

Study Note - 7 (Revised)

PROVISION RELATING TO AUDIT UNDER COMPANIES ACT



This Study Note includes

- 7.1 Auditor's qualifications, disqualifications, appointment, remuneration, removal, powers and duties.
- 7.2 Cost Audit, Secretarial Audit
- 7.3 Reporting requirements under Companies Act, Report vs. Certificate, contents of the reports and qualifications in the report.
- 7.4 Miscellaneous Audit
 - (i) Branch Audit, Joint Audit
 - (ii) Audit of Shares and debentures
 - (iii) Audit of divisible Profits and dividends
 - (iv) Statutory Auditors Vs. Internal Auditors
 - (v) Auditing and Assurance Standards relating to Audit of Inventories and Audit of fixed assets.
 - (vi) Auditing of different types of undertaking – Education, Hospitals, Co-operative Societies, Banks, Trusts, Municipalities, Panchayats.

7.1 AUDITOR'S QUALIFICATIONS, DISQUALIFICATIONS, APPOINTMENT, REMUNERATION, REMOVAL, POWERS AND DUTIES.

Introduction

The Companies Act 2013 has made the audit of accounts of companies in India compulsory.

Section 139 to 148 provide for the qualifications, disqualifications, appointment, removal, rights, duties & liabilities of company auditors.

APPOINTMENT OF AUDITORS [SECTION 139]

- (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 members of the company at such meeting shall be such as prescribed in rule 3 of chapter X under the act.

Rule 3 : Manner and Procedure of Selection and Appointment of Auditors

(1) In case of a company that is required to constitute an 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;

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) If the auditor does not comply with the provision of sub-section (2), 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.

(4) (i) Special notice shall be required for a resolution at an annual general meeting appointing as auditor a person other 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 with respect thereto 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.

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

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.

(5) 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.

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.



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.

Explanation I.— It is hereby clarified that the case of a firm, the liability shall be of the firm and that of every partner or partners who acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its director or officers.

Explanation II.— For the purposes of this Chapter the word “auditor” includes a firm of auditors.

Summary at Glance

Removal

By a special resolution of the company and after obtaining the previous approval of the central Government, the auditor appointed under section 139 may be removed from his office before the expiry of his term;

Resignation

The auditor shall file within 30 days from the date of resignation, a statement in prescribed form with the company and the registrar;

In case of Government company, the auditor shall send such statement with the CAG, indicating the reason and other facts with regards to his resignation;

If fails to comply with sub-section (2), punishable with fine not less than ₹ 50,000 but may extend to ₹5,00,000;

Special notice

Special notice for resolution at an annual general meeting for appointment of auditor other than a retiring auditor;

On receipt of notice of such a resolution, the company shall forthwith send a copy thereof to the retiring auditor;

Where notice is given of such a resolution and the retiring auditor makes with respect thereto representation in writing to the company 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,—

in any notice of the resolution given to members of the company, state the fact of the representation having been made; and

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,

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 require that the representation shall be read out at the meeting.

ELIGIBILITY, QUALIFICATIONS AND DISQUALIFICATIONS OF AUDITORS [SECTION 141]

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



Provided that a firm whereof majority of partners practicing in India are qualified for appointment as aforesaid may be appointed by its firm name to be auditor of a company.

(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, namely:—

(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 or such sum as prescribed in rule 10 of chapter X under the act;

Rule 10 : Disqualifications of Auditor

(1) For the purpose of proviso to sub-clause (i) of clause (d) of sub-section (3) of section 141, a relative of an auditor may hold securities in the company of face value not exceeding rupees one lakh:

Provided that the condition under this sub-rule shall, wherever relevant, be also applicable in the case of a company not having share capital or other securities:

Provided further that in the event of acquiring any security or interest 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.

(2) For the purpose of sub-clause (ii) of clause (d) of sub-section (3) of section 141, a person who or whose relative or partner is indebted to the company or its subsidiary or its holding or associate company or a subsidiary of such holding company, in excess of rupees five lakh shall not be eligible for appointment.

(3) For the purpose of sub-clause (iii) of clause (d) of sub-section (3) of section 141, a person who or whose relative or partner 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.

(4) For the purpose of clause (e) of sub-section (3) of section 141, 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.



(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 such amount as prescribed in rule 10 of chapter X under the act; or

(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, for such amount as prescribed in rule 10 of chapter X under the act;

(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;

(f) a person whose relative is a director or is in the employment of the company as a 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.

Explanation.— For the purposes of this clause, the term “directly or indirectly” shall have the meaning assigned to it in the Explanation to section 144.

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.

Provided that the Board may fix remuneration of the first auditor appointed by it.

(2) The remuneration under sub-section (1) shall, 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 and any facility extended to him but does not include any remuneration paid to him for any other service rendered by him at the request of the company.



