AUDITING

Price: ₹150

For users who are benefited, pay to…

Account holder name: Singar Educational and Charitable Trust

Account number: 1262 1150 0000 9481

IFSC code: KVBL0001262

Bank name: Karur Vysya Bank

CALL OR VISIT FOR COPIES

Published by

SINGAR BOOKS AND PUBLICATIONS

Head Office: 32-B, Vivekananda Nagar, Ramalinga Nagar, Woriur, Trichy 620 003, TN

Branch Office: 76/1, New Street, ValluvarKottam High Road,

Nungambakkam, Chennai – 600 034

Ph: Trichy: 93451 22645 | Chennai: 93453 96855

www.singaracademy.in | singaracademy@gmail.com

AUDITING

1: AUDITING CONCEPTS

AUDITING

- The term Auditing has been derived from the Latin word "audire" which means to listen.
- Audit is an**independent examination** of financial information of any entity
- Whether **Profit oriented or not**
- And **irrespective of its size or legal form**
- When such an examination is conducted with a view **to express an Opinion** thereon.

NATURE OF AUDITING

- The Financial statements should be prepared in all material aspects in accordance with applicable **financial reporting framework**
- The accounting data has to be verified with the view to report on the **reliability** of the accounting statements
- Verification of accounting data involves careful **evaluation of evidence** available to the Auditor
- Evidence includes internal and external evidence
- Evidence generated within the entity is known as internal evidence and evidence generated outside the entity is known external evidence
- The information under audit need not be accounting information but it must be in **verifiable form**
- There should be standards for evaluation of Information

SCOPE OF AUDITING

- The Scope of an audit is the determination of the range of the activities and the period of record that are to be subjected to an audit examination
- Earlier audit covers only financial audit but in recent time it includes cost audit, Management Audit, Internal Audit, Energy Audit, GST Audit, Government Audit etc.
- The Auditor should perform the duties which are within the scope of his competence
- He should exercise due diligence and professional care in his work
- Auditing begins where accounting ends

AUDITOR

- The person conducting the Audit is known as the Auditor
- He must be professionally qualified.
- For Ex: Under the Companies Act, 2013 only chartered Accountants who are professionally qualified and possess valid certificate of practice are allowed to conduct the audit of the accounts of the companies

QUALITIES OF A SUCCESSFUL AUDITOR

- Sound knowledge of various disciplines along with audit such as accountancy, mathematics, economics etc.

- As per SA 200 "Basic principles governing an Audit" the auditor must **possess integrity, objectivity and independence** in his approach to the audit work
- Knowledge of the **general principles of the law** governing the auditee enterprise. For Ex: while auditing the company knowledge of the Companies Act, 2013 is necessary
- Understanding of special feature which are **peculiar** to particular business
- **Technical knowledge** backed by basic human qualities
- An auditor must be **honest**, that is, he must not certify what he does not believe to be true and must take reasonable care and skill before he believes that what he certifies is true

DISTINCTION BETWEEN ACCOUNTING AND AUDITING		
	ACCOUNTING	**AUDITING**
i	Collection, classification and summarization of data for preparation of books of accounts, and to make financial statements	Analytical and critical examination of books of accounts, financial records and the financial statements prepared thereon.
ii	Recording of transactions at the time of occurrence	Post mortem examination of recorded transactions
iii	Measures the business events in monetary terms, records them, and communicates the financial results through Financial Statements	Reviews financial records to form an opinion on the authenticity of Financial Statements.
iv	The primary responsibility is of the management towards the shareholders/ owners, to maintain the Financial records in such a manner that Financial Statements can be prepared from the records.	The auditor is an independent person appointed by the business entity to review the Financial Statements and to give his opinion thereon.
v	An accountant is not expected to review/ report on the Financial Statement but to report the compilation of records to the management	An auditor is required to submit a report with his opinion on 'true and fair' assertions made in the Financial Statements to the owners.
vi	An accountant works for/ under the management.	The auditor is an independent person answerable/ liable to the owners/ shareholders and not just to the management
vii	No such liability	In certain circumstances, the auditor could be held liable to third parties also.
viii	Maintenance of accounts may not be mandatory for small individuals or partnership firms, e. g. under section 44AA of the Income Tax Act, but could be mandatory under other laws, e. g. for companies under the Companies	Audit could be exempt for various individuals or small partnerships, e. g. under section 44AB of the Income tax Act, and even in case where maintaining books of accounts is a statutory requirement under section 44AA, but may be mandatory under other laws e. g. for

	Act.	Companies under the companies Act.
ix	Accounting is done as per the principles set by Indian Accounting standards (Ind AS)	Auditing is done as per the principal set in standards on auditing

DISTINCTION BETWEEN AUDIT AND INVESTIGATION			
	BASIS	**AUDIT**	**INVESTIGATION**
i	Definition	Auditing is an independent and systematic examination of the evidence underlying the accounting or other data in accordance with the generally accepted auditing practices to ascertain the true and fair view of the financial statements of an enterprise	An investigation may be defined as an examination of accounts and records with a view to ascertain any fact for some special purpose which varies from assignment to assignment
ii	Scope	The audit has a wide scope. In statutory audit, the scope is determined by the relevant law and in case of a private audit by a client	It is limited as regards the period or areas to be covered.
iii	Objective	ln audit, the accounts and records are verified as to their truth and fairness.	Investigation is for special purpose
iv	Audit Procedure	The audit is conducted in accordance with the generally accepted auditing principle.	Investigations involve an extended auditing procedure.
v	Evidence	An auditor will evaluate the accounting records predominantly based on persuasive evidence.	An investigator can draw his conclusions only on the basis of substantial or sometimes conclusive evidence
vi	Approach	Audit is not suspicious	Starts with suspicion and collects evidence to either confirm or dispel that suspicion.
vii	Periodicity	Auditing is a routine exercise	Investigation may spread over a gap period longer than one year

ASPECTS TO BE COVERED IN AUDIT BY THE AUDITOR

1) Accounting and Internal control system

- Develop an understanding of the accounting and the internal control system operating in the enterprise
- Such understanding will increase the reliance on the information obtained during the Audit
- Review the System from time to time to ascertain its adequacy andcomprehensiveness

2) Examination of Books, Records etc.

- Check the arithmetical accuracy, authenticity and validity of transactions entered into the Books of Accounts
- Ensure that the entries entered in the books of accounts are adequately supported by the underlying papers, documents and other evidence
- None of the entries in the books of accounts should be omitted in the process of compilation and nothing which is not in the books of accounts should be found in financial statements

3) Compliance with the Generally Accepted Accounting Standards and Applicable Statutory Regulations

- The Financial statements should be prepared in accordance with applicable laws, Indian Accounting standards, guidance notes etc.
- For Ex: Proper distinction should be made between items of capital and revenue nature

4) Reporting

- Once the Audit is carried out, the audit findings need to be communicated to the appropriate personal body. Ex – Shareholders in case of company
- An audit report states the opinion of the auditor as to the true and fair view of the financial position and operating results of the enterprise.

OBJECTIVES OF AUDITING

1) Primary objective

- The main objective of an audit is to determine whether the financial statements present a 'true and fair view' of the financial position and financial performance
- The Balance sheet shows the financial position on a particular date and the profit and loss account shows the financial performance of the business over that period
- Section 143 of the companies Act, 2013 requires the auditor of the company to state if in his opinion the financial statement present 'true and fair view' of the state of company's affairs at the end of its financial year

2) Secondary objective

- **Deduct frauds and errors** in the books of accounts and financial records of the client's business.
- Such deduction of frauds and errors is called the secondary objective of the audit
- If the auditor suspects the **presence of material misstatements** or defalcations in the records of the business, he is expected to look into the matter with greater detail by applying various audit procedures to satisfy himself about their existence or non- existence
- He is also to report on the existence of such misstatement and their **magnitude** through his audit report

BASIC PRINCIPLES GOVERNING AUDIT [D18, 6m]

- **Integrity, objectivity and independence**: The auditor should be straight-forward, honest, sincere and free form any influence on his audit work. He should maintain impartiality and be free of any interest.
- **Confidentiality**: - He should not disclose the client's information to anybody without the client's permission or under any regulatory requirement.

- **Skills and competence**: - The audit should be performed and audit report is prepared by adequately trained, experienced and competent person.
- **Work performed by others**: - The auditor should carefully supervise the work performed by others (such as his subordinates, other auditors, experts etc.) as remains responsible for the work delegated by him to his assistants, other auditors or experts.
- **Documentation**: - Proper working papers should be maintained by the auditor to evidence the audit work. Working paper which is maintained is to demonstrate that the audit is in adherence to the basic principles.
- **Planning**: - The auditor should obtain the knowledge about client's business to determine the nature, timing and the extent of the audit procedures.
- **Audit evidence**: - The auditor should obtain sufficient appropriate audit evidence through performing the compliance and substantive procedures.
- **Accounting system and internal controls**: - An understanding of the accounting system and the related internal controls help in determining the nature, timing and extent of other audit procedures.
- **Audit conclusions and reporting**: - On the basis of conclusions drawn from the audit evidence obtained the auditor should give unqualified report or qualified report or adverse report or the disclaimer report.

SIGNIFICANCE OF AUDIT

1) **From Legal Point of View**
    - **Filing of Income Tax return** - Income Tax authorities generally accept the profit and loss account that has been prepared by a qualified auditor
    - **Borrowing of money from external sources**- Money can be borrowed easily on the basis of audited balance sheet from the external sources. Most of the financial institution sanctions various loans on the basis of audited financial statements.
    - **Statement of Insurance Claim**- In case of flood, fire, other natural calamities and the like unexpected happenings the insurance company may settle the claim for loss or damages on the basis of audited accounts of the previous year.
    - **Sales tax payments**- The audited books of accounts may generally be accepted by the sales tax authorities.
    - **Action against bankruptcy**- The audited accounts serve as a basis to determine action in bankruptcy and insolvency cases.

2) **From Internal Control Point of View**
    - **Quick discovery of errors and frauds**- Errors and frauds are located at an early date, so that in future no attempt is made to commit such frauds as one is rather careful not to commit an error or a fraud as the accounts are subject to regular audit.
    - **Moral check on the employees**- The auditing of the accounts keeps the accounts clerks and the accountants regular and vigilant as they know that the auditor would complain against them if the accounts are not prepared upto date or if there is any irregularity.
    - **Advice to the management**- It may happen that the management may consult the auditor and seek advice on certain technical points although it is not the duty of the auditor to give advice.

- **Uniformity in accounts**- If the accounts have been prepared on a uniform basis, accounts of one year can be compared with other years and if there is any discrepancy, the cause may be enquired into.

3) **From External Affairs Point of View**
   - **Settlement of accounts**- The audited accounts would facilitate the settlement of accounts of a deceased partner.
   - **Valuation of assets and goodwill**- If the business is to be sold as a going concern basis, there may not be much difficulty regarding the valuation of assets and goodwill as the accounts have already been audited by an independent person.
   - **Future trend of the business**- From the audited books of accounts, the future trend of the business can be assessed easily with certainty

ADVANTAGES OF AUDIT

- Audit is a tool, which different **stakeholders** can use to protect their interests in the enterprise.
- Audit is not only a corrective measure but has a deterrent effect. It serves as a moral **check on the employees** from committing defalcations or embezzlements.
- The employees of the organisation remain **alert and vigilant** as regards the updating of books of accounts and other records.
- Audited accounts are considered **more reliable** by different cadres of Government. For example, the tax audit report filed with the Taxation authorities.
- It facilitates detection of **wastages and losses and** helps in instituting corrective actions.
- Audited accounts are taken to be more reliable and useful **during corporate restructuring exercises, valuations** etc.
- Banks, Financial Institutions and Government require audited accounts before granting any **financial assistance** to the enterprise.
- Audited accounts are taken to be more helpful in the settlement of accounts between the partners and thus **avoiding any dispute** amongst them

INHERENT LIMITATIONS OF AN AUDIT

An audit does not guarantee that all the material misstatements will be detected because of the following inherent limitations of audit:

a. Test nature of the audit
b. The audit evidence available to the auditor is persuasive rather than conclusive in nature;
c. Inherent limitations of internal control, e.g., certain levels of management may be in a position to override controls.

CONCEPT OF PROFESSIONAL SKEPTICISM

Professional skepticism means an approach that would ensure that **if something is wrong it is detected**. This behavior of auditor helps him in identifying and evaluating

a. matters that increase the risk of **material misstatements** resulting from fraud or error,
b. circumstances that make the auditor to **suspect** material misstatements,

c. the question of management's representations reliability. The auditor is entitled to accept the records and documents as genuine unless there is some evidence to the contrary.

CONCEPT OF TRUE AND FAIR

The concept of true and fair is a fundamental concept in auditing. To ensure trueand fair view, an auditor has to see the following

- That the assets are neither undervalued or overvalued, according to the applicable accounting principles
- No material asset is omitted
- The charge, if any, on assets are disclosed
- Material liability should not be omitted
- The profit and loss account discloses all the matters required to be disclosed by Part II of Schedule III and the balance sheet has been prepared in accordance with part I of Schedule III
- All unusual, exception or non- recurring items have been disclosed separately.

CONCEPT OF "MATERIALITY" IN PLANNING AND PERFORMING THE AUDIT

Materiality is one of the basic fundamental concepts in the process of Accounting and Auditing. It is a continuous process and covers in its ambit all the stages from recording to classification and presentation. An auditor has to constantly judge whether a particular item or transaction is material or not

The main factors to be considered for determining materiality of an item are:

- **Individually**: It may be determined individually. E.g., a payment of ` 1000 may be material in a small business, but even `1 lac could be immaterial for a big business entity.
- **Aggregate**: It may be determined in aggregate. E.g., total income from investment in mutual funds could be more material than looking into each individual investment.
- **Legal Considerations**: It depends on the statutory or legal considerations. E.g., where the terms of appointment of a whole-time director are not according to law, the remuneration paid to him is a material item even if the financial implication is not much.
- **Legal Definition**: It may be defined or described in law itself. E.g., Schedule III requires separate disclosure of items of all expenses exceeding 1% of turnover or to write off capital assets purchased for less than ` 5000.
- **Relative overall impact:** It may depend on the relative degree of relevance to the overall accounts or the group, or class of transactions to which it pertains. E.g., short recoveries from debtors.
- **Qualitative:** It may be qualitative and not often reckoned with respect to quantitative details alone. E.g., improper disclosure of an accounting policy in the Notes to the Annual Financial Statements may affect economic decisions.
- **Insignificant quantity but special context**: It maybe of an insignificant quantity otherwise, but material in special circumstances. E.g., rounding off to the nearest rupee the fraction of 0.666 as 0.67 in computer software. It may be material in future due to cumulative effect even if insignificant now.

FUNDAMENTAL ACCOUNTING ASSUMPTIONS

1) **Going Concern**
   - It means that the enterprise has an intention to carry on its operations for the foreseeable future (i.e., coming 1 or 2 years).
   - There is no intention on the part of the enterprise to discontinue the business nor has any need arisen as to the liquidation of the organisation.
   - It is because of this fundamental assumption that depreciation etc. is provided in the books of accounts.
2) **Consistency**
   - Accounting policies are followed on consistent basis from one period to another. For example, ABC Ltd. values its inventory on FIFO basis.
   - The same basis of valuation is adopted in subsequent year also as per the Principle of consistency.
3) **Accrual**
   - Revenues and cost are accrued, i.e., they are recognised when they are earned or incurred.
   - Actual receipt or payment is not necessary. In other words, the accounts are maintained on 'mercantile system' only

DISCLOSURE OF ACCOUNTING POLICIES

- Accounting policies refer to the specific accounting principles and the methods of applying those principles adopted by the enterprise in the preparation and presentation of the financial statements
- Adequate disclosure of accounting policies is very necessary so that the view presented in the financial statements can be apprehended by the users of the financial statements.
- The Institute of Chartered Accountants of India (ICAI-CA) has issued AS-1 on Disclosure of Accounting Policies in this regard.
- The purpose of this Accounting Standard is to promote better understanding of the financial statements by laying down the principles as to the manner of disclosure of accounting policies.

AREAS WHERE DIFFERENT ACCOUNTING POLICIES MAY BE FOLLOWED

- Valuation of inventories - First in First Out (FIFO), Weighted Average, Last in First Out (LIFO) method
- Methods of providing depreciation -Straight Line, WDV
- Conversion of foreign currency items -Average rate, TT rate
- Treatment of retirement benefits
- Expenditure during the construction period
- Government grants, etc.

FACTORS DECIDING ACCOUNTING POLICIES

1) Prudence
   - It states to 'provide for all losses and anticipate no profits.'
   - At the time of preparation of financial statements, the preparer may face various uncertainties, for example, as to recoverability of receivables, warranty claims etc.

- Thus, estimates are made for uncertainties and provided for in the books of accounts. For example, provision for bad and doubtful debts.

2) Substance over Form

- The transaction should be accounted for in accordance with its actual happening and the economic reliability.
- The legal form is not relevant. For example, in case of hire purchase transaction, the assets purchased under hire purchase are shown under the asset side of the balance sheet of the hire purchaser even though he is not the legal owner.
- The reason being the ultimately the legal ownership of the asset would be transferred to the hire purchaser.

3) **Materiality**

- Financial statements should disclose all the items and facts which are sufficient enough to influence the decisions of the user of the financial statements

AUDITOR'S ENGAGEMENT [J17, 2+6m]

- In case of a statutory audit the objective and scope of an audit is clearly described in the relevant law.
- However, in a non-statutory audit it has to be stated with absolute clarity so as to avoid any kind of ambiguity as to the objective and scope of audit. A misunderstanding may arise about the exact scope of the work

CONTENTS OF AUDIT ENGAGEMENT LETTER

- The objective and the scope of the engagement.
- Management's responsibility for the financial statements.
- The existence of inherent limitations of audit and resulting material misstatements that may remain undiscovered
- The need for use of services of internal auditors and/ or other experts that may arise during the course of the engagement.
- The requirement of management confirmation letter as regards representations made by them concerning audit.
- Restriction of the auditor's liability, if any.
- Basis for computation of audit fees and billing arrangements.
- The form of reports or other communication of results of the engagement.

ADVANTAGES OF AUDITING FOR SOLE PROPRIETORS

- It evaluates the internal control system and strengthens it by removing weaknesses, if any.
- It increases the reliability and authenticity of Financial Statements.
- It helps in timely finalization of Annual Financial Statements and tax assessments.
- It keeps a moral check on the working of employees.
- It helps them in obtaining funds easily from financial institutions, based on more reliable Financial Statements available to the banks and financial institutions.
- It helps in settling: - Trade disputes - Labour disputes - Insurance claims

ADVANTAGES OF AUDITING FOR PARTNERSHIP FIRMS

- It helps in settlement of accounts among the partners on the basis of more reliable accounting records.
- It protects the interest of minors, sleeping partners/partners who are not involved in day-to-day operations, and keeps a check on persons who are working on behalf of others.
- It helps in partnership firms for settlement of goodwill at the time of admission, retirement and death of partners.
- It enables firm to get loans from banks, financial institutions as they rely on audited accounts of firm.
- Due to these advantages, even the entities which are not under any statutory obligation of statutory audit get their accounts voluntarily audited to get the underlying benefits.

STATUTORY AUDIT

- Statutory audit is the checking of accounts as required by law and mandatory in nature
- A statute or law may require having an annual audit of financial records of a company or any other entity.
- The law may require the audit to be conducted in the specified manner.
- The manner of reporting, contents of the report and the authority to which the report of auditors should be presented are all specified by the statute.
- The statutory auditor is generally the principal auditor in an organization.
- In the case of companies, the Companies Act, 2013 governs the audit of accounts, its reporting, and manner of preparing the audit report.
- In the case of audit of a government body, the scope and audit programmes are set by the Comptroller and Auditor General (CAG) of India and the Companies Act, 2013.
- In the case of audit of an insurance company or a nationalized bank, the audit is governed by specific statutes and IRDAI/RBI (Insurance regulatory & Development Authority of India & Reserve Bank of India) guidelines.
- Co-operative banks are also governed by the Co-operative Societies Act, 1912.
- A statutory audit should be performed by a qualified Chartered Accountant holding a valid Certificate of Practice (COP) and not by any other person.

ADVANTAGES OF STATUTORY AUDIT

- The members/shareholders/stakeholders, for their economic decisions and for exercising their voting rights.
- For timely tax assessments.
- For determining the purchase or sale consideration in case of ongoing concern.
- Settlement of partners' accounts in case of admission, retirement or death of partner on account of goodwill or otherwise.
- Before the court, in case of settlement of disputes with employees, creditors or debtors.
- For determining the actual value of business or shares in case of merger, acquisition, etc.
- For getting financial assistance from financial institutions, banks or investors.
- In case of non-profit organizations, for getting government grants and availing tax exemptions.
- Evaluation of the internal control systems and strengthening it by removing the inherent weaknesses, and checking the efficacy of the internal checks.

- For other users of financial statements like creditors, investors and government agencies, it ensures that any assertions in the Financial Statements are neither overstated/understated nor misrepresented.
- For the proper distribution of profits by way of payment of wages and other benefits.
- For ensuring of proper distribution of profits as dividends.
- For ensuring that all legal requirements are fulfilled and statutory compliances are adhered.
- For settlement of insurance claims or other recoveries from government bodies or otherwise

GOVERMENT AUDIT

- Government auditing is the objective, systematic, professional and independent examination of financial, administrative and other operations of a **public entity** for the purpose of evaluating and verifying them
- Presenting a report containing comments, conclusions, and recommendations and expressing the appropriate professional opinion in respect of financial statements.

Authorization:

The Comptroller & Auditor General (CAG) of India is the Supreme Audit Institution.

Types of Government Audit

a. **Transaction audit**i. Expenditure Audit ii. Receipts Audit

b. Efficiency cum Performance Audit

Expenditure Audit: The basic standards set for audit of expenditure are to ensure that there is provision of funds authorized by competent authority fixing the limits within which expenditure can be incurred. Some standards are briefly explained below;

i) Audit against Rules & Orders:

- It is also known as Regularity Audit.
- Under this, the auditor has to see that the expenditure incurred conforms to the relevant provisions of the statutory enactment
- It should be in accordance with the financial rules and orders framed by the competent authority.

ii) Audit of Sanctions:

- The auditor has to ensure that each item of expenditure is covered by a sanction, either general or special, accorded by the competent authority, authorizing such expenditure.
- In case expenditure exceeds the sanctioned limit, objection is raised.

iii) Audit against Provision of Funds:

It contemplates that there is a provision of funds out of which expenditure can be incurred and the amount of such expenditure does not exceed the sanctioned amount as well as examine whether the money has been spent for the specified purpose.

iv) Audit of financial propriety:

The auditor has to ensure that the expenditure incurred are with respect to the recognized standards of financial propriety i.e**., quantity, quality, morality and ethics**

DIFFERENCE BETWEEN PRIVATE AUDIT AND STATUTORY AUDIT [J17, 4m], [D18, 4m]			
	BASIS	**PRIVATE AUDIT**	**STATUTORY AUDIT**
I	**Appointing authority**	Discretionary for the management	Mandatory and prescribed by different statute/ laws
ii	**Object**	Review of internal controls, checks on employees, & Checking financial or non-financial operations.	Ensure truthfulness and fairness of the Financial Statements
iii	**Approach**	Proprietary oriented approach.	Compliance oriented approach.
iv	**Scope**	Decided by the management	Scope is prescribed by the governing law
v	**Report**	Report is to be given to the management within the stipulated time as mutually decided. However, there is no specific format for report	Report is to be given to the shareholder or owner within the stipulated time as stated by the statue as per the format prescribe by the Law

DIFFERENCE BETWEEN STATUTORY AUDIT AND GOVERNMENT AUDIT			
	BASIS	**STATUTORY AUDIT**	**GOVERNMENT AUDIT**
I	**Applicability**	All private companies. All co-operative societies Proprietorship and partnership concerns in some cases. E.g., Tax audit under section 44AB of the Income Tax Act, 1961.	Government departments, Statutory corporations, Government companies
Ii	**Appointing authority**	a. In case of private companies: shareholders. b. In case of sole proprietor and partnership: proprietor or partners. c. In case of trust: trustee or Managing Committee. d. In case of co-operative societies: Managing Committee with prior approval of the Registrar	a. In case of government departments: Comptroller and Auditor General **b.** In case of statutory corporation: as per the provisions of the special statute for that corporation. **c.** In case of government company: Company Law Board, on the advice of the Comptroller and Auditor General
Iii	**Report**	Report is submitted to the owners/ shareholders in a format prescribed by the Companies Act, 2013, in the case of Companies	Report is submitted to the shareholders and a copy is given to the Comptroller and Auditor General in a format prescribed by the CAG.

