most of the students were confused in calculating % of share and disqualification of directors.
Question no. 3	Satisfactory Performance
Question no. 4	Students failed to answer the registration process for an enterprise as per Industrial Enterprises Act
Question no. 5	Most mistakes were on credentials
Question no. 6	Bailment was not mentioned by most of the students.
Question no. 7	Satisfactory Performance.