POWERS AND DUTIES OF AUDITORS [SECTION 143]

(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, namely:—

(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.

Provided that 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 associates companies in so far as it relates to the consolidation of its financial statements with that of its subsidiaries and associates 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 by or 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 sub-section (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.

Rule 11 : Other Matters to be Included in Auditors Report

The auditor's report shall also include their views and comments on the following matters, namely:-

(a) whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;

(b) 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;



(c) whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.

d) whether the company had provided requisite disclosures in its financial statements as to holdings as well as dealings in Specified Bank Notes during the period from 8th November, 2016 to 30th December, 2016 and if so, whether these are in accordance with the books of accounts maintained by the company.

(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 sub-section (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;

(e) whether, in his opinion, the financial statements comply with the accounting standards;

(f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;

(g) whether any director is disqualified from being appointed as a director under sub-section (2) of section 164;

(h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

(i) whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such controls;

(j) 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 therefor.

(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 Auditor-General 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; and
- (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 sub-sections (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.

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.

Provided that until any auditing standards are notified, any standard or standards of auditing specified by the Institute of Chartered Accountants of India shall be deemed to be the auditing standards.

(11) The Central Government may, in consultation with the National Financial Reporting Authority, by general or special order, direct, in respect of such class or description of companies, as may be specified in the order, that the auditor's report shall also include a statement on such matters as may be specified therein.

Provided that until the National Financial Reporting Authority is constituted under section 132, the Central Government may hold consultation required under this sub-section with the Committee chaired by an officer of the rank of Joint Secretary or equivalent in the Ministry of corporate Affairs and the committee shall have the representatives from the Institute of Chartered Accountants of India and Industry Chambers and also special invitees from the National Advisory Committee on Accounting Standards and the office of the Comptroller and Auditor-General.

(12) 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 and Other Matters:

(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; and

(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 immediately 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; and

(c) Parties involved.

(4) The following details of each of the fraud reported to the Audit Committee or the Board under sub-rule (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; and

(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."]

(13) No duty to which an auditor of a company may be subject to shall be regarded as having been contravened by reason of his reporting the matter referred to in sub-section (12) if it is done in good faith.

(14) The provisions of this section shall mutatis mutandis apply to—

(a) the cost accountant in practice conducting cost audit under section 148; or

(b) the company secretary in practice conducting secretarial audit under section 204.



(15) If any auditor, cost accountant or company secretary in practice do 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

The auditor's report shall also include their views and comments on the following matters, namely:-

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.

DUTIES AND POWERS OF THE COMPANY'S AUDITOR WITH REFERENCE TO THE AUDIT OF THE BRANCH AND THE BRANCH AUDITOR

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 sub-sections (1) to (4) of section 143.

The branch auditor shall submit his report to the company's auditor.

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.

REPORTING OF FRAUDS BY AUDITOR

(1) For the purpose of sub-section (12) of section 143, in case the auditor has sufficient reason to believe that an offence involving fraud, is being or has been committed against the company by officers or employees of the company, he shall report the matter to the Central Government immediately but not later than sixty days of his knowledge and after following the procedure indicated herein below.

auditor shall forward his report to the Board or the Audit Committee, as the case may be, immediately after he comes to knowledge of the fraud, seeking their reply or observations within forty-five days;

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 of receipt of such reply or observations;



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 failed to receive any reply or observations within the stipulated time.

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.

The report shall be on the letter-head of the auditor containing postal address, e-mail address and contact number and be signed by the auditor with his seal and shall indicate his Membership Number.

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

The provision of this rule shall also, mutatis mutandis, to a cost auditor and a secretarial auditor during the performance of his duties under section 148 and section 204 respectively.

AUDITOR NOT TO RENDER CERTAIN SERVICES [SECTION 144]

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:—

- (a) accounting and book keeping services;
- (b) internal audit;
- (c) design and implementation of any financial information system;
- (d) actuarial services;
- (e) investment advisory services;
- (f) investment banking services;
- (g) rendering of outsourced financial services;
- (h) management services; and
- (i) any other kind of services as may be prescribed.

Provided that an auditor or audit firm who or which has been performing any non-audit services on or before the commencement of this Act shall comply with the provisions of this section before the closure of the first financial year after the date of such commencement.

Explanation.—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]

(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; and
- (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 sub-section (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; and
- Such directors or classes of the companies, as may be prescribed.

As per the Rule 6 of the Companies (Meetings of the Board and its Power) Rules, 2014 following class of the companies have been prescribed for this purpose;

- 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: The various Functions of the Audit Committee is enumerated below;

- 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: The powers of the Audit Committee are enumerated below;

- 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 perview 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.