INDEPENDENT FINANCIAL AUDIT

- An independent financial audit may be conducted by a qualified auditor at the request of a client, which may be a sole-proprietorship, partnership, non-profit organization or any other entity.
- Its objective is to comment on the truthfulness and fairness of the Financial Statements, and it may be compulsory under some Acts which govern the entity

INTERNAL AUDIT

- It is an independent management function
- It involves a continuous and critical appraisal of the functioning of entity with a view to suggest improvements, add value and strengthen the overall governance mechanism of the entity
- It provides assurance that there is transparency in reporting, a part of good governance".
- It ensures objectivity and consultation which enhances the value and improves an organization's operations.
- It not only includes matters related to finance but also critical appraisal of the policies and procedures of the company.
- Internal Audit is based on principle of "early detection & prevention of further damage".
- It points out irregularities, non-compliances timely and not after year end as in case of Statutory Audit. It believes that "prevention is better than cure".

FORENSIC AUDIT

- Forensic audit involves examination of legalities by blending the techniques of propriety audit, regularity, investigative and financial audits.
- The objective is to find out whether or not true business value has been reflected in the Financial Statements and in the course of examination to find whether any fraud has taken place.
- Major accounting scandals involving Enron, Worldtel, Parmalat and Satyam have been widely reported.
- In all these cases, the methods and purpose of manipulations in the Financial Statements were peculiar to the motives of such manipulations.
- The Companies (Auditors' Report) Order, 2016, requires auditors to report, amongst others, "whether any fraud on or by the company has been noticed or reported during the year. If yes, the nature and the amount involved are to be indicated". In this background, the techniques of forensic auditing have gained importance.

SOCIAL AUDIT

- Organizations, these days, focus on attaining economic growth through performing processes that ensure social and environmental development simultaneously.
- A social audit is a way of measuring, understanding, reporting and improving an organization's performance towards meeting its social and ethical objectives.

OBJECTIVES OF SOCIAL AUDIT

- Assessing the needs of the society and resources available for fulfilling them.

- Spreading awareness among beneficiaries about the business efforts towards attaining social objectives.
- Increasing efficiency and effectiveness of the organization's Corporate Social Responsibility (CSR) programmes.
- Scrutiny of policy decisions, keeping in view the interests of stakeholders.

ADVANTAGES OF SOCIAL AUDIT

- Encourages community participation among different business entities.
- Ensures continuous efforts towards environmental protection and use of environment friendly production processes.
- Builds customer satisfaction and trust through ethical business practices.
- Promotes collective decision making and sharing responsibilities.
- Develops human resources by working towards improvement of workers' and the underprivileged persons' working/ living conditions

ENVIRONMENTAL AUDIT

- It is a systematic, documented, periodic and objective review by a regulated entity of facility operations and practices related to meeting environmental requirements."
- It protects environment from pollution of Air, Water, and Earth etc.

SCOPE AND OBJECT OF ENVIRONMENTAL AUDIT

- All emissions to air, land and water
- Legal constraints
- The effects on the neighbouring community, landscape and ecology
- The public's perception of the operating company in the local area
- It provides expert opinion on hazards in the environment
- Associated risks
- The measures that may need to be taken for the management and control of risks.

DIFFERENT STEPS OF AN ENVIRONMENTAL AUDIT

1. **Pre-audit activities:**
    - Selection and scheduling of facility to audit.
    - Selection of audit team.
    - Contact with facility.
    - Planning of the audit.
2. **Site activities**:
    - Understanding of internal controls.
    - Assessment of internal controls.
    - Gathering of audit evidence.
    - Evaluation of audit findings.
    - Report of findings to facility.
3. **Post audit activities:**
    - Production of a draft report

- Production of a final report.
- Preparation and implementation of an action plan.

EFFICIENCY – CUM- PERFORMANCE AUDIT

- It is an examination of the financial and operational performance of an entity.
- It includes identification of opportunities of greater economy as well as removal of weaknesses after evaluation.
- Actual performance is compared with the standards set by the entity.
- If the auditor at the time of evaluation comes across any deviations with respect to the pre-determined standards, it is further investigated.

SCOPE OF EPA

1. **ECONOMY AUDIT**
    - It ensures that entity has acquired the financial, human and physical resources economically.
    - It implies that resources have been procured in appropriate quantity, quality and at minimum cost
2. **EFFICIENCY AUDIT**
    - It ensures the economical execution of various schemes and policies.
    - It refers to the relationship **between inputs and output** i.e., the goods and services produced and resources used to produce them, yielding the expected results
3. **EFFECTIVENESS AUDIT**
    - It is an appraisal of the performance of schemes and projects with reference to the overall targeted objectives as well as efficiency of the way's methods adopted for the **attainment of objectives.**

PROPRIETY AUDIT

- A propriety audit is not just concerned with the truthfulness and fairness of the Financial Statements and books of accounts of the client, but also ensures that the transactions entered into by the client, business practices and activities undertaken are **not against public interest**.
- Its objective is to see that the business lives upto standards of proper conduct.
- Legal, economic and financial are all equally important aspects that require to be looked into during the course of the audit.
- It is an essential element of a Government Audit.
- The Comptroller and Auditor General (CAG) examines the propriety of all government expenditures to ensure that they have been incurred in the interest of the general public, and are not influenced by personal interests of the government authorities sanctioning it.
- Section 143 of the Companies Act, 2013 requires the auditor to look into some specified matters to ensure that the Directors of the company do not engage in misappropriationof funds.

OPERATIONAL AUDIT

Operational Audit involves examination of all the operations and activities of the entity under audit.

OBJECTIVE

- The examination of the control structure of the entity.
- The relation of **department controls** to general policies and its relation with control of other departments.
- It provides an appraisal of whether the department is operating in conformity with prescribed standards and procedures lay down by the management.
- It checks whether standards of efficiency and economy are maintained.
- It is concerned with formulation of plans and checking of the implementation of systems and controls in respect of other departments of the entity.
- It checks whether **capacity utilization** in production department and achievement of short-term targets in marketing departments and other activities are so economically performed to achieve the pre-set overall goals of the entity

ADVANTAGES

- Operational audit is one of the management tools to get first-hand information.
- It is more useful in an entity where **the management is at a distance from actual operations.**
- It is very useful in large organizations where management cannot control the actual operations due to layers of delegation of responsibility.
- The management information system has various tools like routine performance report from department heads, internal audit reports, surprise checks, periodic inspections and investigation to control the managers responsible for their departments.
- The operational audit is also one of the tools used in large or geographically vast entities to control the operation at first stage and to fill up the gaps of information provided by department heads through periodic reports

CONTINUOUS AUDIT

- A method used to perform control and risk assessments automatically on a more frequent basis.
- Continuous auditing changes the audit paradigm from periodic reviews of a sample of transactions to ongoing audit testing of **100 percent of transactions.**
- Continuous audit may be defined as the examination and verification of a firm's financial transactions and their supporting documents, continuously throughout the year, at regular or irregular intervals.
- A continuous audit driven system generates alarm triggers that provide advance notice about anomalies and errors detected by the system.
- It is performed usually by the firm's internal auditors to eliminate the year-end workload.

THE BASIC FEATURES OF CONTINUOUS AUDIT

- It is a process conducted throughout the year.
- It is conducted at regular or irregular intervals.
- It focuses on testing 100% of transactions.
- Technology is important to enable it.
- It provides advance notice about errors and irregularities detected.
- Surprise visits by the auditor are involved.

NECESSASITY OF CONTINUOUS AUDIT

- Internal controls are inadequate.
- The transactions run in large numbers.
- The management is interested in getting statements of accounts audited periodically for enabling better management of resources.

ADVANTAGES OF CONTINUOUS AUDIT

- **Early location of errors and frauds**: It helps in detecting errors and frauds immediately on their occurrence, and not at the year end when it would become difficult to install corrective control mechanisms.
- **Quick rectification**: rectification of errors at an early stage is possible.
- **Guidance**: Continuous guidance to client.
- **Finalizations of accounts completion in time:** Just at the end of the accounting period.
- **Moral check:** Make employees of the client alert and more efficient in conducting their work.
- **Improves statutory auditor's focus:** It relieves statutory auditors of routine testing and allows them to focus efforts on more valuable activities.

DISADVANTAGES OF CONTINUOUS AUDIT

- The records and figures in the books of accounts, which have already been checked by the auditor, may be altered after the audit is over.
- Frequent visits made by the auditor may cause inconvenience at times inconvenient at work.
- The client may suffer due to the clash of duties between his staff and that of the auditor clash of work.
- It is more expensive because the auditor has to devote more time to this audit.
- The work of audit becomes too mechanical and repetitive work.

INFORMATION SYSTEMS AUDIT [D19, 4m]

Information systems auditing is an organizational function that evaluates asset safeguarding, data integrity, system effectiveness, and system efficiency in computer-based information system. It has arisen for seven major reasons:

- The consequences of losing the data resource
- The possibility of misallocating resources because of decision based on incorrect data or decision rules
- The possibility of computer abuse if computer systems are not controlled
- The high value of computer hardware, software, and personnel
- The high costs of computer error
- The need to maintain the privacy of individual persons
- The need to control the evolutionary use of computers.

FINAL AUDIT

Final Audit is conducted at the end of the accounting year, after the books of accounts have been closed.

PROCEDURE

- It does not interrupt with the regular functioning of the client's accounting or operations functions and ensures completion of work in one session due to continuity.
- The auditor may use statistical sampling methods and techniques which lead to time effectiveness.
- The possibility of tampering with the books of accounts during the audit is considerably reduced as the audit work starts only after the books are closed.

LIMITATIONS AND PRECAUTIONS

- A major disadvantage of annual audit is that all the errors and frauds are found at the end of the accounting year, which makes it very difficult to fix responsibility for defalcations.
- It delays the presentation of Audited Financial Statements to the shareholders and to prevent the delay, the auditor uses sample testing, which also reduces the possibility of detection of frauds and errors.

INTERIM AUDIT

- Interim audit is an audit conducted between two annual audits.
- It may be conducted for a specific period, such as a quarter or half year, with an interim object of declaration of interim dividend or valuation of shares on a certain date, in case of mergers.
- It is carried out by professionals, but has no legal status as the figures may be altered subsequently.

USE OF INTERIM AUDIT

- Early detection and rectification of errors & frauds
- Publishing of interim results in some cases
- Timely completion of records and final audit
- Moral checks on employees

BALANCE SHEET AUDIT

- It is generally synonymous with statutory audit.
- The auditor reviews and critically examines the Financial Statements, which include the Balance Sheet and Profit & Loss Account prepared by the management.
- He verifies each assertion in the Financial Statements, working backwards and checking through original entries made in the books of accounts and evidences to support the entries recorded

OBJECTIVE

- While conducting a balance sheet audit, the auditor can rely upon the system of internal controls and internal checks and also on the reports of the internal auditor.
- Wherever internal controls and checks are sound, he can reduce the extent of routine checking of vouching, posting, casting and other routine tests.
- However, he should increase the extent of checking to obtain audit assurance if he finds that there are weaknesses in the internal control systems.

PROCEDURE

- For identification of areas where sample testing is sufficient.
- For performance of certain compliance procedures and substantive procedures in some areas.
- For analytical review of Financial Statements.
- For verification of assets and liabilities stated in the Financial Statements.
- For scrutiny of books of accounts to check whether Financial Statements are in conformity with the records.
- For evaluation of the internal control system and critical examination of the assertions made in the Financial Statements.
- For ensuring the compliance of all legal requirements relating to adequate disclosure of material facts in the Financial Statements

ADVANTAGES OF BALANCE SHEET AUDIT

Balance sheet audit commences after the completion of books of accounts.

- The management prepares the Balance Sheet, therefore changes in the accounts is not possible once the verification process is started.
- No interruption in the accounts department.
- Checking can be done smoothly without any breaks in between.
- No loose links because audit is conducted in a continuous flow, which reduces the chances of missing the verification of any aspect
- Sample tests reduce the time involved for routine checking. The saving on account of time results in cost effectiveness

COMPLETE AUDIT

- A complete audit is an audit where the scope of audit is not confined to specific limits, which may be set by the management or any other authority.
- The auditor is required to check all the possible aspects of a business, including manufacturing operations, data flow processes, accounting records and procedures, etc.
- In general business practices, it is not feasible to get a complete audit conducted

PARTIAL AUDIT

- A partial audit is a non-statutory audit, which restricts the scope of the auditor to checking of certain specific aspects only.
- The auditor’s powers to enquiry are restricted by his terms of engagement.
- He may not be allowed to obtain information which falls outside the purview of the scope defined for him.
- E.g., an auditor may be appointed to check the accuracy of recording of transactions relating to cash sales, or he may be appointed to conduct an audit for the month of Diwali only.

DETAILED AUDIT

- Detailed audit is also known as audit-in-depth.

- It involves checking of transactions from the time of their recording till their final effect on the Financial Statements.

Every stage that a transaction goes through in the accounting process is closely examined by the auditor using various audit evidences.

2: STANDARDS ON AUDITING

AUDIT PROGRAMME [SA – 300 AUDIT PLANNING] [J19, 1M]

- It is a detailed plan of the auditing work to be performed
- Specifying the procedures to be followed
- In verification of each item and the financial statements
- And the estimated time required

CATEGORIES OF AUDIT PROGRAMME

1. Programme common to all types of audit. For example, checking of books of accounts
2. Special programme containing the work relating to a particular audit. For example, the audit programme for a partnership firm would be different from that of a company

ADVANTAGES OF AUDIT PROGRAMME [J19, 5M]

1. It serves as a ready check list of audit procedures to be performed.
2. The audit work can be properly allocated to the audit assistants or the article clerks.
3. The auditor may easily know the extent of work done at any point of time. Thus, the progress of work done can be under the supervision and control of the auditor.
4. Accounts for the individual responsibilities.
5. A uniformity of the work can be attained as the same programme would be followed from time to time.
6. It is a useful basis for planning the programme for the following year it is useful in selection of team members & delegation of responsibilities to them.
7. It may be used as evidence by the auditor in the event when any charge is brought against him.

DISADVANTAGES OF AUDIT PROGRAMME

1. The auditor's task becomes mechanical and the auditors may lose interest and initiative.
2. Drawing up of an audit programme may be unnecessary for a small concern.
3. Though audit programme helps in fixing responsibilities but inefficient staff may defend themselves by stating that the matter was not contained in the audit programme.
4. Rigid programmes cannot be laid down for each type of business.

AUDIT WORKING PAPERS [SA 230 – AUDIT DOCUMENTATION]

- These are the record of the planning and execution of the audit engagement
- The audit working papers for the current year are referred to as the current working papers.
- Working papers that are relevant to more than one audit engagement are referred to as permanent working papers.

PURPOSE OF WORKING PAPERS

- Aid in planning and performance of the audit;
- Aid in supervision and review of the audit work
- These papers serve as an evidence of the audit work performed by the auditor to support his opinion.

MATTERS THAT AFFECT AUDIT WORKING PAPERS

- nature of engagement
- form of audit report
- nature and complexity of client's business
- nature and condition of client's records
- degree of reliance of internal controls
- supervision of work performed by assistants

TYPES OF WORKING PAPER FILES

- Working papers files are classified into permanent audit files and current audit files
- Permanent audit file contains the Information of continuing importance
- Current audit file contains information relating to audit of a single period.

DISTINCTION BETWEEN PERMANENT AND CURRENT AUDIT FILE [J18, 6M]		
	PERMANENT AUDIT FILE	**CURRENT AUDIT FILE**
1	Legal and organizational structure of the entity, e.g., Memorandum of Association and Article of Association in case of a company.	Correspondence relating to acceptance of annual reappointment.
2	Extracts or copies of legal documents, agreements and minutes relevant to the audit.	Extracts of important matters in the minutes of Board Meetings and General Meetings relevant to the audit
3	A record of study and evaluation of internal controls	Copies of management letters.
4	Analysis of significant ratios & trends.	Analysis of transactions and balances
5	Copies of the audited financial statements of previous year(s)	Copies of communication with other auditors, experts and third parties
6	Notes regarding significant accounting policies.	Audit programme
7	Significant audit observations of the earlier years	Conclusions reached on significant aspects of audit

OWNERSHIP OF WORKING PAPERS

- Working papers are the property of the auditor
- The portions or extracts of which can be had at his discretion.

- These working papers should be kept in safe custody and in confidential manner for such time as is sufficient to meet the requirements of his practice or to satisfy any related legal or professional requirement of record retention.
- However, if required by some legislation, the auditor has to make working papers available to the regulatory authority
- ICAI has prescribed that the members have to retain the working papers for a period of **7 years** otherwise; the member is guilty of professional misconduct.

AUDIT NOTE BOOK

- An audit book is usually a bound book in which a large variety of maters observed during the course of audit are recorded.
- The audit note book is a permanent record of the auditor.
- For each individual audit, the auditor usually maintains a separate audit note book.
- The audit note book should be maintained clearly, completely and systematically.
- An audit note book is a great evidential tool available as a defence with the auditors in the event of any charge is brought against them.

CONTENTS OF AUDIT NOTE BOOK

1. Name of the business enterprise.
2. Organisation structure.
3. Important provisions of Memorandum of Association (MOA) and Articles of Association (AOA).
4. Communication with the previous auditor, if any.
5. Management representations and instructions.
6. List of books of accounts maintained by the enterprise
7. Accounting methods, internal control systems followed by the enterprise, applicable laws etc.
8. Key managerial personnel.
9. Errors and fraud discovered.
10. Matters requiring explanations or clarifications.
11. Special points that need attention in the audit report.

AUDIT RISK

- "Audit risk" is the risk that the auditor gives an inappropriate audit opinion when the financial statements are materially misstated.
- There is always some risk of material misstatement due to the limitations inherent in both accounting and auditing
- Such misstatements can result from either fraud or error.
    1. **Inherent risk** – It is the susceptibility of an account balance or class of transaction to misstatements that could be material, either individually or when taken together with misstatements in other balance or classes, assuming that there were **no internal controls.**
    2. **Control risk-** It is the risk that misstatement, that could occur in an account balance or class of transactions and that could be material, either individually or when taken together with misstatements in other balances or classes, **will not be prevented/detected/corrected on timely basis by the accounting and internal control systems.**

3. **Detection risk** -It is the risk that an auditor's substantive procedures (the procedures designed to obtain evidence as to the completeness, accuracy and validity of the data produced by the accounting system) **will not detect a misstatement** that exists in account balance or class of transactions that could be material, either individually or when taken together with misstatements in other balances or classes

SURPRISE CHECKS

1. Auditor and his staff have to visit the client's place for carrying out the audit.
2. Normally, the visit is given to understand the accounting system, to evaluate the system of internal controls, stock taking etc.
3. It is well accepted that the audit constitutes a moral check on the employees of the client and thus have a deterrent effect.
4. But at the same time, if the auditor or his staff visits at regular intervals, the client or his staff may get time to be well prepared in advance for the audit queries. This may impair the deterrent effect.
5. Thus, there is a need of element of surprise.
6. An element of surprise can significantly improve the effectiveness of an audit and therefore, wherever practicable, an element of surprise should be incorporated into the audit programme.
7. The Council of ICAI has made the following recommendations in this regard:
   - Surprise checks should be considered as a desirable part of each audit.
   - The areas over which surprise checks should be employed would depend upon the circumstances of each audit but should normally include
     - Verification of cash and investments.
     - Test verification of stores and stocks and the records relating thereto.
     - Verification of books of prime entry and statutory registers normally required to be examined for the purposes of audit.
   - The frequency of surprise checks may be determined by the auditor in the circumstances of each audit but should normally be **at least once** in the course of an audit.
   - The results of the surprise checks should be communicated to the management if they reveal weakness in the internal control system or the existence of fraud or error.
   - The auditor should satisfy himself that adequate action is taken by the management on the matters communicated by him.
   - The results of surprise checks should be included in the audit report if they are material and affect the true and fair view of the accounts on which the reporting is done.

AUDIT EVIDENCE [SA – 500]

- The auditor comes across various assertions of the management while auditing.
- The auditor has to evaluate these assertions so that he would be able to express his opinion on the financial statements.
- These facts and reasons are called Audit Evidence
- The auditor should evaluate whether he has obtained **sufficient appropriate** audit evidence so that reasonable conclusions can be drawn there from.
- Sufficiency refers to **the quantum of audit evidence** obtained and appropriateness relates to its **relevance and reliability**.
- The following factors influence auditor's judgement while obtaining audit evidence:

- the nature of the item
- the adequacy of internal controls
- the nature and size of the business carried on by the entity
- Situations which may exert an unusual influence on the management
- The financial position of the entity
- The materiality
- of the item
- The experience gained during the previous audits
- The results of auditing procedures, including fraud or error which may have been found
- The type of information available
- The trend indicated by accounting ratios and analysis.

NEED FOR AUDIT EVIDENCE

- Audit evidence provides the auditor a reasonable assurance in respect of the assertions made by the management.
- While obtaining evidence through substantive procedures, the different assertions made by the management can be as follows
  - **Existence –** that an asset or a liability exists at a given date
  - **Rights and Obligations** - that an asset is a right of the entity and a liability is an obligation of the entity at a given date
  - **Occurrence** -that a transaction or event took place which pertains to the entity during the relevant period
  - **Valuation** - that an asset or liability is recorded at an appropriate carrying value
  - **Measurement** -that a transaction is recorded in the proper amount and revenue or expense is allocated to the proper period
  - **Presentation and Disclosure** - an item is disclosed, classified and described in accordance with recognized accounting policies and practices and relevant statutory requirements, if any.

  While obtaining evidence through compliance procedures, the different assertions made by the management can be as follows:

  - **Existence** -that the internal controls exist
  - **Effectiveness** - that the internal controls are operating effectively
  - **Continuity** - that the internal controls have been so operated throughout the period of intended reliance.