Self Examination Questions

1. Is an auditor entitled to attend the general meetings? Discuss the rights of an auditor while he is present in general meeting?
2. Discuss the procedure of appointment of the first auditor of a company.
3. State the procedure of for removal of statutory auditor before the expiry of his term.
4. Discuss the provision of section 140 of the companies Act 2013.
5. Who are qualified to act as auditor of the company? Discuss the person who is disqualified to become as an auditor of a company.
6. State the provision relating to audit of branch office of a company in India and Abroad.
7. Discuss the reporting requirement of Frauds by Auditor.
8. List down the certain services which are not to be rendered by the Auditor of the Company.
9. Write short notes on Audit Committee.
10. Why Central Government permission is required, when the auditor is to be removed before the expiry of their term?



State whether the following statements are true or false.

1. In case of Government Company auditor is appointed by the CAG within 182 Days from the commencement of Financial Year.
2. Cooling period of Individual Auditor is 2 consecutive terms of 5 years.
3. The first auditor appointed shall hold office till the conclusion of first AGM.
4. Government Company means a company where 21% of shares are hold by the Central government or State Government or partly by Central Government or State Government.
5. A Body Corporate can become Auditor of the company.
6. The auditor shall have access at all times to the books of account and voucher of the company.
7. An auditor of a company can render Investment Banking Service.
8. The auditor report shall be signed only by the person appointed as an auditor of the company.
9. All notices of the general meeting shall be forwarded to the auditor of the company.
10. An audit committee shall have minimum 5 directors.

[Answer: False, False, True, False, False, True, False, True, True, False]

Fill in the blanks:

1. An Audit committee shall have _____ directors.
2. Audit committee formation is mandatory for a public company having _____ paid up share capital.
3. Cost Audit is mandatory only when specific order is issued by the _____.
4. Cost Audit report is submitted to the Central Government within _____ days.
5. First auditor is appointed by the BOD of the company within ____ days.
6. Cost Audit is conducted by the _____ in practice.
7. Any fraud to involve an amount of _____ is to be reported to the Central Government.
8. The auditor shall have a right to be _____ at Annual General Meetings.
9. Punishment for contravention of section 139 is _____.
10. Auditor of Government Company is appointed by _____.

[Answer: 3, 10 Crore or more, Central Government, 30 days, 30 days, Cost Accountants, 1 crore, Heard, 25000, Comptroller and Auditor General of India.]

**Match the following**

	Column A		Column B
1	Maximum term of Firm as Auditor	A	2 Consecutive terms of 5 years
2	Minimum fees for contravention of section 139	B	BOD
3	Maximum fees for contravention of section 139	C	A company which is a subsidiary of Government Company.
4	Independent Directors	D	Section 145 of the Companies Act 2013
5	First auditor appointment is done by	E	1 term of 5 years
6	Auditor Remuneration is to be fixed at	F	Special Resolution
7	Government Company	G	₹ 25,000
8	Maximum term of Individual Auditor	H	₹ 5,00,000
9	Resolution for removal of auditor before expiry of term	I	General Meeting
10	Signing of audit report	J	Audit Committee

[Answer: E, G, H, J, B, I, C, A, F, D]

Multiple choice questions

1. First auditor of the company is appointed by the BOD within
 - (a) 15 days
 - (b) 30 days
 - (c) 45 days
 - (d) 60 days
2. Cost Audit is covered under
 - (a) Section 204
 - (b) Section 148
 - (c) Section 139
 - (d) None of the above
3. Secretarial Audit is covered under section
 - (a) Section 204
 - (b) Section 148
 - (c) Section 139
 - (d) None of the above



4. Appointment of auditor for government company is done by
 - (a) BOD
 - (b) Audit committee
 - (c) Managing Director
 - (d) CAG

5. While conducting audit of financial statement auditor need to comply with
 - (a) Cost Audit Standards
 - (b) Secretarial standards
 - (c) Auditing Standards
 - (d) None of the above

[Answer: B, B, A, D, C]

7.2 COST AUDIT, SECRETARIAL AUDIT

Cost Audit Provision of Section 148 of the Companies Act.

148. (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:

Provided that the Central Government shall, before issuing such order in respect of any class of companies regulated under a special Act, consult the regulatory body constituted or established under such special Act.

(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:



- 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 ₹ 10 to ₹ 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:

The following aspects are required to be examined by the auditor in conducting the share transfer audit:

- i. Inspection of the Articles of Association regarding the prescribed form of transfer and other provisions, particularly the time limits laid down by the Articles or law.
- ii. 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.
- iii. 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 effected only on receipt of 'non-objection' received from him.



iv. 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; and
 - That the name and address of the transferee have been recorded completely and fully for purposes of correspondence.
- (v) 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).
- (vi) Ascertaining that none of the transferees is disqualified from holding shares in the company.
- (vi) 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; and
 - the distinctive numbers, if any, of the shares transferred.
- (vii) Verification of postings from the Share Journal to the Register of Members.
- (viii) 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.



- (ix) Check whether the transfer to firms, etc. have been rejected or not and whether notes of trust has been entered in the share register.
- (x) 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.
- (ix) Inspection of the power of attorney and specimen signatures if transfer executed by an agent.
- (x) Inspection of letters of indemnity for lost certificates and ensuring that duplicate certificates have been issued on proper authority.
- (xi) 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.
- (xii) Refer to the minutes book to ensure that all transfers recorded in the share transfer journal have been approved by the Board.
- (xiii) Checking of counterfoils of new certificates.
- (xiv) 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.
- (xv) 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.
- (xvi) Ensuring that, in case of any share transactions by directors, corresponding entries have been made in the Register of Directors' shareholding.

Re-issue of forfeited shares

- i. 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.
- ii. 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.
- iii. Verify that computation of surplus amount arising on the reissue of shares credited to Capital Reserve Account and
- iv. 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.



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 Debenture

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 mandatory 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 & redress 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.

Auditor's Duty:

- The auditor should verify that the prospectus had been duly filed with the registrar before the date of allotment of debentures.
- He should check the amount collected in the cash book with the counterfoils of receipts issued to the applicants and also cross check the amount into the application and allotment book.
- He should examine the debenture trust deed and note the conditions contained therein as to issue and repayment.
- If the debentures are covered by a mortgage or a charge, it should be verified that the charge has been correctly recorded in the register of mortgage and charges and it has also been registered with the registrar of the companies.
- Compliance with SEBI guidelines should also be ensured.
- Where debentures have been issued as fully paid up to vendors as a part of the purchase consideration, the contract in this regard should be checked.



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 rank ahead of the claims of the shareholders.

Auditor's Duty:

- i. The payment of interest should be vouched by the auditor with the acknowledgement of the debenture-holders, endorsed warrants and in case of bearer debentures with the coupons surrendered.
- ii. The auditor should reconcile the total amount paid with the total amount due and payable with the amount of interest outstanding for payment.
- iii. He should ensure that the interest paid on debenture like that on other fixed loans, must be disclosed as a separate item in the profit & loss account.

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.

Auditor's Duty:

- i. The auditor should inspect the debentures or trust deed for the terms and conditions regarding redemption of debentures.
- ii. He should see the Director's minute book authorizing the redemption of debentures.
- iii. He should also vouch the redemption with the help of debenture bonds cancelled and the cash book.
- iv. He should also examine the accounting treatment thoroughly.



Debenture issued as Collateral Security

If the debentures are issued as collateral security to the banks or creditors then auditor needs to ensure that such issue is approved by Board of Directors and very by the term as per loan agreement.

AUDIT OF DIVISIBLE PROFITS & DIVIDENDS

Declaration of dividend [Section 123]

Final dividend is declared in the general meeting. Board of Directors have to recommend a dividend. Declaration of dividend is 'Ordinary Business' in general meeting.

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.

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.

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.

Provided also that no dividend shall be declared or paid by a company from its reserves other than free reserves.

Provided also that no company shall declare dividend unless carried over previous losses and depreciation not pro-vided in previous year or years are set off against profit of the company for the current year.

For the purposes of clause (a) of sub-section (1), depreciation shall be provided in accordance with the provisions of Schedule II.



Interim Dividend:

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.

Declaration of interim dividend if company has incurred losses in current financial year:

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.

Legal Provisions applicable to interim dividend:

The amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate ac-count 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.

Consequences on non-compliance:

A company which fails to comply with the provisions of sections 73 and 74 shall not, so long as such failure continues, declare any dividend on its equity shares.

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, within 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 sub-section (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 and 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 enure 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 Investor Protection Fund:

- 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 sub-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 Investor Education and Protection Fund (herein referred to as the Fund).



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 sub-section (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;
- 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 to in clauses (h) to (j);
- 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; and
- such other amount as may be prescribed:

Provided that no such amount referred to in clauses (h) to (j) 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; and
- 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.

Authority to administer the fund:

- The Central Government shall constitute, by notification, an authority for administration of the Fund consisting of a chairperson and such other members, not exceeding seven and a chief executive officer, as the Central Government may appoint.
- Any person claiming to be entitled to the amount referred in sub-section (2) may apply to the authority constituted under sub-section (5) for the payment of the money claimed.

Administration and procedures of the fund:

- i. The manner of administration of the Fund, appointment of chairperson, members and chief executive officer, holding of meetings of the authority shall be in accordance with such rules as may be prescribed.
- ii. The Central Government may provide to the authority such offices, officers, employees and other resources in accordance with such rules as may be prescribed.



- iii. The authority shall administer the Fund and maintain separate accounts and other relevant records in relation to the Fund in such form as may be prescribed after consultation with the Comptroller and Auditor-General of India.
- iv. It shall be competent for the authority constituted under sub-section (5) to spend money out of the Fund for carrying out the objects specified in sub-section (3).