RELIABILITY OF AUDIT EVIDENCE [D17, 3M]

- The reliability of audit evidence depends on **its source - internal or external** and on its **nature - visual, documentary or oral.**
- While the reliability of audit evidence is dependent on the circumstances under which it is obtained, the following generalizations may be useful in assessing the reliability of audit evidence:
  - External evidence (e.g., confirmation received from a third party) is generally more reliable than internal evidence
  - Internal evidence is more reliable when related internal control is satisfactory

- Evidence in the form of documents and written representation is usually more reliable than oral representations
- Evidence obtained by the auditor himself is more reliable than that obtained through the entity

METHODS TO OBTAIN AUDIT EVIDENCE [D17, 5M& D18, 6M]

Auditor obtains evidence in performing **compliance** and **substantive procedures** by any one or more of the following methods

- **Inspection** - It consists of examining records, documents, or tangible assets. Inspection of records and documents provides evidence of varying degrees of reliability depending on their nature, source and the effectiveness of internal controls over their processing.
- **Observation** - It consists of witnessing a process or procedure being performed by others.
- **Inquiry and Confirmation** - Inquiry consists of seeking appropriate information from a knowledgeable person inside or outside the entity; Confirmation consists of the response to an inquiry to corroborate information contained in the accounting records.
- **Computation** - It consists of checking the arithmetical accuracy of source documents and accounting records or performing independent calculations.
- **Analytical Review** - It consists of studying significant ratios and trends and investigating unusual fluctuations and items.

AUDIT REPORT

While conducting every audit auditor has to go through three phases

- ✓ Preliminary work for audit
- ✓ Conduct of actual audit
- ✓ Conclusion of audit, which means submission of Audit Report.

Therefore, **Audit Report is called as the ultimate and final product of every audit.**

IMPORTANCE OF AUDIT REPORT

- An Audit report is the end product of the auditing and concluding part of the audit process.
- Audit report gives the auditor's opinion on the accounts & record of the company, as examined by him.
- Audit Report reflects the work done by the auditor.
- Audit report is the instrument which, measures the auditor's responsibility in regard to the true & fair view on the financial statement of the company.
- Audit Report indicates the real position of the financial status of the company. It is used by different people as a reliable document

THE BASIC ELEMENTS OF THE AUDITORS' REPORT ARE [D17, 8M]

1. **Title**: The Auditor's Report should have an appropriate title i.e., "Auditor's Report". It should be distinguished from other Reports, e.g., reports of officers of the entity, Board of Directors.
2. **Addressee**: The Auditor's Report should be appropriately addressed as required by the circumstances of the engagement and applicable laws and regulations. Ordinarily, the Auditor's Report is addressed to the authority appointing the Auditor.

3. **Opening or Introductory Paragraph**
   - The Auditor's Report should identify the Financial Statements of the entity that have been audited, including the date of and period covered by the Financial Statements.
   - The Report should include a Statement that the Financial Statements are the responsibility of the entity's management and a Statement that the responsibility of the Auditor is to express an opinion on the Financial Statements based on the audit.
4. **Scope Paragraph**:
   - The Auditor's Report should describe the scope of the audit by stating that the audit was conducted in accordance with auditing Standards generally accepted in India.
   - The Report should include a statement that the audit was planned and performed to obtain reasonable assurance whether the Financial Statements are free of material misstatement.
   - The Auditor's Report should describe the Audit as including examining, on a test basis, evidence to support the amounts and disclosures in Financial Statements, assessing the accounting principles used in the preparation of the Financial Statements, assessing significant estimates made by management, in the preparation of Financial Statements, & evaluating the overall position of Financial Statements.
   - The Report should include a statement by the Auditor that the audit provides a reasonable basis for his opinion.
5. **Opinion Paragraph**: The Opinion paragraph of the Report should indicate the Financial Reporting framework used to prepare the Financial Statements. It should state the Auditor's opinion as to whether the Financial Statements give a true and fair view in accordance with the financial reporting framework and, where appropriate, whether the Financial Statements comply with the statutory requirements.
6. **Date of the Report:** The date of an Auditor's Report is the date on which the Auditor signs the Report expressing an opinion on the Financial Statements. The Auditor should not date the Report earlier than the date on which the Financial Statements are signed or approved by Management.
7. **Place of Signature:** The Report should name the specific location, which is ordinarily the city where the Audit Report is signed.

Auditor's Signature: The Report should be signed by the Auditor in his personal name. Where a Firm is appointed as the Auditor, the Report should be signed in the personal name of the Auditor and in the name of the Audit Firm. The Partner / Proprietor signing the Report should mention his ICAI Membership Number.

3: INTERNAL CHECK, INTERNAL CONTROL AND INTERNAL AUDIT

INTERNAL CHECK

- The accounting of transactions has a number of steps such as posting to the concerned books of accounts, recording receipts and payments of cash etc.
- These processes involve a various number of staffs.
- Thus, in an internal check system, practically a continuous internal audit is carried on by the staff itself.
- The work of one individual is checked by the other staff.
- Thus, internal check is an **arrangement of staff duties** where none is allowed to carry through and record every aspect of a transaction so that, without collusion between any two or more persons, fraud is prevented and at the same time the possibilities of errors and frauds are reduced to the minimum

AIM OF INTERNAL CHECK

- To pin down to definite persons responsibility for particular acts, default or omission, by the **segregation of tasks.**
- To obtain **confirmation of facts and entries**, physical and financial, by the creation and preservation of necessary records.
- To facilitate the "breakdown" of routine procedures so as to **avoid bottlenecks** and to establish an even flow of work.
- To reduce to a minimum the **possibility of fraud and error**

INTERNAL CONTROL

- The internal control system comprises **all the methods and procedures** adopted to assist in **achieving the objective** of efficient conduct of business, ensure adherence to management policies, safeguarding of assets, prevention and detection of frauds and errors, and checking the accuracy and completeness of the accounting records.
- Internal checks and internal audit are integral parts of the overall internal control system.
- Internal control refers to a process that is designed for helping the organization to accomplish goals and objectives through people of the organization and IT (information Technology) systems
- It refers to the **accounting procedure** that acts as a safeguard against frauds and losses.

ESSENTIALS OF AN INTERNAL CONTROL SYSTEM

An efficient internal control system should provide the following

- For proper division of **functional responsibilities**
- For proper review, **authorization and assignment of duties** to perform and record the transactions.
- For adoption of **proper practices** for adherence with management policies.
- Safeguard all business assets.
- Proper internal checks
- Proper internal audit system.

OBJECTIVES OF INTERNAL CONTROL

1. **Compliance:** To have compliance with law, accounting process and the accounting practices generally accepted and followed in the country.
2. **Reliance**: To increase the reliance on the internal systems, people and accounting practices followed by the organization, so that the chances of frauds are reduced.
3. **Safeguarding:** To safeguard the organization's accounts, employees and assets by formation of fool-proof policies, rules and regulations.
4. **Security:** To provide security to customers, employees and property of the organization. Physical security systems like security guards, locks and anti-theft devices are used for providing protection.
5. I**ncreased efficiency**: To assist in human resource and performance management, and to keep proper control over business activities to achieve maximum levels of efficiency.
6. **Evaluation:** To evaluate the accounting system for proper authorization of transactions.
7. **Review and correction**: To review the working of the business, locate weak points in operations and to take corrective measures for proper working.
8. **Authorization:** To provide proper authority for purchase, sale, valuation, verification and possession of assets.
9. **Delegation:** To provide for division of duties among the employees where all staff members work cohesively.
10. **Accurate planning**: To ensure that the auditors and the accountants of the organization make all the financial reports correctly and to ensure that financial planning is done accurately.
11. **Conformity with accounting principles:** To conform to the basic accounting concepts, and principles that was governing an organization.
12. **Resource utilization:** To ensure that all the resources: Man, Material, Money and Machines of the organization are optimally used.
13. **Safeguarding of resources:** To protect the resources of the organization against mismanagement or fraud and to ensure that the company's activities are in accordance with laws and regulations.
14. **Setting future Corporate Goals:** An efficient system of internal control helps the organization in goal setting. However, the organization should have certain policies, rules and regulations in place to achieve the pre-set goals.

ADVANTAGES OF INTERNAL CONTROL

1. **Efficiency, effectiveness and economy:** A good internal control system ensures that the resources are utilized only for their intended purposes and helps to overcome the risk associated with the misuse of organization's funds and other resources.
2. **Prevention of errors and irregularities:** It prevents errors and irregularities by detecting them in a timely manner, thereby promoting reliable and accurate accounting records.
3. **Safeguard from irregularities or misappropriations:** A good internal control system errors the protection of organisation resources from misappropriation and do safeguard from any irregularities.
4. **Employees' satisfaction:** It protects the interests of employees by segregation of duties and delegation of responsibilities

TYPES OF INTERNAL CONTROL SYSTEMS [J19, 6M]

- The type of internal control system to be employed in an organization depends upon the **requirements and nature** of the business.
- Generally, there are two types of Internal Control in an Organisation: **preventive and detective controls.**
- Both types of controls are essential to an effective internal control system.

PREVENTIVE CONTROLS

These are designed to discourage errors or irregularities from occurring. They are **proactive controls** that help to ensure departmental **objectives are being met**. Examples of preventive controls are:

- **Segregation of Duties:** Duties are segregated among different people to reduce the risk of error or inappropriate action. Normally, responsibilities for authorizing transactions (approval), recording transactions (accounting) and handling the related asset (custody) are divided.
- **Approvals, Authorizations, and Verifications**: Management authorizes employees to perform certain activities and to execute certain transactions within limited parameters. In addition, management specifies those activities or transactions that need supervisory approval before they are performed or executed by employees. A supervisor's approval (manual or electronic) implies that he or she has verified and validated that the activity or transaction conforms to established policies and procedures.
- **Security of Assets**: Access to equipment, inventories, securities, cash and other assets is restricted; assets are periodically counted and compared to amounts shown on control records.

DETECTIVE CONTROLS

These are designed to find errors or irregularities **after they have occurred**. Examples of detective controls are:

- **Review of Performance:** Management compares information about current performance to budgets, forecasts, prior periods, or other benchmarks to measure the extent to which goals and objectives are being achieved and to identify unexpected results or unusual conditions that require follow-up.
- **Reconciliations**: An employee relates different sets of data to one another, identifies and investigates differences, and takes corrective action, when necessary.
- Physical Inventories
- Audits

CORRECTIVE CONTROLS

Corrective controls target at the correction of errors and irregularities **as soon as** they are detected.

STEPS IN INTERNAL CONTROL

1. **Control Environment**: Establish Integrity & ethical value.
2. **Assessment of Risk**: Establishment of plan to prevent risks.
3. **Control Activities**: Formulating policies & procedures.
4. **Information & communication:** Evaluation of employee performance.

5. **Monitoring:** Assessing overall performance of the Organisation

BASIC ELEMENTS OF INTERNAL CONTROL

1. **Financial and other Organizational Plans**: It should specify the various duties and responsibilities of both management and staff, stating the powers of authorisation that reside with various members. This is important as in the event of staff absence or otherwise the correct flow of work and the internal control system could be vitiated by any wrong implementation of procedures by staff either unintentionally or wilfully.
2. **Competent Personnel:** In any internal control system, personnel are the most important element. When the employees are competent and efficient in their assigned work, the internal control system can be worked and operated efficiently and effectively even if some of the other elements of the internal control system are absent.
3. **Division of Work**: This refers to the procedure of division of work properly among the employees of the organization. Each and every work of the organization. Each and every work of the organization should be divided in different stages and should be allocated to the employees in accordance with quality and skill.
4. **Separation of operational responsibility from record keeping:** If each department of an organization is being assigned to prepare its own records and reports, there may be a tendency to manipulate results for showing better performance. So, in order to ensure reliable records and information, record- keeping function is separated from the operational responsibility of the concerned department.
5. **Separation of the custody of assets from accounting:** To protect against misuse of assets and their misappropriation, it is required that the custody of assets and their accounting should be done by separate persons. When a particular person performs both the functions, there is a chance of utilizing the organisation’s assets for his personal interest and adjusting the records to relieve himself from the responsibility of the assets.
6. **Authorization**: In an internal control system, all the activities must be authorized by a proper authority. The individual or group which can grant either specific or general authority for the transactions
7. **Managerial supervision and review**: The internal control system should be implemented and maintained in conformity with the environmental and elemental changes of the concern. By adapting any specific control system permanently, the extent to which the procedures of flexible controls have been followed in real practice should be observed and re-examined.

IMPORTANCE OF INTERNAL CONTROL

1. **Attainment of goal & Objectives:** - A sound internal control helps the entity towards the attainment of goal & objective of the business.
2. **Reliable financial Information**: A sound internal control helps the organization to set reliable financial information for managerial decision making.
3. **Compliance with law & Regulations**: Sound Internal control system ensures various compliance with laws & regulation prevailing in the country
4. **Efficient & Effective operation:** - A sound internal control system ensures efficient and effective operations that accomplish the goals of the organizations and protect employees and assets of the business.

5. **Prevention of fraud & errors**: - A sound internal control system prevents and detects frauds and errors and ensures timely preparations of financial statements and various reports for decision making.

LIMITATIONS OF INTERNAL CONTROL

1. **Organizational Structure**: Deficiencies in organizational structure make internal control ineffective.
2. **Size of the Organization**: Small organizations have very low levels of internal control, which are almost negligible due to more interference by owners and management.
3. **Unusual Transactions**: The internal control procedures normally fail to keep a check on unusual transactions.
4. **Costly**: The implementation of internal control procedures and processes involves incurring costs in terms of time, effort and resources.
5. **Abuse of Power**: Members at the top-level management may override/interfere with control.
6. **Collusion of two or more People**: It may lead to internal controls being over- ridden.
7. **Obsolescence**: Control system may become redundant with passage of time if not updated with change in the size and nature of business.
8. **Potential for human error:** Due to misunderstanding of the concept of internal control human errors may occur while carrying out Internal Control System.
9. **Frequent follow-up measures**: Follow-up procedures need to be frequent to ensure its effectiveness, which is extremely time-consuming.

TESTING OF INTERNAL CONTROL

- **PROCEDURAL TEST**
  - These tests deal with checking the compliance of the procedures laid down by the management in respect of transactional flow at each stage.
  - They provide reasonable assurance about the proper implementation and effectiveness of internal controls.

- **EXAMINATION IN DEPTH**
  - This involves examination of a few selected transactions from the **beginning till the end**.
  - Recording of transactions at various stages, documentation of the same, and authenticity of authorizations is checked in detail

EXAMINATION IN DEPTH/AUDITING IN DEPTH: "WALK THROUGH TEST"

- Fixations of the maximum tolerable error limit/desired confidence level.
- Selecting a few transactions in each area of audit to be checked.
- Verification of those selected transactions- 100% by verifying the accounting aspects, internal control aspects, documentation and audit trail.
- **Audit trail** refers to the documents, records, books and files, which enable an auditor to trace a transaction from its **source till it is summed up, recorded and presented in an accounting report.**
- Analysis of the results with the maximum tolerable error limit.

TECHNIQUES FOR EVALUATION OF INTERNAL CONTROL SYSTEM [D17, 4M]

- **NARRATIVE RECORD**
  - It is a complete and exhaustive description of the system.
  - It is appropriate in circumstances where a formal control system is lacking, like in the case of small businesses.
  - Gaps in the control system are difficult to identify using a narrative record.
- **CHECK LIST**
  - It is a series of instructions that a member of the audit staff is required to follow.
  - They have to be signed/ initialled by the audit assistant as proof for having followed the instructions given.
  - A specific statement is required for every weakness area.
- **FLOW CHART**
  - It is **a pictorial representation** of the internal control system depicting its various elements such as operations, processes and controls, which help in giving a concise and comprehensive view of the organization's working to the auditor.
  - A complete flow chart would depict the process of raising documents, personnel involved in doing so, the flow of documents through various departments, maintenance of records, flow of goods and consideration, and dealing with results.
  - The internal control evaluation process becomes easier through a flow chart as a broad picture of all the controls involved can be gauged in a glimpse.
- **INTERNAL CONTROL QUESTIONARIES**
  - This is the most widely used method for collecting information regarding the internal control system and involves asking questions to various people at different levels in the organization.
  - The questionnaire is in a pre-designed format to ensure collection of complete and all relevant information.
  - The questions are formed in a manner that would facilitate obtaining full information through answers in "Yes" or "No"

DISTINCTION BETWEEN CHECK LIST &INTERNAL CONTROL QUESTIONNARE [J17, 4M]			
	BASIS	**CHECK LIST**	**INTERNAL CONTROL QUESTIONNARE**
1	**Point of Time**	It is issued at the commencement of audit and reported back after completion of audit	It can be issued at any point of time and reported back immediately.
2	**Issued to**	It is issued to the audit staff to be followed by them during audit and reported back at completion	It is issued to various people at different levels in the organization
3	**Contents**	It contains instructions to be followed by audit assistants	It contains questions to be answered by the employees of the organization.
4	**Objective**	It works as a guideline for audit staff so that no major issues remain unchecked.	This is used to collect the information to know about the internal control system and to evaluate the weaknesses therein
5	**Negative**	Always requires further examination	May have to qualify his audit report

	answer		depending on the seriousness of the situation.

INTERNAL AUDIT

- Internal audit is **an independent appraisal activity** within the organization by the staff of the entity or by an independent professional appointed for that purpose, for review of accounting, financial and other operations and controls established within an organization as a service to the organization.
- The objective of internal audit is to furnish the analysis, appraisals, suggestions and information concerning the activities reviewed to the management for promoting effective control at reasonable cost
- Internal Audit under **section 138** of Companies Act, 2013: Internal Audit is required by
    1. Such class or classes of companies as may be prescribed shall be required to appoint an internal auditor, who shall either be a chartered accountant or a cost accountant, or such other professional as may be decided by the Board to conduct internal audit of the functions and activities of the company.
    2. The Central Government may, by rules, prescribe the manner and the intervals in which the internal audit shall be conducted and reported to the Board

AREAS OF OPERATION OF INTERNAL AUDIT

1. **Reliability and integrity of financial and operating information:** Internal auditors should review the reliability and integrity of financial and operating information and the means used to identify, measures, classify and report such information.
2. **Compliance with laws, policies, plans, procedures and regulations**: Internal auditor should review the systems established to ensure compliance with those policies, plan and procedures, law and regulations which could have a significant impact on operations and reports and should determine whether the organization is in compliance thereof.
3. **Safeguarding of Assets**: Internal auditors should verify the existence of assets and should review the means of safeguarding assets.
4. **Economic and efficient use of resources:** Internal auditor should ensure the economic and efficient use of resources available.
5. **Accomplishing of established objectives and goals for operations:** Internal auditor should review operation or programmes to ascertain whether results are consistent with established objectives and goals and whether the operations or programmes are being carried out as planned

FEATURES OF INTERNAL AUDIT

1. It is an independent appraisal activity within the organization.
2. It can be conducted by the staff of the entity or by an independent professional appointed for that purpose.
3. It is conducted for review of accounting, financial and other operations and controls established within an organization.
4. It is conducted as a service to the organization and is not a part of the organization.

5. It intends to furnish the analysis, appraisals, suggestions and information concerning the activities reviewed to the management.
6. Internal auditing functions as a continuous effort for promoting effective control at reasonable cost

FUNCTIONS OF INTERNAL AUDIT

1. **An appraisal function**: The internal auditor's job is to appraise the activity of others, not to perform a specific part of data processing.
2. **As a service to the organization:** The management requires that the auditor ensures the following:
   - That its policies are fulfilled.
   - That the information it requires to manage effectively is reliable and complete
   - That the organisation's assets are safeguarded.
   - That the internal control system is well designed.
   - That the internal control system works in practice.
3. **Other duties:**
   - Being concerned with the implementation of social responsibility policies adopted by top management.
   - Being concerned with the response of the internal control system to errors and required changes to prevent errors.
   - Acting as a training officer in internal control matters.
   - Auditing the information given to management particularly interim accounts and management accounting reports.
   - Taking a share of the external auditor's responsibility in relation to the figures in the annual accounts and
   - Being concerned with the compliance with external regulations such as those on the environment, financial services, related parties etc

NEED FOR INTERNAL AUDIT

1. Increased size and complexity of businesses.
2. Enhanced compliance requirements.
3. Focus on risk management and internal controls to manage them.
4. Unconventional business models.
5. Intensive use of information technology.
6. Stringent norms mandated by regulators to protect investors.
7. An increasingly competitive environment.

INTERNAL AUDIT – IMPORTANT MANAGEMENT TOOL [J18, 6M]

- Internal audit ensures compliance of Companies (Auditors Report) Order, 2016.
- It ensures compliance of accounting standards and policies.
- It looks into the standard of efficiency of business operation.
- It can evaluate various problems independently and suggest improvement.
- This system makes the internal control system effective.

- It ensures adequacy, reliability, accuracy and understandability of financial and operational data.
- It can add valuable assistance to management in acquiring new business, promoting new products and expansion or diversification of business etc.

ADVANTAGES OF INTERNAL AUDIT

(A) TO THE MANAGEMENT IN SPECIFIC:

- It gives a **review of overall internal control system** established by the management.
- It furnishes **the deviations** in following the procedures adopted for safeguarding assets.
- It appraises the organizational structure and management information system.
- It establishesthe policies, plans and strategies implemented are well in place and gives suggestions on management information systems reports for promoting effective control at reasonable cost.

(B) TO THE STATUTARY AUDIT IN SPECIFIC

- It evaluates the internal control system, so the statutory auditor can **reduce the number of tests** that he may have had to conduct in case there was no internal audit
- It carries out physical stock taking procedures, so reliance on stock valuation is increased.
- It helps in timely completion of accounts and accuracy of records.
- It evaluates the contingent liability existing at the year end.
- It ensures correctness of financial statements through a system of pre-audit or continuous audit.

(C) TO THE ORGANISATION AS A WHOLE AND OTHER STAKEHOLDERS IN GENERAL

- The regular audit and checks result in accurate and efficient accounting system.
- It is a critical review of the business' performance and management.
- It provides strict supervision and direction to have effective controls
- It provides safeguard to the business assets and prevents misuse and misappropriation of all business assets.
- The auditor can suggest ways and means to improve performance of the business.
- It prevents occurrence of errors and frauds.
- It enhances the performance of the business by division of duties and responsibilities as per the capability of the employees.
- It keeps a check on proper utilization of resources, which leads to reduction in costs

DIFFERENCE BETWEEN INTERNAL AUDIT AND OPERATIONAL AUDIT		
	INTERNAL AUDIT	**OPERATIONAL AUDIT**
1	Compliance objective	Risk identification, process improvement objective
2	Financial accounts focus	Business focus
3	Audit focus	Efficiency & improvement focus
4	Transaction-based	Process-based
5	Policies and procedures focus	Risk management focus
6	Cost Centre wise budget monitoring	Accountability for performance improvement Results

7	Focus on policies, transactions and compliance	Focus on goals, strategies and risk management Processes

DISTINCTION BETWEEN INTERNAL AUDIT, CONTROL & CHECK[D18, 6M]				
	BASIS	**INTERNAL AUDIT**	**INTERNAL CONTROL**	**INTERNAL CHECK**
1	Definition	It is a continuous critical review of financial and operating activities by a staff member of the auditor	It consists of all the methods and procedures adopted to assist in achieving the objective of efficient conduct of business. It includes internal checks and internal audit.	A system of allocation of responsibility, division of work, and methods of recording transactions, whereby the work of an employee is checked continuously by another.
2	Way of checking	Each component of work is checked	work of one person is automatically checked by another	It operates in routine to doubly check every part of a transaction at the time of occurrence and recording of the same
3	Objective	To evaluate the internal control system and to detect frauds and errors.	To ensure adherence to management policies, safeguarding of assets, prevention and detection of frauds and errors, accuracy and completeness of accounting records	To ensure that no one employee has exclusive control over any transaction or group of transactions and their recording in the books
4	Point of Time	work is checked after it is done	Checking is done simultaneously with the conduct of work.	Methods of recording transactions are devised where work of an employee is checked continuously by correlating it with the work of others.
5	Thrust of system	To detect errors and frauds	To prevent errors.	To fix the responsibility and division of work to avoid duplication
6	Cost Involvement	Cost is involved in addition to accounting	The system proves to be costly in case of small businesses because a greater number of employees are engaged	Does not add to the cost

7	Report	The internal auditor submits his report to the management	Internal Controls provide for built in MIS reports	The summary of day-to-day transactions work as report for the senior.