Books of Accounts:

- The accounts of the Fund shall be audited by the Comptroller and Auditor- General of India at such intervals as may be specified by him and such audited accounts together with the audit report thereon shall be forwarded annually by the authority to the Central Government.
- The authority shall prepare in such form and at such time for each financial year as may be prescribed its annual report giving a full account of its activities during the financial year and forward a copy thereof to the Central Government and the Central Government shall cause the annual report and the audit report given by the Comptroller and Auditor-General of India to be laid before each House of Parliament.

STATUTORY AUDITOR VS. INTERNAL AUDITOR

Statutory Audit is the act of checking books of accounts as per the provision of Companies Act, whereas Internal Audit is conducted by the either be a chartered accountant or a cost accountant, or such other professional as may be decided by the Board of the Company to detect weakness in internal control system and for their improvement. However both of these types of audit check books of accounts, detect frauds & errors however they differ from each other which is reproduced below;

SL No.	Basis	Statutory Audit	Internal Audit
i.	Appointing Authority	Statutory Auditor is appointed by the shareholder in the general meeting.	Internal Auditor is appointed by the Board.
ii.	Scope of the work	The scope of work is defined in the Companies Act.	The scope of work includes the adherence of management policies and procedures and indentifies the weakness in the internal control.
iii.	Removal of Auditor	Statutory Auditor can be removed by the shareholders.	Internal Auditor can be removed by the Board.
iv.	Remuneration	It is fixed by the shareholders.	It is fixed by the board.
v	Audit Report	It is submitted to the appointing Authority.	It is submitted to the Board as a suggestion to improve weakness in the internal control.



E. (i) AUDITING AND ASSURANCE STANDARDS RELATING TO AUDIT OF INVENTORIES

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 consum-able 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.

The following features of inventories have an impact on the related 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 jewelry.

(ii) AUDITING AND ASSURANCE STANDARDS RELATING TO AUDIT OF FIXED ASSETS

Introduction

- i. 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; and
 - are expected to be used during more than one period.



- ii. 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".

EDUCATION INSTITUTION

The special steps involved in the audit of an educational institution are the following:

- 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.
- 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, specially the decisions as regards the operation of bank accounts and sanctioning of expenditure.
- 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.
- 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.
- 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.
- 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.
- See that free studentship and concessions have been granted by a person authorised to do so, having regard to the prescribed Rules.
- Confirm that fines for late payment or absence, etc., have either been collected or remitted under proper authority.
- Confirm that hostel dues were recovered before students' accounts were closed and their deposits of caution money refunded.
- Verify rental income from landed property with the rent rolls, etc.



- Vouch income from endowments and legacies, as well as interest and dividends from investment; also inspect the securities in respect of investments held.
- 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.
- Report any old heavy arrears on account of fees, dormitory rents, etc., to the Managing Committee.
- 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.
- 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.
- Verify that the Provident Fund money of the staff has been invested in appropriate securities.
- 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.
- Vouch all capital expenditure in the usual way and verify the same with the sanction for the Committee as contained in the minute book.
- Vouch in the usual manner all establishment expenses and enquire into any unduly heavy expenditure under any head.
- See that increase in the salaries of the staff have been sanctioned and minuted by the Committee.
- 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.
- 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.
- 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.
- 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.



AUDIT OF HOSPITAL

The following points are to be considered necessary for conducting an audit of Hospital.

- Check the letter of appointment to ascertain the scope of responsibilities.
- 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.
- Examine, evaluate and verify the system of internal check, internal control and determine the nature, timing and the extent of the audit procedures.
- Vouch the entries in the Patient's Bill Register with a copies 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.
- 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.
- Interest and/ or dividend income should be vouched with reference to the Investment Register and Interest and Dividend warrants.
- 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.
- Where receipts of subscription show a significant deviations from budgeted figures, it should be thoroughly inquired into and the matter be brought to the notice of the trustees or the Managing Committee.
- Government grants or grants from local bodies should be verifies with the reference to the correspondence with the concerned authorities.
- Clear distinction should be made between the items of capital and revenue nature.
- The capital expenditure should be incurred under proper authorization by a valid resolution of the trustees or the Managing Committee.
- Verify the system of internal check as regards purchases and issue of stores, medicines etc.
- Examine that the appointment of the staff, payment of salaries etc. are duly authorized.
- Physically verify the investments, fixed assets and inventories.
- Check that adequate depreciation has been provided on all the depreciable assets.



CO- OPERATIVE SOCIETIES

Definition: 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 as per Section 17 of the Co-Operative Societies Act, 1912

- 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 under sub-section (1) 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 Co operative Societies under this Act.

The following points should be kept in mind where awains of an Co-operative society;

- 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 Co-operative 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.

For example In Maharashtra the co-operative societies are required to maintain cash book, general ledger, personal ledger, stock register, property register, etc.