CUT OFF PROCEDURES

1. **Definition**: Periods usually coincide with calendar months, which lead to the need for specific demarcation between transactions forming the part of one period from those included in the following period. Thus, cut-off procedures are adopted to allocate revenues and costs to the proper accounting period.
2. **Areas of concern:** Close attention should be paid to the accounts payable and accounts receivable functions. These two functions are the most susceptible to recording of transactions in the wrong accounting period.
3. **Cut-of points:** Serially numbered documents like invoice for sales or purchase bills are allocated to the respective accounting periods by establishing cut-off points based on the serial numbers.
4. **Importance**: Cut-off procedures require detailed testing by the auditor so as to ensure proper accounting of assets and liabilities, which may arise without the corresponding physical delivery of goods taking place.
5. **Example**: The purchase procedure involves a number of steps, like issuing purchase requisitions, inviting quotations, selecting sellers and defining the terms of purchase, entering agreement, receipt of goods, storage of goods, payment, etc. All the documents and vouchers that substantiate the proof of authentication of these transactions are serially numbered. It is the auditor's duty to examine the cut-off points and ensure that the transaction has been recorded in the period in which the title in goods is transferred, irrespective of the period of physical delivery of goods and to ensure compliance of the Indian Accounting Standards and the relevant Statute.

The existence of a good internal check system reduces to a great extent the work of the auditor but does not reduce his liability - Discuss [D19, 6M]

- In an organisation, an auditor is appointed to authenticate the books of accounts and final financial statements based on all available evidences.
- He is also to express an unbiased opinion of true and fair view of the financial performance and financial state of affairs through the Income Statement and the Balance Sheet respectively.
- Thus, keeping in mind such an objective, the auditor needs to decide the extent of examination that he should conduct to arrive at any conclusion.
- The auditor, in this context, can resort to either detailed checking or test checking.
- Detailed checking refers to the examination of books of accounts in detail.
- Test checkingis the technique of checking some transactions selected as sample from the group of transactions and drawing conclusion on that basis, taking sample transactions selected to be the representative of the remaining transactions.
- Detailed checking is time consuming as well as laborious whereas test checking relieves the auditor from such pain.
- Thus, in actual practice, often the auditor is found reporting to test checking, provided the internal check system is satisfactory.

- Reliance on an effective internal check system and thereby streamlining the audit process enables the auditor to devote more time in examining the critical areas of accounting including valuation of closing stock, valuation of assets and liabilities, determining the reasonableness of provisions etc.
- However, such reliance simultaneously increases the risk of the auditor.
- This is because even a **sound internal check system cannot guarantee the non-existence of any error or fraud in the accounts** and thus it does not reduce his liability
- Thus, when the auditor applies test checking instead of a detailed checking, there is every possibility that any such error or fraud remains undetected.

DIFFERENCE BETWEEN TEST CHECKING AND STATISTICAL SAMPLING			
	BASIS	**TEST CHECKING**	**STATISTICAL SAMPLING**
1	**Selection**	Selective transactions are verified.	Drawing a sample from a Large number of transactions
2	**Technique**	No specific technique is used.	Statistical technique used is: Selection on random basis
3	**Subjective**	It is subjective and depends upon the choice of the auditor	It depends upon the statistical technique applied.
4	**Risk & method**	It involves more risk as there are no specific methods for test check.	It carries lesser risk and various statistical methods can be used at different times.

4: VOUCHING AND VERIFICATION

VOUCHER

- A voucher is a piece of evidence, in the form of a written record of expenditure, disbursement, or completed transaction.
- Examples of types of vouchers: Cash Memo, Sale Invoice, Purchase Requisition Slip, Purchase Invoice, Gate Keeper's Note, Bank Paying Slip, Bank Statements, Minutes Book, etc

TYPES OF VOUCHERS

1. **Original and Collateral Vouchers:** Original vouchers are called primary vouchers, and their copies or supporting documents are called collateral vouchers.
2. **Internal and External Vouchers**: Vouchers may generate inside the company (internal vouchers) or outside the company (external vouchers).
3. **Missing Vouchers:**
   - A missing voucher can be any of the following: missing Cash Memo, missing page in a Cash Collection Statement, missing TDS Certificate for tax deductions at source, missing Bank Statement for a day or a month, etc.
   - A voucher could become missing due to:
     - **Wrong or careless filing of document**. E.g., missing Bank Statement for a day or a month, missing TDS Certificate.
     - **Unintentional** non-awareness of statutory requirements. E.g., missing Resolution to authorize increase in borrowing power by the company, or accidental fire, or lost otherwise.
     - **Intention** to hide the misappropriation by a person. E.g., non-recording of Purchas Invoices received later for goods received and taken in stocks, missing Cash Memo, etc.
   - The auditor should be careful and should carry out cross verification processes from other sources and documents to be able to form a firm opinion in the case of missing vouchers.
   - The auditor should qualify his report or give a **Disclaimer of Opinion** in this case, or may give an adverse report with reasoning on a particular issue depending upon the materiality of the missing voucher as necessary evidence on the issue

VOUCHING

- "Vouching is the examination by the auditor of all documentary evidences, which are available to support the authenticity of the transaction entered in the client's record."
- **The act of examining all documentary evidences (vouchers) is referred to as vouching.**
- Its basic objective is to establish the authenticity of the transactions recorded in the primary books of account.
- Vouching is said to be "the essence of auditing" or may be termed as the "backbone of auditing"

TEEMING & LADING/ LAPPING

- Teeming & Lading is a commonly followed method of misappropriation of cash by concealing cash shortages and covering them through recoveries from another customer.

- It is not uncommon in case of cash collections if the internal check and internal control on cash transactions are not proper.
- E.g., a salesman recovers `10,000 from customer C and misappropriates the same, but to conceal the misappropriation, he declares `10,000 received later from another customer D as received from C so that the balance of C confirms to the client's debtor list, and so on for recovery from E of same amount declared as from D.
- Teeming and lading may not amount to fraud, but negligence on the part of the management and weaknesses in internal checks or controls may lead to substantial amounts being misappropriated by the cashier.
- This may result in a huge loss if he is not in a position to clear the debts when caught.

PROCEDURE FOR TIMELY DEDUCTION OF TEEMING AND LADING

1. Ascertain if the Cash Memos are consecutively numbered, and the dates, name and amount as per the Daily Summary reconcile with relevant cash receipt records.
2. Reconcile individual cash amounts as per receipts with records in the Rough Cash Book.
3. Reconcile the receipts as recorded in the Rough Cash Book, main Cash Book, pre-numbered Cash Memos, with counterfoils of the pay-in-slips.
4. Ensure whether cash receipts are deposited in the bank on a timely basis.
5. Examine the Debtors Ledger, especially entries showing part payments, to satisfy that the debtors concerned have indeed made part payments.
6. Confirmations may be obtained from the debtors from time to time

AUDIT OF RECEIPTS

1. Cash sales
   - Ensure that the entity internal control is in place over receipt from sales. Examine authorisation level for making cash sales and receiving the amount.
   - Examine few bills in order to check the accuracy of rate, amount, discount and tax computations.
   - Examine the cash sales summary book if the volume of cash sales is voluminous
   - Cash sales need to be verified with carbon copy of cash memos.
   - Examine with the entry made in cash book with reference to date on memos.
   - Examine the system followed by the entity to deposit the cash sales in bank account. It needs to be verified with the bank statement.
   - Examine the cancelled cash memos with its original copy to prevent misappropriation.
2. Sale of Assets
   - Ensure that the entity internal control is in place in respect of authorisation for making the sale.
   - Ensure the means to sale the assets, is it is a direct sale or by means of agent. If it is a direct sale then check the amount collected with reference of copy of receipt issued and if it is by agent then examines terms with them.
   - Ensure the sale value of assets is reasonable.
   - Check that the amount of sale proceeds is duly accounted for.
   - The profit or loss arising from the sale of assets is duly reflected in the financial statement.

AUDIT OF EXPENDITURE

1. **Transactions with Directors**
   - **Compliance with Sec 188 of Co. Act, 2013:** Check that any contract entered into by the director or his relatives etc. with the company is in accordance with the provisions of section 188 of the Companies Act, 2013.
   - **Disclosure of interest by Director**: Every director of a company who is directly or indirectly, concerned or interested in a contract or agreement entered or proposed to be entered into with the company, must disclose his interest to the company at the Board meeting (Section 184).
   - **Compliance with Sec 197 of Co. Act, 2013**: The remuneration paid to the directors of public companies or the private companies which are the subsidiaries of public companies should be in accordance with the provisions of section 197 of the Companies Act, 2013.
2. **Payment for Acquisition of Assets**
   - **Authorization**: The payment for acquisition of assets should be made under proper authorization and be duly supported by receipt for amount paid.
   - **Ownership:** Check the title deeds in case of purchase of immovable properties. Also ensure that the ownership in case of the moveable asset has been registered in the name the purchaser.
   - **Existence:** The auditor should also verify the existence, value and the title of the assets acquired.
   - **Compliance with Sec 179 of Co. Act, 2013**: In case of a company, ensure that the provisions of section 179 of the Companies Act, 2013 have been complied with.
   - **Capitalization of Assets**: Check that the cost of the asset purchased has been properly capitalized in the books of account. Thus, the amounts paid to bring the asset to their present condition or location and incurred upto the asset being put into use should be capitalized.

VERIFICATION OF ASSETS AND LIABILITIES

1. Verification means **"Proving the truth".**
2. An auditor has not only to see the arithmetical accuracy but has also to see that the assets as recorded in the balance sheet actually exist.
3. Verification of liabilities is also as important as the verification and assets.
4. If the liabilities are overstated or understated, the balance sheet will not represent a true and fair view of the state of affairs of the Company.
5. In short, verification is a function of examining assets & liabilities to check the value, ownership, title, Existence and possession to see whether the assets are free from any charge or encumbrance etc

IMPORTANCE OF VERIFICATION

- **True and fair view of Balance Sheet –** verification of assets and liabilities enables the auditor to comment on true and fair state of affairs of the business.
- **Valuation –** verification enables the auditor to determine whether the assets or liabilities are overstated or understated.

- **Omissions** – verification facilitates the act of confirming the omission of any asset or liability in the balance sheet.

OBJECTIVES OF VERIFICATION

1. To know whether the Balance-Sheet exhibits a true and fair view of the State of affairs of the business.
2. To find out whether the assets were in existence
3. To find out the ownership and title of the assets
4. To show correct valuation of assets and liabilities
5. To verify the arithmetical accuracy of the books of accounts
6. To ensure that the assets have been recorded properly
7. To detect frauds & errors, if any
8. To find out whether there is an adequate internal control regarding acquisition, utilization and disposal of assets

ADVANTAGES OF VERIFICATION

- It avoids manipulation of accounts
- It guards against improper use of assets
- It ensures Proper recording and valuation of assets.
- It exhibits true and fair view of the state of affairs of the Company

TECHNIQUE OF VERIFICATION

1. Inspection – This means physical inspection of the assets like counting cash in hand, measuring inventory, inspection of securities, share certificate etc.,
2. Observation – The auditor may observe or witness the inspection of assets done by others.
3. Confirmation – This means obtaining written evidence from outside parties regarding existence of assets like, confirmation from Debtors and Creditors about the balance outstanding etc

POINTS TO BE KEPT IN MIND WHILE VERIFYING THE ASSETS AND LIABILITIES

1. Whether the assets and liabilities are properly traced from ledger to Balance Sheet
2. Whether the assets are acquired for the business and liabilities got created for the purpose of business and are clearly stated in the Balance Sheet.
3. Whether the assets and liabilities are properly grouped under specified heads in the balance Sheet.
4. Whether the assets & liabilities are in actual existence on Balance Sheet date.
5. Whether along with ownership the possession of assets lies with the client.
6. Whether the assets are properly valued in the Balance Sheet
7. Whether the liabilities stated in the Balance Sheet tallies with the confirmation certificate.

5: PROVISIONS RELATING TO AUDIT UNDER COMPANIES ACT [S.139-148]

139	Appointment of Auditors
140	Removal, Resignation of Auditors
141	Eligibility, Qualification and Disqualification of Auditors
142	Remuneration of Auditors
143	Powers and Duties of Auditors
144	Auditor not to render certain services
145	Auditors to Sign Audit report
146	Auditors to attend general meeting
147	Punishment for contravention
148	Cost Audit

RULE 3: **MANNER AND PROCEDURE OF SELECTION AND APPPOINTMENT OF AUDITORS**

1. In case of a company that is required to constitute on **Audit Committee** under section 177, **the committee,** and, in cases where such a committee is not required to be constituted, **the Board**, shall take into consideration the **qualifications and experience of the individual or the firm** proposed to be considered for appointment as auditor and whether such qualifications and experience are commensurate with the size and requirements of the company;
2. Provided that while considering the appointment, the Audit Committee or the Board, as the case may be, shall have regard to any **order or pending proceeding relating to professional matters of conduct against the proposed auditor** before the Institute of Chartered Accountants of India or any competent authority or any Court.
3. The Audit Committee or the Board, as the case may be, may call for such other **information** from the proposed auditor as it may deem fit.
4. Where a company is required to constitute the Audit Committee, **the committee shall recommend the name of an individual or a firm as auditor to the Board** for consideration and in other cases; the Board shall consider and recommend an individual or a firm as auditor to the **members in the annual general** meeting for appointment.
5. If the Board agrees with the recommendation of the Audit Committee, it **shall further recommend** the appointment of an individual or a firm as auditor to the members in the annual general meeting.
6. If the **Board disagrees** with the recommendation of the Audit Committee, it shall **refer back** the recommendation to the committee for reconsideration citing reasons for such disagreement.
7. If the Audit Committee, after considering the reasons given by the Board, decides **not to reconsider its original recommendation**, the Board shall record reasons for its disagreement with the committee and send its own recommendation for consideration of the members in the annual general meeting; and if the Board agrees with the recommendations of the Audit Committee, it shall place the matter for consideration by **members in the annual general meeting.**
8. The auditor appointed in the annual general meeting shall hold office from the **conclusion of that meeting till the conclusion of the sixth annual general meeting**, with the meeting wherein such appointment has been made being counted as the first meeting.

RULE 4: CONDITIONS FOR APPOINTMENT AND NOTICE TO REGISTRAR

1. The auditor appointed under **rule 3** shall submit a certificate that –
   (a) the individual or the firm, as the case may be, is **eligible for appointment and is not disqualified** for appointment under the Act, the Chartered Accountants Act, 1949 and the rules or regulations made thereunder;
   (b) the proposed appointment is as per the term **provided under the Act;**
   (c) the proposed appointment is within the limits laid down by or under the authority of the Act;
   (d) **The list of proceedings** against the auditor or audit firm or any partner of the audit firm pending with respect to **professional matters of conduct**, as disclosed in the certificate, is true and correct.
2. The notice to Registrar about appointment of auditor under section 139 shall be in **Form ADT-1.**

RULE 5: ROTATION OF AUDITORS

- Every listed company excluding one person company and small company
- all unlisted public companies having paid up share capital of rupees **ten crore or more**
- all private limited companies having paid up share capital of rupees **fiftycrore or more**
- all companies having paid up share capital **of below threshold** limit mentioned in (a) and (b) above, but having public borrowings from financial institutions, banks or public deposits of **rupees fifty crores or more.**

RULE 6: Manner of Rotation of Auditors by the Companies on Expiry of Their Term [J18, 6M]

(1) The Audit Committee shall recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent.

(2) Where a company is required to constitute an Audit Committee, the Board shall consider the recommendation of such committee, and in other cases, the Board shall itself consider the matter of rotation of auditors and make its recommendation for appointment of the next auditor by the members in annual general meeting.

(3) For the purpose of the rotation of auditors

   (i) in case of an auditor (whether an individual or audit firm), the period for which the individual or the firm has held office as auditor **prior to the commencement of the Act** shall be taken into account for calculating the period of five consecutive years or ten consecutive years, as the case may be;

   (ii) the incoming auditor or audit firm shall not be eligible if such auditor or audit firm is associated with the outgoing auditor or audit firm under the same network of audit firms.

Explanation I - For the purposes of these rules the term "**same network**" includes the firms operating or functioning, hitherto or in future, under the same brand name, trade name or common control.

Explanation II - For the purpose of rotation of auditors

if a partner, who is in charge of an audit firm and also certifies the financial statements of the company, retires from the said firm and joins another firm of chartered accountants, such other firm shall also **be ineligible to be appointed for a period of five years**.

SECTION 139 – APPOINTMENT OF AUDITORS

(1) Subject to the provisions of this Chapter, every company shall, at the **first annual general meeting**, appoint **an individual or a firm** as an auditor who shall hold office from the **conclusion of that meeting till the conclusion of its sixth annual general meeting** and thereafter till the conclusion of every sixth meeting and the manner and procedure of selection of auditors by the member of the company at such meeting shall be such as prescribed in rule 3 of chapter X under the act
(2) Provided further that before such appointment is made, the written consent of the auditor to such appointment, and a certificate from him or it that the appointment, if made, shall be in accordance with the conditions as prescribed in rule 4 of chapter X under the Act, shall be obtained from the auditor
(3) Provided also that the certificate shall also indicate whether the auditor satisfies the criteria **provided in section 141.**
(4) **No listed company** or a company belonging to such class or classes of companies as prescribed in rule 5 of chapter X under the act, shall appoint or re-appoint—
   (a) an **individual** as auditor for more than **one term of five consecutive years**
   (b) **an audit firm** as auditor for more than **two terms of five consecutive years**
(5) Provided that
   (i) an individual auditor who has completed his term under clause (a) shall not be eligible for reappointment as auditor in the same company for five years from the completion of his term;
   (ii) an audit firm which has completed its term under clause (b) shall not be eligible for re-appointment as auditor in the same company for five years from the completion of such term.
(6) Provided further that as on the date of appointment no audit firm having **a common partner** or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of five years.
(7) Provided also that every company, existing on or before the commencement of this Act which is required to comply with provisions of this sub-section, shall comply with the requirements of this subsection **within three years from the date of commencement** of this Act.
(8) Provided also that, nothing contained in this sub-section shall prejudice the right of the company **to remove an auditor or the right of the auditor to resign from such office** of the company.
(9) The Central Government may, by **rule 6** of chapter X, prescribe the manner in which the companies shall rotate their auditors in pursuance of sub-section (2).
(10) Notwithstanding anything contained in sub-section (1), in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, **the Comptroller and Auditor-General of India** shall, in respect of a financial year, appoint an auditor duly qualified to be appointed as an auditor of companies under this Act, within a period of one hundred eighty days from the commencement of the financial year, who shall hold office till the conclusion of the annual general meeting.
(11) Where at any annual general meeting, **no auditor is appointed or re-appointed, the existing auditor shall continue** to be the auditor of the company.
(12) Where a company is required to constitute an Audit Committee under section 177, all appointments, including the **filling of a casual vacancy of an auditor** under this section shall be made after taking into account the recommendations of such committee

CASUAL VACANCY

- In the case of a**Non- Government company** the casual vacancy should be filled by **the Board of Directors within thirty days**, but if such casual vacancy is as a result of the **resignation of an auditor,** such appointment shall also be **approved by the company at a general meeting** convened within **three months of the recommendation of the Board** and he shall hold the office till the conclusion of **the next annual general meeting**
- In the case of a **Government company**the casual vacancy should be filled by the **Comptroller and Auditor-General of India within thirty days**. Provided that in case the Comptroller and Auditor-General of India does not fill the vacancy within the said period, **the Board of Directors shall fill the vacancy within next thirty days.**

REAPPOINTMENT OF RETIRING AUDITOR

A retiring auditor may be re-appointed at an annual general meeting, if

- he is **not disqualified** for re-appointment
- he has **not given** the company a **notice in writing** of his **unwillingness** to be re-appointed
- a **special resolution has not been passed** at that meeting appointing **some other auditor** or providing expressly that he shall not be re-appointed.

APPOINTMENT OF FIRST AUDITORS

APPOINTMENT OF FIRST AUDITOR OF A NON – GOVERNMENT COMPANY- 139(6)

1) The first auditor of a company, other than a government company, shall be appointed by **the BOD within 30 days from the date of registration of the company. The auditor so appointed shall hold office until the conclusion of the first AGM**
2) If BOD fails to appoint, by **the member of the company within 90 days at** an extraordinary general meeting appoint the first auditor;

APPOINTMENT OF FIRST AUDITOR OF A GOVERNMENT COMPANY - 139(7) [D17, 4M]

1) In case of Government company, first auditor shall be appointed by **CAG within 60 days from the date of registration;**
2) If CAG fails to appoint, by **the BOD of the company within next 30 days**
3) If again BOD fails to appoint the first auditor of the company, by the member of the company **within 60 days at an extraordinary general meeting**;

APPOINTMENT OF SUBSEQUENT AUDITOR OF A NON – GOVERNMENT COMPANY-139(1)

Every Non – Government Company shall at the first Annual general meeting appoint an individual or a firm as on auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting and thereafter till the conclusion of every sixth meeting

APPOINTMENT OF SUBSEQUENT AUDITOR OF A GOVERNMENT COMPANY-139(5)

In the case of Government company or any other company owned or controlled, directly or indirectly by the central government or state government or governments or partly by the central government and partly by one or more state governments, the Comptroller and Audit general of India shall in respect of a Financial year appoint an auditor duly qualified to be appointed as an auditor of companies under this act, within a **period of 180 days** from the commencement of the financial year, who shall hold office till the conclusion of the annual general meeting.

REMOVAL, RESIGNATION OF AUDITOR AND GIVING OF SPECIAL NOTICE [SECTION 140]

(1) The auditor appointed under section 139 may be removed from his office before the expiry of his term only by a **special resolution of the company**, after obtaining the previous approval of the **Central Government** in that behalf in the manner prescribed in rule 7 ofthe acts.

RULE 7: Removal of the Auditor before Expiry of his Term [D17, 3M], [J19, 4M]

1) The application to the Central Government for removal of auditor shall be made in e - Form **ADT-2** and shall be accompanied with fees as provided.
2) The application shall be made to the **Central Government within thirty days** of the resolution passed by the Board.
3) The company shall hold the **general meeting within sixty days** of receipt of approval of the Central Government for passing the special resolution.
4) Provided that before taking any action under this sub-section, the auditor concerned shall be given a reasonable opportunity of being heard.

(2) The auditor who has resigned from the company shall file within a **period of thirty days** from the date of resignation, a statement in the **form ADT – 3**with the **company and the Registrar**,

(3) In case **ofGovernment companies** and companies where CAG, appoints auditor, the auditor shall also file such statement with the **Comptroller and Auditor-General of India**, indicating the reasons and other facts as may be relevant with regard to his resignation.