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-in-trade, 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. A co-operative society cannot prescribe any other limit in its bye-laws which is violative of this provision. In addition to this, the Acts passed by the states may also passed by the States may also prescribe other restrictions as regards shareholding.

The auditor should see that the provision regarding shareholding is duly followed.

Restriction on Loan: As per section 29 A registered co-operative society can only grant loans to its members though, with prior approval of the Registrar, it may grant loans to other registered co-operative 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 (Sec.32 of the Central Co-operative Societies Act):

- 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.

Auditor's duty: The auditor should ascertain whether the requirement as to investment of the society funds are being observed.

Appropriation of profits: According to the Central Co-operatives Societies Act, 25% of the profits of a co-operatives society should be transferred to a Reserve Fund before distribution of dividend or payment of bonus to its members. However, the Registrar may, having regard to the financial position of the society, reduce the percentage of profits to be transferred to the Reserve Fund. But in any case, he cannot reduce it to less than 10% of the profits of the society.

Apart from the above mandatory provision, a co-operative society may, subject to the provisions of its bye-laws, appropriate its profits by way of transfer to other reserves, distribution of dividends to members, etc. However, appropriation of profits must be duly approved by the members of the society in the general meeting called for the purpose.

Contributions to charitable Purposes: According to Section 34, a registered society may, with the sanction of the Registrar, contribute an amount not exceeding 10% of the net profits remaining after the compulsory transfer to the reserve fund for any charitable purpose as defined in section 2 of the Charitable Endowments Act, 1890.

SPECIAL POINTS IN A CO-OPERATIVE SOCIETY

General Points: - In general while conducting audit of Co-operative society 'The auditor need to look into the followings: -

- 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 points:

- 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.

BANK AUDIT

Introduction:

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.

Type of Banking institutions prevailing in India:

- Commercial banks;
- Regional Rural banks;
- Co-operative banks;
- Development banks (more commonly known as 'term-lending institutions');
- Payment Banks; and
- Small Finance Banks

Financial Statements of a bank

As per the Third Schedule to the Banking Regulation Act, 1949, the Balance Sheet of a Bank should be presented in the following manner, with comparative figures for previous financial year –

Balance Sheet (Form A)	Schedule	P & L Account (Form B)	Schedule
Capital and Liabilities:		I. Income:	
Capital	1	Interest Earned	13
Reserves and Surplus	2	Other Income	14
Deposits	3		
borrowings	4		
Other Liabilities & Provisions	5		
Total		Total	
		II. Expenditure:	
		Interest Expended	15
		Operating Expenses	16
		Provisions & Contingencies	
		Total	
Assets:		III. Profit / Loss:	
Cash & Balances with RBI	6	Net Profit / (Loss) for the year Profit /	
Balances with Banks & Money at Call & Short Notice	7	(Loss) brought forward	
Investments	8		
		Total	
Advances	9	IV. Appropriations:	
Fixed Assets	10	Transfer to Statutory Reserves	
Other Assets	11	Transfer to Other Reserves	
		Transfer to Government / Proposed Dividend	
		Balance carried over to Balance Sheet	
Total		Total	

Auditing aspects of banking of financial Statement.



Advances: In relation advances made by bank an auditor need to review the followings:

- 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 scrutinising 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 with the banks cash book balance.
- To verify the amount of foreign currency held by bank and its translation at make rate on the date at which financial statement is prepared.

Balance with RBI:

- Inspect the ledger balance in each account with (a) bank confirmation certificates from Reserve Bank of India and (b) 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

Money at call & short notice:

- Examines the system of authorisation for unding money at short and call notice
- The call loan made by bank are not nettled off against call loan received by it.
- Ensure that money market lending's for more than 6th days are not classified under this head but as a deposit or advance based on their nature of learning.

Fixed and other Assets: -



The auditor has to ensure the following while audit of F .A (Fixed Assets) held by banks

- Accounting method of bank
- Ownership document
- To examine with reference to schedule of fixed assets to find neew assets acquired.
- To examise 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:

Barrowings:

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

Deposits: -

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

Capital Reserve and Surplus:

Capital:

- Examine the opening balance of capital
- Examine with special resolution of shareholder or MOA about increase in authorized capital durig 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.

Other Liabilities and provision:

The auditor may verify the various items under the head "other liabilities and provisions" in the following manner.

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.
- All the telegraphic transfers and demand drafts issued by a branch should be immediately confirmed by advices to the branches concerned. On payment of these instruments, the paying branch should send a debit advice to the originating branch.
- If the paying branch does not receive proper confirmation of any telegraphic transfers or demand draft from the issuing branch, it should take immediate steps to ascertain the reasons.
- 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 are entered.) Cases of frequent cancellation and reissuance of drafts, pay orders, etc., should be carefully looked into by a responsible official.

Others (Including Provisions)

It may be noted that the figure of advances and investments in the balance sheet of a bank excludes provisions in respect thereof made to the satisfaction of auditors. The issue of determining the adequacy of provision for doubtful advances is discussed in detail under advances chapter of this Guidance Note. The auditor should examine other provisions and other items of liabilities in the same manner as in the case of other entities. Specifically, in case of tax deducted by the bank and payable to the government authorities before the due date, this function may be centralized or decentralized. While verifying this, the auditor must check whether tax has been correctly deducted from payments as per the provisions of the Income Tax /Act, 1961 and paid on or before the due date as specified under the /Act or Rules therefore. Many a times in case of branch audit, reporting has to be done before the due date of paying tax deducted at source for the month of March. In such cases the auditor should report delays observed till the date of his verification and clearly bring out the fact that he has not verified the payment of tax, due date of which would be after the date of the audit report.

Contingent Liabilities and Bills for Collection:

In respect of contingent liabilities, the auditor is primarily concerned with seeking reasonable assurance that all contingent liabilities are identified and properly valued. To this end, the auditor should, generally follow the audit procedures given below:

- The auditor should verify whether there exists a system whereby the non fund based facilities to parties are extended only to their regular constituents, etc.
- Ascertain whether there are adequate internal controls to ensure that transactions giving rise to contingent liabilities are executed only by persons authorised to do so and in accordance with the laid down procedures.
- The auditor should also examine whether in case of LCs for import of goods, as required by the abovementioned Master Circular on guarantees and co-acceptances, the payment to the overseas suppliers is made on the basis of shipping documents and after ensuring that the said documents are in strict conformity with the terms of LCs.
- Ascertain whether the accounting system of the bank provides for maintenance of adequate records in respect of such obligations and whether the internal controls ensure that contingent liabilities are properly identified and recorded.
- Performs substantive audit tests to establish the completeness of the recorded obligations. Such tests include confirmation procedures as well as examination of relevant records in appropriate cases.
- Review the reasonableness of the year-end amount of contingent liabilities in the light of previous experience and knowledge of the current year's activities.



- Review whether comfort letters issued by the bank has been considered for disclosure of contingent liabilities.

Bills for Collection

- The auditor should examine whether the bills drawn on other branches of the bank are not included in bills for collection.
- Inward bills are generally available with the bank on the closing day and the auditor may inspect them at that time. The bank dispatches outward bills for collection soon after they are received. They are, therefore, not likely to be in hand at the date of the balance sheet. The auditor may verify them with reference to the register maintained for outward bills for collection.
- The auditor should also examine collections made subsequent to the date of the balance sheet to obtain further evidence about the existence and completeness of bills for collection.
- In regard to bills for collection, the auditor should also examine the procedure for crediting the party on whose behalf the bill has been collected. The procedure is usually such that the customer's account is credited only after the bill has actually been collected from the drawee either by the bank itself or through its agents, etc. This procedure is in consonance with the nature of obligations of the bank in respect of bills for collection.

Treasury Operation-Foreign Exchange and Derivatives:

- While innovative products and ways of trading create new possibilities for earnings for the bank, they also introduce novel and sometimes unfamiliar risks that must be identified and managed. Failure to do so can result losses entailing financial and reputational consequences that linger long after the loss has been recognized in financial statements. Hence, auditor should assess controls as part of audit work.
- It is imperative that an auditor obtains a complete overview of the treasury operations of a bank before the commencement of the statutory audit. After conducting appropriate risk assessment of the treasury processes, the audit program needs to be designed in a manner that it dovetails into not just the control assessments of the treasury process but there is an assurance that the figures appearing in the financial statements as well as the disclosures are true and reflect fairly the affairs of the bank treasury.

Reports to be given to be given by bank Auditors:

- The Auditors' Report should state whether the Balance Sheet, Profit and Loss Account and Cash Flow Statement of the Bank, show a true and fair view of the financial position / result of operations / cash flows respectively, for the period under audit. This is applicable in respect of Nationalised Banks, as well as Banking Companies.
- **Unaudited Branches:** Information relating to number of unaudited Branches should be given. Also, information in respect of Advances, Deposits, Interest Income and Interest Expense for such unaudited Branches should be collected and disclosed in the Audit Report.



- **Additional Matters:** Sec.30 (3) of Banking Regulation Act requires the Auditor to state the following-
 - Whether or not the information and explanations required by him have been found to be satisfactory,
 - Whether or not transactions of the Company fall within the powers of a Banking Company,
 - Whether or not the returns received from the Branch Offices of the Company have been found adequate for the purposes of his audit,
 - Whether the Profit & Loss Account shows a true balance of Profit or Loss for the period covered by such account, &
 - Any other matter, which the Auditor considers should be brought to the notice of Shareholders of the Company.
- **LFAR:** Auditors of Public Sector Banks, Private Sector Banks & Foreign Banks (as well as their Branches), are required to submit Long Form Audit Report (LFAR) on various matters specified by RBI.
- **Certificates:** In addition to Reports, the Auditors of Bank Branches as well as Central Statutory Auditors of Banks, have to furnish / issue various "Certificates" as required by RBI and other Regulations.