(4) If the auditor does not comply with theseprovisions, he or it shall be liable to a penalty of fifty thousand rupees or an amount equal to the remuneration of the auditor, whichever is less, and in case of continuing failure, with further penalty of five hundred rupees for each day after the first during which such failure continues, subject to a maximum of five lakh rupees.

(5) **SPECIAL NOTICE**

(i) Special notice shall be required for a resolution at an annual general meeting **appointing as auditor a personother than a retiring auditor**, or providing expressly that a retiring auditor shall not be re-appointed, except where the retiring auditor has completed a consecutive tenure of five years or, as the case may be, ten years, as provided under sub-section (2) of section 139.

(ii) On receipt of notice of such a resolution, the company shall forthwith send a copy thereof to the retiring auditor.

(iii) Where notice is given of such a resolution and **the retiring auditor makes a representation in writing to the company (not exceeding a reasonable length)** and requests its notification to members of the company, the company shall, unless the representation is received by it too late for it to do so,— (a) in any notice of the resolution given to members of the company, state the fact of the representation having been made; and (b) send a copy of the representation to every member of the company to whom notice of the meeting is sent, whether before or after the receipt of the representation by the company, and if a copy of the representation is not sent as aforesaid because it was received too late or because of the company's default, the auditor may (without prejudice to his right to be heard orally) require that the **representation shall be read out at the meeting**.

(iv) Provided that if a copy of representation is not sent as aforesaid, a copy thereof shall be filed with the Registrar.

(v) Provided further that if **the Tribunal is satisfied** on an application either of the company or of any other aggrieved person that the rights conferred by this sub-section are being abused by the auditor, then, the copy of the representation may not be sent and **the representation need not be read out at the meeting.**

(6) Without prejudice to any action under the provisions of this Act or any other law for the time being in force, the Tribunal either suo motu or on an application made to it by the Central Government or by any person concerned, if it is satisfied that the auditor of a company has, whether directly or indirectly, acted in a **fraudulent manner or abetted or colluded** in any fraud by, or in relation to, the company or its directors or officers, it may, by order, direct the company to **change its auditors**.

(7) Provided that if the application is made by the Central Government and the Tribunal is satisfied that any change of the auditor is required, it shall **within fifteen days** of receipt of such application, make an order that he shall not function as an auditor and the Central Government may appoint another auditor in his place.

(8) Provided further that an auditor, whether individual or firm, against whom final order has been passed by the Tribunal under this section shall not be eligible to be appointed as an auditor of any company for a period of five years from the date of passing of the order and the auditor shall also be liable for action under section 447.

ELIGIBILITY, QUALIFICATIONS AND DISQUALIFICATIONS OF AUDITORS [SECTION 141]

Who are the persons not qualified for appointment as an Auditor of a company under section 141 of the Companies Act 2013? [J17, 7M] ANS: 141(3)

(1) A person shall be eligible for appointment as an auditor of a company only if he is **a chartered accountant.**

(2) Where a firm including a limited liability, partnership is appointed as an auditor of a company, **only the partners who are chartered accountants** shall be authorised to act and sign on behalf of the firm.

(3) The following persons **shall not be eligible for appointment** as an auditor of a company

a. a **body corporate** other than a limited liability partnership registered under the Limited Liability Partnership Act, 2008;

b. an **officer or employee** of the company;

c. a person who is a **partner**, or who is in the **employment, of an officer or employee** of the company;

d. a person who, or his **relative or partner—**

(i) is holding **any security of or interest** in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company. Provided that the **relative** may hold security or interest in the company of **face value not exceeding one thousand rupees**.

Note:

- in the event of acquiring any security by a relative, above the threshold prescribed, the **corrective action** to maintain the limits as specified above shall be taken by the auditor **within sixty days** of such acquisition or interest.

(ii) is **indebted to the company**, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, **in excess of rupeesfive lakh**

(iii) has given a **guarantee or provided any security** in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, **in excess of one lakh rupees shall not be eligible for appointment**

e. a person or a firm who, whether directly or indirectly, has **business relationship** with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as prescribed in rule 10 of chapter X under the act

Note: the term "business relationship" shall be construed as any transaction entered into for a commercial purpose, except –

(i) commercial transactions which are in the nature of **professional services** permitted to be rendered by an auditor or audit firm under the Act and the Chartered Accountants Act, 1949 and the rules or the regulations made under those Acts;

(ii) commercial transactions which are in the ordinary course of business of the company at **arm's length price** - like sale of products or services to the auditor, as customer, in the **ordinary course of business**, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses

f. a person whose relative is a director or is in the employment of the company as director or **key managerial personnel**

g. a person who is in **full time employment** elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor **of more than twenty companies**

h. a person who has been **convicted by a court** of an offence involving fraud and a period of **ten years has not elapsed** from the date of such conviction

i. A person who, directly or indirectly, renders any service referred to in **section 144** to the company or its holding company or its subsidiary company.

(4) Where a person appointed as an auditor of a company incurs any of the disqualifications mentioned in sub-section (3) after his appointment, he shall **vacate his office as such auditor and** such vacation shall be **deemed to be a casual vacancy** in the office of the auditor

REMUNERATION OF AUDITORS [SECTION 142]

1. The remuneration of the auditor of a company shall be **fixed in its general meeting** or in such manner as may be determined therein.
2. **The Board may** fix remuneration of the first auditor appointed by it.
3. The remuneration mentioned shall be in addition **to the fee payable to an auditor, include the expenses, if any, incurred** by the auditor in connection with the audit of the company

RIGHTS OF AN AUDITOR – [J19, 8M]

a) **Right to Inspect Books of Accounts and Vouchers**: Every auditor of a company shall have a right of access at all times to the books of account and vouchers of the company, whether kept at the registered office of the company or at any other place. In addition, auditor of a holding company shall also have the right of access to the records of all its subsidiaries in so far as it relates to the consolidation of its financial statements with that of its subsidiaries. [Section 143(1)

b) **Right to Obtain Information and Explanations**: The auditor shall be entitled to require from the officers of the company such information and explanation as he may consider necessary for the performance of his duties as auditor. [Section 143(1)]

c) **Right to Inspect Branch Offices and Branch Accounts**: The company auditor is also entitled to inspect the accounts of any branch office in case he considers it necessary in order to discharge his duties as the company auditor. He can do so even if a separate auditor has already been appointed to audit the branch accounts. [Section 143(8)]

d) **Right to Receive the Report of Branch Audit from the Branch Auditor**: In case a separate auditor has been appointed to audit the branch accounts, the company auditor has the right to receive the branch audit report from the branch auditor so appointed and use it to prepare the overall audit report. [Section 143(8)]

e) **Right to Receive Notices and Attend General Meetings**: The company auditor is also entitled to receive all notices of, and other communications relating to, any general meeting and to attend such meetings either by himself or through his authorised representative, who shall also be qualified to be an auditor. The auditor shall also have the right to be heard at such meeting on any part of the business which concerns him as the auditor. [Section 146]

f) **Right to Sign the Audit Report and Other Documents**: The company auditor also has the right to sign the auditor's report or sign or certify any other document of the company in accordance with the provisions of sub-section (2) of section 141. [Section 145]

g) **Right to Have Audit Report Read at the AGM**: The company auditor has the right to have the report read before the company in the General Meeting (especially in case the qualifications, observations or comments on financial transactions or matters, mentioned in the auditor's report, have any adverse effect on the functioning of the company) and the same shall be opened to inspection by any member of the company. [Section 145]

h) **Right to Attend the Meeting of the Audit Committee**: The auditors of a company shall have a right to attend the meetings of the Audit Committee and to be heard in the meetings when the Committee considers the auditor's report but shall not have the right to vote. [Section 177(7)]

i) **Right to be Indemnified**: The auditor of a company shall also have the right to be indemnified for any expenses incurred by him in defending himself in case the judgement in any law suit (whether civil or criminal) against the company goes in favour of the auditor

POWERS AND DUTIES OF AUDITORS [SECTION 143(1)]

MATTERS TO INQUIRE

1. Every auditor of a company shall have a **right of access** at all times to the **books of account and vouchers of the company**, whether kept at the registered office of the company or at any other place and shall be entitled to require from the officers of the company such information and explanation as he may consider necessary for the performance of his duties as auditor and amongst other matters inquire into the following matters
   a. whether **loans and advances** made by the company on the basis of security have been **properly secured** and whether the terms on which they have been made are prejudicial to the **interests of the company** or its members;

b. whether **transactions of the company** which are represented merely by book entries are prejudicial to the interests of the company;
c. where the company **not being an investment company or a banking company**, whether so much of the assets of the company as consist of shares, debentures and other securities have been **sold at a price less than that at which they were purchased by the company;**
d. **whether loans and advances** made by the company have been **shown as deposits**;
e. whether personal expenses have been charged to revenue account;
f. where it is stated in the books and documents of the company that any shares have been **allotted for cash,** whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading.

Note: The auditor of a company which is a holding company shall also have the **right of access to the records of all its subsidiaries and associate companies** in so far as it relates to the consolidation of its financial statements with that of its subsidiaries and associate companies.

2. The auditor shall make a **report to the members of the company** on the accounts examined by him and on every financial statements which are required under this Act to be laid before the company in **general meeting** and the report shall after taking into account **the provisions of this Act, the accounting and auditing standards** and matters which are required to be included in the audit report under the provisions of this Act or any rules made thereunder or under any order made under subsection (11) and to the best of his information and knowledge, the said accounts, financial statements give a **true and fair view** of the state of the company's affairs as at the end of its financial year and **profit or loss and cash flow** for the year and such other matters as prescribed in rule 11 of chapter X under Act.

DUTY OF AN AUDITOR TO REPORT ON CERTAIN MATTERS – 143(3) [D17, 5M]

3. The auditor's report shall also state—
   a. whether he has **sought and obtained all the information and explanations** which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;
   b. whether, in his opinion, **proper books of account** as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;
   c. whether the report on the accounts of **any branch office** of the company audited under subsection (8) by a person other than the company's auditor has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report; (d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns
   d. whether, in his opinion, the financial statements comply with the **accounting standards**
   e. the **observations or comments** of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company
   f. whether **any director is disqualified** from being appointed as a director under **sub-section (2) of section 164**
   g. any **qualification, reservation or adverse remark** relating to the maintenance of accounts and other matters connected therewith

h. whether the company has adequate **internal financial controls** with reference to financial statements in place and the operating effectiveness of such controls

i. such other matters as may be prescribed.

4. Where any of the matters required to be included in the audit report under this section is answered in **the negative or with a qualification**, the report shall state **the reasons thereof**.
5. In the case of a **Government company** or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Government, or partly by the Central Government and partly by one or more State Government, the Comptroller and AuditorGeneral of India shall appoint the auditor under sub-section (5) or sub-section (7) of section 139 and direct such auditor the manner in which the accounts of the company are required to be audited and thereupon the auditor so appointed shall submit a copy of the audit report to the **Comptroller and Auditor-General** of India which, among other things, include the directions, if any, issued by the Comptroller and Auditor-General of India, the action taken thereon and its impact on the accounts and financial statement of the company.
6. The Comptroller and Auditor-General of India shall **within sixty days from the date of receipt of the audit report** under sub-section (5) have a right to
   a. **conduct a supplementary audit** of the financial statement of the company by such person or persons as he may authorise in this behalf; and for the purposes of such audit, require information or additional information to be furnished to any person or persons, so authorised, on such matters, by such person or persons, and in such form, as the Comptroller and Auditor- General of India may direct;
   b. **comment upon or supplement** such audit report. Provided that any comments given by the Comptroller and Auditor-General of India upon, or supplement to, the audit report shall be sent by the company to every person entitled to copies of audited financial statements under sub section (1) of section 136 and also be placed before the annual general meeting of the company at the same time and in the same manner as the audit report.
7. Without prejudice to the provisions of this Chapter, the Comptroller and Auditor- General of India may, in case of any company covered under sub-section (5) or sub-section (7) of section 139 of Companies Act, 2013, if he considers necessary, by an order, cause **test audit** to be conducted of the accounts of such company and the provisions of section 19A of the Comptroller and Auditor-General's (Duties, Powers and Conditions of Service) Act, 1971, shall apply to the report of such test audit.
8. Where a company has **a branch office**, the accounts of that office shall be audited either by the auditor appointed for the company (herein referred to as the company's auditor) under this Act or by any other person qualified for appointment as an auditor of the company under this Act and appointed as such under section 139, or where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country and the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be such as prescribed in rule 12 of chapter X under the act.

   Rule 12: Duties and Powers of the Company's Auditor with Reference to the Audit of the Branch and the Branch Auditor

1) For the purposes of sub-section (8) of section 143, the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be as contained in subsections (1) to (4) of section 143.
2) The branch auditor shall **submit his report to the company's auditor**.
3) The provisions of sub-section (12) of section 143 read with rule 12 hereunder regarding **reporting of fraud by the auditor** shall also extend to such branch auditor to the extent it relates to the concerned branch.
4) Provided that the branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

9. Every auditor shall comply with **the auditing standards**
10. The Central Government may prescribe the standards of auditing or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949, in consultation with and after examination of the recommendations made by the **National Financial Reporting Authority**.
11. Notwithstanding anything contained in this section, if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an **offence of fraud involving** such amount or amounts as prescribed in rule 13 of chapter X under the act, is being or has been committed in the company by its officers or employees the auditor shall report the matter to the Central Government within such time and in such manner as prescribed in rule 13 of chapter X under the act: Provided that in case of a fraud involving lesser than the specified amount, the auditor shall report the matter to the audit committee constituted under section 177 or to the Board in other cases within such time and in such manner as prescribed in rule 13 of chapter X under the act: Provided further that the companies, whose auditors have reported frauds under this sub-section to the audit committee or the Board but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as prescribed in rule 13 of chapter X under the act.

RULE 13 – REPORTING OF FRAUDS BY AUDITOR [J18, 6M]

1. If an auditor of a company, in the course of the performance of his duties as statutory auditor, has reason to believe that an offence of fraud, which involves or is expected to **involve individually an amount of rupees one crore or above,** is being or has been committed against the company by its officers or employees, the auditor shall report the matter to the Central Government.
2. The auditor shall report the matter to the Central Government as under
   (a) the auditor shall report the **matter to the Board or the Audit Committee**, as the case may be, immediately **but not later than two days** of his knowledge of the fraud, seeking their **reply or observations within forty-five days**;
   (b) on receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government **within fifteen days from the date of receipt of such reply or observations**;
   (c) in case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of forty-five days**, he shall forward his report to the Central Government along with a note** containing the details of his report that was earlier

forwarded to the Board or the Audit Committee for which he has **not received any reply** or observations;

(d) the report shall be sent to the **Secretary, Ministry of Corporate Affairs** in a sealed cover by Registered Post with Acknowledgement Due or by Speed Post followed by an e-mail in confirmation of the same;

(e) the report shall be on **the letter-head of the auditor** containing postal address, e-mail address and contact telephone number or mobile number and be signed by the auditor with his seal and shall indicate his Membership Number;

(f) The report shall be in the form of a statement as specified in **Form ADT-4.**

3. In case of **a fraud involving lesser than the amount** specified in sub-rule (1), the auditor shall report the matter to **Audit Committee** constituted under section 177 or to the **Board i**mmediately **but not later than two days of his knowledge of the fraud** and he shall report the matter specifying the following
   a. Nature of Fraud with description
   b. Approximate amount involved
   c. Parties involved.
4. The following details of each of the fraud reported to the Audit Committee or the Board under subrule (3) during the year shall **be disclosed in the Board's Report**: -
   a. Nature of Fraud with description;
   b. Approximate Amount involved;
   c. Parties involved, if remedial action not taken;
   d. Remedial actions taken.
5. The provision of this rule shall also apply, mutatis mutandis, to a **Cost Auditor and a Secretarial Auditor** during the performance of his duties under section 148 and section 204 respectively.

12. If any auditor, cost accountant or company secretary in practice does not comply with the provisions of sub-section (12), he shall be punishable with fine **which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees.**

OTHER MATTERS TO BE INCLUDED IN AUDITOR'S REPORT

- whether the company has disclosed the impact, if any, of **pending litigations** on its financial position in its financial statement;
- whether the company has made provision, as required under any law or accounting standards, for **material foreseeable losses**, if any, on long term contracts including derivative contracts;
- whether there has been any **delay in transferring amounts**, required to be transferred, to the **Investor Education and Protection Fund** by the company.
- Report of the Auditor shall state about existence of **adequate internal financial control systems** and operating effectiveness.

AUDITOR NOT TO RENDER CERTAIN SERVICES [SECTION 144] [J17, 5M] [D19, 6M]

An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case maybe, but **which shall not**

include any of the following services whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company, namely

1. **accounting and book keeping services;**
2. **internal audit;**
3. **design and implementation of any financial information system;**
4. **actuarial services;**
5. **investment advisory services;**
6. **investment banking services;**
7. **rendering of outsourced financial services;**
8. **management services;**
9. **any other kind of services as may be prescribed**

For the purposes of this sub-section, the term "**directly or indirectly**" shall include rendering of services by the auditor, —

(i) In case of auditor being an individual, **either himself or through his relative or any other person connected or associated with such individual or through any other entity**, whatsoever, in which such individual has significant influence or control, or whose name or trade mark or brand is used by such individual

(ii) In case of auditor being a firm, either itself or through any of its partners or through **its parent, subsidiary or associate entity or through any other entity**, whatsoever, in which the firm or any partner of the firm has significant influence or control, or whose name or trade mark or brand is used by the firm or any of its partners.

AUDITOR TO SIGN AUDIT REPORTS, ETC. [SECTION 145]

The person appointed as an auditor of the company shall **sign the auditor's report** or sign or certify any other document of the company in accordance with the provisions of sub-section (2) of section 141, and the qualifications, observations or comments on financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

AUDITORS TO ATTEND GENERAL MEETING [SECTION 146]

All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company, and the auditor shall, unless otherwise exempted by the company, attend either by himself or through his authorised representative, who shall also be qualified to be an auditor, any general meeting and **shall have right to be heard at such meeting** on any part of the business which concerns him as the auditor.

PUNISHMENT FOR CONTRAVENTION [SECTION 147] [D19, 6M]

1. If any of the provisions of sections **139 to 146 (both inclusive) is contravened**, the company shall be punishable with fine which shall **not be less than twenty-five thousand rupees but which**

may extend to five lakh rupees and **every officer** of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall **not be less than ten thousand rupees but which may extend to one lakh rupees, or with both**.

2. If an auditor of a company contravenes any of the **provisions of section 139, section 143, section 144 or section 145**, the auditor shall be punishable with fine **which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees or four times the remuneration of the auditor, whichever is less**. Provided that if an auditor has contravened such provisions **knowingly or wilfully** with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than fifty thousand rupees but **which may extend to twenty-five lakh rupees or eight times the remuneration of the auditor, whichever is less.**
3. Where an auditor has been convicted under sub-section (2), he shall be liable to—
   (i) **refund the remuneration received by him to the company;**
   (ii) **pay for damages to the company, statutory bodies or authorities or to members** and creditors of the company for loss arising out of incorrect or misleading statements of particulars made in his audit report.
4. The Central Government shall, by notification, specify any statutory body or authority or an officer for ensuring **prompt payment of damages to the company** or the persons under clause (ii) of subsection (3) and such body, authority or officer shall after payment of damages to such company or persons file a report with the Central Government in respect of making such damages in such manner as may be specified in the said notification.
5. Where, in case of audit of a company being conducted by an audit firm, it is proved that the partner or partners of the audit firm has or have acted in **a fraudulent manner or abetted or colluded in any fraud** by, or in relation to or by, the company or its directors or officers, the liability, whether civil or criminal as provided in this Act or in any other law for the time being in force, for such act shall be of the partner or partners concerned of the audit firm and of the firm jointly and severally. Provided that in case of criminal liability of an audit firm, in respect of liability other than fine, the concerned partner or partners, who acted in a fraudulent manner or abetted or, as the case may be, colluded in any fraud shall only be liable.

AUDIT COMMITTEE – SECTION 177

Constitution of an Audit committee is mandatory for the;

- Every **listed Company**
- All **public companies** with a **paid-up share capital ` 10 Crore or more;**
- All Public Companies having **turnover of ` 100 Crore or more**;
- All Public Companies having in **aggregate, outstanding Loans, or borrowings and debentures or deposits exceeding ` 50 Crore or more**.

An Audit committee shall have **minimum 3 Directors** majority of them should be **Independent Directors**. Majority of the member of the Audit Committee should be **able to read & understand the financial statement.**

FUNCTION OF AUDIT COMMITTEE [D18, 3M]

- Recommend the appointment and fixation of **the remuneration of Auditor**.

- Review and monitor the **Auditors independence and performance and effectiveness** of audit process.
- Examination of the **Financial Statement and Auditor's report thereon.**
- Scrutiny of **Inter Corporate Loans and Investment**
- **Valuation of the Assets** of the Company
- Evaluation of the **internal financial control and risk management system of the entity**.
- Evaluation of the **use of the funds rose through public offers**.
- Evaluation **of any related party transaction**.

POWERS OF THE AUDIT COMMITTEE [D18, 3M]

- Audit Committee has the power to **call for comments of the Auditor about Internal Control Systems and the scope of the Audit** including its observation.
- Before submission of the report to the Board the Audit Committee have the power to **review the Financial Statement.**
- Power to discuss any issues with the **Statutory & Internal Auditor** and the Management of the Company in relation to matter contained in the Financial Statement.
- Power to investigate **into any matter under the preview of Audit Committee**.
- Auditors of the company and key managerial personnel shall have a **right to be heard into the meeting.**
- **Composition of Audit Committee is to be disclosed in Board's Report.**
- In case recommendation of the Audit Committee is not accepted by the Board, **the Board shall disclose in Board's report along with reasons.**

6: **COST AUDIT AND SECRETARIAL AUDIT**

COST AUIT – SECTION 148 [J17, 8M]

1. Notwithstanding anything contained in this Chapter, the **Central Government** may, by order, in respect of such class of companies engaged in the production of such goods or providing such services as may be prescribed, direct that particulars relating to the utilisation of material or labour or to other **items of cost** as may be prescribed shall also be included in the books of account kept by that class of companies
2. If the Central Government is of the opinion, that it is necessary to do so, it may, by order, direct that the audit of cost records of class of companies, which are covered under subsection (1) and which have **a net worth** of such amount as may be prescribed or **a turnover** of such amount as may be prescribed, shall be conducted in the manner specified in the order.
3. The audit under sub-section (2) shall be conducted by a **Cost Accountant** who shall be appointed by the Board on such remuneration as may be determined by the members in such manner as may be prescribed: Provided **that no person appointed under section 139 as an auditor of the company shall be appointed for conducting the audit of cost records**: Provided further that the auditor conducting the cost audit shall comply with the **cost auditing standards**.
4. An audit conducted under this section shall be in addition to the audit conducted under **section 143.**
5. The qualifications, disqualifications, rights, duties and obligations applicable to auditors under this Chapter shall, so far as may be applicable, apply to a cost auditor appointed under this section and it shall be the duty of the company to give all assistance and facilities to the cost auditor appointed under this section for auditing the cost records of the company: Provided that the report on the audit of **cost records shall be submitted by the cost accountant to the Board of Directors of the company.**
6. A company shall within **thirty days** from the date of receipt of a copy of the cost audit report prepared in pursuance of a direction under sub-section (2) furnish the **Central Government** with such report along with full information and explanation on every reservation or qualification contained therein.
7. If, after considering the cost audit report referred to under this section and the information and explanation furnished by the company under sub-section (6), the Central Government is of the opinion that **any further information or explanation** is necessary, it m**ay call for such further information and explanation** and the company shall furnish the same within such time as may be specified by that Government.
8. If any default is made in complying with the provisions of this section, — (a) The company and every officer of the company who is in default shall be punishable in the manner as provided in sub-section (1) of section 147; (b) The cost auditor of the company who is in default shall be punishable in the manner as provided in sub-sections (2) to (4) of section 147

MAINTENANCE OF COST ACCOUNTING RECORDS AND COST AUDIT

- The Rules state that cost records are to be maintained in **Form CRA-1**, which provides principles to be followed for different cost elements.
- The cost audit report is required to be in conformity with the **"cost auditing standards**" as referred to in Section 148 of the Companies Act, 2013.
- It may be noted that the Council of the Institute of Cost Accountants of India has made it mandatory for cost accountants in practice to follow and conform to the Cost Accounting

Standards issued by it and it is incumbent on the cost auditors to **report any deviations from cost accounting standards.**

APPLICABILITY OF MAINTENANCE OF COST RECORDS [D19, 3M]

- The Rules have classified sectors/industries **under Regulated and Non-Regulated sectors**.
- The sectors/ industries covered under Table A of the Rules are under the Regulated Sector and sectors/industries covered under Table B are under the Non-Regulated Sector.
- Every company including foreign company engaged in the production of the goods or providing services specified in Tables A and Tables B having an **overall turnover from all its products and services of Rs. 35 crore or more during the immediately proceeding financial year shall include cost records** for such products and services in their Books of Accounts

APPLICABILITY OF COST AUDIT [D18, 6M], [D19, 3M]

- Every company, under regulated category (table A) shall get cost records audited if the turnover from all its products or services is ` **50 crores or more and the aggregate turnover from individual product or services is ` 25 cores or more**.
- Every company, undernon-regulated category (table B) shall get cost records audited if the turnover from all its products or services is**100 crores or more and the aggregate turnover from individual product or services is 35 crores or more.**

NON- APPLICABILITY OF COST AUDIT RULES

The cost audit rules shall not apply if

- revenue from **export exceeds 75% of total revenue**
- which is operating from **SEZ**
- which is engaged in generation of **electricity for captive consumption** through Captive Generating Plant

REGULATED SECTORS - TABLE – A

1. Telecommunication
2. Telecom Regulatory Authority of India
3. Generation, transmission, distribution and supply of electricity
4. Petroleum products
5. Drugs and pharmaceuticals
6. Fertilizers
7. Sugar and industrial alcohol

APPOINTMENT OF COST AUDITOR [D17, 4M]

- The cost auditor is to be appointed by the **Board of Directors (BOD)** on the recommendation of the Audit Committee, where the company is required to have an Audit Committee.

- The cost auditor proposed to be appointed is required to give a **letter of consent** to the Board of Directors.
- The company shall inform the cost auditor concerned of his or its appointment as such and file a notice of such appointment with the Central Government within a **period of thirty days** of the Board meeting in which such appointment is made or within a period of one hundred and eighty days of the commencement of the financial year, whichever is earlier, through electronic mode, in form **CRA-2** along with the fee as specified in Companies (Registration Offices and Fees) Rules, 2014
- Any casual vacancy in the office of a cost auditor, whether due to resignation, death or removal, shall be filled by the **Board of Directors (BOD)** within **thirty days of occurrence of such vacancy** and the company shall inform the Central Government in **Form CRA-2** within thirty days of such appointment of cost auditor.

WHO CAN BE APPOINTED AS A COST AUDITOR?

- Only a **Cost Accountant**, as defined under the Companies Act, 2013, can be appointed as a cost auditor.
- It means a Cost Accountant who holds a **valid certificate of practice** underthe Cost and Works Accountants Act, 1959 and is in **whole-time practice**.
- Cost Accountant includes a **Firm of Cost Accountants and an LLP of cost accountants.**

ELIGIBILITY CRITERIA FOR APPOINTMENT AS A COST AUDITOR

[Same as Company Audit]

IS ROTATION OF AUDITOR APPLICABLE TO COST AUDITOR? [J19, 2M]

- Section 139 of the companies Act deals with Appointment of Auditors
- Section 139(3) of the Act, applicable to appointment of auditors (financial), and Rule 6 of Companies (Audit and Auditors) Rules, 2014 deals with the provision of rotation of auditors and these provisions are **applicable only to appointment of auditors (financial).**
- The Act **does not provide** for rotation in case of appointment of cost auditors and the same is not applicable to a cost auditor.
- It may, however, be noted that though there is no statutory provision for rotation of cost auditors, individual companies may do so **as a part of their policy**, as is the practice with Public Sector Undertakings.

REMUNERATION OF THE COST AUDITOR [J18, 5M], [J19, 3M]

- In the case of companies which are **required to constitute an audit committee** the **Board** shall appoint an individual, who is a cost accountant in practice, or a firm of cost accountants in practice, as cost audit**or on the recommendations of the Audit committee**, which shall also recommend remuneration for such cost auditor; the remuneration recommended by the Audit Committee shall be **considered and approved by the Board of Directors and ratified subsequently by the shareholders**
- In the case of other companies which are **not required to constitute an audit committee**, the **Board** shall appoint an individual who is a cost accountant in practice or a firm of cost

accountants in practice as cost auditor and the remuneration of such cost auditor shall be **ratified by shareholders subsequently**.

Obligation to report offence of fraud

[As same as financial auditor]

Cost Audit Report [J19, 2M]

- Cost Auditor is required to submit the Cost Audit Report along with his or its reservations or qualifications or observations or suggestions, if any.
- It has to be submitted in form **CRA-3 to Board of Directors** of the company within a period of **one hundred and eighty days from the closure of the financial year** to which the report relates.

FORM FOR FILING COST AUDIT REPORT WITH THE CENTRAL GOVERNMENT

- Every company to who cost auditor submits his or its report shall, within a period of thirty days from the date of receipt of a copy of the cost audit report, furnish the **Central Government** with such report along with full information and explanation on every reservation or qualification contained therein, in **form CRA-4** along with fees specified.
- The report shall be filed using **XBRL taxonomy.**
- It is to be noted that the cost audit report is required to be filed in **XBRL format.**

SECRETARIAL AUDIT – SECTION 204

(1) APPLICABILITY OF SECRETARIAL AUDIT REPORT
   - Every **listed company**
   - Every **public company** having a **paid-up share capital of fifty crore rupees or more**
   - Every public company having a **turnover of two hundred fifty crore rupees or more**

(2) The Secretarial Audit Report has to be annexed along with the Board's Report

(3) The format of the Secretarial Audit Report shall be in **Form No. MR.3.**

(4) It shall be the duty of the company to give all assistance and facilities to the company secretary in practice, for auditing the secretarial and related records of the company.

(5) The Board of Directors, in their report made in terms of sub-section (3) of section 134, shall explain in full any qualification or observation or other remarks made by the company secretary in practice in his report under sub-section (1).

(6) If a company or any officer of the company or the company secretary in practice contravenes the provisions of this section, the company, every officer of the company or the company secretary in practice, who is in default, shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

PROCEDURES OF APPOINTMENT OF SECRETARIAL AUDITOR

- Secretarial Auditor is required to be appointed by means of **resolution passed at a duly convened Board meeting.**
- It is advisable for the Secretarial Auditor to get a **letter of engagement** from the company.
- Secretarial Auditor should accept the letter of engagement.
- However, it is advisable that any changes in the Secretarial Auditor during the financial year are to be reported to the members in the Board's Report.

- The qualifications, observations or comments / remarks of the secretarial Audit Report shall be read at the annual general meeting of the company along with the explanation and comments of the Board of Directors

7: AUDIT REPORT

Audit Report is the ultimate and final product of every audit

UNQUALIFIED OPINION

- An opinion is said to be unqualified, when the Auditor concludes that the Financial Statements give a **true and fair view** in accordance with the financial reporting framework used for the preparation and presentation of the Financial Statements.
- The Auditor gives **a Clean or Unqualified Report**, when he does not have any significant negative reservation in respect of matters contained in the Financial Statements.
- Unqualified opinion is **the best audit report which company can expect**.
- An Unqualified Opinion indicates the following
  - The Financial Statements have been prepared using **the Generally Accepted Accounting Principles,** which have been **consistently** applied
  - The Financial Statements comply with **relevant statutory requirements** and regulations
  - There are adequate **disclosures of all material matters** relevant to the proper presentation of the financial information, subject to statutory requirements, where applicable.
  - Any **changes in the accounting principles** or in the method of their application, and the effects have been properly determined and **disclosed in the Financial Statements**.

MODIFIED AUDIT REPORT

- When the Auditor issues any Report **other than unqualified**, his Report is said to be modified.
- An Auditor's Report is considered to be modified when it includes
  - Matters That **Do Not Affect** the Auditor's Opinion - with Emphasis of Matter Paragraph.
  - Matters That **Do Affect** the Auditor's Opinion - Qualified Opinion, Disclaimer of Opinion, and, Adverse Opinion

EMPHASIS OF MATTERS THAT DO NOT AFFECT THE AUDITOR'S UNQUALIFIED OPINION

1. **Going Concern Not Resolved**: The Auditor should modify the Auditor's Report by adding a paragraph to highlight a material matter regarding a going concern problem where the going concern question is not resolved and adequate disclosures have been made in the Financial Statements.
2. **Significant Uncertainty:** The Auditor should consider modifying his Report by adding a paragraph if there is a significant uncertainty (other than going concern problem), the resolution of which is dependent upon future events and which may affect the Financial Statements.
3. **Multiple Uncertainties**: In extreme cases, e.g., multiple uncertainties that are significant to the Financial Statements, the Auditor may consider it appropriate to express a Disclaimer of Opinion instead of adding an emphasis of matter paragraph.
4. **Impact of Paragraph**: The addition of an emphasis of matter paragraph does not affect the Auditor's opinion. The paragraph would preferably be included preceding the Opinion Paragraph and would ordinarily refer to the fact that the Auditor's opinion is not qualified in this respect.

CIRCUMSTANCES THAT MAY RESULT IN OTHER THAN AN UNQUALIFIED OPINION

1. **Limitation on Scope:** Limitation on scope of Auditor's work may be imposed by the clients or imposed by circumstances. It may lead to situations where the Auditor may have to issue a Qualified Opinion or a Disclaimer of Opinion.
2. **Disagreement with management**:
   The Auditor may disagree with the Management as to
   a. the acceptability of the accounting policies selected, or the method of their application
   b. the adequacy of disclosure in the Financial Statements,
   c. the compliance of the Financial Statements with relevant regulations and statutory requirements. In such cases, he may have to give an Adverse Opinion or a Qualified Opinion.
3. Significant **Uncertainty**: If there is a significant uncertainty affecting the Financial Statements (other than Going Concern problem), for example, litigation involving legal claims, etc. the result of which is dependent upon the resolution of the future events, the Auditor may have to quality his opinion or disclaim an opinion. However, where such **significant uncertainty is not material, the Auditor may issue an Unqualified Opinion, by adding an "Emphasis of Matter" paragraph, without qualifying his opinion.**

QUALIFIED REPORT [D18, 2M]

1. A Qualified Audit Report is one where an Auditor gives an opinion on the truth and fairness of Financial Statements**, subject to certain reservations**.
2. The Auditor's Reservation is generally stated as: "Subject to the above, we report that the Balance Sheet shows a true and fair view."
3. The overall impact of all reservations or qualification taken together is **not material enough to vitiate the overall true and fair view of Financial Statements**, but it is important that such a matter(s) should be **brought to the attention of the shareholders.**
4. The Report should also give detailed reasons along with quantitative impact on the qualifications on Financial Statements.
5. A Qualified Opinion should be expressed when the Auditor concludes that an Unqualified Opinion cannot he expressed, or the effect of any disagreement with Management is not so **material and pervasive** as to require an **Adverse Opinion**, or The Limitation on scope is not so material and pervasive as to require a Disclaimer of Opinion

SITUATIONS CALLING FOR QUALIFIED AUDIT REPORT [D18, 4M], [D19, 6M]

1. Where the Auditors are **unable to obtain all the information and explanations** which they consider necessary for the purposes of their audit, e.g. –
   - Absence of satisfactory documentary evidence of the existence of ownership of the material assets, such as, title deeds in respect of land,
   - Absence of vouchers in respect of material payments made by the Company,
   - Destruction of books and records by fire or accident,
   - Non-availability of books and records owing to unavoidable circumstances, such as books and records of a foreign branch with which no communication is possible.
2. Where **proper books of accounts have not been kept** in accordance with the law.
3. Where the **Balance Sheet and P&L Account are not in agreement with the books of account** and returns.

4. When the **information required by law is notfurnished.**
5. **Board of Directors is required to reply to the qualifications** which forms part of the Board's report which is circulated to shareholders.
6. When the **accounts do not disclose a true and fair view**
7. Where the **accounting practices followed by the Company are not considered appropriate** to the circumstances and nature of the business
8. Where there has been a **change in accounting principles or procedures** in relation to material items, such, valuation of stock, depreciation, treatment of by-product cost, etc. **without adequate explanation and disclosure of effect of the change**
9. Where **difference of opinion with management** has arisen regarding valuation or realisability of assets, such as Stock-in-Trade, Debtors, Loans & Advances or the extent of liabilities, contingent or otherwise,
10. **Where income or expenditure is not properly reflected** so as to show a fair figure of profit for the year,
11. **Where information is not required by law to be disclosed** but the disclosure of which is considered **essential by the Auditors** in order to show a true and fair view,
12. Where there is a **contravention of the provisions of the Companies Act** having a bearing upon the accounts and transactions of the Company EX: donations to political parties or for **political purposes in contravention of Section 182, or contributions to charitable or other funds in excess of the limitation specified in Section 181;**
13. Where the Company **has contravened the provisions of its Memorandum and Articles of Associat**ion

DISCLAIMER OF OPINION

1. A Disclaimer of Opinion Report is given when the Auditor is **unable to form an overall opinion** about the matters contained in the Financial Statements.
2. A Disclaimer of Opinion should be expressed when the possible effect of a limitation on scope is so material and pervasive that the Auditor has **not been able to obtain sufficient appropriate audit evidence** and is, accordingly, unable to express an opinion on the Financial Statements.
3. It may happen in situations such as -- (a) when books of account of the Company seized by Income Tax Authorities, (b) when it is not possible for the Auditor to obtain certain information or (c) when scope of audit work is restricted.
4. The Auditor will state in his Report that he is unable to term an opinion on the Financial Statements. Such Report is called as "Disclaimer of Opinion Report".

PIECEMEAL OPINION

- The Auditor, May in some cases, find that the Financial Statements he has examined present only **a partial true and fair view**.
- In such cases, he may report that he **is unable to express an opinion, limited to certain items in the statement, with which he is satisfied.**
- Such a situation would warrant a Piecemeal Opinion.
- As the name suggests, the Auditor gives a **divided opinion on matters** with which he is satisfied and with which he is not.

- The Auditor **should state the reasons** for having given a Piecemeal Opinion.

ADVERSE OR NEGATIVE REPORT

- An Adverse or Negative Report is given when the Auditor concludes that based on his examination, he **does not agree with the affirmations** made in the Financial Statements / Financial Report.
- The Auditor states that the Financial Statements **do not present a true and fair view** of the state of affairs and the working results of the organisation.
- The Auditor **should state the reasons** for issuing such a report.
- An Adverse Opinion should be expressed when the **effect of a disagreement is so material and pervasive** to the Financial Statements, that the Auditor concludes that a qualification of the report is not adequate to disclose the misleading or incomplete nature of the Financial Statements.

DISTINGUISH BETWEEN EXPLANATORY AND QUALIFICATORY NOTES		
	EXPLANATORY NOTES	**QUALIFICATORY NOTES**
1	An Explanatory Note is meant to explain or **supplement a matter** contained in or related to Financial Statements	A Qualificatory Note is intended to communicate the **Auditor's reservation** on the accounts.
2	The matter on which an Explanatory Note is given is one on which the **Auditor has not taken an adverse view**	Qualificatory Notes on which the **Auditor has taken an adverse view** e.g., tax provision not made in the accounts
3	Explanatory Notes are given by the **Directors of the Company**	Qualifications are **made by the Auditor** in his Report to the Company's shareholders.
4	These are usually shown **under "Notes to Accounts**". All Notes, wherever shown, including those required by the Schedule III constitute an integral part of the accounting statement.	These notes are included in the **Auditors' Report before the Opinion Paragraph**. The reader's attention is drawn to the Qualification paragraph by use of the word "Subject to".

DISTINGUISH BETWEEN QUALIFIED AND ADVERSE REPORT[J17,4M]		
	QUALIFIED REPORT	**ADVERSE REPORT**
1	A Qualified Audit Report is one where an Auditor gives an opinion subject to **certain reservations**.	An Adverse Report is given when the concludes that based on his examination, **he does not agree** with the affirmations made in the Financial Statements / Financial Report.
2	The Auditor's reservation is generally Stated as: "**Subject to the above, we report that the Balance Sheet shows a true and fair view.**"	The Auditor states that the Financial Statements **do not present a true and fair view** of the state of affairs and working results of the organisation
3	The accounts present **a true and fair view subject to certain reservations**.	The accounts **do not present a true and fair view on the whole**

4	A Qualification is made in the Audit Report when the Auditor has **reservation on specific item(s) of material nature**	An Adverse Report is given when the Auditor has **his reservations on the true and fair view** presented by the Financial Statements.

CARO – COMPANIES (AUDITOR'S REPORT) ORDER, 2016

1. It is issued by **the Central Government** as per the power granted **under section 143(11)** of the Companies Act, 2013.
2. This new order is applicable to every company except
   - banking company as defined inthe Banking Regulation Act, 1949
   - insurance company as defined in the Insurance Act, 1938
   - company licensed to operate under section 8 of the Companies Act;
   - One Person Company as defined under clause (62) of section 2 of the Companies Act
   - small company as defined under the Companies Act
   - private limited company, not being a subsidiary or holding company of a public company, having **a paid-up capital and reserves and surplus not more than rupees one crore** as on the balance sheet date and **which does not have total borrowings exceeding rupees one crore from any bank or financial institution at any point of time during the financial year** and which **does not have a total revenue exceeding rupees ten crore during the financial year as per the financial statements.**
3. The Order **shall not apply to the auditor's report on consolidated financial statements**

MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT– CARO, 2016

1. **FIXED ASSETS:**
   - Whether the company is maintaining **proper records** showing full particulars, including quantitative details and situation of fixed assets
   - Whether these fixed assets have been **physically verified** by the management at reasonable intervals
   - Whether any **material discrepancies** were noticed on such verification and if so, whether the same have been properly dealt with in the books of account
   - Whether the **title deeds of immovable properties** are held in the name of the company. If not, provide the details thereof
2. **INVENTORIES:**
   - Whether **physical verification of inventory** has been conducted at reasonable intervals by the management
   - Whether any **material discrepancies** were noticed and if so, whether they have been properly dealt with in the books of account.

3. **LOANS AND ADVANCES:**
   - Whether the company has **granted any loans, secured or unsecured to companies, firms, Limited Liability Partnerships or other parties** covered in the register maintained under **section 189 of the Companies Act, 2013**. If so,

- Whether the terms and conditions of the grant of **such loans are not prejudicial** to the company's interest;
- whether the **schedule of repayment of principal and payment of interest** has been stipulated and whether the repayments or receipts are regular;
- if the amount **is overdue**, state the total **amount overdue for more than ninety days**, and whether reasonable steps have been taken by the company for recovery of the principal and interest;

4. LOANS, INVESTMENTS, GUARANTEES AND SECURITY:

- In respect of loans, investments, guarantees, and security whether provisions of **section 185 and 186 of the Companies Act, 2013** have been complied with. If not, provide the details thereof.

5. DEPOSITS:

- In case, the company has accepted deposits, whether the directives issued by the Reserve Bank of India and the provisions of **sections 73 to 76** or any other relevant provisions of the Companies Act, 2013 and the rules framed there under, where applicable, have been complied with? If not, the nature of such contraventions be stated; If an order has been passed by Company Law Board or National Company Law Tribunal or Reserve Bank of India or any court or any other tribunal, whether the same has been complied with or not?

6. COST RECORDS:

- Whether maintenance of cost records has been specified by the Central Government under subsection (1) of section 148 of the Companies Act, 2013 and whether such accounts and records have been so made and maintained.

7. STATUTORY DUES:

- whether the company is regular in depositing undisputed statutory dues including provident fund, employees' state insurance, income-tax, sales-tax, service tax, duty of customs, duty of excise, value added tax, cess and any other statutory dues to the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as on the last day of the financial year concerned for a period of more than six months from the date, they became payable. shall be indicated;
- where dues of income tax or sales tax or service tax or duty of customs or duty of excise or value added tax have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned. (A mere representation to the concerned Department shall not be treated as a dispute).

8. LOANS AND BORROWINGS:

- Whether the company has defaulted in repayment of loans or borrowing to a financial institution, bank, Government or dues to debenture holders? If yes, the period and the amount of default to be reported (in case of defaults to banks, financial institutions, and Government, lender wise details to be provided).

9. INITIAL AND FURTHER PUBLIC OFFER:

- Whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans were applied for the purposes for which those are raised. If not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported;

10. FRAUD BY COMPANY:

- whether any fraud by the company or any fraud on the Company by its officers or employees has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated;

11. **MANAGERIAL REMUNERATION:**
    - Whether managerial remuneration has been paid or provided in accordance with the requisite approvals mandated by the provisions of section 197 read with Schedule V to the Companies Act? If not, state the amount involved and steps taken by the company for securing refund of the same;
12. **NIDHI COMPANY:**
    - Whether the Nidhi Company has complied with **the Net Owned Funds to Deposits** in the ratio **of 1: 20** to meet out the liability and whether the Nidhi Company is maintaining ten per cent unencumbered term deposits as specified in the Nidhi Rules, 2014 to meet out the liability;
13. **RELATED PARTY TRANSACTION:**
    - Whether all transactions with the related parties are in compliance with sections 177 and 188 of Companies Act, 2013 where applicable and the details have been disclosed in the Financial Statements etc., as required by the applicable accounting standards;
14. **PREFERENTIAL ALLOTMENT AND PRIVATE PLACEMENT:**
    - Whether the company has made any preferential allotment or private placement of shares or fully or partly convertible debentures during the year under review and if so, as to whether the requirement of section 42 of the Companies Act, 2013 have been complied with and the amount raised have been used for the purposes for which the funds were raised. If not, provide the details in respect of the amount involved and nature of non-compliance;
15. **NON-CASH TRANSACTION:**
    - Whether the company has entered into any non-cash transactions with directors or persons connected with him and if so, whether the provisions of section 192 of Companies Act, 2013 have been complied with;
16. **REGISTRATION UNDER RBI:**
    - Whether the company is required to be registered under section 45-IA of the Reserve Bank of India Act, 1934 and if so, whether the registration has been obtained.