AUDIT OF TRUSTS

When conducting the audit of a charitable institution, the auditor should consider the following matters:

- **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.
- **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.
- **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.
- **Internal Check:** Examination of the system of internal check, especially as regards the accounting of the amounts collected.
- **Collection & Deposit of income:** Check that the amounts received towards income have been duly collected, received and deposited into the bank regularly and promptly.



- **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.
- Legacies received: Verify the amounts of legacies received by reference to correspondence with any figures and other available information's.
- 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.
- **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.
- **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.
- **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.
- **Physical verification:** The auditor should physically verify the cash in hand, inventories and fixed assets.

AUDIT OF MUNICIPALITIES AND PANCHAYATS (LOCAL BODIES)

The major objective of audit of Municipalities and Panchayats are enumerated below;

- 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.



The following points are to be considered necessary for carrying on audit of Municipalities and panchayats (Local Bodies);

- To ensure that the expenditures 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.

Self Examination Questions:

1. Write short notes on Branch and Joint Audit.
2. What are the factors to be considered while carrying on audit of Share and Debentures?
3. Precautions to be taken care of while carrying on audit of divisible profits and dividends.
4. Distinguish between Statutory and Internal Audit.
5. Discuss the Auditing and Assurance Standards relating to audit of Inventories and Fixed Assets.
6. Mention the special steps involved in conducting the audit of college?
7. What are the points which you as an Auditor would look into while auditing the accounts of a Hospital?
8. Discuss the important points in an audit of Co operative Society.
9. While carrying an audit of a Bank what are the special factors considered by you.
10. Write short notes on audit of Local Bodies.

State whether the following statements are true or false.

1. "Branch office", in relation to a company, means any establishment described as such by the company.
2. Where a company has a branch office, the accounts of that office shall be audited by auditor appointed at EGM.



3. Where the branch office of a company 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.
4. The branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the Audit committee.
5. In big corporate more than one persons or firm of Chartered Accountants are appointed as a Joint Auditor for conducting the audit of the company.
6. "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.
7. Final dividend is declared in the general meeting.
8. Statutory Auditor is appointed by the shareholder in the general meeting.
9. Internal Auditor can be removed by the Board.
10. If the debentures are issued as collateral security to the banks or creditors then auditor needs to ensure that such issue is approved by debenture trustee.

[Answer: True, False, True, False, True, True, True, True, True, False.]

Fill in the blanks:

1. Final dividend is declared in the _____.
2. If the debentures are issued as collateral security to the banks or creditors then auditor needs to ensure that such issue is approved by _____.
3. A predetermined _____ rate of interest is payable on debentures irrespective of the fact that company has earned the profit or not.
4. Debenture holders are _____ of the company.
5. Where debentures are issued by a company, then company shall create a _____ account out of the profits of the company.
6. For protecting the interest of debenture holders the company is bound to form _____.
7. Responsibility to report fraud, as applicable to company's auditor applies to _____ auditor.
8. Splitting of shares shall be authorised by _____.



9. A company may issue debentures with an option to convert such debentures into _____.
10. Statutory Auditor is appointed by the shareholder in the _____ meeting.

[Answer: General Meeting, BOD, Rate, Creditors, Debenture Redemption Reserve, Debenture Trustee, Branch, AOA, Shares, General]

Match the Following:

	Column A		Column B
1	More than one persons or firm of Chartered Accountants are appointed	A	Branch Audit
2	Section 68 of the Co. Act 2013	B	Alteration of Share Capital
3	Section 63 the Co. Act 2013	C	Power of company to Purchase its Own Securities
4	Section 61 of the Co. Act 2013	D	Joint Audit
5	Section 139 of the Companies Act 2013.	E	Issue of Bonus Shares

[Answer: D, C, E, B, A]

Multiple choice questions:

- Audit of debenture is covered under section-
 (A)Section 70
 (B)Section 71
 (C)Section 72
 (D)Section 73
- Declaration of dividend is covered under setion-
 (A)Section 122
 (B)Section 123
 (C)Section 124
 (D)Section 125
- Statutory Auditor is appointed by the shareholder in the
 (A)General Meeting
 (B)Statutory Meeting
 (C)EGM
 (D)Board Meeting



4. Statutory Auditor can be removed by the
(A) Shareholders
(B) Audit committee
(C) BOD
(D) None of the above.
5. Internal Auditor is appointed by the
(A) Board
(B) Audit committee
(C) Shareholder
(D) None of the above

[Answer: B, B, A, A, A]