AUDIT CERTIFICATE

1. Sometimes apart from an audit report for general use, an auditor is often called upon **to give a certificate for special purpose.**
2. The certificate should include the following
    - Auditor should see that there is a suitable **declaration by the management about the subject matter.**
    - Auditor should give the certificate on his **letter head** or on stationary carrying his name and address to avoid misunderstanding.
    - Auditor should clearly state **his limitations and indicate the extent** to which he has relied upon a **technical expert** if any.
    - Auditor should indicate in the certificate if he has made **certain fundamental assumptions**.

- Auditor should mention whether he has used **any general-purpose statement** like Profit & Loss Account for his investigation and also, state whether that general purpose statement has been audited by other auditors.
- Auditor should be careful while **interpreting any law related** matter, he should clearly mention that he is expressing merely his own opinion.
- Auditor should address the certificate to the client or the Public Authority or the person requiring it as the case may be. In appropriate circumstances it may be issued by using the words as "**to whom so ever it may concern "**

DISTINGUISH BETWEEN AUDIT REPORT AND CERTIFICATE [J18,7M]			
	BASIS	**AUDIT REPORT**	**AUDIT CERTIFICATE**
1	Meaning	Audit Report is a statement of collected and considered information so as to give a clear picture of the **state of affairs** of the business to the persons who are not in possession of the full facts	While Audit Certificate is a written confirmation of **the accuracy of the information** stated there in.
2	Opinion	Audit Report contains **the opinion** of the auditor on the accounts	while Audit Certificate **does not contain any opinion** but only **confirms the accuracy of the figures** with the books of accounts
3	Basis	Audit Report is made out on the basis of **information obtained**& books of account verified by the auditor,	While Audit Certificate is made out on the basis of the **particular data** capable of verification as regards accuracy.
4	Guarantee	Audit Report **may not guarantee correctness** of financial statement in absolute terms	While Audit Certificate guarantees **absolute correctness** of the figures & information mentioned in the certificate.
5	Coverage	Audit Report always covers **entire accounts of the concern**	While Audit Certificate covers only certain **part of the accounts** of the concern
6	Responsibility	Audit **Report does not hold auditor responsible for anything wrong** in the accounts	While Audit Certificate makes an **auditor responsible** if anything mentioned in the certificate found as wrong later on
7	Suggestion	Audit Report **may provide certain suggestions** for improvement	While Audit certificate **does not provide any such suggestion.**
8	Nature	Audit Report is based on the **vouching & verification of books of accounts, voucher, assets & liabilities**	while Audit Certificate is based **on checking arithmetical accuracy** of the facts
9	Scope	Audit Report covers **all transactions** done during the year	While the Audit Certificate is **very specific**.

10	Characteristics	Audit Report is **subjective** as it is opinion oriented	While Audit certificate is **objective** as it is fact oriented.
11	Form	Audit Report is required to be presented in the **prescribed format**,	While Audit Certificate, except in few cases, is **not required to be presented in any standard format**
12	Address	Audit report is addressed **to the members** of the company at large or appointing authority	While Audit Certificate is addressed to **particular person** or sometimes may include the words like "To Whomsoever it may concern".

(b) "**Disclaimer of Opinion and Adverse Report do not serve the same purpose**". **Discuss. [J19, 5M]**

8: MISCELLANEOUS AUDIT

1. **AUDIT OF INVENTORIES [J17,4M][J18,4M] [D18,4M]**
   - Inventories are tangible property held for sale in the ordinary course of business, or in the process of production for such sale, or for consumption in the production of goods or services for sale, including maintenance supplies and consumable stores and spare parts meant for replacement in the normal course.
   - Inventories normally comprise raw materials including components, work-in-process, finished goods including by-products, maintenance supplies, stores and spare parts, and loose tools.
   - Inventories normally constitute a significant portion of the total assets, particularly in the case of manufacturing and trading entities as well as some service rendering entities.
   - Audit of inventories, therefore, assumes special importance.

FEATURES OF INVENTORIES – AUDIT PROCEDURES

- By their very nature, inventories normally turn over rapidly.
- Inventories are susceptible to obsolescence and spoilage. Further, some of the items of inventory may be slow-moving while others may follow a seasonal pattern of movement.
- Inventories are normally movable in nature, although there may be some instances of immovable inventories also, e.g., in the case of an entity dealing in real-estate.
- All the items of inventory may not be located at one place but may be held at different locations such as factories and warehouses, or with third parties such as selling agents.
- The individual items of inventory may not be significant in value, but taken together, they normally constitute a significant proportion of total assets and current assets of manufacturing, trading and certain service entities.
- Physical condition (e.g., stage of completion of work-in-process in certain industries) and existence of certain items of inventories may be difficult to determine.
- Valuation of inventories may involve varying degrees of estimation, including expert opinions, e.g., in the case of jewellery

2. **AUDIT OF PPE [J19, 4M]**
   - The term Property, plant and equipment in respect of those entities which are required to comply with the relevant Revised AS refers to such tangible items that:
     - are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes
     - are expected to be used during more than one period.
   - An asset can be classified as a PPE or otherwise, depending upon the use to which it is put or intended to be put.
   - For example, assets which are classified as PPE in one type of business may be considered as current assets in another. Similarly, the same asset may be classified differently in an entity at different points of time.
   - The recognition of Property, Plant and Equipment should be done as per the principles laid down in the “relevant applicable AS”.

3. AUDIT OF EDUCATION INSTITUTION[J18,4M]

1. Examine the Trust Deed or Regulations in the case of school or college and note all the provisions affecting accounts. In the case of a university, refer to the Act of Legislature and the Regulations framed thereunder.
2. Read through the minutes of the meetings of the Managing Committee or Governing Body, noting resolutions affecting accounts to see that these have been duly complied with, especially the decisions as regards the operation of bank accounts and sanctioning of expenditure
3. Check names entered in the Students' Fee Register for each month or term, with the respective class registers, showing names of students on rolls and test amount of fees charged; and verify that there operates a system of internal check which ensures that demands against the students are properly raised.
4. Check fees received by comparing counterfoils of receipts granted with entries in the cash book and tracing the collections in the Fee Register to confirm that the revenue from this source has been duly accounted for.
5. Total up the various columns of the Fees Register for each month or term to ascertain that fees paid in advance have been carried forward and the arrears that are irrecoverable have been written off under the sanction of an appropriate authority.
6. Check admission fees with admission slips signed by the head of the institution and confirm that the amount had been credited to a Capital Fund, unless the Managing Committee has taken a decision to the contrary.
7. See that free studentship and concessions have been granted by a person authorised to do so, having regard to the prescribed Rules.
8. Confirm that fines for late payment or absence, etc., have either been collected or remitted under proper authority.
9. Confirm that hostel dues were recovered before students' accounts were closed and their deposits of caution money refunded.
10. Verify rental income from landed property with the rent rolls, etc
11. Vouch income from endowments and legacies, as well as interest and dividends from investment; also inspect the securities in respect of investments held.
12. Verify any Government or local authority grant with the relevant papers of grant. If any expense has been disallowed for purposes of grant, ascertain the reasons and compliance thereof.
13. Report any old heavy arrears on account of fees, dormitory rents, etc, to the Managing Committee.
14. Confirm that caution money and other deposits paid by students on admission have been shown as liability in the balance sheet and not transferred to revenue.
15. See that the investments representing endowment funds for prizes are kept separate and any income in excess of the prizes has been accumulated and invested along with the corpus.
16. Verify that the Provident Fund money of the staff has been invested in appropriate securities.
17. Vouch donations, if any, with the list published with the annual report. If some donations were meant for any specific purpose, see that the money was utilised for the purpose.

18. Vouch all capital expenditure in the usual way and verify the same with the sanction for the Committee as contained in the minute book.
19. Vouch in the usual manner all establishment expenses and enquire into any unduly heavy expenditure under any head.
20. See that increase in the salaries of the staff have been sanctioned and minuted by the Committee.
21. Ascertain that the system ordering inspection on receipt and issue of provisions, foodstuffs, clothing and other equipment is efficient and all bills are duly authorised and passed before payment.
22. Verify the inventories of furniture, stationery, clothing, provision and all equipment, etc. These should be checked by reference to Stock Register and values applied to various items should be test checked.
23. Confirm that the refund of taxes deducted from the income from investment (interest on securities, etc.) has been claimed and recovered since the institutions are generally exempted from the payment of income-tax.
24. Verify the annual statements of accounts and while doing so see that separate statements of account have been prepared as regards Poor Boys Fund, Games Fund, Hostel and Provident Fund of Staff, etc.

4. AUDIT OF HOSPITAL [J17, 4M]

1. Check the letter of appointment to ascertain the scope of responsibilities.
2. Study the Charter or Trust Deed under which the hospital has been set up and take a special note of the provisions affecting the accounts.
3. Examine, evaluate and verify the system of internal check, internal control and determine the nature, timing and the extent of the audit procedures.
4. Vouch the entries in the Patient's Bill Register with a copy of bill issued. Test check the selected bills to see that these have been correctly prepared taking into consideration the period of stay of each patient as recorded in the Attendance Schedule.
5. Vouch the collection from patients with copies of bills and entries in Bills Register. Arrears of dues should be properly carried forward and where these are deemed to be irrecoverable, they should be written off under due authorizations.
6. Interest and/ or dividend income should be vouched with reference to the Investment Register and Interest and Dividend warrants.
7. In case of legacies and donations which are received for specific purposes, it should be ensured that any income therefrom is not utilized for any other purposes.
8. Where receipts of subscription show a significant deviation from budgeted figures, it should be thoroughly inquired into and the matter be brought to the notice of the trustees or the Managing Committee.
9. Government grants or grants from local bodies should be verifies with the reference to the correspondence with the concerned authorities.
10. Clear distinction should be made between the items of capital and revenue nature.
11. The capital expenditure should be incurred under proper authorization by a valid resolution of the trustees or the Managing Committee.
12. Verify the system of internal check as regards purchases and issue of stores, medicines etc.

13. Examine that the appointment of the staff, payment of salaries etc. are duly authorized.
14. Physically verify the investments, fixed assets and inventories.
15. Check that adequate depreciation has been provided on all the depreciable assets.4

5. AUDIT OF TRUST [J19, 4M]

1. **Constitution**: The auditor should study the constitution of the charitable institution, for example, whether it is set up under the Societies Registration Act or as per section 8 of the Companies Act or as a trust.
2. **Interest of members**: Obtain a list of members of the governing body. This will help the auditor in identifying whether any of the members of the governing body has any interest in the charitable institution.
3. **Budget:** The auditor should obtain a copy of the budget sanctioned or the financial statement. This would enable him to acquaint himself with the different heads of income and expenditures of incomes and expenditures of the institution.
4. **Internal Check:** Examination of the system of internal check, especially as regards the accounting of the amounts collected.
5. **Collection & Deposit of income:** Check that the amounts received towards income have been duly collected, received and deposited into the bank regularly and promptly.
6. **Subscription and donation**: These institutions receive subscriptions and donations which form the major part of their collections. Therefore, the auditor should check the following:
   - The amount or the rate of the annual subscription.
   - Any instructions given by the donors as to the specific utilization of donation.
   - Adequacy of internal controls existing as regards unused receipt books, counter foils, etc.
   - Where subscriptions are received in advance these should be properly dealt with in the accounts.
7. **Legacies received**: Verify the amounts of legacies received by reference to correspondence with any figures and other available information's.
8. **Income from Investment**: Where the institution has made any investments or given loans, the amount of dividend and interest should be properly vouched with reference to the counterfoils or dividend warrants received. It should be ensured that such loans or grants are given under proper authorizations.
9. **Rent:** If some property is given or taken on rent, then the auditor should check the tenancy agreement, the rent slips and the authorized person for the collection or payment, as the case may be, of the rent.
10. **Income/Expenditure relating to concert:** Most of the organisations organize special functions such as concert etc. The auditor should be careful in such cases. All the gross receipts and outgoings are to be properly vouched by him. It should be ensured that proper internal check was maintained as regards the receipts and outgoings. For example, the person responsible for collection and disbursements should be separate persons.
11. **Expenditure-a major area of concern**: The expenditure of charitable institution is also one of the major areas of concern. Thus, the auditor should verify that the expenditure is made only for the charitable purpose. If the expenditure is not for the charitable purpose, then the auditor should examine the implications of applicable law and document for the same.

12. **Physical verification**: The auditor should physically verify the cash in hand, inventories and fixed assets.

6. AUDIT OF MUNICIPALITIES AND PANCHAYATS (LOCAL BODIES) [D17,4M]

OBJECTIVE

- To ensure on the fairness and correctness of contents in the Financial Statement
- To report on adequacy of Internal control
- To ensure value of money is fully received on amount spent.
- To detect the frauds and errors.

POINTS TO BE CONSIDERED NECESSARY

- To ensure that the expediters incurred conform to the relevant provision of the law and is in accordance with the financial Rules and regulation formed by the compliant authority.
- To ensure that sanction is accorded by the competent authority either special or general.
- To ensure that there is provision of funds for expenditure and is authorized by competent Authority.
- To ensure that where huge financial expenditure is made is run economically and is expected to contribute growth.

7. AUDIT OF ABRIDGED FINANCIAL STATEMENT

- **Legal Requirements**: The Auditor should examine whether the requirements relating to Abridged Balance Sheet and Abridged Profit & Loss Account as laid down in Section 136 have been duly complied with.
- **Subsequent Events**: If the Audit Report on Abridged Financial Statements is issued on a date subsequent to the issuance of the Audit Report on Annual Accounts as per Schedule III, the Auditor's responsibility in relation to events occurring after the Balance Sheet date is limited to the events occurring up to the date of his report on the annual accounts.
- **Unqualified Report:** If the Auditor is satisfied that the Abridged Financial Statements are proper in all respects, he should issue an Unqualified Audit Report.
- **Qualified Report:** The Auditor should express a Qualified Opinion or an Adverse Opinion, as appropriate, if he has certain reservations about the Abridged Financial Statements, e.g. if a material piece of information has not been disclosed in the Abridged Financial Statements or has been disclosed in an inappropriate manner

8. BRANCH AUDIT [D17,4M]

1) "Branch office", in relation to a company, means any establishment described as such by the company
2) **Audit of Branch Office by company's auditor or branch auditor** - Where a company has a branch office, the accounts of that office shall be audited either by the company's auditor or by any other person qualified for appointment as an auditor of the company under the 2013 Act.
3) **Audit of branch offices outside India** - Where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's

auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country.

4) **Report by Branch Auditor to company's auditor** - The branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the company's auditor. The company's auditor shall deal with the report of branch auditor in his report in such manner as he considers necessary proviso to section 143(8) of the 2013 Act.
5) **Duties and powers of company's auditors in connection with branch audit** - Duties and powers of company's auditor with reference audit of branch and branch auditor shall be as contained in section 143(1) to 143(4) of the 2013.Thus; the company's auditor is responsible even if branch auditor is appointed.
6) **Branch auditor's responsibility to report fraud** - Responsibility to report fraud, as applicable to company's auditor applies to branch auditor.

9. **JOINT AUDIT [SA 299]**
   - In big corporate more than one person or firm of Chartered Accountants are appointed as a Joint Auditor for conducting the audit of the company.
   - This practice of appointing joint auditor accrues great advantages to the company.
   - In a big organisation the task of carrying audit cannot be accomplished with single individual so for overcoming such situation joint auditor whereas appointed.

ADVANTAGES OF JOINT AUDIT [J17, 4M]

- Lower workload
- Timely completion of work
- Sharing of expertise
- Improved quality of services
- Healthy competition
- Quality of performance
- Knowledge pool

DISADVANTAGES OF JOINT AUDIT

- Superiority complex of some auditor
- Costly for small entity
- Lack of coordination in work
- Uncertainty about liability of work
- Adjustment / Psychological problem amongst the auditor
- Difficulty in fixation of work among other

RESPONSIBILITY OF JOINT AUDITOR [J18, 4M]

- The joint auditors are able to arrive at an agreed report.
- However, where the joint auditors are in disagreement with regard to any matters to be covered by the report, each one of them should express his own opinion through a separate report.

- A joint auditor is not bound by the views of the majority of the joint auditors regarding matters to be covered in the report and should express his opinion in a separate report in case of a disagreement.
- In respect of audit work divided among the joint auditors, each joint auditor is responsible only for the work allocated to him, whether or not he has prepared a separate report on the work performed by him.

JOINT AND SEVERAL LIABILITY OF JOINT AUDITORS

- in respect of the audit work which is not divided among the joint auditors and is carried out by all of them
- in respect of decisions taken by all the joint auditors concerning the nature, timing or extent of the audit procedures to be performed by any of the joint auditors. It may, however, be clarified that all the joint auditors are responsible only in respect of the appropriateness of the decisions concerning the nature
- timing or extent of the audit procedures agreed upon among them; proper execution of these audit procedures is the separate and specific responsibility of the joint auditor concerned
- in respect of matters which are brought to the notice of the joint auditors by any one of them and on which there is an agreement among the joint auditors
- for examining that the financial statements of the entity comply with the disclosure requirements of the relevant statute
- for ensuring that the audit report complies with the requirements of the relevant statute

10. AUDIT OF SHARES

ALLOTMENT OF SHARES

- Study of the contract pursuant to which the issue is made to determine how many shares are agreed to be issued and for what value and the nature and other details of the consideration.
- Examination of the prospectus to see the substance of the contract and the relevant terms of the issue including the mode of payment of the purchase consideration in case of an issue to a vendor of the business or pay ability of commission to the underwriters or pay ability of the preliminary expenses.
- To check whether minimum amount has been subscribed or not as stated in the prospectus.
- To check whether the sums payable on application for the amount so stated have been paid to and received by the company by cheque or other instrument.
- To check whether the amount payable on application on every security shall not be less than five per cent. Of the nominal amount of the security or such other percentage or amount, as may be specified by the Securities and Exchange Board by making regulations in this behalf.
- Examine the Board meeting minutes for the purpose for which securities is issued and utilized for the same.
- Check whether the amount is refunded to the applicant within prescribed time period in case of minimum amount has not been subscribed and the sum payable on application is not received within a period of thirty days from the date of issue of the prospectus.
- To check whether the company has file with the Registrar a return of allotment or not, where the Company having a share capital makes any allotment of securities.

- To check whether the Company has defaulted under sub-section (3) or sub-section (4). In case the company is found default under above provision then the same should be reported by the auditor in his report.

AUDIT OF ALTERATION OF SHARE CAPITAL – SECTION 61 [J19, 4M]

- Confirm that alteration was authorised by articles.
- Verify the minutes of the Board meeting and ordinary resolution passed in the general meeting in which the approval of members is obtained.
- Verify that alteration had been affected in copies of Memorandum, Articles, etc.
- Obtain the reasons for which the memorandum of the company is altered.
- Check whether there is any change in the voting percentage of shareholders due to consolidate and divide all or any of its share capital into shares of a larger amount than its existing shares.
- To confirm that the alter share capital's denomination should be more than R1.
- Verify that proper accounting entries have been passed. Register of members may also be checked to see that the necessary alteration has been affected therein.

AUDIT OF ISSUE OF BONUS SHARES – SECTION 63 [D17, 4M]

- Confirm that issue of Bonus Share was authorized by articles.
- Verify the minutes of the Board meeting and ordinary resolution passed in the general meeting in which the approval of members is obtained.
- Check that the company has issue fully paid-up bonus shares to its members only.
- Confirm that the issue of bonus shares shall not be made by capitalising reserves created by the revaluation of assets.
- Check whether the company has made any default in payment of interest or principal in respect of fixed deposits or debt securities issued by it.
- Check whether the company has made any default in payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus.
- Whether the partly paid-up shares are made fully paid-up.
- Check whether the bonus shares shall not be issued in lieu of dividend.

BUYBACK OF SHARES – SECTION 68

- Confirm that Buy-Back was authorized by articles.
- Verify the minutes of the Board meeting and special resolution passed in the general meeting in which the approval of members is obtained.
- Where the buy-back has been authorised by the Board by means of a resolution passed at its meeting then check that the buy-back is not more than ten per cent. Or less of the total paid-up equity capital and free reserves of the company.
- Check that the no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.
- To check that the buy-back shall not be more than twenty-five per cent. Of the aggregate of paid up capital and free reserves of the company. In case of buy-back of equity shares in any financial

year, the reference to twenty-five per cent. In this clause shall be construed with respect to its total paid-up equity capital in that financial year.

- To check that the ratio of the aggregate of secured and unsecured debts owed by the company after buy-back is not more than twice the paid-up capital and its free reserves.
- To check that all the shares or other specified securities for buy-back should be fully paid-up.
- To check whether the buy-back is made as per SEBI regulations in case of buy-back of the shares or other specified securities listed on any recognized stock exchange.
- To check that no offer of buy-back under this sub-section shall be made within a period of one year reckoned from the date of the closure of the preceding offer of buy-back.
- To ensure that buy-back shall be completed within a period of one year from the date of passing of the special resolution, or as the case may be, the resolution passed by the Board under clause (b) of sub-section (2).
- Ensure that the buy-back has been done only out of the company's free reserves or its securities premium account or out of the proceeds of any shares or other specified securities other than out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.
- Ascertain that declaration of solvency was filed with the SEBI and/or the Registrar of Companies before making buy-back but subsequent the passing of the special resolution.
- To ensure that company shall extinguish and physically destroy the shares or securities so bought back within seven days of the last date of completion of buy-back.
- To ensure that the company shall not make a further issue of the same kind of shares or other securities including allotment of new shares or other specified securities within a period of six months except by way of a bonus issue.
- Whether the company has maintained any register of the shares or securities so bought.
- Check whether that the after the completion of the buy-back under this section the company file with the Registrar and the Securities and Exchange Board a return containing such particulars relating to the buy-back within thirty days of such completion.

SPLITTING OF SHARES OF FACE VALUE FROM Rs.10 to Rs.1 PER SHARE

- Confirm that alteration was authorised by articles.
- Verify the minutes of the Board meeting and ordinary resolution passed in the general meeting in which the approval of members is obtained.
- Verify that alteration had been effected in copies of Memorandum, Articles, etc.
- Verify that proper accounting entries have been passed. Register of members may also be checked to see that the necessary alteration have been effected therein

SHARE TRANSFER AUDIT

1. Inspection of the Articles of Association regarding the prescribed form of transfer and other provisions, particularly the time limits lay down by the Articles or law.
2. Notification by transferor of the lodgement made by the transferee and inspect the objections received, if any. Also see, where calls due or not paid, whether transfer can be refused under the articles and whether any transfer was so refused.

3. Examining in the case of particularly partly-paid shares, where the application for registration was made by the transferor, a notice was sent to the transferee and registration was affected only on receipt of 'non-objection' received from him.
4. Scrutiny of transfer forms, noting specially:
   - That in every case, the application for transfer was made in the prescribed form and the prescribed authority had stamped the date on which it was presented to it; also that it was delivered to the company within 60 days exaction.
   - That each transfer form is properly executed and bears the proper stamp duty.
   - That the name of the company is correctly stated on the form.
   - That where the consideration for transfer appears to be inadequate, an inquiry was made by the company for ascertaining the reasons therefor. (This is not necessary if the transfer form bears the seal of the Collector of Stamps.)
   - That the alterations, if any, have been suitably initiated
   - That the name and address of the transferee have been recorded completely and fully for purposes of correspondence.
5. Comparison of the signatures of each transferor on the transfer form with his signature on the original application for shares or on the transfer form (if the shares were acquired on a transfer)
6. Ascertaining that none of the transferees is disqualified from holding shares in the company.
7. Vouching the entries in the Shares Transfer Journal by reference to the transfer forms, noting in each case:
   - the name of transferor
   - the name and address of the transferee
   - the number and class of shares transferred
   - the distinctive numbers, if any, of the shares transferred.
8. Verification of postings from the Share Journal to the Register of Members.
9. Inspection of each transfer as to names, addresses, occupations, form of document, description, number (in words), distinctive number of shares, stamp, date, signature, witnesses, etc.
10. Check whether the transfer to firms, etc. has been rejected or not and whether notes of trust have been entered in the share register.
11. Noting transferor's name, etc. and class, number and distinctive number of shares, as stated in the transfers, with old certificates and Register of Members. See that old certificates were cancelled.
12. Inspection of the power of attorney and specimen signatures if transfer executed by an agent.
13. Inspection of letters of indemnity for lost certificates and ensuring that duplicate certificates have been issued on proper authority.
14. Where part of the shares have been transferred, the issue of balance certificates to the transferors should be seen and confirm that the distinctive number of shares have been correctly stated.
15. Refer to the minute's book to ensure that all transfers recorded in the share transfer journal have been approved by the Board.
16. Checking of counterfoils of new certificates.
17. Reconciliation of the amount of transfer fees collected with the total number of transfers lodged and verifying that the amount of transfer fees have been accounted for.
18. Reconciliation of the total number of shares of different classes issued by the company with the total amount of capital issue and its sub-divisions by extracting balances of shares held by different members from the Register of members.

19. Ensuring that, in case of any share transactions by directors, corresponding entries have been made in the Register of Directors' shareholding.

REISSUE OF FORFEITED SHARES

- The auditor should ascertain that the board of directors has the authority under the Articles of Association of the company to reissue forfeited shares. Check the relevant resolution of the Board of Directors.
- Vouch the amounts collected from persons to whom the shares have been allotted and verify the entries recorded from re-allotment. Auditor should check the total amount received on the shares including received prior to forfeiture, is not less than the par value of shares.
- Verify that computation of surplus amount arising on the reissue of shares credited to Capital Reserve Account
- Where partly paid shares are forfeited for non-payment of call, and re-issued as fully paid, the reissue is considered as an allotment at a discount and compliance of the provisions of Section 53 is essential.

11. AUDIT OF DEBENTURES – SECTION 71

"Debenture" includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not

ISSUE OF DEBENTURES [J18, 4M]

- A company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption.
- Provided that the issue of debentures with an option to convert such debentures into shares, wholly or partly, shall be approved by a special resolution passed at a general meeting.
- No company shall issue any debentures carrying any voting rights.
- Secured debentures may be issued by a company subject to such terms and conditions as may be prescribed.
- Where debentures are issued by a company under this section, the company shall create a debenture redemption reserve account out of the profits of the company available for payment of dividend and the amount credited to such account shall not be utilised by the company except for the redemption of debentures.
- Appointment debenture trustee is mandatary for the following –
  - The offer of issue of debenture is made to public
  - The company makes the offer to members exceeding five hundred in number.
- The purpose of appointment of debenture trustee is for the protection of interest L & redden grievances of debenture holders.
- Now a days, the share accounting is done by Registering and Transfer Agents (RTA): The auditor may have to check the records of RTA with dematerialisation and electronic record keeping, the concept of audit has changed

INTEREST ON DEBENTURES

- A predetermined fixed rate of interest is payable on debentures irrespective of the fact that company has earned the profit or not.
- Debenture holders are creditors of the company, they are not the owners.
- They have no voting powers and cannot influence the management but their claim of interest ranks ahead of the claims of the shareholders

REDEMPTION OF DEBENTURES

A company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption. If debentures are redeemable it can be redeemed in any of the following way:

- By way of periodical drawing i.e., by creating Debenture Redemption Reserve Account.
- By way of payment on fixed date.
- By payment whenever the company desires to do so

12. DECLARATION OF DIVIDEND [SECTION 123][D17,4M]

1. Final dividend is declared in the **general meeting.**
2. **Board of Directors** have to recommend a dividend.
3. Declaration of dividend is '**Ordinary Business**" in general meeting.
4. No dividend shall be declared or paid by a company for any financial year except
    - **out of the profits of the company** for that year arrived at after providing for depreciation in accordance with the provisions of sub-section (2), or **out of the profits of the company for any previous financial year** or years arrived at **after providing for depreciation** in accordance with the provisions of that sub-section and remaining undistributed, or out of both; or
    - out of money provided by the **Central Government or a State Government** for the payment of dividend by the company in pursuance of a guarantee given by that Government.
5. Provided that a company may, before the declaration of any dividend in any financial year, transfer such **percent-age of its profits for that financial year as it may consider appropriate to the reserves of the company.**
6. Provided further that where, owing to **inadequacy or absence of profits** in any financial year, any company proposes to declare dividend out of the accumulated profits earned by it in previous years and transferred by the company to the reserves, such declaration of dividend shall not be made except in accordance with such rules as may be prescribed in this behalf.
7. Provided also that no dividend shall be declared or paid by a company from its reserves other than **free reserves**.
8. Provided also that no company shall declare dividend unless carried over **previous losses and depreciation** not provided in previous year or years are **set off against profit** of the company for the current year.

INTERIM DIVIDEND [J19, 4M]

- The Board of Directors of a company may declare interim dividend **during any financial year** out of the surplus in the profit and loss account and out of profits of the financial year in which such interim dividend is sought to be declared
- In case the company has **incurred loss** during the current financial year up to the **end of the quarter** immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the **average dividends** declared by the company during the immediately **preceding three financial years.**
- The amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate account **within five days from the date of declaration** of such dividend.

ENTITLEMENT OF DIVIDEND

- No dividend shall be paid by a company in respect of any share therein except to the **registered shareholder** of such share or to his order or to his banker and shall **not be payable except in cash**.
- Provided that nothing in this sub-section shall be deemed to prohibit the **capitalisation of profits** or reserves of a company for the purpose of issuing fully paid-up bonus shares or paying up any amount for the time **being unpaid on any shares** held by the members of the company.
- Provided further that any dividend payable in cash may be paid **by cheque or warrant** or in any **electronic mode** to the shareholder entitled to the payment of the dividend

UNPAID DIVIDEND ACCOUNT [Section 124] Transfer of unpaid dividend to separate account:

- Where a dividend has been declared by a company but **has not been paid or claimed within thirty days from the date of the declaration** to any shareholder entitled to the payment of the dividend, the company shall, w**ithin seven days from the date of expiry of the said period of thirty days,** transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in that behalf in any scheduled bank to be called the **Unpaid Dividend Account.**

INFORMATION ABOUT UNPAID DIVIDEND ON COMPANY'S WEBSITE

- The company shall, within a period **of ninety days** of making any transfer of an amount under subsection (1) to the Unpaid Dividend Account, **prepare a statement** containing the names, their last known addresses and the unpaid dividend to be paid to each person
- **place it on the website of the company,** if any, and also on any other website approved by the Central Government for this purpose, in such form, manner and other particulars as may be prescribed.

EFFECT OF NON - TRANSFER

- If any default is made in transferring the total amount referred to in sub-section (1) or any part thereof to the Unpaid Dividend Account of the company, it shall pay, from the date of such default, interest on so much of the amount as has not been transferred to the said account, at the **rate of twelve per cent. per annum** and the interest accruing on such amount shall ensure to the **benefit of the members of the company** in proportion to the amount remaining unpaid to them.

TRANSFER OF UNCLAIMED DIVIDEND AND ALSO SHARES TO IEPF [D18, 4M]

- Any money transferred to the Unpaid Dividend Account of a company in pursuance of this section which remains unpaid or unclaimed for a **period of seven years** from the date of such transfer shall be transferred by the company along with interest accrued, if any, thereon to the Fund established under sub-section (1) of section 125 and the company shall send a statement in the prescribed form of the details of such transfer to the authority which administers the said Fund and that authority shall issue a receipt to the company as evidence of such transfer.
- All shares in respect of which dividend has not been paid or claimed for seven consecutive years or more under sun-section (5) shall also be transferred by the company in the name of Investor Education and Protection Fund along with a statement containing such details as may be prescribed.
- Provided that any claimant of shares transferred above shall be entitled to claim the transfer of shares from Investor Education and Protection Fund in accordance with such procedure and on submission of such documents as may be prescribed.
- If a company fails to comply with any of the requirements of this section, **the company** shall be punishable with fine which shall **not be less than five lakh rupees but which may extend to twenty-five lakh rupees** and every **officer of the company** who is in default shall be punishable with fine which shall **not be less than one lakh rupees but which may extend to five lakh rupees.**

INVESTOR EDUCATION AND PROTECTION FUND [SECTION 125]

The Central Government shall establish a Fund to be called the IEPF

There shall be credited to the Fund—

- the amount given by the **Central Government** by way of grants after due appropriation made by Parliament by law in this behalf for being utilised for the purposes of the Fund;
- **donations** given to the Fund by the Central Government, State Governments, companies or any other institution for the purposes of the Fund;
- the amount in the **Unpaid Dividend Account** of companies transferred to the Fund under subsection (5) of section 124;
- the amount in the **general revenue** account of the Central Government which had been transferred to that account under sub-section (5) of section 205A of the Companies Act, 1956, as it stood immediately before the commencement of the Companies (Amendment) Act, 1999, and remaining **unpaid or unclaimed** on the commencement of this Act;
- the amount lying in the Investor Education and Protection Fund under section 205C of the Companies Act, 1956;
- the **interest or other income** received out of investments made from the Fund;
- the amount received under sub-section **(4) of section 38 (amount received through disposal of securities)**
- the **application money** received by companies for allotment of any securities and **due for refund**;
- matured deposits with companies other than banking companies;
- matured debentures with companies;
- interest accrued on the amounts referred above

- sale proceeds of fractional shares arising out of issuance **of bonus shares, merger and amalgamation for seven or more years**
- **redemption amount of preference shares** remaining unpaid or unclaimed for seven or more years
- such other amount as may be prescribed
- Noamount shall form part of the Fund unless such amount has **remained unclaimed and unpaid for a period of seven years from the date it became due for payment**

THE FUND SHALL BE UTILISED FOR

- education, awareness and protection;
- the refund in respect of unclaimed dividends, matured deposits, matured debentures, the application money due for refund and interest thereon; promotion of investors'
- distribution of any disgorged amount among eligible and identifiable applicants for shares or debentures, shareholders, debenture-holders or depositors who have suffered losses due to wrong actions by any person, in accordance with the orders made by the Court which had ordered disgorgement
- reimbursement of legal expenses incurred in pursuing class action suits under sections 37 and 245 by members, debenture-holders or depositors as may be sanctioned by the Tribunal
- any other purpose incidental thereto, in accordance with such rules as may be prescribed Provided that the person whose amounts referred to in clauses (a) to (d) of sub-section (2) of section 205C transferred to Investor Education and Protection Fund, after the expiry of the period of seven years as per provisions of the Companies Act, 1956, shall be entitled to get refund out of the Fund in respect of such claims in accordance with rules made under this section.

13. AUDIT OF CONSOLIDATED FINANCIAL STATEMENTS (CFS)

Parent Company: The Parent Company (i.e., Holding Company) has the following responsibilities –

- **Identifying components**, and including the financial information of the components to be included in the Consolidated Financial Statements,
- Identifying reportable segments for segmental reporting,
- Identifying related parties and related party transactions for reporting,
- Obtaining accurate and complete financial information from components, and
- Making appropriate consolidation adjustments.

Objective of Audit of CFS:

- To satisfy that the CFS have been prepared as per the requirements of Ind AS - 27, 18 & 31.
- To enable the Auditor to express an opinion on the true and fair view presented by the CFS

Features of CFS:

CFS are prepared using the Separate Financial Statements of the Parent, Subsidiaries, Associates and Joint Ventures and also other financial information, which might not be covered by the Separate Financial Statements of these entities.

14. SECTION 182 OF THE COMPANIES ACT, 2013

Conditions for contribution to **Political Party / Political Purpose**

1. The **Board should pass a resolution** authorizing such contribution.
2. The aggregate of the amount contributed in any financial year **should not exceed 5% of the average net profits during three immediately preceding financial years**.
3. Payments covered under Political Contribution:
   - Contribution made **directly** to a Political Party whether in cash or in other form.
   - Expenditure incurred on **printing and distribution of posters** and leaflets, either directly concerned or connected with elections or otherwise for a political purpose.
   - Contribution made directly to a political party whether **in cash** or in other form for running an educational institution or for undertaking **philanthropic activities**.
   - Expenditure incurred directly or indirectly by a Company on advertisement in any publication **like Souvenir, Brochure, Tract, etc by or on behalf of a Political Party or for its advantage.**
   - **Donation, Subscription or payment by A Company** to any person which can be regarded as likely to affect public support for a Political Party shall be deemed as contribution for a political purpose.

15. CO- OPERATIVE SOCIETIES

- A Co-operative society may broadly be defined as an **association of persons** who have voluntarily joined together to achieve a **common economic objective** through the formation of a democratically-controlled business organization, making equitable contributions to the capital as required, and accepting a fair share of risks and benefits of the undertaking.
- Elimination of **middlemen and sharing of gains** of economic activities seems to be the hallmark of a co-operative society.
- A co-operative society may be formed for different purposes.
- Accordingly, there may be consumers’ co-operative societies, housing co-operative societies, industrial co-operative societies, urban and rural co-operative banks, etc.

AUDIT OF THE CO-OPERATIVE SOCIETIES ACT, 1912 [D18, 4M]

- The **Registrar** shall audit or cause to be audited by some person authorised by him by general or special order in writing in this behalf the accounts of every registered society **once at least in every year**
- The audit shall include an examination of **overdue debts**, if any, and **a valuation** of the assets and liabilities of the society.
- The Registrar, the Collector or any person authorised by general or special order in writing in this behalf by the Registrar shall at all times have **access to all the books**, accounts, papers and securities of a society, and every officer of the society shall furnish such information in regard to the transactions and working of the society as the person making such inspection may require.
- “Registrar” means a person appointed to perform the duties of a Registrar of Cooperative Societies under this Act

QUALIFICATIONS OF AUDITOR

- Generally, only **a chartered accountant** within the meaning of the Chartered Accountants Act 1949 can be appointed as the auditor of a co-operative society.
- However, in certain State Co-operative societies Act, a person **holding a government diploma** in co-operative accounts, or in co-operation and accounts, or a reason who has served as an auditor in the Co-operative Department of Government, may also be appointed as the auditor.
- The auditor should ensure that he is duly qualified to act as auditor of the society.

APPOINTMENT OF THE AUDITOR

- An auditor of a co-operative society is **appointed by the Registrar of Cooperative Societies**and the auditor so appointed conducts the audit on behalf of the Registrar and submits his report to him as also to the society.
- The audit fees are paid by the society on the basis of statutory **scale of fees** prescribed by the Registrar, according to the category of the society audited.
- For example, the audit fees of co-operative credit society and Urban Co-operative Banks are to be calculated with reference to **working capital** at the prescribed rates.
- 'Working Capital' here means funds at the disposal of the society inclusive of paid-up share capital, funds built up out of profits and monies raised by borrowing and by other means.

BOOKS OF ACCOUNTING RECORDS

- Under section 43(h) of the Co-operative Societies Act, a state government can frame rules prescribing the books and accounts to be kept by a co-operative society
- **Cash book**: It may be maintained to record particulars regarding cash receipts and expenses under suitable heads, with clear distinction between capital and revenue items of receipts and expenses.
- **Stock register:** It may contain detailed information as regards receipts, issues and balances of stock-intrade, date-wise. In a producers' co-operative society, perpetual inventory records may be maintained based on an appropriate costing method.
- **Register of assets and investments**: It will contain detailed particulars regarding the various immovable and movable assets belonging to the society, such as, types of assets, location, date of acquisition, cost, depreciation provided, and so on.
- **Register of fixed deposits**: In the case of a co-operative credit society, or a co-operative bank, or any other society which is authorised by its bye-laws to accept deposits from members/non-members, a register of fixed deposits may be maintained giving details as regards the dates of acceptance, maturity, interest accrual, repayment, etc.
- **Register of sureties**: In the case of a co-operative credit society, loans are given against personal security of members as also surety (guarantee) provided by two other members. The Register of Sureties will give particulars about the number of borrowers in respect of which a member has stood surety, and show whether it is within the overall limit of surety-ship that may.
- **Restriction on shareholding**: Shareholding in a co-operative society is subject to the limit prescribed in Sec. 5 of the Co-operative Societies Act 1912. Accordingly, no member of the society, other than a registered society, can hold **more than twenty per cent of the total number of shares of the society, or such number of shares which in value exceeds Rs. 1,000**.

- **Restriction on Loan**: As per section 29 A registered co-operative societies can only grant loans to **its members though**, with prior approval of the **Registrar,** it may grant loans to other registered cooperative societies. The auditor should see that the loans granted by the society are in conformity with this provision.
- **Restriction on Borrowing**: Subject to the restrictions imposed by its bye-laws, a co-operative society may accept loans and deposits from its members as well as non-members. It is the, auditor's duty to ascertain that the restrictions, if any, laid down by the bye-laws are carefully observed

INVESTMENT OF FUNDS

- There are restrictions on investment of funds belonging to a co-operative society.
- Accordingly, a society may invest its funds in any of the following
  - Central or State Co-operative Bank,
  - Any securities specified in Section 20 of the Indian Trusts Act, 1882.
  - Any shares, securities, bonds or debentures of any other Co-operative society with limited liability.
  - Any bank, or person carrying on banking business or a Co- operative bank, other than a Central or State co-operative bank, as duly approved by the Registrar;
  - In any other manners as duly permitted by the requisite authority.

SPECIAL POINTS IN A CO-OPERATIVE SOCIETY

GENERAL POINTS

- The auditor should carefully go through the **bye-laws of the society** and see that they are being observed both in letter and spirit.
- He should examine the **Register of Members of the society and individual shareholdings**.
- He should test-check the **internal check and control system** operated by the society and model his audit examination based on its strengths and weaknesses.

AUDIT OF INCOME

- He should carefully vouch the receipt of cash.
- Cash receipts on account of share capital should be vouched with the Register of Members.
- Cash received against sales should be vouched with the cash memos and invoices issued to customers as also Sales Account.
- Receipt of cash in respect of payment of interest and repayment of loans advanced by the society should be vouched with the loan agreements.
- Cash received from members towards construction of houses or their maintenance, should be vouched with the Register of Members, demands made by the society from time to time, and money receipts.

AUDIT OF EXPENDITURE

- He should vouch all expenditure with reference to authorisation from the Managing Committee, particularly in the case of large capital expenditure, as also the bills received from individual parties, the money receipts obtained from them, and entries in the Bank Pass Book along with counter-foils of cheques.

- He should vouch the payment of loans from the loan agreements entered into with borrower members.
- He should vouch establishment expenses with reference to the resolutions of the Managing Committee, agreements with the persons concerned, and money receipts obtained from them.

OTHER ASPECTS

- He should appropriately classify overdue debts for a period from **six months to five years** and more, and report them to the members, with a note regarding the effects these might have on the financial position of the society. He should also put a note regarding the **probability of recovery** of such debts.
- Similarly, he should make a special reference to the **overdue amount of interest from members**. Generally, interest on overdue debts should not be credited to Interest Account but to the Overdue Interest Reserve Account.
- **Writing off of bad debts** should be **after prior authorisation** from the Managing Committee of the society. According to the Maharashtra Co-operative Societies Rules, a bad debt can be written off only when it is certified to be irrecoverable by the auditor. This casts a special obligation on the auditor to ascertain whether the debt in question was created within the Rules of the society, and whether it has now really become bad and irrecoverable

16. AUDIT OF BANK

- The banking industry is the pivot of any economy and its financial system.
- Banks are one of the foremost agents of financial intermediation in an economy like India and, therefore, development of a strong banking system is of utmost importance.
- The banking institutions in the country are working in a competitive environment and their regulatory framework is aligned with the international best practices.
- Thus, financial deepening has taken place in India and continues to be in progress with a focus on orderly conditions in financial markets while sustaining the growth momentum.
- The Reserve Bank of India (hereinafter referred to as RBI) acts as the monetary authority and the central bank of the country.

TYPES OF BANKING INSTITUTIONS PREVAILING IN INDIA

- Commercial banks
- Regional Rural banks
- Co-operative banks
- Development banks
- Payment Banks
- Small Finance Banks

ADVANCES

- Ensure the internal control is in place in relation to advances made.
- To scrutinise the subsidiary, ledger, & control accounts

- To ensure the proper documentation of account.
- To scrutinise the overdue account and scheme for recovery of such amount.
- Cash balance with RBI and other bank and money at call and short Notice.

CASH IN HAND

- Ensure that the internal control is in place.
- Visit the bank branch and inspects physical cash and ensure that it will tallies withs the banks cash book balance.
- Verity the amount of foreign currency held by bank on the date at which financial statement is prepared.

BALANCE WITH RBI

Inspect the ledger balance in each account with

- Bank confirmation certificates from Reserve Bank of India
- Reconciliation Statement.

BALANCE WITH OTHER BANK

- Inspection of reconciliation statement to ensure that no debit or credit for interest have been taken to Revenue account to the year.
- To examines the large transition and balances with banks outside India. Ensure that they are converted at market rate as on financial statement preparation

FIXED ASSETS

- Accounting method of bank
- Ownership document
- To examine with reference to schedule of fixed assets to find new assets acquired.
- To examine sale deed in relation to sale of assets by bank.
- To ensure appropriateness of basis of revaluation of fixed assets.
- Ensure compliance of sec 9 of banking Regulation Act.

BANKING AND DEPOSITS

BORROWINGS

- To ensure that amount have been property disclosed for
- Borrowing in India from RBI.
- Borrowing outside India.
- Ensure the rate of interest paid payable with duration of borrowing.
- Verity whether the barrowings of money at call and short notice are property authorized.

DEPOSITS

- To ensure the interest accrued but not due on deposits is not under other liabilities and provision
- See whether there are any instances of **window dressing reporting in LFAR.**

CAPITAL RESERVE AND SURPLUS

- Examine the opening balance of capital
- Examine with special resolution of shareholder or MOA about increase in authorized capital during the year.
- Examine with prospectus about increase in subscribed/ paid up capital
- Examine with Government notification for any fresh contribution from them. Reserve and Surplus
- To examine the opening balance of different type of Reserve.
- Addition/ deduction from reserves.
- Reason for appropriation of any fund from such account.
- Dividend paid by bank
- In respect of foreign branch ensure compliance with foreign laws

BILLS PAYABLE

The auditor should evaluate the **existence, effectiveness and continuity of internal controls** over bills payable.

Such controls should usually include the following:

- Drafts, mail transfers, traveller's cheques, etc., should be made out in standard printed forms.
- Unused forms relating to drafts, traveller's cheques, etc., should be kept under the custody of a responsible officer.
- The bank should have a reliable private code known only to the responsible officers of its branches coding and decoding of the telegrams should be done only by such officers.
- The signatures on a demand draft should be checked by an officer with the specimen signature book.
- In case an instrument prepared on a security paper, e.g., draft, has to be cancelled (say, due to error in preparation), it should be examined whether the manner of cancellation is such that the instrument cannot be misused. (For example, in the case of drafts, banks generally cut the distinctive serial number printed on the form and paste it in the book in which drafts issued is entered.) Cases of frequent cancellation and reissuance of drafts, pay orders, etc., should be carefully looked into by a responsible official.